

OFFICIAL STATEMENT

New Issue
Book-Entry Only

Ratings: Moody's: Aa2
Standard & Poor's: AA-

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.

\$257,375,000

THE CITY OF SEATTLE, WASHINGTON

MUNICIPAL LIGHT AND POWER IMPROVEMENT AND REFUNDING REVENUE BONDS, 2008

DATED: DATE OF INITIAL DELIVERY

DUE: APRIL 1, AS SHOWN ON INSIDE COVER

The City of Seattle Municipal Light and Power Improvement and Refunding Revenue Bonds, 2008 (the "Bonds"), will be issued as fully registered bonds under a book-entry only system, registered in the name of Cede & Co. as registered owner and nominee for The Depository Trust Company ("DTC"), New York, New York. 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 is payable semiannually on each April 1 and October 1, beginning April 1, 2009. The principal of and interest on the Bonds are payable by the Bond Registrar (currently, The Bank of New York Mellon 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 (i) finance certain capital improvements to and conservation programs for the Light System of The City of Seattle (the "City"), (ii) refund certain of the City's outstanding Municipal Light and Power bonds, and (iii) pay the costs of issuance of the Bonds. See "Use of Proceeds."

The Bonds are subject to 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 \$1,299,755,000 par amount of Outstanding Parity Bonds (as of December 1, 2008) 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 and Cost of Power—Purchased Power Arrangements." See "Security for the 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.

The Bonds are offered when, as and if issued, subject to the approving legal opinion of Foster Pepper PLLC, Seattle, Washington, Bond Counsel. 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 30, 2008.

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: December 10, 2008

\$257,375,000

THE CITY OF SEATTLE, WASHINGTON
MUNICIPAL LIGHT AND POWER IMPROVEMENT AND REFUNDING REVENUE BONDS,
2008

SERIAL BONDS

<u>DUE</u> <u>APRIL 1</u>	<u>AMOUNTS</u>	<u>INTEREST</u> <u>RATES</u>	<u>YIELDS</u>	<u>CUSIP NUMBERS*</u>
2009	\$ 6,360,000	4.00%	1.04%	812643BQ6
2010	9,210,000	5.00	2.50	812643BR4
2011	12,680,000	5.00	2.75	812643BS2
2012	13,485,000	5.00	3.25	812643BT0
2013	14,500,000	5.00	3.50	812643BU7
2014	15,340,000	5.00	3.75	812643BV5
2015	16,335,000	5.25	4.00	812643BW3
2016	15,155,000	5.00	4.53	812643BX1
2017	10,460,000	5.00	4.83	812643BY9
2018	11,045,000	5.00	5.09	812643BZ6
2019	10,020,000	5.25	5.25	812643CA0
2020	10,560,000	5.25	5.50	812643CB8
2021	11,145,000	5.50	5.60	812643CC6
2022	10,220,000	5.50	5.75	812643CD4
2023	10,810,000	5.75	5.85	812643CE2

TERM BONDS

<u>DUE</u> <u>APRIL 1</u>	<u>AMOUNTS</u>	<u>INTEREST</u> <u>RATES</u>	<u>YIELDS</u>	<u>CUSIP NUMBERS*</u>
2025	\$ 23,640,000	6.00%	6.05%	812643CG7
2029	56,410,000	5.75	5.90	812643CL6

* CUSIP is a trademark of the American Bankers Association. The CUSIP numbers herein are provided by Standard and Poor's, CUSIP Service Bureau, a division of The McGraw-Hill Companies, Inc. CUSIP numbers are provided for convenience of reference only. CUSIP numbers are subject to change. The City takes no responsibility for the accuracy of such CUSIP numbers.

THE CITY OF SEATTLE

CITY OFFICIALS AND CONSULTANTS

MAYOR AND CITY COUNCIL

Greg Nickels	Mayor
Richard Conlin	President, City Council
Tim Burgess	Council Member
Sally Clark	Council Member
Jan Drago	Council Member
Jean Godden	Council Member
Bruce Harrell	Council Member
Nick Licata	Council Member
Richard McIver	Council Member
Tom Rasmussen	Council Member

SEATTLE CITY LIGHT DEPARTMENT

Jorge Carrasco	Superintendent
Sung Yang	Chief of Staff
Roy Lum	Interim Chief Financial Officer
Andrew Gallo	Chief Compliance Officer
Chris Heimgartner	Customer Service and Energy Delivery Officer
Steve Kern	Power Supply and Environmental Affairs Officer
DaVonna Johnson	Interim Human Resources Officer

CITY ADMINISTRATION

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

BOND COUNSEL

Foster Pepper 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 the City believes to be reliable. However, the City makes no representation regarding the accuracy or completeness of the information provided in Appendix E—Book-Entry Transfer System, which has been furnished by DTC. The information and expressions of opinion in this Official Statement are subject to change without notice, and neither the delivery of this Official Statement nor any sale made hereunder will, under any circumstances, create an implication that there has been no material change in the affairs of the City since the date of this Official Statement. 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.

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

\$257,375,000

THE CITY OF SEATTLE, WASHINGTON

MUNICIPAL LIGHT AND POWER IMPROVEMENT AND REFUNDING REVENUE BONDS,
2008

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"), its municipal light and power plant and system (the "Light System"), and its Municipal Light and Power Improvement and Refunding Revenue Bonds, 2008 (the "Bonds"), in connection with the offering and sale of the Bonds. The Bonds are to be issued by the City in accordance with Ordinance 121941, passed on September 26, 2005, as amended by Ordinance 122838, passed on November 10, 2008, and Ordinance 122807, passed on September 22, 2008, (collectively, the "Bond Ordinance"), and Resolution 31105, adopted on December 10, 2008 (the "Bond Resolution" and together with the Bond Ordinance, the "Bond Legislation").

The Bond Ordinance is attached hereto as Appendix A. Appendix B contains the form of legal opinion of Foster Pepper PLLC ("Bond Counsel"). Appendix C contains the Department's audited 2007 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. Capitalized terms that are not defined herein have the meanings set forth in the Bond Legislation.

IN THE PREPARATION OF THE PROJECTIONS SET FORTH IN THIS OFFICIAL STATEMENT, THE CITY HAS MADE CERTAIN ASSUMPTIONS WITH RESPECT TO FUTURE CONDITIONS. WHILE THE CITY BELIEVES THESE ASSUMPTIONS ARE REASONABLE FOR THE PURPOSE OF THE PROJECTIONS, ACTUAL RESULTS DEPEND UPON FUTURE CONDITIONS THAT MAY DIFFER FROM THOSE ASSUMPTIONS. THE CITY DOES NOT REPRESENT OR GUARANTEE THAT ACTUAL RESULTS WILL REPLICATE SUCH PROJECTIONS. THE ELECTRIC INDUSTRY HAS UNDERGONE 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. THE CITY HAS NOT COMMITTED TO PROVIDE INVESTORS WITH UPDATED PROJECTIONS.

NEITHER THE DEPARTMENT'S INDEPENDENT AUDITORS NOR ANY OTHER INDEPENDENT ACCOUNTANTS HAVE COMPILED, EXAMINED OR PERFORMED ANY PROCEDURES WITH RESPECT TO THE PROSPECTIVE 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.

DESCRIPTION OF THE BONDS

General

The Bonds are issuable only as fully registered bonds under a book-entry transfer system, registered in the name of Cede & Co. as bondowner and nominee for The Depository Trust Company ("DTC"), New York, New York. DTC will act as initial securities depository for the Bonds. Purchasers will not receive certificates representing their interest in the Bonds purchased.

The Bonds will be dated the date of their initial delivery, and will mature on the dates and in the amounts set forth on the inside cover of this Official Statement. Interest on the Bonds is payable semiannually on each April 1 and October 1, beginning April 1, 2009, at the rates set forth on the inside cover of this Official

Statement. Interest on the Bonds will be computed on the basis of a 360-day year consisting of twelve 30-day months. Principal is payable on April 1 in the years and in the amounts shown on the inside cover of this Official Statement.

The principal of and interest on the Bonds are payable by the City’s Bond Registrar, currently the fiscal agent of the State of Washington (currently The Bank of New York Mellon in New York, New York) to DTC, which is obligated in turn to remit such payments to its participants for subsequent disbursement to beneficial owners of the Bonds, as described herein under “Description of the Bonds—Book-Entry Transfer System” and Appendix E.

Redemption of the Bonds

Optional Redemption. The Bonds maturing on or before April 1, 2019, are not subject to redemption prior to maturity. The City reserves the right and option to redeem the Bonds maturing on or after April 1, 2020, at any time on or after April 1, 2019, in whole or in part (within one or more maturities to be selected by the City and randomly within a maturity in such manner as the Bond Registrar may determine) at the price of par plus accrued interest.

Mandatory Redemption. If not previously redeemed as described above, the Term Bonds will be called for redemption (in such manner as DTC will determine) at a price of par plus accrued interest to the redemption date, on April 1 in the years and amounts so designated.

<u>TERM BOND</u>		<u>TERM BOND</u>	
<u>Years</u>	<u>Amounts</u>	<u>Years</u>	<u>Amounts</u>
2024	\$ 11,465,000	2026	\$ 12,910,000
2025*	12,175,000	2027	13,675,000
		2028	14,485,000
		2029*	15,340,000

* Maturity.

If the City redeems Term Bonds under the optional redemption provisions described above or purchases or defeases Term Bonds, the Term Bonds so redeemed, purchased or defeased (irrespective of their actual redemption or purchase prices) will be credited at the par amount thereof against one or more scheduled mandatory redemption requirements for those Term Bonds in a manner to be determined by the City or, if no such determination is made, on a *pro rata* basis.

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.”

Effect of Redemption. Interest on Bonds called for redemption will cease to accrue on the date fixed for redemption unless the Bond or Bonds called are not redeemed when presented pursuant to the call.

Purchase

The City reserves the right to purchase any of the Bonds 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 & 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.

Refunding or Defeasance of Bonds

The City may issue refunding bonds or use money available from any other lawful source to redeem and retire, release, refund, or defease the Bonds (the “Defeased Bonds”). If sufficient money and/or Government Obligations (taking into account known earned income from the investment thereof) are set aside in a special fund pledged irrevocably to the redemption, retirement or defeasance of the Defeased Bonds (the “Trust Account”), then all right and interest of the owners of the Defeased Bonds in the covenants of the Ordinance and in the Gross Revenues and the funds and accounts pledged to the payment of the Defeased Bonds, other than the right to receive the funds so set aside and pledged, will cease and become void. Such owners thereafter will have the right to receive payment of the principal of and interest or redemption price on the Defeased Bonds from the Trust Account.

USE OF PROCEEDS

Purpose

The Bonds are being issued to (i) finance certain capital improvements to and conservation programs for the Light System, (ii) refund certain of the City’s outstanding Municipal Light and Power bonds, as described under “Refunding Plan,” (iii) pay the costs of issuance of the Bonds.

Refunding Plan

A portion of the proceeds from the sale of the Bonds is expected to be used to refund all or a portion of the City’s outstanding Municipal Light and Power Adjustable Rate Revenue Bonds described below (collectively, the “Refunded Bonds”). A portion of the proceeds of the Bonds, together with other available money of the City, will be used to pay principal of and accrued interest on the redemption date of the refunded bonds, following the publication of the required notices of redemption for each respective series of refunded bonds.

REFUNDED BONDS

	Maturity	Amount (\$)	Redemption Price	Redemption Date	Cusip Number
Adjustable Rate Revenue Bonds, 1990	11/01/2015	12,600,000	100	02/04/2009	812642VQ6
Adjustable Rate Revenue Bonds, 1991A	05/01/2016	25,000,000	100	02/04/2009	812642VS2
Adjustable Rate Revenue Bonds, 1991B	05/01/2011	7,000,000	100	02/04/2009	812642VR4
Adjustable Rate Revenue Bonds, 1993	11/01/2018	12,800,000	100	02/04/2009	812642ZY5
Adjustable Rate Revenue Bonds, 1996	06/01/2021	<u>14,575,000</u>	100	02/04/2009	812642J64
Total		71,975,000			

Sources and Uses of Funds

The proceeds of the Bonds are expected to be applied as follows:

SOURCES OF FUNDS

Par Amount of the Bonds	\$ 257,375,000
Net Original Issue Premium (Discount)	<u>3,243,923</u>
Total Sources of Funds	<u>\$ 260,618,923</u>

USES OF FUNDS

Construction Fund Deposit	\$ 185,000,000
Redemption of Refunded Bonds	71,975,000
Costs of Issuance*	<u>3,643,923</u>
Total Uses of Funds	<u>\$ 260,618,923</u>

* Includes legal fees, financial advisory fees, rating agency and printing costs, underwriter's discount, contingency, 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 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 14 and 15(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 "Financial Information—Taxation and Intergovernmental Payments"), but do include the unconditional obligation to make payments under certain power purchase contracts. See "Contingent Obligations" below.

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 nine series of bonds issued since 1997. As of December 1, 2008, the City had \$1,299,755,000 principal amount of Outstanding Parity Bonds. See “Use of Proceeds—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, any Future Parity Bonds, and all other obligations for which revenues have been pledged, 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 “Financial Information” and Appendix A—Bond Ordinance—Section 18(d).

Reserve Fund Requirement

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, or
- (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, which is defined in the Bond Ordinance as the date on which no Parity Bonds issued prior to 2001 are outstanding, “Reserve Fund Requirement” will mean, for any issue of 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 Requirement for all such Future Parity Bonds.

Under the Bond Ordinance, the City is permitted to provide for the Reserve Fund Requirement with a surety bond or letter of credit consistent with the Bond Ordinance requirements. The City currently has a surety bond purchased from Financial Security Assurance, Inc. in the amount of \$109,513,320, expiring on August 1, 2029, providing the entire Reserve Fund Requirement before the issuance of the Bonds. After the issuance of the Bonds, the Reserve Fund Requirement will be \$122,892,850. The City will satisfy the amount of the Reserve Fund Requirement beyond the amount of the surety bond within five years from the date of issuance of the Bonds.

Future Parity Bonds

The Bond Ordinance authorizes the issuance of 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 Net Revenue (see definition below) 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.

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. See Appendix A—Bond Ordinance—Section 15(g).

The Bond Ordinance authorizes the issuance of Refunding Parity Bonds without the requirement of meeting the above provisions. See Appendix A—Bond Ordinance—Section 15(h).

Payment Agreements

The City may enter into Parity Payment Agreements that constitute a charge and lien on Net Revenue equal to that of the Parity Bonds. The prerequisites described above for the issuance of Future Parity Bonds apply to the City’s incurrence of obligations under any Parity Payment Agreements. See Appendix A—Bond Ordinance—Section 1—Definitions—Annual Debt Service—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 \$71,975,000 principal amount of outstanding Municipal Light and Power Subordinate Lien Bonds as of December 1, 2008, all in variable rate mode, all of which will be refunded by the Bonds. 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. Those 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.

City Cash Pool

The City’s Director of Finance is authorized to make loans to individual funds participating in the City’s common investment portfolio (the “Cash Pool”) by carrying such funds in a negative cash position for a period of up to 90 days, or for a longer period upon approval by the City Council by ordinance, to the extent such loans can be supported prudently by the Cash Pool and the borrowing fund is reasonably expected to be able to repay the loan. Such loans bear interest at the Cash Pool’s rate of return. Currently, there are no Cash Pool loans to the Department. See “The City of Seattle—Financial Management—Interfund Loans.”

Contingent Obligations

The Department has in the past and may in the future enter into various agreements, such as power purchase agreements or financial derivative contracts, 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 Bonds and the Subordinate Lien Bonds. See “Power Resources and Cost of Power—Purchased Power Arrangements.”

SEATTLE CITY LIGHT

Introduction

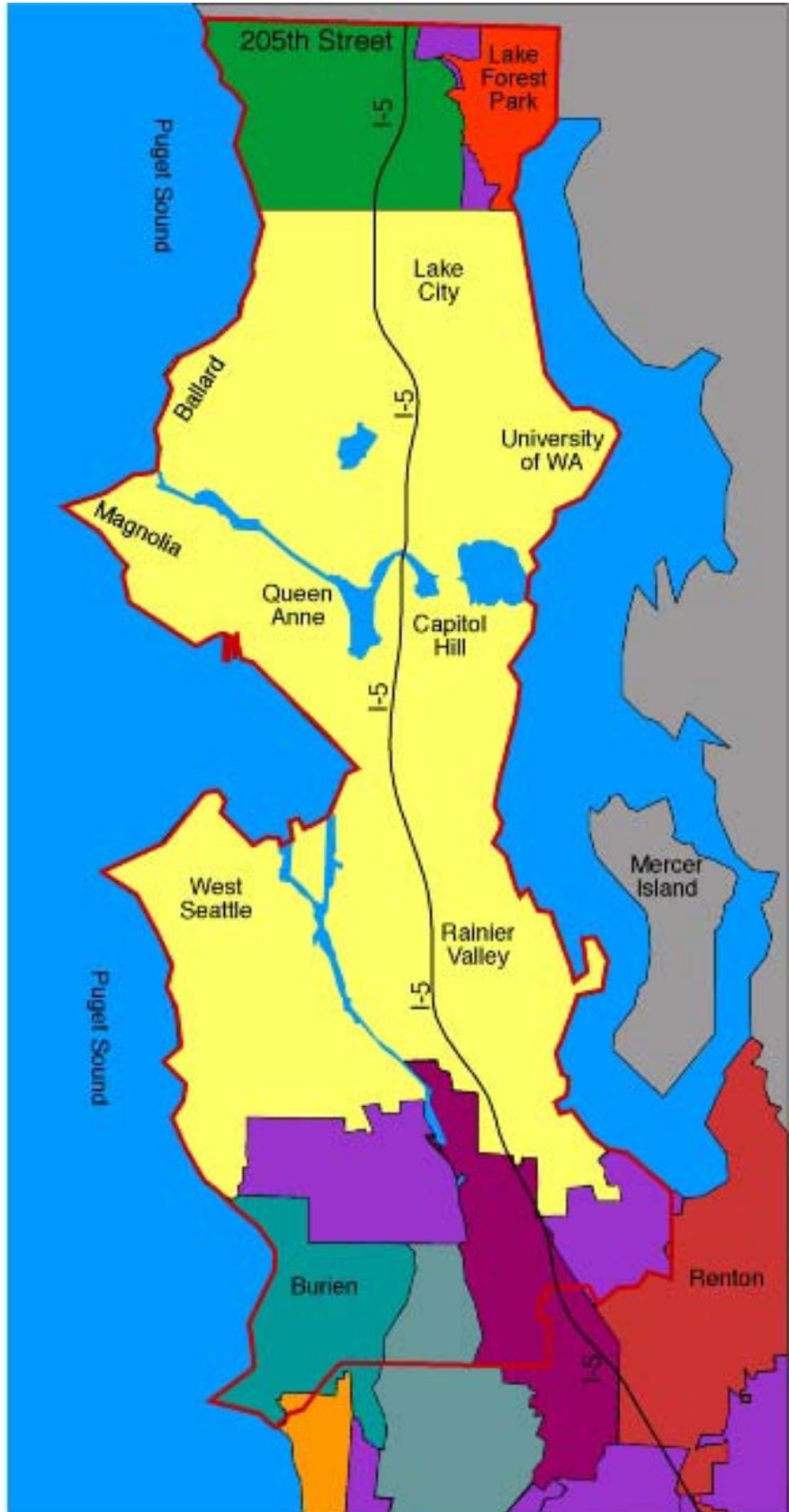
The Department is a municipally-owned electric utility. In 1905, the City began providing its customers with electricity generated by the Cedar Falls Hydroelectric Plant (the “Cedar Falls Project”), which was the first municipally-owned hydroelectric facility in the nation. By 1910, operational responsibility for the City’s electric system had been assigned to 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 “Service Area” immediately below for a description of the Department’s service area.

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. The growth of the Department’s electric load since 1951 has resulted exclusively from development within the service area. The map on the following page depicts the Department’s service area.

Sales to customers located outside the City’s boundaries but within the service area represent approximately one-sixth of retail power sales and revenues. The Department has two franchise agreements with King County that have expired and are in the process of being renewed, and franchises with the cities of Shoreline, Burien, Lake Forest Park, SeaTac, and Tukwila that expire between 2015 and 2018. These six jurisdictions represented over 99 percent of the Department’s retail power sales outside the City in 2007. The Department’s service area also includes portions of the cities of Normandy Park and Renton.

- Service Area
- Burien
- Lake Forest Park
- Normandy Park
- Renton
- SeaTac
- Seattle
- Shoreline
- Tukwila
- Unincorporated King County



Management

Seattle City Light 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 set forth 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, subject to reconfirmation every four years.

In 2006, the City established the City Light Advisory Committee (the "Advisory Committee"), consisting of three members designated by the Mayor and three by the City Council. The Advisory Committee terminates on January 31, 2010, and its responsibilities are purely advisory. In January 2008, the Advisory Committee issued its most recent annual report, in which it made a number of recommendations in the areas of financial policies, risk management and integrated resource planning.

The Department is organized into four operating units: Power Supply and Environmental Affairs, Customer Service and Energy Delivery, Financial Services, and Human Resources. An officer leads each unit, and each officer reports to the Superintendent. The Chief of Staff coordinates communication, government relations, and external affairs, and reports to the Superintendent.

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

Jorge Carrasco, Superintendent, was appointed Superintendent of the Department in 2004 and reconfirmed by the City Council in 2008. Prior to joining the Department, Mr. Carrasco was president of American Water Services, an investor-owned provider of water and wastewater services to cities and industrial and federal facilities. Mr. Carrasco has also served as general manager of East Bay Municipal Utility District and as city manager for the cities of Scottsdale, Arizona, and Austin, Texas. In Austin, his responsibilities included oversight of the city's electric utility. Mr. Carrasco holds a bachelor's degree from the University of Texas and a master's degree in Business Administration from St. Edwards University in Austin.

Sung Yang, Chief of Staff, was appointed as Chief of Staff of the Department in 2006. Prior to joining the Department, Mr. Yang served as Director of Council Relations and Senior Policy Advisor to the Mayor. He has also served as both Deputy Director and Director of Government Relations for the Washington State Department of Community Trade and Economic Development, and has taught graduate level courses in Public Administration as an adjunct professor at Seattle University. Mr. Yang holds a bachelor's degree from the University of Washington, and a *juris* doctor degree from the University of Washington School of Law.

Roy Lum, Interim Chief Financial Officer, was appointed as Interim Chief Financial Officer in October 2008. Mr. Lum has been the Director of the Information Services Technology Division of the Department since June 2006. Prior to joining the Department, he served as chief information officer for LifeEra, a member of United Health Group, and worked for two years as deputy director of the Washington State Department of Information Services. Mr. Lum has a bachelor's degree from the University of California at Davis and a master's degree in computer information systems from Boston University.

Andrew Gallo, Chief Compliance Officer, was appointed as Chief Compliance Officer in August 2008. He previously worked as the assistant general counsel to the Electric Reliability Council of Texas. He is a licensed attorney in the state of Texas and received his law degree from the College of William and Mary.

Chris Heimgartner, Customer Service and Energy Delivery Officer, was appointed as Customer Service and Energy Delivery Officer in 2006. Prior to joining the Department, he worked for Pacific Gas and Electric for over 20 years, most recently as Division Construction Superintendent. Mr. Heimgartner holds a bachelor's degree from Rensselaer Polytechnic Institute and a master's degree in Business Administration from St. Mary's College.

Steve Kern, Power Supply and Environmental Affairs Officer, was appointed to this position in 2007. He has worked with the Department as a consultant on power marketing and also has served as an interim Power

Supply and Environmental Affairs Officer. Previously, he worked for Puget Sound Energy and Avista Corporation in both the gas and electric energy sides of the business. His experience also includes work at Duke Energy, Arizona Public Services and PNGC Power, and as a principal in Lands Energy Consulting. He has a bachelor of science degree in Geological Sciences from the University of Washington, and has completed graduate work in business at Seattle University.

DaVonna Johnson, Interim Human Resources Officer, joined the Department in 2004 and most recently served as the Talent Acquisition and Development Manager in Human Resources. Prior to joining the Department, she worked for the City for five years, and has worked in both the public and private sectors. Ms. Johnson has bachelor's and master's degrees in Business Administration from Washington State University.

Employee Relations

As of January 1, 2008, the Department had 1,821 full-time equivalent employees. State law requires municipal agencies to bargain collectively with formally recognized collective bargaining units. Currently, 14 bargaining units represent approximately 80 percent of the Department's regular full-time employees. Most contracts will expire on December 31, 2010. The carpenters union, which previously was part of the Joint Crafts Council, is bargaining a separate agreement with the City. The City is also bargaining with the auto mechanics union. Both of these contracts expired on December 31, 2007. The machinists union's contract expires on December 31, 2008, and negotiations have yet to begin. The City has reached an agreement with the electrical workers union for a new contract that would begin in January 2009. 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."

Almost all of the Department's employees 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."

POWER RESOURCES AND COST OF POWER

Overview of Resources

The Department typically meets the majority of its power requirements from three major sources: the Boundary Hydroelectric Project (the "Boundary Project"), the Skagit Hydroelectric Project (the "Skagit Project"), and the Bonneville Power Administration ("BPA"). The Boundary Project and the Skagit Project together include four large hydroelectric facilities and, together with three small hydroelectric facilities, generated approximately 6.5 million megawatt hours ("MWh") of electrical energy in 2007, which was about 60 percent of the Department's firm requirements. Output from the Department's hydroelectric plants can vary significantly from year to year due to the variability of water conditions, and has been less than average in recent years.

The Department and 15 other public and investor-owned utilities in the Pacific Northwest have agreed to coordinate the operation of their power generation systems through the Pacific Northwest Coordination Agreement (the "Coordination Agreement"), in order to maximize the firm capability and reliability of the coordinated system. The Coordination Agreement went into effect in 1965 and terminates in 2024.

Table 1 provides a summary of the Department's owned and contracted power resources as of January 1, 2008, together with estimates of power available under critical and average water conditions. The Federal Energy Regulatory Commission ("FERC") licenses most hydroelectric projects in the United States. Table 2 provides actual output for power resources, including exchanges and market sales and purchases, for the past five years.

TABLE 1
OWNED AND PURCHASED POWER RESOURCES
(AS OF SEPTEMBER 1, 2008, UNAUDITED)

	Nameplate 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 Project ⁽³⁾	1,070	3,017,509	4,297,884	2011
Skagit Hydroelectric Project				
Gorge	173	698,909	957,456	2025
Diablo	169	583,621	822,300	2025
Ross	460	556,353	872,314	2025
Small Hydro ⁽⁴⁾	48	142,065	181,598	varies
Purchased Resources				
Bonneville ⁽⁵⁾	970	4,918,018	5,982,801	N/A
Priest Rapids ⁽⁶⁾	5	17,940	21,607	2052
GCPHA ⁽⁷⁾	64	237,736	237,736	2030/2031
High Ross ⁽⁸⁾	varies	311,836	311,836	N/A
Lucky Peak ⁽⁹⁾	113	236,814	236,814	2030
Stateline Wind Project ⁽¹⁰⁾	54	N/A	365,800	N/A
Boundary Article 49 ⁽¹¹⁾	(48)	(374,201)	(374,201)	N/A

FOOTNOTES TO TABLE 1:

- (1) Critical water conditions represent the lowest sequence of streamflows experienced in the Pacific Northwest over a historical period of record (1929-1998). The firm energy capability of hydroelectric resources is the amount of electrical energy produced under critical water conditions. Actual water conditions are expected to be better than critical water conditions about 95 percent of the time.
- (2) Figures in this column represent the average amount of electrical energy that would be produced over all of the water conditions in the period 1929-1998.
- (3) The Department has commenced the relicensing process. See “Department-Owned Resources—Boundary Project.”
- (4) The Newhalem Project’s FERC license expires in 2027, and the Tolt Project’s FERC license expires in 2028. The Cedar Falls Project is not subject to FERC licensing requirements
- (5) Approximate. The Department has a contract with BPA for its Slice product, which entitles the Department to 4.6676 percent of the actual output and costs of the Federal System. The Department has a contract for 239 average megawatts (“aMW”) of the Block product. The Department’s contract extends through October 2011, and all parties are currently engaged in negotiating the terms of a new contract. See “Purchased Power Arrangements—Bonneville Power Administration.”
- (6) The Department’s share of the Priest Rapids project.
- (7) Grand Coulee Project Hydroelectric Authority, the Department’s 50 percent share of installed capacity of five hydroelectric plants, which have different FERC license expiration dates. The project is part of an irrigation project and does not provide capacity in January.
- (8) The Department’s contract with British Columbia provides capacity from November through March in an amount equal to 532 megawatts (“MW”) minus the actual peak capability of the Ross Plant, which varies depending on water conditions. The contract extends until 2066.
- (9) The project is part of an irrigation project and does not provide capacity in January.
- (10) Stateline Wind Project is not a hydroelectric project. Average output is based on contract terms.
- (11) The Department’s obligation to Public Utility District No. 1 of Pend Oreille County (“Pend Oreille PUD”) related to the Boundary Project.

Source: Seattle City Light, Power Production Division and Power Management Division

TABLE 2
HISTORICAL ENERGY RESOURCES
(MWh) (UNAUDITED)

	2003	2004	2005	2006	2007
Department-Owned Generation					
Boundary Project	3,589,057	3,515,550	3,476,443	4,342,243	3,648,913
Skagit Hydroelectric Project					
Gorge	930,783	923,815	777,054	872,070	1,076,525
Diablo	744,016	777,727	655,039	745,604	834,982
Ross	727,698	681,221	563,263	640,799	859,267
Cedar Falls/Newhalem	71,914	73,468	43,174	84,053	71,579
South Fork Tolt	49,000	60,696	45,102	53,823	56,106
Subtotal	6,112,468	6,032,477	5,560,075	6,738,592	6,547,372
Energy Purchases					
Bonneville	4,713,124	4,661,054	4,332,240	5,479,386	5,723,841
Box Canyon	47,452	59,062	25,874	0	0
Priest Rapids	310,716	316,203	288,329	24,505	25,396
Columbia Storage Power Exchange	26,350	0	0	0	0
GCPHA ⁽¹⁾	235,496	254,030	249,331	242,188	255,297
High Ross	315,246	305,246	310,246	316,044	313,903
Lucky Peak	292,348	275,248	226,256	407,209	273,137
Metro Cogeneration ⁽²⁾	14,333	6,027	0	0	0
Klamath Falls ⁽³⁾	654,502	718,638	581,497	100,003	0
Stateline Wind Project	216,290	348,672	327,302	384,539	385,546
Seasonal Exchanges Received ⁽⁴⁾	145,946	108,696	108,696	39,432	360,996
Wholesale Market Purchases ⁽⁵⁾	1,218,705	2,389,071	1,034,211	1,333,979	947,937
Subtotal	8,190,508	9,441,947	7,483,982	8,327,285	8,286,053
Total Department Resources	14,302,976	15,474,424	13,044,057	15,065,877	14,833,425
Minus Offsetting Energy Sales:					
Firm Energy Sales and Marketing Losses ⁽⁶⁾	383,313	463,425	403,832	404,486	444,249
Seasonal Exchange Delivered ⁽⁴⁾	124,480	90,580	90,580	90,580	363,663
Wholesale Market Sales	4,265,168	5,359,491	2,846,599	4,580,325	3,822,098
Total Net Energy Resources	9,530,015	9,560,928	9,703,046	9,990,486	10,203,415

FOOTNOTES TO TABLE 2:

- (1) Grand Coulee Project Hydroelectric Authority.
- (2) The purchased power contract with King County for West Point cogeneration expired in 2005 and was not renewed.
- (3) The purchased power contract with Klamath Falls expired in 2006.
- (4) The Northern California Power Agency (“NCPA”) was the primary counterparty with which power exchange contracts existed through 2006. In 2007, contracts with several additional counterparties, such as Sacramento Municipal Utility District and the Lucky Peak Project, took effect; thus there was more power exchange activity during 2007.
- (5) Purchases to compensate for low water conditions and to balance loads and resources.
- (6) Energy provided to Pend Oreille PUD under the Boundary Project’s FERC license. Figures on this line also include incremental losses due to expanded activity in the wholesale market.

Source: Seattle City Light, Accounting Division

Table 3 provides actual payments related to owned and contracted resources and revenue, in the case of Department sales to third parties. Production expenses are for operations and maintenance and do not include capital or debt service. Department-owned resources are discussed in detail first, followed by contract resources.

In 2005, low rainfall in the Pacific Northwest, approximately 75 percent of normal, resulted in less hydroelectric output. Combined with high prices for natural gas, this resulted in higher market prices for electricity in 2005 than the rest of the 2003-2007 period. Given the lower than normal water conditions, the Department sold less power in 2005 than other years in the 2003-2007 period, and net revenue is the lowest during this period. See “Wholesale Market Sales and Purchases.”

In 2006, the Department ended a contractual purchase from the Klamath Falls combustion turbine, and replaced the purchase with lower-priced electricity from BPA. These two changes explain the decrease in the average unit cost of power in 2006 and 2007.

TABLE 3
COST OF POWER SUPPLY: 2003-2007
(\$000) (UNAUDITED)

	2003	2004	2005	2006	2007	2007 Average Unit Cost
Wholesale Market Purchases ⁽¹⁾	\$ 24,233	\$ 49,714	\$ 62,214	\$ 47,361	\$ 33,431	\$ 35.27
Other Power Purchases:						
Bonneville	\$ 157,088	\$ 130,975	\$ 131,517	\$ 154,718	\$ 175,791	
Box Canyon	1,278	1,501	421	0	0	
Priest Rapids	2,614	2,450	2,589	1,348	1,361	
Grand Coulee	4,830	5,679	3,307	5,964	3,531	
High Ross	13,358	13,371	13,377	13,387	13,395	
Lucky Peak	12,239	16,783	15,767	16,438	15,473	
Metro Cogeneration	786	267	100	0	0	
Klamath Falls	36,281	42,022	43,806	12,006	0	
Stateline Wind Project	11,326	18,254	18,004	20,335	20,448	
Integration of Wind Resources	1,551	0	0	0	0	
Seasonal Exchanges Received ⁽²⁾	2,804	2,359	33	382	3,189	
Booked-Out Long-Term Contra-Purchases ⁽³⁾	0	0	0	(11,261)	(9,582)	
Power-Related and Other ^{(4) (5)}	13,204	(1,081)	(354)	22,661	68,047	
Bonneville Billing Credits ⁽⁶⁾	(2,965)	(3,047)	(3,066)	(3,078)	(3,411)	
Subtotal ⁽⁷⁾	\$ 254,394	\$ 229,533	\$ 225,501	\$ 232,900	\$ 288,242	\$ 39.28
Production:						
Hydro Projects ⁽⁸⁾	\$ 20,211	\$ 20,283	\$ 18,896	\$ 19,564	\$ 24,974	
Control and Other	7,251	6,959	7,802	8,049	8,936	
Subtotal	\$ 27,462	\$ 27,242	\$ 26,698	\$ 27,613	\$ 33,910	\$ 5.18
Total Power Supply Expense	\$ 306,089	\$ 306,489	\$ 314,413	\$ 307,874	\$ 355,583	
Minus Offsetting Power Revenue:						
Wholesale Power Sales	\$ 137,651	\$ 163,265	\$ 149,650	\$ 176,244	\$ 161,154	\$ 42.16
Other Power Sales ⁽⁵⁾	34,082	20,028	23,332	52,720	109,305	
Subtotal	\$ 171,733	\$ 183,293	\$ 172,982	\$ 228,964	\$ 270,459	
Net Cost of Power	\$ 134,356	\$ 123,196	\$ 141,431	\$ 78,910	\$ 85,124	
Total Energy Requirement (MWh)	9,530,015	9,560,928	9,703,046	9,990,486	10,203,415	
Average Unit Cost (Dollars/MWh) ⁽⁹⁾	\$ 14.10	\$ 12.89	\$ 14.58	\$ 7.90	\$ 8.34	

FOOTNOTES TO TABLE 3:

- (1) Purchases to compensate for low water conditions and to balance loads and resources. Excludes wheeling costs. The Department experienced severe low water conditions in 2005. See “Wholesale Market Sales and Purchases.”
- (2) Beginning in 2006, non-monetary power exchange transactions were measured at fair value in accordance with a new accounting standard. Previously, these transactions were valued at the blended weighted-average cost of power.
- (3) Effective December 2006, revenues and long-term purchased power are reported net of long-term purchased power booked out against short-term sales that were not physically delivered. Amounts prior to 2006 have not been reclassified.
- (4) Includes power-related wholesale purchases less Boundary Project encroachment.
- (5) Non-monetary power exchange transactions have increased significantly in recent years and these transactions are recorded at fair value effective in 2006, for both sales and purchases. These transactions include basis, shaping capacity, parking, related bookouts, and other. Prior to 2006, non-monetary power exchange transactions were recorded at the weighted average cost of power.
- (6) Billing credits received from BPA for the Tolt Project.
- (7) 2003 and 2004 exclude the effect of \$100 million of amortized power costs. \$300 million of power costs were deferred in 2001 and amortized at \$100 million per year over a three-year period from 2002 through 2004.
- (8) Includes operation and maintenance costs only.
- (9) Average cost of power supplied to service area customers after recognizing the net revenue or cost associated with wholesale power sales and purchases. See “Wholesale Market Sales and Purchases.”

Source: Seattle City Light, Accounting Division

Department-Owned Resources

The Department owns and operates the Boundary Project on the Pend Oreille River in eastern Washington, the Skagit Project on the Skagit River in western Washington, and three smaller hydroelectric plants in western Washington: the Newhalem Project, the Cedar Falls Project and the Tolt Project.

Boundary Project. The Boundary Project is located on the Pend Oreille River in northeastern Washington near the British Columbia and Idaho borders, approximately 250 miles from Seattle. The plant was placed in service in 1967, and is a significant factor in the Department's ability to meet its load requirements. It has a nameplate peak capability of 1,070 MW and expected power output of 4.3 million MWh under average water conditions. The Boundary Project is operated under a FERC license that expires on September 30, 2011. The Department has started the process to relicense the Boundary Project, using FERC's Integrated License Process. The Department plans to file its preliminary licensing proposal in April 2009 and the final license application in September 2009. As of September 1, 2008, there were no competing proposals on file at FERC.

The most recent FERC-mandated independent safety inspection in August 2005 concluded that the Boundary Project facilities were in good condition.

The Boundary Project's FERC license requires that up to 48 MW of the Boundary Project's capacity be assigned, at cost, to 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 increased to the maximum allowable amount of 48 MW in August 2005. The Department's delivery obligation to Pend Oreille PUD is expected to remain at this level through the term of the next FERC license for the Boundary Project.

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 immediately below under "Skagit Project."

Skagit Project. The Ross, Diablo and Gorge hydroelectric plants, which comprise the Skagit Project, 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 nameplate capability of the three plants is 802 MW. Expected power output under average water conditions is 2.7 million MWh.

The three plants that comprise the Skagit Project are licensed as a unit by FERC. FERC-required independent inspections of the Skagit Project in 2007 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 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 protested on environmental and other grounds. After a protracted period of litigation and negotiation, an agreement (the "High Ross Agreement") was reached under which British Columbia agreed to provide the Department, for 80 years commencing in 1986, with power equivalent to the planned increase in the output of the Ross Plant in lieu of the Department's construction of the addition. The agreement is subject to review by the parties every ten years. The most recent review concluded in 1998 and did not result in any changes to the agreement. The Department is expected to recommend seeking a waiver of the pending 2008 review.

The Department's annual payments to British Columbia 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 remaining annual \$21.8 million payments over the period through 2035. Payment of equivalent maintenance and operation costs and certain other charges began in 1986 and will continue for 80 years. The power delivered from B.C. Hydro under this agreement in 2007 amounted to 313,903 MWh. The Department's contract with British Columbia provides capacity from November through March in an amount equal to 532 MW minus the actual peak capability of the Ross Plant, which fluctuates with water conditions.

If British Columbia discontinues power deliveries, the High Ross Agreement authorizes the Department to proceed with the originally proposed construction and obligates British Columbia 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. In 2007, this encroachment amounted to 0.5 percent of the Boundary Project's electrical energy output.

Cedar Falls Project. The Cedar Falls Project, built in 1905, is located on the Cedar River, approximately 30 miles southeast of Seattle. The Cedar Falls Project was constructed before the adoption of the Federal Water Power Act of 1920 and is not subject to licensing by FERC. Cedar Falls Project power is delivered through an interconnection with Puget Sound Energy. The nameplate peak capability of the plant is 30 MW. Power production in 2007 at the Cedar Falls Project was 66,298 MWh.

Newhalem Project. The Newhalem Creek Hydroelectric Project (the "Newhalem Project") is located on Newhalem Creek, a tributary of the Skagit River, and 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 nameplate peak capability of the plant is 2.3 MW. Power generation in 2007 was 5,281 MWh.

Tolt Project. 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 nameplate peak capability of the installed unit is 16 MW. Power production at the Tolt Project in 2007 was 56,106 MWh. To reduce its cost of power from the Tolt Project, the Department entered into a Billing Credits Generation Agreement with BPA in 1993, under which BPA 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 BPA. Payments to the Department under the agreement commenced in 1996 and amounted to \$3.4 million in 2007.

Purchased Power Arrangements

In 2007, the Department purchased approximately 46 percent of its total Department resources from other utilities in the region, including BPA, under long-term purchase contracts. Some of these contracts 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 regularly purchases power under the WSPP Inc. (formerly Western Systems Power Pool) Agreement and the Block and Slice Power Sales Agreement described immediately below. Some of 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 into, 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 contingent obligations are permitted to be characterized as maintenance and operation charges, and thus would be payable from Gross Revenues of the Department prior to the payment of Parity Bond debt service.

Bonneville Power Administration. BPA markets power from the Federal Columbia River Power System (the “Federal System”), comprised of 31 federal hydroelectric projects, several non-federally-owned hydroelectric and thermal projects in the Pacific Northwest region, and various contractual rights with installed generating capacity of 22,000 MW and a firm power capability of approximately 8,600 aMW. Of this amount, approximately 7,400 aMW is available for Tier I System Resources that can be sold to the Department. 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 33 percent of the region’s electrical energy requirements. BPA’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. BPA sells electric power at cost-based wholesale rates to more than 130 utility, industrial and governmental customers in the Pacific Northwest. BPA is required by law to give preference to government-owned utilities and to customers in the Pacific Northwest region in its wholesale power sales.

A Block and Slice Power Sales Agreement with BPA provides for purchases of power by the Department over the ten-year period beginning October 1, 2001. Under the contract, power is delivered in two forms: a shaped block product (“Block”) and a slice of the system product (“Slice”). Under the Block product, power is delivered to the Department in monthly amounts approximately 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 aMW annually as a Block for the period from October 1, 2001, through September 30, 2006, and 278.2 aMW from October 1, 2006, through September 30, 2011.

The Department’s share of Block power has been gradually reduced by approximately 40.6 aMW to 237.6 aMW, due to the savings from energy efficiency programs. BPA pays some of the costs of the Department’s programs, and BPA purchases some of the energy savings realized by the Department’s conservation programs. The Department’s entitlement to Block power is reduced by the amount of conserved energy savings purchased. In 2007, BPA’s payment was \$5.7 million.

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 currently subject to an annual true-up adjustment to reflect actual costs. Power available under the Slice product varies with water conditions, federal generating capabilities and fish and wildlife restoration requirements. The Department may resell output from the Slice under specified conditions, and may use the Slice to displace Department generation. Under critical water conditions, the Slice product provides approximately 325 aMW of power annually.

Although the current Block and Slice Power Sales Agreement does not expire until September 30, 2011, the Department has executed a new, 17-year Block and Slice Power Sales Agreement that will continue the delivery of BPA power, starting on October 1, 2011. Under this contract, which BPA executed on December 5, 2008, the Department is estimated to be able to purchase approximately 533.7 aMW, or 94 percent of the amount of power it is currently purchasing from BPA under similar pricing terms. However, because BPA limited the portion of the Federal System available for the Slice product, the Department’s portion of the Slice product will be reduced to an estimated 3.43167 percent of the actual output of the Federal System. Based on this BPA allocation, the Department’s power from BPA will be delivered in roughly equal Slice and Block components. Exact amounts of power eligible to be purchased by the Department, together with the corresponding Block and Slice components, will be determined by BPA based on the Department’s actual 2010 load, the BPA preference customer load and estimated future loads, and through public processes run by BPA.

Energy Northwest. The City is a member of Energy Northwest, a municipal corporation and joint operating agency organized under State law that currently has, as members, ten public utility districts and three municipalities (including the City), 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, of which one was placed in commercial operation in 1984 and the others were terminated in the 1980s. Pursuant to separate Net Billing Agreements with Energy Northwest and BPA with respect to certain of the projects (the “Net Billed Projects”), the Department is obligated unconditionally to pay Energy Northwest its *pro rata* share of the total annual costs of the Net Billed Projects, including debt service. Payment by BPA 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 BPA credits against amounts that the Department owes BPA 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 Department’s share 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 BPA, BPA 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.

Lucky Peak Project. The Lucky Peak Hydroelectric Power Plant (the “Lucky Peak Project”) 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. Power generation in 2007 was 273,137 MWh. The nameplate peak capacity is 113 MW, but the plant operates only during the irrigation season, so it provides no peak capacity in the winter.

The Department entered into a 50-year power purchase and sales contract in 1984 with the Districts under which the Department will purchase all power generated by the Lucky Peak Project, 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 the Lucky Peak Project to a point of interconnection with the BPA transmission system. In 2007 and 2008, the Department entered into separate one-year exchange agreements for the output of the Lucky Peak Project.

Priest Rapids Project. Under two agreements effective through 2052, the Department purchases a portion of the output of the Priest Rapids Project, which is owned and operated by Public Utility District No. 2 of Grant County (“Grant PUD”). The Priest Rapids Project, which is comprised of two developments, Priest Rapids and Wanapum, both located on the Columbia River, has an installed capacity of 1,893 MW. Through October 2009, the Department is obligated to purchase 12.28 percent of the output of the Priest Rapids development available after Grant PUD meets its retail load. Beginning in November 2009, the Department is obligated to purchase 6.14 percent of the output of both the Priest Rapids development (855 MW total) and the Wanapum development (1,038 MW total), available after Grant PUD meets its retail load. However, because of Grant PUD’s rapidly increasing retail load, much of this contractually purchased power has been recalled by Grant PUD, and the Department currently receives only about 2 aMW from these contracts.

Grand Coulee Project Hydroelectric Authority. The Department, in conjunction with the City of Tacoma, Department of Public Utilities, Light Division (“Tacoma Power”), has power purchase agreements with three Columbia Basin irrigation districts for acquisition of power 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. The plants generate power only in the summer and thus have no winter peak capability. Plant output and costs are shared equally between the Department and Tacoma Power. In 2007, the Department received 255,297 MWh from the project.

Stateline Wind Project. An agreement with PacifiCorp Power Marketing, Inc. (now Iberdrola Renewables) provides for the Department’s purchase of wind-generated power and associated renewable energy credits

from the Stateline Wind Project in eastern Washington and Oregon. Through the end of the contract in 2021, the Department receives wind power with a maximum delivery rate of 175 MW per hour. Power delivered under the contract is expected to average about 27 percent of the maximum delivery rate.

The Department also entered into a related ten-year agreement with PacifiCorp to purchase integration and exchange services for up to 150 MW of the Stateline Wind Project output. Under this agreement, PacifiCorp delivers the Department's share of the Stateline Wind Project output to the Mid-Columbia market hub two months after it is generated. The balance of the Department's Stateline Wind Project output (25 MW) is currently scheduled and delivered to the Department by Iberdrola Renewables. The integration and exchange agreement with PacifiCorp terminates at the end of 2011. The Department received 385,546 MWh of wind-generated power under the Stateline Wind Project purchase contract in 2007.

Seasonal Exchanges. The Northern California Power Agency ("NCPA") exchange agreement provides for the Department to deliver 60 MW of capacity and 90,580 MWh of power to NCPA in the summer. In return, NCPA delivers 46 MW of capacity and 108,696 MWh of power 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 (upon seven years' notice) after 2014.

In 2007, the Department began a seasonal exchange with the Sacramento Municipal Utility District ("SMUD"), in which the Department provides scheduling and delivery services for up to 15 MW of power at the California-Oregon border that SMUD purchased from a renewable resource in the Pacific Northwest, the Sierra Pacific Industries Burlington Biomass Facility, which burns wood waste and produces electrical energy. The Department receives up to 25 MW of winter energy in payment for such services, and purchases from SMUD all of the renewable energy and environmental attributes associated with the resource in excess of 15 MW. The contract expires in 2018.

Wholesale Market Sales and Purchases

The Department has historically bought and sold power in wholesale power markets to balance its loads and resources. The amount of wholesale power purchased or sold has varied with water conditions and with changes in the Department's firm resource base. With its current resource portfolio, the Department expects to have surplus power available for sale in the wholesale market through 2011, even under adverse water conditions.

In 2005, low rainfall in the Pacific Northwest, approximately 75 percent of normal, resulted in less hydroelectric output. Combined with high prices for natural gas, this resulted in higher market prices for electricity in 2005 than the rest of the period 2003 through 2007. In the same year, the Boundary Project's output was 82 percent of normal and the Skagit Project's output was 69 percent of normal. The Department had less surplus electricity to sell than under normal conditions, and net revenue was the lowest in 2005 of any year in the 2003-2007 period. The average cost of the Department's wholesale purchases in 2005 was almost \$61 per MWh, compared to an average of \$31 per MWh for the period 2003 through 2007. Given the lower than normal water conditions, the Department sold less power in 2005 than in other years from 2003 to 2007, and net revenue was the lowest during this period.

Table 4 displays the Department's purchases and sales of power in the wholesale market over the period from 2003 through 2007.

TABLE 4
WHOLESALE MARKET SALES AND PURCHASES
(UNAUDITED)

	2003	2004	2005	2006	2007
Cost of Wholesale Purchases (\$000)*	\$ 24,233	\$ 49,714	\$ 62,214	\$ 47,361	\$ 33,431
Wholesale Market Purchases (MWh)	1,218,705	2,389,071	1,034,211	1,333,979	947,937
Average Cost (\$/MWh)	\$ 19.88	\$ 20.81	\$ 60.16	\$ 35.50	\$ 35.27
Revenue from Sales (\$000)*	\$ 137,651	\$ 163,265	\$ 149,650	\$ 176,244	\$ 161,154
Wholesale Market Sales (MWh)	4,265,168	5,359,491	2,846,599	4,580,325	3,822,098
Average Revenue (\$/MWh)	\$ 32.27	\$ 30.46	\$ 52.57	\$ 38.48	\$ 42.16
Net Revenue (\$000)	\$ 113,418	\$ 113,551	\$ 87,436	\$ 128,883	\$ 127,723
Sales Net of Purchases (MWh)	3,046,463	2,970,420	1,812,388	3,246,346	2,874,161

* Effective in 2003, wholesale sales and purchases that are bookouts are reported on a net basis.

Source: *Seattle City Light, Accounting Division*

Energy Risk Management

The Department's energy risk exposures are managed by the Power Management Division. Oversight of these risk management activities is carried out by the Risk Oversight Division. A Risk Oversight Council ("ROC"), consisting of the Department's Chief Financial Officer, Power Supply and Environmental Affairs Officer, Power Management Executive, and Director of Risk Management, meets at least twice per month to review recent events in the wholesale power markets and review the Department's market positions, exposures, risk policy compliance, and portfolio balancing strategies and plans. To manage energy risk exposure and thereby protect the interests of the ratepayers, the Department is authorized to buy or sell physical energy and associated products in the wholesale energy market up to 18 months prior to, and all the way up to, the hour of delivery. For longer term transactions, City Council approval is required. The Department's principal objective is to ensure that the Department meets its retail customer demand obligation in a way that generates additional value from its generation portfolio, with due consideration of risk. Risk tolerance levels are documented in a Wholesale Energy Risk Management Policy approved by the Mayor and the City Council.

Market Risk. The Department executes transactions in the wholesale energy 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.

Credit Risk. The Risk Oversight Division recommends credit limits to the Department's Chief Financial Officer based on its credit scoring and analysis. Credit exposures are calculated and monitored daily, and reports are provided to the ROC weekly. Before the Department enters into power sales transactions with a delivery period of one full month or more in the future, Risk Oversight Division staff determine whether the counterparty has sufficient available credit.

Conservation

The Department has pursued a policy of managing energy demand through a significant energy efficiency effort. As a result of the "Energy 1990" study, prepared in 1976, the City decided to pursue conservation, known in most parts of the country as energy efficiency, as an alternative to participating in certain Energy Northwest projects. During the 1980s, single-family residential measures dominated the Department's conservation program. Conservation incentive programs in the commercial, industrial and multifamily sectors were added in the 1990s. Because commercial and industrial programs are more cost-effective than residential programs, they now represent about 70 percent of the Department's cumulative savings, while residential accounts for the remaining 30 percent. In 2007, the Department achieved 7.57 aMW (66,312 MWh) of energy savings. Total savings since the program's inception amount to 119 aMW (1,044,000 MWh), representing nearly 11 percent of the Department's total energy needs in 2008.

The Department's 2008 Integrated Resource Plan ("IRP") calls for continued conservation of approximately 7.5 aMW per year and required additional study and effort to develop an accelerated conservation program that would increase this number significantly. The Department has released a Five-Year Conservation Action Plan that is expected to increase conservation savings to over 15 aMW (135,000 MWh savings in the first year) by 2011.

The power sales contract with BPA that took effect on October 1, 2006, provides a credit of \$0.50 per MWh against the amounts payable under BPA's rate schedules for investments in conservation and renewable resources. In BPA's fiscal year 2007, the Department received credits totaling \$2.5 million on the Department's power bill. The Department expects to receive similar credits in BPA's next two fiscal years.

A secondary power sales contract, the Conservation Acquisition Agreement, allows the Department to either self-fund energy savings or to request funding from BPA for energy saving projects initiated after October 1, 2006. In 2007, the Department reported energy savings as self-funded, and no financial transactions have transpired for projects initiated after October 1, 2006. As part of the Conservation Acquisition Agreement, the Department is allowed to report energy savings from projects initiated prior to October 1, 2006. These

energy savings fall under the terms and conditions of the previous agreement, the Conservation Augmentation Agreement. In 2007, the Department reported energy savings of 15,261 MWh and received \$1.9 million.

Integrated Resource Plan

The Department's 2008 IRP identifies how much additional power the Department needs through 2027. It considers options for the Department to meet growing resource demand, estimated at 1.3 percent per year on an annual average basis before the effect of new conservation programs. The IRP combines options into resource portfolios, and evaluates candidate resource portfolios against four criteria: reliability, cost, environmental impact, and risk.

The recommended strategy identifies how the Department can meet expected customer needs through 2027. The resource acquisition steps are:

- (i) Accelerate the acquisition of cost-effective conservation;
- (ii) Institute cost-effective seasonal power exchanges designed to increase available winter energy, beginning in 2009;
- (iii) Exercise the Department's preference rights to purchase power from BPA in a new contract beginning in 2011;
- (iv) Plan for the near- to mid-term purchase of output from low-cost renewable resources such as a small, new landfill gas project; and
- (v) Acquire output from other renewable resources such as geothermal, biomass and wind beginning in 2012, to meet resource adequacy requirements and comply with State requirements.

The recommended resource strategy is a continuation of the Department's policy of obtaining low-cost power with low environmental impacts for its ratepayers, while making the most of its existing resources. Conservation is the first choice, followed by seasonal exchanges that help shape resources to load.

Renewable Portfolio Standards and I-937

Initiative 937 ("I-937") was approved by State voters in November 2006. Under I-937, utilities with a retail load of more than 25,000 customers, such as the Department, are required to use eligible renewable resources or acquire equivalent renewable energy credits, or a combination of both, to serve three percent of their load by January 1, 2012, nine percent by January 1, 2016, and 15 percent by January 1, 2020. I-937 also requires utilities to pursue all available conservation that is cost-effective, reliable and feasible, and imposes deadlines for meeting conservation targets.

Under I-937, existing hydropower is not considered a renewable resource, but incremental hydropower is considered a renewable resource if it is produced as a result of efficiency improvements completed after March 30, 1999, to hydroelectric projects owned by a qualifying utility or to hydroelectric generation in irrigation pipes and canals located in the Pacific Northwest, where the additional generation does not result in new water diversions or impoundments.

The City evaluated the impacts of I-937 in its 2008 IRP and is evaluating the potential for cost effective, reliable and feasible conservation measures that could be derived from more efficient energy use, production and distribution within the Light System. The City does not anticipate having to acquire additional renewable resources to meet I-937's requirements prior to 2016. To comply with the requirements due on January 1, 2016, and beyond, the Department expects to acquire new renewable resources to serve its needs.

TRANSMISSION AND DISTRIBUTION

Department-Owned Transmission

The Department operates 657 miles of transmission facilities. The principal transmission line is a generation interconnection line transmitting power from the Skagit Project to the Department's service area.

In 1994, the Department signed an agreement with BPA for the acquisition of ownership rights to 160 MW of transmission capability over BPA's share of the Third AC Intertie, which connects the Pacific Northwest region with California and the Southwest. The benefits from this investment include avoidance of BPA'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 City's contractual arrangement with BPA does not allow Seattle to market excess transmission capabilities to third parties.

Transmission Contracts

Transmission Arrangements with BPA. The bulk of the Department's remote generation and other market transactions utilize BPA's point-to-point ("PTP") transmission service agreement. Contracts with BPA provide the Department with 1,962 MW of transmission capacity under the PTP through 2025. The Department uses this for delivery of power from remote generators to serve load and for short-term transactions. BPA has announced that it will revise its transmission tariff in 2011, but the terms and conditions are not yet known.

Power supplied to the Department by B.C. Hydro under the High Ross Agreement is transmitted over BPA's lines under a separate PTP transmission service agreement extending through 2035. This agreement has been assigned to Powerex Corporation, a British Columbia corporation tasked with carrying out certain responsibilities of B.C. Hydro with respect to the High Ross Agreement, including the delivery of High Ross power. Under the provisions of the transmission assignment agreement, Powerex pays BPA directly for all costs associated with the High Ross PTP 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 and Grant PUD for transmission of power from the Grand Coulee Project Hydroelectric Authority, with Puget Sound Energy for transmission of power from the Cedar Falls Project and Tolt Project, and with other utilities. The Department also has a contract with PacifiCorp for future transmission of power from the Stateline Wind Project.

The Department will require additional purchases of transmission in the future in order to accommodate the delivery of additional renewable resource acquisitions to the Department's retail customers. The Department may purchase non-firm transmission for its sales of power in the wholesale market.

ColumbiaGrid

In 2006, a group of investor-owned and public utilities, including the Department, joined together with BPA to form ColumbiaGrid. ColumbiaGrid is currently providing transmission planning services to the Pacific Northwest and is considering additional transmission-related service offerings. ColumbiaGrid is not a Regional Transmission Organization and provides services on a bilateral, contractual basis.

Open Access Transmission Services

The Department currently has no transmission customers, but is committed to offering comparable service upon receiving a request for transmission services. The Department is finalizing an open access transmission tariff, which will be publicly available on the Department's website and will not be filed with FERC.

Retail Service

The Department owns, operates and maintains overhead and underground transmission and distribution facilities within a 131-square-mile service territory. The distribution system consists of 1,692 miles of overhead and 438 miles of underground wiring. The Department operates 18 unattended distribution substations throughout the service area, which supply power to the distribution system's primary feeders and ultimately to the Department's retail customers. Most of the distribution system is radial design, which means that a single feeder provides electrical energy to customers; they would lose service if that feeder failed. Customers in the downtown Seattle, University District and First Hill neighborhoods are served by a more reliable, multiple-feeder network.

Operation and Maintenance

The Department updates its Transmission and Distribution Capacity Plan as needed to track the changing electrical power system loads. Through this plan, the Department makes provisions and recommendations for capacity projects related to transmission, substation, communications, and distribution facilities to serve the system loads. The budget submittal requests the funds and defines the scope of work to implement these recommendations.

The Department's System Control Center is staffed 24 hours a day, every day; it provides control over dam operations and monitors delivery of power to the service area. Staff use an Energy Management System, which is a real-time distributed computer system that provides information about loads and resources to the power dispatchers so they can properly balance load and resources.

The Department is enhancing student outreach and apprenticeship programs. The Department's goal is to maintain an adequate number of skilled employees, as many of the Department's current employees reach retirement eligibility and begin to retire.

The Department is implementing an Outage Management System and Work Management System to collectively improve customer service while making the most of the Department's staff and other resources. Formed in 2007, the Asset Management Division will complement the above technologies and programs by incorporating a long-term, comprehensive perspective into asset repair or replacement decisions.

FINANCIAL INFORMATION

Historical Sales

Total sales of power to residential customers, which constituted 32.3 percent of the Department's power sales in 2007, increased slightly during the 2003-2007 period. A 0.9 percent average annual increase in the number of customers and 0.3 percent average annual increase in consumption per customer led to a 1.3 percent average annual increase in residential sales.

Total sales of electrical power to non-residential customers, which constituted 67.7 percent of the Department's electrical power sales in 2007, increased 2.2 percent on an average annual basis during the period 2003-2007. The total number of non-residential customers has increased at an average annual rate of 3.5 percent, but sales per customer have fallen by 1.3 percent on an average annual basis.

Power sales in the Department's service area can be affected by variations in weather conditions. Annual peak loads are typically experienced in the winter season. Colder than normal winter weather patterns can result in higher consumption, due to the extensive use of electricity for heating. However, warmer than normal conditions in summer months do not lead to increases in load of comparable magnitude because of the limited use of residential air conditioning.

A record peak load of 2,060 MW was recorded in December 1990 due to unusually cold weather. The peak load for the period 2003-2007 was 1,822 MW and occurred in 2006, during a period of cold temperatures and record rainfall.

TABLE 5
RETAIL CUSTOMERS, POWER SALES AND ENERGY REQUIREMENTS
(UNAUDITED)

	2003	2004	2005	2006	2007
Average Number of Customers					
Residential	330,979	333,560	336,364	339,640	343,542
Non-Residential	34,466	36,939	39,506	39,590	39,585
Total Customers	365,445	370,499	375,870	379,230	383,127
Energy Sales (MWh)					
Residential	2,952,615	2,952,664	2,954,848	3,060,651	3,103,550
Non-Residential	5,953,329	6,067,861	6,206,617	6,393,854	6,496,361
Total Energy Sales	8,905,944	9,020,525	9,161,465	9,454,505	9,599,911
Peak Demand (MW)	1,646	1,799	1,714	1,822	1,768
Energy Requirements (MWh)					
Total Energy Sales	8,905,944	9,020,525	9,161,465	9,454,505	9,599,911
Energy used in Operation	31,556	31,812	32,939	33,709	33,515
Energy for Public Lighting ⁽¹⁾	72,357	0	0	0	0
System Losses ⁽²⁾	520,158	508,591	508,642	502,272	569,989
Total Energy Requirements ⁽³⁾	9,530,015	9,560,928	9,703,046	9,990,486	10,203,415

(1) From 2000 through 2003 (2000 through 2002 are not shown), the cost of streetlighting in the City was recovered through the rates charged to all City rate classes. Prior to 2000 and after 2004, these costs were paid by the City's General Fund, and the power imputed to streetlighting from 2004 through 2007 is included in the figure shown for the Non-Residential rate class in Table 5.

(2) Includes transmission and distribution losses.

(3) Firm energy required in the Department's service area.

Source: *Seattle City Light, Accounting Division*

Largest Customers

The Department's ten largest customers in 2007, in order of their annual dollar amount billed, are shown in Table 6.

TABLE 6
TOP TEN CUSTOMERS

Name	Annual \$ Amt. Billed	% of Total Revenue	Annual MWh
Nucor Corporation	\$ 17,878,166	3.30	402,633
City of Seattle*	15,632,676	2.88	194,545
University of Washington	14,666,376	2.70	315,491
Boeing Company	12,181,079	2.25	240,319
Sabey Corporation	7,954,939	1.47	161,617
King County	7,661,404	1.41	149,717
U.S. Government	5,751,579	1.06	109,883
Saint Gobain	5,100,667	0.94	112,143
Unico Properties/Union Square Ltd.	4,026,363	0.74	68,182
Ash Grove Cement	3,744,915	0.69	82,788
Total	\$ 94,598,164	17.44	1,837,318
Total Retail Revenue	\$ 542,363,032	100.00	

* Includes streetlighting, which covers both the costs to provide electricity to streetlights and the costs to install, service, repair, and replace streetlights.

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, in both 2005 and 2006, the City Council adopted resolutions establishing a financial policy that rates should be set to produce a debt service coverage ratio of 2.0x on all Parity Bonds and Subordinate Lien Bonds. Coverage was 2.37x in 2006, but it was 1.88x in 2007.

The Department's current rates allow it to address other financial policies adopted by the City Council. Resolutions adopted by the City Council require that the Department's rates be set at levels that will ensure that net revenue available to fund capital requirements in each calendar year will be positive with a probability of at least 95 percent, taking into account the variability of cash flows resulting from the uncertainty of water conditions, market prices and system load. For purposes of implementing this financial policy, net revenue available to fund capital requirements is defined as the amount of revenue remaining after payment of operating and maintenance costs, principal of and interest on outstanding debt, taxes, deposits to the Bond Reserve Account, all other current obligations, and deposits to the Contingency Reserve Account.

City Council resolutions also established the Contingency Reserve Account, which was to reach and maintain a balance of \$25 million, and required that the Department target a minimum month-end operating cash balance of \$30 million to absorb fluctuations in its operating cash flow. In May 2005, the City funded the Contingency Reserve Account with \$25 million taken from the Bond Reserve Account and authorized the Department to withdraw the funds from the Bond Reserve Account and meet the reserve requirement with a surety bond.

The resolutions further required that the Department set rates to achieve a debt-to-capitalization ratio of 60 percent by year-end 2010. The debt-to-capitalization ratio is the total amount of debt outstanding divided by the sum of the accumulated equity and debt outstanding.

Taxation and Intergovernmental Payments

The Department pays a utility tax to the City equal to six percent of Gross Revenues from retail sales, 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 by these jurisdictions where the Department has generating facilities. In addition, under the terms of franchise agreements with several suburban cities, the Department makes monthly payments to the Cities of Shoreline, Burien, Lake Forest Park, SeaTac, and Tukwila in amounts ranging from 3.9051 percent to six percent of the revenue from rates charged to customers residing in those cities. See "Retail Rates" immediately below.

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 ("PURPA"). The Department never has been cited for failing to comply with PURPA, and believes that it is operating in compliance with PURPA's requirements.

Since 1980, the City Council has conducted periodic reviews of the Department's rate levels and rate structure, normally 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 operating budget, capital improvements 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 that will allocate the revenue requirement among the various rate classes in accordance with City policy. The City Council makes final decisions through passage of a rate ordinance.

Rate Changes: 2004-2008. Over the last five years, the Department's rates have decreased by about 12 percent. In April 2004 and November 2005, the Department passed through decreases in BPA power rates resulting in Department rate decreases of about two percent each time. There were no rate changes in 2006. As of January 1, 2007, a general rate decrease of 8.4 percent was implemented. In the rate review leading to that decrease, rates were set for the two-year period 2007-2008.

Current Rates. See Table 7 for comparative rates and bills paid by the various customer classes, and Table 8 for a comparison of annual amounts paid by the Department's customers and the customers of neighboring utilities.

Rates for Customers Outside the City of Seattle. Rates for Department customers in suburban franchise cities and unincorporated King County are higher than rates for customers located within the Seattle city limits. In 1998 and 1999, the Cities of Shoreline, Lake Forest Park, SeaTac, and Burien granted franchises to the Department that recognized the right of the Department to set rates for customers located in those cities that are higher than the rates charged to Seattle customers. In 2003, the City of Tukwila granted a similar franchise to the Department. The rate ordinances that took effect in 1999 and thereafter have set rates for customers in these cities and in unincorporated King County at the maximum level permitted under the franchises. The power portion of rates for suburban customers is eight percent higher than the power portion of rates for Department customers. The franchise agreements also allow for a differential of up to six percent on the distribution portion of rates, but not all franchise cities have activated that aspect of the agreements. Current distribution differentials are six percent for Tukwila and three percent for Shoreline.

The franchise agreements also include provisions for payment for service levels that exceed the standard levels normally provided by the Department. Within the last two years, the Department has completed two underground distribution projects in the City of Shoreline that fall into this category. A charge equivalent to a one percent rate increase for Shoreline customers became effective on January 1, 2008, to recover the cost of the first project. A second charge, equivalent to a three percent rate increase for these customers, was implemented as of June 1, 2008. These undergrounding charges will be in effect for approximately 25 years, or until the Department has been reimbursed with interest for the capital cost of the projects.

Voluntary Green Power Program. Pursuant to State law, the Department 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 are used by the Department to fund the acquisition of energy from renewable resources, such as solar, wind, fuel cells, and landfill gas. As of December 31, 2007, 6,900 customers had elected to participate in the program.

TABLE 7
AVERAGE RATE IN CENTS PER KWH AND MONTHLY BILLS
(UNAUDITED, AS OF JUNE 1, 2008)

	Average Rate in Cents per kWh				Average Monthly Bills			
	City Standard	City Network	Suburban ⁽¹⁾	City of Tukwila	City Standard	City Network	Suburban ⁽¹⁾	City of Tukwila
Residential								
500 kWh per month	5.7		5.8	6.1	\$29		\$29	\$30
1,000 kWh per month	7.1	(2)	7.2	7.5	71	(2)	72	75
2,000 kWh per month	7.8		7.9	8.2	157		159	164
Small General Service								
10,000 kWh per month (40kW)	6.0	(2)	6.1	6.3	\$600	(2)	\$611	\$630
Medium General Service								
20,000 kWh per month (60kW)	6.1	6.8	6.2	6.4	\$1,224	\$1,355	\$1,246	\$1,286
200,000 kWh per month (500kW)	6.1	6.7	6.2	6.4	12,135	13,395	12,355	12,755
Large General Service								
400,000 kWh per month (1,000kW)	5.7	6.1	5.8	5.9	\$22,671	\$24,502	\$23,094	\$23,744
1,800,000 kWh per month (5,000kW)	5.7	6.2	5.8	6.0	102,221	110,910	104,240	107,188
High Demand General Service								
6,000,000 kWh per month (20,000kW)	5.5	(3)	(3)	6.0	\$327,723	(3)	(3)	\$359,529
18,000,000 kWh per month (60,000kW)	5.5			6.0	1,006,925			1,077,262

(1) All franchise jurisdictions outside the City of Seattle, except the Cities of Shoreline and Tukwila.

(2) Residential and Small General Service customers receiving network service are charged City standard rates.

(3) All High Demand General Service customers are located in Seattle or Tukwila.

Source: *Seattle City Light, Finance Division*

TABLE 8
ANNUAL BILL COMPARISONS WITH OTHER PUGET SOUND UTILITIES
(UNAUDITED)

Monthly Use		Seattle City Light	Puget Sound Energy ⁽¹⁾	Snohomish County PUD ⁽²⁾	Tacoma Power ⁽³⁾
kWh	kW				
Residential					
100		\$ 80	\$ 176	\$ 162	\$ 140
500		316	577	493	438
1,000		791	1,169	985	811
3,000		2,695	3,624	2,956	2,300
Small General Service					
300	1	\$ 198	\$ 524	\$ 377	\$ 335
3,000	10	1,984	3,332	2,790	2,381
12,000	40	7,934	12,695	10,831	9,199
Medium General Service					
150,000	500	\$ 90,240	\$ 157,824	\$ 129,491	\$ 93,844
200,000	500	118,260	197,116	164,665	113,482
360,000	900	212,868	354,324	295,382	203,825
Large General Service					
300,000	1,000	\$ 177,108	\$ 294,618	\$ 219,826	\$ 187,136
1,000,000	5,000	606,208	1,101,908	790,647	737,100
2,500,000	7,500	1,467,973	2,363,634	1,802,939	1,784,129
High Demand General Service					
6,000,000	20,000	\$ 3,312,138	\$ 4,525,164	\$ 4,396,524	\$ 3,732,240
18,000,000	60,000	9,936,413	13,575,492	13,189,572	11,195,616
24,000,000	60,000	13,057,679	17,309,376	16,891,380	13,552,104
Last Rate Change		01/01/2007	04/01/2008	04/04/2005	04/04/2005

FOOTNOTES TO TABLE 8:

- (1) Puget Sound Energy's Primary General Service is compared to the Department's Large General Service, and its High Voltage General Service is compared to the Department's High Demand General Service.
- (2) Snohomish PUD's Large Primary Service is compared to the Department's High Demand General Service, and its General Service is compared to the Department's Medium and Large General Service.
- (3) Tacoma Power's Small General Service is compared to the Department's Small General Service, and its General Service is compared to the Department's Medium, Large and High Demand General Service.

Source: Seattle City Light, Finance Division

Billing and Collection Processes

The Department currently bills the majority of its residential customers and some small commercial customers bi-monthly, and all other customers monthly. All bills are due within 21 days of receipt.

The Department has established various payment programs for its customers, including a levelized payment program to allow for monthly payments, and an electronic funds transfer program. The majority of the customers on the levelized payment program are billed bi-monthly with an option to pay one half of the amount by the bill due date and the remainder in the following month. An exception is made when a customer is enrolled in both the levelized payment plan and the Automatic Bill Payment program, in which case all of the billed amount is drafted from the customer's bank account by the bill due date. Customers who are on a monthly bill cycle are billed monthly.

Accounts receivable write-offs by the Department in 2007 were equal to 3.6 percent of retail electrical energy sales revenue. This included a one-time write-off totaling \$14.3 million for older inactive accounts processed by the billing system. If the one-time write-off were excluded, accounts receivable write-offs would have been one percent of retail electrical energy sales revenue. The Department's collection policy provides for disconnection of power for nonpayment of amounts due the Department.

Management Discussion of Historical Operating Results 2006-2007

This section provides a discussion of results of operations for the years 2006-2007 included in Table 9. Information in this discussion is a summary of the Management Discussion and Analysis ("MD&A") included in Appendix C—2007 Audited Financial Statements of the Department.

TABLE 9
SUMMARY OF HISTORICAL OPERATING RESULTS
(\$000) (UNAUDITED)

	2003	2004	2005	2006	2007
Operating Revenues					
Retail Energy Sales in Seattle Service Area					
Residential	\$ 199,392	\$ 199,339	\$ 195,487	\$ 201,450	\$ 196,247
Non-Residential	352,841	377,353	367,061	381,664	346,116
Subtotal	\$ 552,233	\$ 576,692	\$ 562,548	\$ 583,114	\$ 542,363
Wholesale Power Sales ⁽¹⁾	137,651	163,265	149,650	176,244	161,155
Power Exchanges and Other ⁽²⁾	31,013	19,130	18,911	48,099	103,464
Transmission Revenues ⁽³⁾	3,069	898	4,422	4,621	5,841
Other Revenue	15,039	17,934	13,022	19,732	19,702
Total Revenue	\$ 739,005	\$ 777,919	\$ 748,553	\$ 831,810	\$ 832,525
Operating Expenses Before Debt Service					
Wholesale Market Purchases	\$ 24,233	\$ 49,714	\$ 62,214	\$ 47,361	\$ 33,431
Long-Term Purchased Power Contracts	240,505	229,417	225,061	210,239	220,195
Power-Related Purchases ⁽²⁾	13,889	116	440	22,661	68,047
Production	27,462	27,242	26,698	27,613	33,910
Wheeling	30,102	30,947	32,580	37,677	38,185
Other Operating and Maintenance Expenses ⁽⁴⁾	133,000	137,270	142,425	158,651	172,235
Taxes (excluding City taxes)	27,994	26,950	27,224	27,963	25,686
Total Operating Expenses Before Debt Service	\$ 497,185	\$ 501,656	\$ 516,642	\$ 532,165	\$ 591,689
Net Operating Revenue	\$ 241,820	\$ 276,263	\$ 231,911	\$ 299,645	\$ 240,836
Add:					
Amortization Included in Operating Expenses ⁽⁴⁾	\$ 10,712	\$ 11,678	\$ 12,907	\$ 12,940	\$ 14,068
Valuation on Exchange Power, Net ⁽⁵⁾	(460)	184	(311)	(1,441)	(3,797)
Gain on Sale of Property	698	2,154	283	2,126	530
Amortization of BPA Conservation Augmentation ⁽²⁾	(3,442)	(5,770)	(5,285)	(5,277)	(5,688)
Interest	5,534	3,466	6,658	8,341	9,505
Non-Cash Expenses ⁽⁶⁾	10,281	7,753	3,329	5,961	6,104
Other	(661)	(349)	(576)	(172)	(5,136)
Revenue Available for Debt Service	\$ 264,482	\$ 295,379	\$ 248,916	\$ 322,123	\$ 256,422

FOOTNOTES TO TABLE 9:

- (1) Since 2003, wholesale power sales and purchases that are bookouts have been reported on a net basis in accordance with accounting standards.
- (2) Includes conservation and renewable credits under the power sales contract with BPA, the recognition of payments from BPA for the purchase of conservation savings, revenue from the provision of integration and exchange services related to the Stateline Wind Project, revenue from deliveries of power to Pend Oreille PUD pursuant to the Boundary Project's FERC license, and other energy credits. Also included is significant activity for the valuation of energy delivered under seasonal exchanges, basis sales, and other power exchange contracts. These non-monetary power-related contracts are being measured at fair value effective in 2006. Prior to 2006, these transactions were measured at the blended weighted-average cost of power (see related note 5 below). Non-monetary power-related contracts generally entail the valuation of power delivered (sales) and power received (expenses).
- (3) Includes revenue from the rental of transmission facilities to BPA and Snohomish PUD and revenue from the sale of transmission capacity.
- (4) Includes certain non-cash amortization expenses. Non-cash expenses are not taken into account in determining the amount of net revenue available for debt service. Net revenues therefore are adjusted to exclude these non-cash items.
- (5) Prior to 2006, short-term and long-term power exchange contracts were recognized by the Department at the blended weighted-average cost of power, in accordance with APB Opinion No. 29, *Accounting for Non-Monetary Exchanges*. Effective January 1, 2006, the Department adopted SFAS No. 153, *Exchanges of Nonmonetary Assets—An Amendment*. Under SFAS No. 153, these contracts are measured at fair value. Years prior to 2006 have not been restated.
- (6) Includes a portion of the claims expenses and capital project expenditures from prior years which were subsequently determined not to be capital expenditures.

Source: Seattle City Light, Accounting Division

Revenues—2007 Compared to 2006. Revenues from sales of power to retail customers decreased from \$583.1 million in 2006 to \$542.4 million in 2007, due to an average system rate decrease of 8.4 percent. Nonresidential revenues experienced the largest decrease in retail revenues, declining \$35.6 million or eight percent.

Sales of surplus power in the wholesale market yielded \$161.1 million in revenue in 2007, a decrease of \$15.1 million from 2006. There was less overall power generation from the Department's facilities, especially at the Boundary Project, which experienced lower stream flows than normal because of lower precipitation in the eastern Washington region. The lower sales of power were offset in part by a ten percent increase in the average power sales price of \$42.16 per MWh in 2007, compared to \$38.48 per MWh in 2006.

Purchases of wholesale power decreased by \$13.9 million in 2007. Power purchased in 2007 was 947,937 MWh, a decrease of 386,042 MWh or 28.9 percent from 2006. Average power purchase prices were nearly unchanged at \$35.27 per MWh in 2007 compared to \$35.50 per MWh in 2006.

Power sales were 4.03 times the amount of power purchased during 2007. The higher ratio of sales to purchases, along with higher average power prices during 2007, resulted in net revenues from wholesale purchases and sales totaling \$127.7 million in 2007, an incremental decrease of \$1.2 million or 0.9 percent from net revenues of \$128.9 million in 2006.

Revenue in the other power-related category increased \$55.4 million to \$103.5 million in 2007. Effective in 2006, power exchanges derived from certain power contracts were valued at fair market in accordance with a new accounting standard. During 2007, valuations for power exchanges increased considerably as the Department expanded into additional ancillary services that included power exchange components.

Revenues from a variety of other sources remained unchanged from 2006 at \$19.7 million.

Expenses—2007 Compared to 2006. Power-related expenses in 2007 totaled \$321.7 million, a \$41.4 million increase from 2006. This increase was due to the \$10 million increase in long-term purchased power

contracts with BPA and others, a \$45.4 million increase in wholesale power-related purchases, and a \$13.9 million decrease in short-term wholesale market purchases. See “Revenues—2007 Compared to 2006.”

BPA long-term power expenses were higher by \$12.1 million due primarily to contractual changes for the Block, which increased power purchases by \$13.6 million in 2007, along with a \$7.5 million increase in the annual true-up for the Slice. This increase was offset by an \$11.1 million decline in other long-term purchased power expenses, primarily due to the expiration of the purchased power contract with the City of Klamath Falls in July 2006. The increase in power-related wholesale purchases was primarily due to the recording of additional power exchanges and basis transactions at fair value.

The balance net increase of \$4.6 million in power-related expenses was a result of the effect of higher fair market valuations of NCPA-exchanged power delivered during 2007 (\$2.8 million) and a lower valuation of long-term purchased power bookouts resulting from short-term wholesale transactions (\$1.7 million).

Production and wheeling costs totaled \$72.1 million in 2007, a \$6.8 million increase from 2006. The increase was primarily due to a \$3.6 million increase in structural and plant maintenance costs at Skagit, Boundary, Diablo and Ross, along with a \$1.6 million increase in FERC administrative fees to correct errors in previous administrative charges. Other power costs related to system control, power marketing, information technology support and system control and load dispatch activities increased \$0.9 million. Wheeling expenses increased \$0.5 million for Lucky Peak, State Line wind energy, Columbia Grid and other contracts.

Other operating and maintenance expenses increased from \$158.7 million in 2006 to \$172.2 million in 2007. The increase was due in large part to an increase in administrative and general costs of \$17.7 million to \$66.7 million in 2007 as a result of higher costs for administrative systems enhancements, pensions, benefits, rents, and environmental clean-up of various Lower Duwamish Waterway superfund sites. The increase in administrative and general costs was offset by a decrease of \$2.2 million in transmission costs resulting from a decrease in damage and repair costs compared to 2006.

Taxes paid to the State Department of Revenue decreased \$2.3 million from 2006 on account of the lower retail revenue base.

Nonoperating Income and Expense—2007 Compared to 2006. Although not included in Table 9, changes in nonoperating income and expense provide additional information on the financial condition of the Department. Nonoperating income decreased from \$12.0 million in 2006 to \$5.6 million in 2007. Investment income increased to \$10.2 million in 2007 from \$10.0 million in 2006. Other deductions were \$4.6 million in 2007, a \$6.6 million unfavorable variance from 2006. A significant portion of this decrease was due to reversal of costs that had been recorded as grant revenues in 2006 (\$3.3 million).

Nonoperating expense decreased \$3.2 million from \$71.8 million in 2006 to \$68.6 million in 2007. The decrease is due primarily to lower interest expense on outstanding bonds, as bonds continued to be repaid with no additional bonds issued in 2007.

Fees and grants increased to \$46.1 million in 2007, an increase of \$14.3 million from 2006. The majority of this increase was the result of completed underground infrastructure improvements for Shoreline and Burien totaling \$12.4 million.

Historical Revenue Available for Debt Service and Debt Service Coverage, 2003-2007. Table 10 presents detailed information on operating results for the five-year period 2003-2007, along with revenue available for debt service. Revenue available for debt service is then used in Table 10 to calculate the debt service coverage ratio in each of those years. Debt service on Parity Bonds increased from \$105.7 million in 2003 to \$128.2 million in 2007, reflecting the increase in Parity Bonds outstanding during that period as the result of issuing \$284.9 million of the Department’s Improvement and Refunding Revenue Bonds, Series 2004. Debt service on Subordinate Lien Bonds increased from \$4.6 million to \$8.4 million in 2007, reflecting the timing of principal repayment and increase in interest rates during the period.

Revenue available for debt service in 2003 and 2004 is adjusted to reflect the deferral of \$300 million in excess power costs incurred in 2001 and authorized by the City Council to be amortized over the next three years. At the same time, the City Council provided that retail rates would remain at levels consistent with the amortization of the excess power costs in 2002, 2003 and 2004. If the deferral and amortization of power costs is taken into account in computing debt service coverage, then coverage over the 2003-2007 period was 1.92x Parity Bond debt service and 1.82x debt service on Parity Bonds and Subordinate Lien Bonds. During the past five years, coverage ranged from a high of 2.51x Parity Bond debt service in 2006 to a low of 1.56x Parity Bond debt service in 2003. If the deferral and amortization of excess power costs is not taken into account, then debt service coverage on Parity Bonds has been at or above 2.00x debt service in all years except 2005, ranging from a low of 1.96 in 2005 to a high of 2.51 in 2006. Under City Council Resolution 30761 and Resolution 30933, it is City policy to set electric rates at a level that would achieve coverage of 2.0x on both Parity Bonds and Subordinate Lien Bonds. As depicted in Table 10, that policy goal was achieved only in 2006.

TABLE 10
HISTORICAL DEBT SERVICE COVERAGE
(\$000) (UNAUDITED)

	2003	2004	2005	2006	2007
Revenue Available for Debt Service	\$ 264,482	\$ 295,379	\$ 248,916	\$ 322,123	\$ 256,422
Deferral/(Amortization) of Power Costs ⁽¹⁾	(100,000)	(100,000)	0	0	0
Adjusted Revenue Available for Debt Service	\$ 164,482	\$ 195,379	\$ 248,916	\$ 322,123	\$ 256,422
Debt Service:					
Parity Bonds	\$ 105,719	\$ 123,373	\$ 127,076	\$ 128,230	\$ 128,216
Subordinate Lien Bonds	4,590	5,192	6,452	7,613	8,397
Total Debt Service	\$ 110,309	\$ 128,565	\$ 133,528	\$ 135,843	\$ 136,613
Debt Service Ratios (giving effect to deferral/amortization of power costs) :					
Times Covered - Parity Bonds ⁽²⁾	1.56	1.58	1.96	2.51	2.00
Times Covered - Parity and Subordinate Lien Bonds ⁽³⁾	1.49	1.52	1.86	2.37	1.88

(1) Deferral of \$300 million in excess power costs from 2001 to 2002 (not shown), 2003 and 2004 was authorized by the City Council.

(2) Adjusted Revenue Available for Debt Service divided by Parity Bond Debt Service.

(3) Adjusted Revenue Available for Debt Service divided by the sum of Parity Bond Debt Service and Subordinate Lien Bond Debt Service.

Source: *Seattle City Light, Accounting Division*

Total Department Debt Service Requirements

As of December 1, 2008, there were outstanding \$1,299,755,000 in Parity Bonds and \$71,975,000 in Subordinate Lien Bonds (all of which are expected to be refunded by the Bonds).

Principal of and interest on the Parity Bonds and the Subordinate Lien Bonds 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 Parity Bonds and Subordinate Lien Bonds are shown in Table 11.

TABLE 11
DEBT SERVICE REQUIREMENTS*

Year	Outstanding Parity Bonds			The Bonds			Total Parity Bonds		
	Principal	Interest	Total	Principal	Interest	Total	Principal	Interest	Total
2008	\$ 64,620,000	\$ 44,691,894	\$ 109,311,894	\$ 0	\$ 0	\$ 0	\$ 64,620,000	\$ 44,691,894	\$ 109,311,894
2009	67,990,000	60,230,933	128,220,933	6,360,000	10,219,589	16,579,589	74,350,000	70,450,522	144,800,522
2010	71,525,000	56,693,264	128,218,264	9,210,000	13,260,163	22,470,163	80,735,000	69,953,426	150,688,426
2011	66,995,000	53,281,733	120,276,733	12,680,000	12,712,913	25,392,913	79,675,000	65,994,645	145,669,645
2012	66,850,000	50,249,108	117,099,108	13,485,000	12,058,788	25,543,788	80,335,000	62,307,895	142,642,895
2013	69,585,000	46,710,226	116,295,226	14,500,000	11,359,163	25,859,163	84,085,000	58,069,389	142,154,389
2014	70,060,000	43,069,820	113,129,820	15,340,000	10,613,163	25,953,163	85,400,000	53,682,983	139,082,983
2015	70,515,000	39,389,795	109,904,795	16,335,000	9,800,869	26,135,869	86,850,000	49,190,664	136,040,664
2016	71,250,000	35,622,020	106,872,020	15,155,000	8,993,200	24,148,200	86,405,000	44,615,220	131,020,220
2017	71,410,000	31,804,033	103,214,033	10,460,000	8,352,825	18,812,825	81,870,000	40,156,858	122,026,858
2018	70,610,000	28,313,283	98,923,283	11,045,000	7,815,200	18,860,200	81,655,000	36,128,483	117,783,483
2019	67,640,000	24,651,676	92,291,676	10,020,000	7,276,050	17,296,050	77,660,000	31,927,726	109,587,726
2020	65,495,000	21,256,189	86,751,189	10,560,000	6,735,825	17,295,825	76,055,000	27,992,014	104,047,014
2021	63,605,000	17,989,444	81,594,444	11,145,000	6,152,138	17,297,138	74,750,000	24,141,581	98,891,581
2022	62,495,000	14,822,891	77,317,891	10,220,000	5,564,600	15,784,600	72,715,000	20,387,491	93,102,491
2023	62,235,000	11,596,849	73,831,849	10,810,000	4,972,763	15,782,763	73,045,000	16,569,612	89,614,612
2024	63,170,000	8,381,356	71,551,356	11,465,000	4,318,025	15,783,025	74,635,000	12,699,381	87,334,381
2025	47,625,000	5,255,548	52,880,548	12,175,000	3,608,825	15,783,825	59,800,000	8,864,373	68,664,373
2026	41,895,000	2,760,869	44,655,869	12,910,000	2,872,413	15,782,413	54,805,000	5,633,281	60,438,281
2027	12,340,000	1,412,950	13,752,950	13,675,000	2,108,094	15,783,094	26,015,000	3,521,044	29,536,044
2028	12,945,000	808,944	13,753,944	14,485,000	1,298,494	15,783,494	27,430,000	2,107,438	29,537,438
2029	3,790,000	175,288	3,965,288	15,340,000	441,025	15,781,025	19,130,000	616,313	19,746,313
Total	\$ 1,264,645,000	\$ 599,168,109	\$ 1,863,813,109	\$ 257,375,000	\$ 150,534,121	\$ 407,909,121	\$ 1,522,020,000	\$ 749,702,230	\$ 2,271,722,230

* Includes the refunding of the Refunded Bonds, as described under "Use of Proceeds-Refunding Plan."

CAPITAL REQUIREMENTS

The sections below describe the Capital Improvement Program (“CIP”) and the Five-Year Conservation Action Plan that the Department intends to implement over the 2009-2014 period.

Generation. The Department plans to spend \$272 million on generation system improvements during the period 2009-2014. Capital improvements at the Boundary Project are expected to cost \$53 million, and a preliminary estimate of costs to comply with a new license expected in 2011 is \$68 million. Capital spending at the Skagit Project is expected to be \$122 million over the six-year period, and environmental mitigation projects required under the terms of the license for the Skagit Project are an additional \$2 million.

Transmission. Over the next six years, the Department expects to spend about \$95 million for expansion and replacement of transmission plant.

Substations. Substation expansion and improvements are projected to cost \$180 million over the 2009-2014 period. Major expenditures are planned to acquire land for and construct a new North Downtown Substation. Projects also include the replacement of existing substation equipment to maintain reliability and to increase capacity to provide for load growth.

Distribution. The Department plans to spend \$966 million over the 2009-2014 period on improvements and additions to its distribution system. A major portion of these expenditures will be required to relocate infrastructure and provide capacity related to a number of large local transportation projects, including the development of a light rail system by Sound Transit and relocating facilities on or adjacent to the Alaskan Way viaduct. The Department expects to be reimbursed for a portion of these costs. Other planned projects include construction of a new North Downtown Network, improvements to the downtown network distribution system, service connections, and capacity additions.

General Plant. Programmed expenditures of \$145 million will support general plant improvements over the 2009-2014 period. Improvements in communications systems are budgeted at \$13 million. Information technology projects include Department-wide software upgrades, an enterprise performance management system, and an outage management system, among others. A new asset management system will cost approximately \$10 million. Replacement of mobile equipment, which has been delayed over the past several years, will require the expenditure of \$48 million. A total of \$10 million is expected to be spent for security enhancements in the Department’s facilities.

High Ross Payment 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 and Cost of Power—Department-Owned Resources—Skagit Project.” 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 2021 through 2035, the deferred costs will be amortized through annual charges of \$9.1 million. The deferred portion of the payments to B.C. Hydro is treated as a component of capital requirements.

Conservation. Capital requirements include \$240 million for the Five-Year Conservation Action Plan and other conservation measures. This level of expenditure is expected to enable the Department to meet its annual targets for energy savings through 2013. See “Power Resources and Cost of Power—Conservation.”

Financing. Capital requirements of \$2.0 billion from 2009 through 2014 are expected to be financed through a combination of net revenues from operations, contributions in aid of construction, external funding of conservation programs, and the proceeds of the Bonds, Future Parity Bonds and Subordinate Lien Bonds. In 2009, capital financing will be provided from the proceeds of the Bonds, contributions in aid of construction, and external conservation funding. From 2009 through 2014, net revenue available for capital funding is expected to total \$656 million, or 33 percent of capital requirements. Bond proceeds are expected to furnish 58 percent of capital financing over that period. The remainder of capital funding is projected to be provided by contributions in aid of construction, reimbursement of costs for transportation-related projects, and external conservation funding.

IN THE PREPARATION OF THE PROJECTIONS IN TABLE 12, THE CITY HAS MADE CERTAIN ASSUMPTIONS WITH RESPECT TO FUTURE CONDITIONS. WHILE THE CITY BELIEVES THESE ASSUMPTIONS ARE REASONABLE FOR THE PURPOSE OF THE PROJECTIONS, ACTUAL RESULTS DEPEND UPON FUTURE CONDITIONS THAT MAY DIFFER FROM THOSE ASSUMPTIONS. THE CITY DOES NOT REPRESENT OR GUARANTEE THAT ACTUAL RESULTS WILL REPLICATE SUCH PROJECTIONS. THE ELECTRIC INDUSTRY HAS UNDERGONE 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. THE CITY HAS NOT COMMITTED TO PROVIDE INVESTORS WITH UPDATED FORECASTS OR PROJECTIONS.

NEITHER THE DEPARTMENT'S INDEPENDENT AUDITORS, NOR ANY OTHER INDEPENDENT ACCOUNTANTS, HAVE COMPILED, EXAMINED OR PERFORMED ANY PROCEDURES WITH RESPECT TO THE PROSPECTIVE 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.

TABLE 12
ADOPTED CAPITAL IMPROVEMENT AND CONSERVATION PROGRAMS 2009-2014
(000S)

	2009	2010	2011	2012	2013	2014	Total
Generation							
Skagit Plant Improvements	\$ 15,759	\$ 7,923	\$ 7,084	\$ 42,530	\$ 41,046	\$ 7,956	\$ 122,297
Boundary Plant Improvements	5,062	14,484	10,629	7,859	5,156	9,775	52,964
Environmental Mitigation	1,331	1,250	1,256	8,702	31,164	31,868	75,570
Other Generation	3,144	3,467	4,575	3,944	2,484	3,748	21,361
Total Generation	\$ 25,295	\$ 27,124	\$ 23,543	\$ 63,035	\$ 79,850	\$ 53,346	\$ 272,192
Transmission							
	\$ 5,239	\$ 6,583	\$ 9,415	\$ 28,801	\$ 29,292	\$ 15,551	\$ 94,881
Substation							
North Downtown Substation	\$ 35,346	\$ 15,108	\$ 2,150	\$ 11,914	\$ 19,889	\$ 16,188	\$ 100,595
Other Substation	11,927	16,145	16,630	15,012	10,346	9,166	79,225
Total Substation	\$ 47,273	\$ 31,253	\$ 18,780	\$ 26,926	\$ 30,235	\$ 25,353	\$ 179,820
Distribution							
Overhead Equipment	\$ 752	\$ 771	\$ 1,023	\$ 1,034	\$ 1,058	\$ 1,138	\$ 5,776
Regional Transit	4,375	2,559	1,244	517	0	0	8,695
Street and Floodlights	3,500	3,499	2,624	2,624	2,663	2,969	17,879
26 kV Conversion	2,967	3,517	3,790	3,875	3,962	3,104	21,214
Suburban Customers	5,397	6,881	6,605	2,458	0	0	21,342
Alaskan Way Viaduct	5,145	5,080	3,827	3,913	3,786	3,871	25,622
Pole Replacements	3,466	3,460	6,194	6,334	6,476	6,621	32,551
Other Distribution	14,143	11,551	11,435	11,906	15,519	18,965	83,519
Network Additions and Services	15,390	20,272	18,195	18,603	19,021	19,501	110,982
Underground Projects	14,114	17,232	26,647	20,818	15,163	17,203	111,177
North Downtown Network	1,111	3,504	29,428	31,118	37,966	44,532	147,659
Capacity Additions	28,556	30,376	30,503	27,278	27,240	35,813	179,767
Service Connections	18,654	24,587	36,631	44,927	46,424	28,243	199,466
Total Distribution	\$ 117,571	\$ 133,290	\$ 178,144	\$ 175,406	\$ 179,278	\$ 181,961	\$ 965,650
General Plant							
Emergency Operations Center	\$ 503	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 503
Security	4,586	1,729	2,137	649	642	466	10,209
Asset Management	3,935	4,778	1,665	41	42	0	10,461
Communications	2,068	2,222	2,219	2,276	2,327	2,276	13,386
Other General Plant	7,274	5,768	5,368	4,338	5,165	2,781	30,694
Information Technology	9,711	8,114	4,478	2,903	2,968	3,035	31,211
Vehicle Replacement	7,191	6,457	8,269	8,736	8,932	8,750	48,335
Total General Plant	\$ 35,267	\$ 29,068	\$ 24,137	\$ 18,944	\$ 20,076	\$ 17,308	\$ 144,799
Conservation							
Deferred High Ross ⁽¹⁾	\$ 9,103	\$ 9,103	\$ 9,103	\$ 9,103	\$ 9,103	\$ 9,103	\$ 54,620
Deferred Relicensing Costs	13,888	9,163	8,197	1,216	1,110	1,131	34,705
Total Expenditure	\$ 283,182	\$ 282,461	\$ 312,253	\$ 365,706	\$ 393,365	\$ 349,222	\$ 1,986,189
Sources of Funds							
Revenue Available for Debt Service	\$ 245,878	\$ 309,954	\$ 305,243	\$ 325,022	\$ 358,196	\$ 389,121	\$ 1,933,416
Less: Debt Service	\$ 145,637	\$ 152,623	\$ 152,622	\$ 162,511	\$ 179,098	\$ 194,560	\$ 987,051
Less: City Taxes	34,404	38,706	40,820	42,717	44,712	45,809	247,168
Less: Bond Reserve Deposits	0	0	0	0	0	0	0
Less: Contingency Reserve Deposits	0	0	0	0	0	0	0
Less: Other Funds Required	2,037	13,799	7,594	7,538	7,937	4,786	43,691
Revenue Available for Capital Projects	\$ 63,800	\$ 104,826	\$ 104,207	\$ 112,256	\$ 126,449	\$ 143,965	\$ 655,504
Proceeds from Contributions ⁽²⁾	39,636	41,487	37,213	27,503	21,759	16,495	184,093
Funding from Bond Proceeds	179,746	136,148	170,833	225,947	245,156	188,761	1,146,591
Total Funding for Capital Projects	\$ 283,182	\$ 282,461	\$ 312,253	\$ 365,706	\$ 393,365	\$ 349,222	\$ 1,986,189

FOOTNOTES TO TABLE 12:

- (1) The City Council has directed the Department to defer and amortize the capital portion of annual payments to B.C. Hydro under the High Ross Agreement over a period extending through 2035. From 2000 until the final capital payment is made in 2020, the Department will defer \$9.1 million in High Ross costs. See “Power Resources and Cost of Power—Department-Owned Resources.”
- (2) Includes contributions in aid of construction and customer payments for conservation. Also included are payments received from BPA to purchase conservation savings. See “Power Resources and Cost of Power—Conservation.”

Source: Seattle City Light, Finance Division

ENVIRONMENTAL MATTERS

Impact of Environmental Matters

Environmental responsibility and stewardship are identified as corporate values in the Department’s mission, strategic and business planning efforts. The Department manages its legal obligations for environmental protection through programs that are expected to produce 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 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 civil and criminal penalties and 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 efforts have reduced hazardous waste generation and disposal costs and the Department maintains those reduced levels. The Department promotes compliance with federal and State hazardous waste regulations through use of operations manuals, staff training and periodic internal inspections or audits. During internal inspections, compliance with other laws, including the Toxic Substances Control Act, Clean Water Act and Underground Storage Tank regulations, is monitored.

Contaminated Site Liability

In 2001, the United States Environmental Protection Agency 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. As of December 31, 2007, the Department had recorded a \$5.6 million environmental liability for its share of actual and estimated future costs associated with the RI/FS. This amount will be evaluated annually and is subject to adjustment based on future developments. It is likely that the Department will be liable for a portion of the costs of future remediation of the Lower Duwamish site. The Department will be liable for some costs of remediation of an area known as Slip 4, due to the Department’s ownership and operation of the Georgetown Steam Plant, which was decommissioned in 1980. The City is taking the lead role in further investigation of contamination at Slip 4. A preliminary estimate of the total cost of investigating and remediating Slip 4 sediments is \$10 million to \$15 million. The Department also will be liable for some of the costs of remediating sediments in an area known as Terminal 117, adjacent to a former asphalt plant. The Port of Seattle has taken the lead role in further investigation of Terminal 117. A preliminary estimate of the total cost of investigating and remediating Terminal 117 sediments, upland and streets is \$28 million to \$38 million. The City has executed a settlement with the Port of Seattle and with the former owner-operators of the asphalt plant. In the

settlement, the Port of Seattle agreed to pay 60 percent and the City agreed to pay 40 percent of future costs for most of the site. The City agreed to pay all future costs for removal of contamination that was conveyed from the site into City streets by vehicles. The Department expects to share the costs of investigating and remediating contamination of Slip 4 and Terminal 117 with other responsible parties; however, the extent of such sharing or later recovery of costs is not known at this time. The Boeing Company has discovered PCB contamination on its Plant II property, some of which Boeing attributes to a substation operated by the Department. The Department has investigated and believes it is unlikely that the PCBs came from the substation; however, work to determine the source and the extent of the contamination is ongoing. If the substation is determined to be a source of the contamination, then the Department may be liable for some of the costs of investigation and remediation.

No assurances can be given that other contaminated 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. Three species have been listed under the Endangered Species Act ("ESA") as either "threatened" or "endangered." Additional species may be listed in the future. The overall long-run implications of these listings are difficult to assess. Two legal mechanisms that typically come into play and that could affect the Department's operations 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 Oceanic and Atmospheric Administration ("NOAA Fisheries," formerly the National Marine Fisheries Service) for salmon and steelhead or the U.S. Fish and Wildlife Service ("USFWS") for freshwater species including bull trout. 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. A FERC decision to issue a hydroelectric project license, or license amendment, has a nexus with ESA and triggers Section 7 consultation. Section 7 consultation can also be triggered through maintenance actions requiring permits with the Corps and through new information in species impacts identified by NOAA Fisheries, USFWS, the licensee, or third parties.

Columbia and Snake River Anadromous Fish Issues. There are three federal "action agencies" responsible for the operation of the Federal System: the Corps, the Bureau of Reclamation, and BPA. These agencies have been engaged in consultation for a number of years, and NOAA Fisheries 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, NOAA Fisheries 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. NOAA Fisheries and USFWS developed supplemental recovery plans in 1998 and 2000 that identified reasonable and prudent alternatives to protect and recover not only listed salmon and steelhead but also bull trout and sturgeon, which have been listed under the ESA in the Columbia River Basin. Final Biological Opinions for the Columbia-Snake River Basin were released by NOAA Fisheries on May 8, 2008. Two of these Biological Opinions govern the federal operation of 14 hydropower dams in the Columbia River system, while the third governs salmon harvest by the states and tribes. These final Biological Opinions are expected to remain in effect until at least 2018.

The Department's power generation at the Boundary Project has been affected by the salmon and steelhead 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, the water not released in the fall and winter on the Pend Oreille River is released in the spring and summer, when it is sometimes spilled because the Boundary Project does not have sufficient hydraulic capacity to use all the available water for generation.

This results in a reduction in the Boundary Project's firm capability under the terms of the Coordination Agreement. See "Power Resources and Cost of Power—Overview of Resources." New Biological Opinions to support recovery plans are expected to result in changes in flows that could have an impact on the Boundary Project. Such Biological Opinions may have similar effects on the amounts the Department receives under contracts with Grant PUD and BPA.

Other Endangered Species Issues. Other ESA fish listings that may affect Department operations include bull trout, chinook salmon and steelhead in Puget Sound. Bull trout, which were listed as threatened species in 1999 by the USFWS, have a wide geographic range in the Pacific Northwest, and populations are present in most of the reservoirs and all of the rivers where the Department's hydroelectric generation facilities are located, including all three reservoirs of the Skagit Project. The Skagit River populations are recognized as being among the healthiest in the United States due to excellent habitat conditions, cold water temperatures and an abundant food supply. Bull trout are also found in the Chester Morse Lake and the Cedar River in the vicinity of the Cedar Falls Project. This species is also occasionally observed in the South Fork Tolt River, downstream of the Tolt Project. The Skagit River downstream of the Skagit Project was listed as Critical Habitat for bull trout by the USFWS, as were the major tributaries to the three project reservoirs. The Skagit, Cedar and Tolt reservoirs were excluded from the Critical Habitat designation.

Chinook salmon were listed as threatened by NOAA Fisheries in 1999, and are present in the Skagit, Cedar and Tolt Rivers downstream of the Department's hydroelectric facilities. Chinook salmon populations increased to 25-year-high levels on the Skagit River from 2004 through 2006. The Skagit River downstream of the Skagit Project continues to sustain the largest native population of chinook salmon in the Puget Sound region. The Skagit, Cedar and Tolt Rivers downstream of the Department's hydroelectric facilities were designated as Critical Habitat for chinook salmon by NOAA Fisheries. The Department's hydroelectric facilities on the Skagit and Tolt Rivers are located above natural passage barriers to salmon and steelhead.

Steelhead were listed as threatened by NOAA Fisheries in 2007. Steelhead are located in the Skagit, Cedar and Tolt Rivers downstream of the Department's hydroelectric facilities. Steelhead populations have declined to 25-year-low levels in most Puget Sound rivers.

While it is unclear how these listings might affect operations, actions already taken by the Department may mitigate the potential adverse impacts on its operations. 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 Project and by an incidental take permit. Both the Skagit Project and the Tolt Project were licensed through a collaborative process involving State and federal regulatory agencies, including NOAA Fisheries 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 continuing an ESA Early Action program that is supporting the recovery of bull trout, chinook salmon and steelhead populations in the Skagit and Tolt watersheds. This program has funded several major habitat restoration projects for the three listed fish species in the Skagit and Tolt watersheds. The Department has also acquired over 2,000 acres of high quality habitat for listed species in these watersheds for permanent conservation protections. Monitoring studies by the Department are continuing in partnership with the State Department of Fish and Wildlife, the Skagit River System Co-op, and the University of Washington to determine the population status and any potential impacts of the hydroelectric projects on bull trout, chinook salmon and steelhead downstream of the Skagit Project and its reservoirs. These studies will be used to develop management plans and mitigation procedures in cooperation with State and federal agencies to reduce or eliminate the impacts of project operations on these listed species.

Bull trout are also found in the vicinity of the Boundary Project. The license for the Boundary Project expires in 2011 and the Department is currently preparing for the relicensing process. Bull trout studies are being conducted in support of relicensing, but it is too early to know if and to what extent bull trout protection measures will be necessary or how they could affect power generation.

Clean Water Act Issues

Section 401 of the federal Clean Water Act requires states to provide a "water quality certification" regarding compliance of discharges with State water quality requirements 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 Project, and incorporated into the FERC license issued in 1997. These minimum flows were a condition of the Section 401 certification issued in 1996. The State Department of Ecology implemented new water quality standards for the State in 2007. The new standards are intended to protect aquatic uses, including federally-listed fish species such as bull trout, chinook salmon and steelhead. Water quality studies at the Boundary Project are currently underway in support of the relicensing process. The Department also participates in other water quality regulatory processes. 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 incremental electric energy needs of the City with no net greenhouse gas emissions. In response, the Department has signed contracts to acquire greenhouse gas offsets (i.e., a reduction in greenhouse gas emissions at one location to compensate for emissions at another location) and has purchased output and associated environmental attributes from the Stateline Wind Project in eastern Washington and Oregon and the Sierra Pacific Industries Burlington Biomass Facility in northwest Washington. See “Power Resources and Cost of Power—Purchased Power Arrangements—Stateline Wind Project.”

The Department’s GreenUp program offers customers the opportunity to support the acquisition of additional renewable resources, as required by State law. See “Financial Information—Retail Rates—Voluntary Green Power Program.” The Department uses funding from the GreenUp program to purchase renewable energy credits to promote the development of new renewable energy sources. See “Power Resources and Cost of Power—Integrated Resource Plan” and “—Renewable Portfolio Standards and I-937.”

DEVELOPMENTS AFFECTING THE ELECTRIC UTILITY INDUSTRY

General

The electric utility industry in the United States is in a period of significant change, resulting in part from actions taken by legislative and regulatory bodies at the national, regional, state and local levels. The industry also is being affected by a variety of other factors that can have an impact on the financial condition of electric utilities, including the effects of increased competition in certain sectors of the industry, such as the wholesale electric energy markets; changes in the availability and cost of fuels such as natural gas; changes in the availability of and demand for electric energy generally, as a result of economic, demographic, regulatory, weather and other factors; regional electric energy shortages; climate change; reliability standards; and the costs and operational impacts of endangered species, environmental, safety, licensing and other federal, state and local laws and regulations.

The Department cannot predict what effects such factors will have on its operations and financial condition, but the effects could be significant. The following is a brief discussion of certain of these factors. However, this discussion does not purport to be comprehensive or definitive, and these matters are subject to change subsequent to the date hereof. Extensive information on the electric utility industry is available from the various regulatory bodies and other sources in the public domain.

Climate Change

Greenhouse Gas Emissions. The Department’s resource mix is more than 90 percent hydro-based generation, and has only a small amount of thermal generation in its portfolio. The Department is studying how the predicted impacts of climate change may affect snowpack and rainfall in the region and thus output from its hydro-based generation.

Federal legislation has been proposed that allocates allowances for greenhouse gas emissions by electric utilities based primarily on historic emissions. Such proposals may result in the Department and its ratepayers shouldering the burden for reducing emissions (through investment in conservation and environmental mitigation for hydro-based generation resources) without receiving future allowances. The Department anticipates that the State will join other western states in developing a region-wide greenhouse gas emission trading program through the Western Climate Initiative, with or without federal legislation.

Recent Federal Regulations

Mandatory Reliability Standards. The Energy Policy Act of 2005 (“EPAAct”) made fundamental changes in the federal regulation of the electric utility industry, particularly with regard to transmission access, market behavior, mandatory reliability standards, and the application of these standards to municipal utilities, including the Department. EPAAct authorized FERC to certify and oversee an Electric Reliability Organization (“ERO”) to set and enforce mandatory reliability standards in North America. FERC has certified the North American Electric Reliability Corporation (“NERC”) as the ERO. The ERO can delegate enforcement authority to regional reliability organizations (“RROs”). The Western Electricity Coordinating Council (“WECC”) is the RRO for the western interconnect, which extends from Canada to Mexico and includes the Department’s service area.

Prohibition on Market Manipulation. EPAAct prohibits entities, including municipal utilities such as the Department, from using any manipulative or deceptive device or contrivance, in connection with the purchase or sale of electric energy or the purchase or sale of transmission. In 2006, FERC issued a final rule that makes it unlawful for any entity, directly or indirectly, in connection with transactions subject to FERC jurisdiction: (i) to defraud using any device, scheme or artifice; (ii) to make any untrue statement of material fact or omit a material fact; or (iii) to engage in any act, practice or course of business that operates or would operate as a fraud or deceit.

Compliance. With respect to reliability standards, the Department recently underwent a compliance audit. The WECC’s audit report indicates four “possible violations” by the Department out of approximately 540 requirements examined by the auditors. Because the WECC has not issued an official Notice of Alleged Violations, the Department’s liability is unknown at this time. With respect to anti-manipulation requirements, the Department has established a biennial training program for all affected employees. In addition, the Department has a Chief Compliance Officer who is responsible for federal regulatory compliance matters, including NERC reliability standards and anti-manipulation rules.

THE CITY OF SEATTLE

The following provides general information about the City.

Municipal Government

Incorporated in 1869, the City is the largest city in the Pacific Northwest and is the seat of King County. The City’s elected officials include 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 and the Department of Executive Administration. 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, 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 the financial affairs of the City.

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. In addition, the City's utilities are audited annually by an external auditor.

Municipal Budget. City operations are guided by a budget prepared under the direction of the Mayor by the Department of Finance pursuant to State statute (chapter 35.32A RCW). 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; the 2008 budget was adopted on November 19, 2007.

Investments. The information in this section does not pertain to pension funds, which are administered by the Seattle City Employees' Retirement System (see "Pension System"), and the proceeds of certain debt 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 Executive Administration. 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 Executive Administration 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. Under its current policy, the City may hold up to 25 percent of its portfolio in commercial paper. Most of the City's current commercial paper investments are asset-backed. The three primary rating agencies have not downgraded any of the commercial paper investments currently held within the investment portfolio since their acquisition. Current City investment policies require periodic reporting on 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 Auditor.

As of September 30, 2008, the combined investment portfolios of the City totaled \$995.5 million at book value. The City's cash pool is constituted solely of City funds. The City does not invest any funds in other pools, with the exception of tax collection receipts initially held by the County. For 2007, the yield on the City's consolidated pool of investments was 5.1 percent. As of September 30, 2008, the average maturity date of the portfolio was August 29, 2010. Approximately 30.3 percent, or \$301.8 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:

Government-Sponsored Enterprises	78.9%
Commercial Paper	12.0
Repurchase Agreements	7.5
U.S. Treasuries	1.6

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 purchases excess liability insurance to address general, automobile, operational, third-party claims, professional, public official, employment practices, and other exposures common to a public entity. The policies provide \$30 million limits above a \$5 million self-insured retention per occurrence. The City purchases all risk property insurance, including earthquake and flood, that provides up to \$500 million in limits subject to a schedule of deductibles and sublimits.

The City also purchases insurance for fiduciary, crime liability, inland marine, volunteers, workers compensation, foreign and domestic travel for employees, several accidental death and dismemberment policies, and other exposures. Bonds are purchased for public officials, notaries public and pension exposures.

The Department and Seattle Public Utilities are included in all of these programs, and insured in the same manner as all departments and functions. The notable exclusions for the Department are failure to supply power, downstream exposure from hydroelectric dams, and property coverage for the dam structures.

Pension System

City employees are covered by one of the following defined benefit pension plans: Seattle City Employees' Retirement System ("SCERS"), Firemen's Pension Fund, Police Relief and Pension Fund, and Law Enforcement Officers' and Fire Fighters' Retirement System ("LEOFF"). The first three are administered by the City; the State administers LEOFF through the Department of Retirement Systems. Information about LEOFF is available from the State by calling (800) 547-6657.

Nearly all permanent non-uniformed City employees participate in SCERS, a single-employer, defined-benefit retirement system. The payroll for City employees covered by SCERS for the year ended December 31, 2007, was \$534.7 million; total City payroll was \$762.3 million. Participating City employees are required to contribute 8.03 percent of their annual base salary to SCERS, which is matched by a comparable City contribution. Combined employee and employer contributions to SCERS totaled approximately \$80.8 million for the year ended December 31, 2007. The latest actuarial evaluation of SCERS was conducted by Milliman as of January 1, 2008. This showed the actuarial value of net assets available for benefits was \$2.119 billion and the actuarial value for accrued liabilities was \$2.295 billion, leaving an unfunded accrued actuarial liability of approximately \$175 million. The resulting funding ratio was 92.4 percent.

The Firemen's Pension Fund and the Police Relief and Pension Fund are single-employer pension plans that were established by the City in compliance with State law. Since the effective date of LEOFF in 1970, no payroll for employees was covered under these City plans, and the primary liability for pension benefits for these City plans shifted from the City to the State. However, the City was still liable for all benefits of employees in service at that time plus certain future benefits. The City's contribution to these City plans and for medical benefits associated with these plans in 2007 was \$34.1 million; there were no current member contributions. The City has been pre-funding future pension obligations in the Firemen's Pension Fund.

Post-Employment Retirement Benefits

The City's liability for other post-employment benefits ("OPEB") is limited to the implicit rate subsidy for retiree health benefits, which is the difference between (i) what retirees pay for their health insurance as a result of their inclusion with active employees for rate-setting purposes, and (ii) the estimated required premiums if their rates were set based on claims experience of the retirees as a separate group. The City is assessing its OPEB liability to satisfy the expanded reporting requirements specified by the Governmental Accounting Standards Board Statement No. 45 ("GASB 45"). While GASB 45 requires reporting and disclosure of the unfunded OPEB liability, it does not require that it be funded. In conformance with GASB 45 requirements, the City began reporting its OPEB liability beginning with the fiscal year ended December 31, 2007.

The City engaged Aon Consulting to prepare an actuarial study quantifying the City's OPEB liability. The study was completed on July 5, 2006, and concluded that as of the actuarial valuation date of January 1, 2006, the City's unfunded actuarial accrued liability, under its current pay-as-you-go policy, was equal to \$84.3 million. In fiscal year 2007, the City contributed approximately \$1.4 million for these benefits on a pay-as-you-go basis. According to the actuarial study, the City's annual required contribution in fiscal year 2007 to fund this liability was \$9.3 million.

Labor Relations

The City has 35 separate departments and offices with approximately 12,000 regular and temporary employees. Twenty-five different unions and 45 bargaining units represent approximately 83 percent of the City's regular employees. In April 2008, the City reached an agreement with the Seattle Police Officers' Guild. Negotiations are underway with Firefighters Local 27, Fire Chiefs Local 2898, and the Seattle Police Management Association for contracts that expire in December 2008. The City has reached an agreement with the International Brotherhood of Electrical Workers for a new contract that would begin in January 2009. The City has finalized most of its contracts with represented general employees through December 31, 2010.

INITIATIVE AND REFERENDUM

Under the State Constitution, Washington voters may initiate legislation (either directly to the voters, or to the Legislature and then, if not enacted, to the voters) and require the Legislature to refer legislation to the voters through the powers of initiative and referendum, respectively. Any law approved in this manner by a majority of the voters may not be amended or repealed by the 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 Legislature. After two years, the law is subject to amendment or repeal by the Legislature in the same manner as other laws. The Washington State Constitution may not be amended by initiative.

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.

In recent years, several state-wide initiative petitions to repeal or reduce the growth of taxes and fees, including City taxes, have garnered sufficient signatures to reach the ballot. Some of those tax and fee initiative measures have been approved by the voters and, of those, some remain in effect while others have been invalidated by the courts. Tax and fee initiative measures continue to be filed, but it cannot be predicted whether any more such initiatives might gain sufficient signatures to qualify for submission to the Legislature and/or the voters or, if submitted, whether they ultimately would become law.

A ballot initiative known as Initiative 937 ("I-937") was approved by State voters in November 2006. Under I-937, utilities with a retail load of more than 25,000 customers, such as the Department, are required to use eligible renewable resources or acquire equivalent renewable energy credits, or a combination of both, to serve a

certain portion of their load. See “Power Resources and Cost of Power—Renewable Portfolio Standards and I-937.”

Under the City Charter, Seattle voters may initiate City Charter amendments and local legislation, including modifications to existing legislation, and through referendum may prevent legislation passed by the City Council from becoming law.

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 PLLC, Bond Counsel. A form of the opinion of such firm with respect to the Bonds is attached hereto as Appendix B. The opinion of Bond Counsel is given based on factual representations made to Bond Counsel and under existing law as of the date of initial delivery of the Bonds, and Bond Counsel assumes no obligation to revise or supplement its opinion to reflect any facts or circumstances that may thereafter come to its attention, or any changes in law that may thereafter occur. The opinion of Bond Counsel is an expression of professional judgment on the matters expressly addressed in such opinion and does not constitute a guarantee of result. 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 will be 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 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 requirement to comply with 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. Bond Counsel has not undertaken and does not undertake to monitor the City’s compliance with such requirements.

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.

A small business corporation is exempt from the corporate alternative minimum tax for any taxable year beginning after December 31, 1997, if its average annual gross receipts during the three-taxable-year period beginning after December 31, 1993, did not exceed \$5,000,000, and its average annual gross receipts during each successive three-taxable-year period thereafter ending before the relevant taxable year did not exceed \$7,500,000.

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.

Possible Consequences of Tax Compliance Audit. The Internal Revenue Service (the “IRS”) has established a general audit program to determine whether issuers of tax-exempt obligations, such as the Bonds, are in compliance with requirements of the Code that must be satisfied in order for interest on those obligations to be, and continue to be, excluded from gross income for federal income tax purposes. Bond Counsel cannot predict whether the IRS would commence an audit of the Bonds. Depending on all the facts and circumstances and the type of audit involved, it is possible that commencement of an audit of the Bonds could adversely affect the market value and liquidity of the Bonds until the audit is concluded, regardless of its ultimate outcome.

Original Issue Discount. The Bonds maturing on April 1 in the years 2018 and 2020 through and including 2023, and the Term Bonds maturing on April 1, 2025, and April 1, 2029, 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.

Original Issue Premium. The Bonds maturing on April 1 in the years 2009 through and including 2017 (the “Premium Bonds”) have been sold at prices reflecting original issue premium. 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.

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 its 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.

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”), as applicable to a participating underwriter for the Bonds, the City will undertake in the Bond 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 or the Municipal Securities Rulemaking Board (“MSRB”) 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, 2008. 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. If the document incorporated is a “final official statement” (as defined by the Rule) with respect to which the City is an obligated person, it must be available from the MSRB.

The City also will provide or cause to be provided to each NRMSIR or the 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.

At its option, the City may make any filing under this Undertaking solely by transmitting such filing to the Texas Municipal Advisory Council (the “MAC”), as provided at <http://www.disclosureusa.org>, unless the SEC has withdrawn the interpretive advice in its letter to the MAC dated September 7, 2004.

Material Events. The City further will provide or cause to be provided to each NRMSIR or the MSRB and the SID, timely notice of the occurrence of any of the following events with respect to the Bonds, if material:

- (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) Bond calls (other than scheduled mandatory redemption of Term Bonds);
- (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 after the primary offering of the Bonds without the consent of any holder of any Bond, 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 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 under the Undertaking 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 (i) 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 (ii) notifies the SID and either the MSRB or each then existing NRMSIR of such termination.

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 Bond 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. The Undertaking will inure to the benefit of the City and any holder of the Bonds, and will not inure to the benefit of or create any rights in any other person.

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 or after July 3, 1995, subject to the Rule. The City is in compliance with all such undertakings.

OTHER BOND INFORMATION

Ratings on the Bonds

The Bonds have been rated “Aa2” and “AA-” by Moody’s Investors Service and Standard & Poor’s Ratings Services, a Division of The McGraw Hill Companies, Inc., respectively. 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 & Co. (the “Purchaser”) at a price of \$257,267,018.15 and reoffered at a price of \$260,618,923.45, which reflects the prices corresponding to the 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 without prior notice to any person.

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

/s/ _____
Director of Finance

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APPENDIX A
BOND ORDINANCE

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THE CITY OF SEATTLE, WASHINGTON

ORDINANCE 122807

AN ORDINANCE relating to the electric system of The City of Seattle; authorizing the issuance and sale of municipal light and power revenue bonds for the purposes of providing funds for certain additions and betterments to and extensions of the existing municipal light and power plant and system of the City, paying the costs of issuing and selling those bonds and providing for the reserve fund requirement; providing for the terms, conditions, covenants and manner of sale of those bonds; and describing the lien of those bonds.

Passed September 22, 2008

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ORDINANCE 122807

1 AN ORDINANCE relating to the electric system of The City of Seattle; authorizing the issuance and
2 sale of municipal light and power revenue bonds for the purposes of providing funds for
3 certain additions and betterments to and extensions of the existing municipal light and power
4 plant and system of the City, paying the costs of issuing and selling those bonds and
5 providing for the reserve fund requirement; providing for the terms, conditions, covenants
6 and manner of sale of those bonds; and describing the lien of those bonds.

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

9 WHEREAS, the City has need to acquire and construct certain additions and betterments to and
10 extensions of the Light System described in the system or plan adopted by this ordinance (the
11 "Plan of Additions"); and

12 WHEREAS, the City has outstanding certain revenue bonds (the "Outstanding Parity Bonds")
13 having a charge and lien upon the Gross Revenue of the Light System prior and superior to
14 all other charges whatsoever, except reasonable charges for maintenance and operation of the
15 Light System; and

16 WHEREAS, pursuant to the respective ordinances and resolutions listed in Exhibit A, the City
17 issued its municipal light and power revenue bonds described in Exhibit A, and provided for
18 the issuance of additional bonds having a lien and charge on the Gross Revenue of the Light
19 System on a parity of lien with those bonds ("Parity Bonds") upon compliance with certain
20 conditions; and

21 WHEREAS, after due consideration, the City finds that it is necessary and in the best interest of the
22 City and its ratepayers to issue municipal light and power revenue bonds as Parity Bonds to
23 pay part of the cost of the Plan of Additions, pay costs of issuing and selling those bonds and
24 provide for the reserve fund requirement; NOW, THEREFORE,

25 BE IT ORDAINED BY THE CITY OF SEATTLE AS FOLLOWS:

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

"Accreted Value" means with respect to any Capital Appreciation Bonds (a) as of any
Valuation Date, the amount set forth for such date in any Parity Bond Ordinance authorizing such
Capital Appreciation Bonds and (b) as of any date other than a Valuation Date, the sum of (i) the
Accreted Value on the preceding Valuation Date and (ii) the product of (A) a fraction, the numerator
of which is the number of days having elapsed from the preceding Valuation Date and the
denominator of which is the number of days from such preceding Valuation Date to the next

1 succeeding Valuation Date, calculated based on the assumption that Accreted Value accrues during
2 any semiannual period in equal daily amounts on the basis of a year of twelve 30-day months, times
3 (B) the difference between the Accreted Values for such Valuation Dates.

4 "Adjusted Net Revenue" has the meaning assigned to that term in Section 15(g)(iii).

5 "Annual Debt Service" for any calendar year means the sum of the amounts required in such
6 calendar year to pay:

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

11 For purposes of this definition, the principal and interest portions of the Accreted Value of
12 Capital Appreciation Bonds becoming due at maturity or by virtue of a Sinking Fund Requirement
13 shall be included in the calculations of accrued and unpaid and accruing interest or principal in such
14 manner and during such period of time as is specified in any Parity Bond Ordinance authorizing such
15 Capital Appreciation Bonds.

16 For purposes of calculating and determining compliance with the Reserve Fund Requirement
17 and conditions for the issuance of Future Parity Bonds and/or entering into Parity Payment
18 Agreements:

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

- 25 (ii) Interest on Variable Interest Rate Bonds. The amount of interest deemed to be
- 26 payable on any issue of Variable Interest Rate Bonds shall be calculated on the assumption that the

1 interest rate on those bonds would be equal to the rate that is 90% of the average RBI during the four
2 calendar quarters preceding the quarter in which the calculation is made;

- 3 (iii) Interest on Parity Bonds With Respect to Which a Payment Agreement is in
- 4 Force. Debt service on Parity Bonds with respect to which a Payment Agreement is in force shall be
- 5 based on the net economic effect on the City expected to be produced by the terms of the Parity
- 6 Bonds and the terms of the Payment Agreement, including but not limited to the effects produced by
- 7 the following: (A) Parity Bonds that would, but for a Payment Agreement, be treated as obligations
- 8 bearing interest at a Variable Interest Rate instead shall be treated as obligations bearing interest at a
- 9 fixed interest rate, and (B) Parity Bonds that would, but for a Payment Agreement, be treated as
- 10 obligations bearing interest at a fixed interest rate instead shall be treated as obligations bearing
- 11 interest at a Variable Interest Rate. Accordingly, the amount of interest deemed to be payable on
- 12 any Parity Bonds with respect to which a Payment Agreement is in force shall be an amount equal to
- 13 the amount of interest that would be payable at the rate or rates stated in those Parity Bonds plus
- 14 Payment Agreement Payments minus Payment Agreement Receipts. For the purposes of calculating
- 15 as nearly as practicable Payment Agreement Receipts and Payment Agreement Payments under a
- 16 Payment Agreement that includes a variable rate component determined by reference to a pricing
- 17 mechanism or index that is not the same as the pricing mechanism or index used to determine the
- 18 variable rate interest component on the Parity Bonds to which the Payment Agreement is related, it
- 19 shall be assumed that the fixed rate used in calculating Payment Agreement Payments will be equal
- 20 to 105% of the fixed rate specified by the Payment Agreement and that the pricing mechanism or
- 21 index specified by the Payment Agreement is the same as the pricing mechanism or index specified
- 22 by the Parity Bonds. Notwithstanding the other provisions of this subparagraph (iii), the City shall
- 23 not be required to (but may in its discretion) take into account in determining Annual Debt Service
- 24 the effects of any Payment Agreement that has a term of ten years or less;

- 25 (iv) Parity Payment Agreements. No additional debt service shall be taken into
- 26 account with respect to a Parity Payment Agreement for any period during which Payment

1 Agreement Payments on that Parity Payment Agreement are taken into account in determining
2 Annual Debt Service on related Parity Bonds under subparagraph (iii) of this definition. However,
3 for any period during which Payment Agreement Payments are not taken into account in calculating
4 Annual Debt Service on any outstanding Parity Bonds because the Parity Payment Agreement is not
5 then related to any outstanding Parity Bonds, payments on that Parity Payment Agreement shall be
6 taken into account by assuming:
7 (A) City Obligated to Make Payments Based on Fixed Rate. If the City is
8 obligated to make Payment Agreement Payments based on a fixed rate and the Qualified
9 Counterparty is obligated to make payments based on a variable rate index, that payments by the
10 City will be based on the assumed fixed payor rate, and that payments by the Qualified Counterparty
11 will be based on a rate equal to the average rate determined by the variable rate index specified by
12 the Parity Payment Agreement during the four calendar quarters preceding the quarter in which the
13 calculation is made, and
14 (B) City Obligated to Make Payments Based on Variable Rate Index. If
15 the City is obligated to make Payment Agreement Payments based on a variable rate index and the
16 Qualified Counterparty is obligated to make payment based on a fixed rate, that payments by the
17 City will be based on a rate equal to the average rate determined by the variable rate index specified
18 by the Parity Payment Agreement during the four calendar quarters preceding the quarter in which
19 the calculation is made, and that the Qualified Counterparty will make payments based on the fixed
20 rate specified by the Parity Payment Agreement.

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

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

25 "Bond Registrar" or "Registrar" means the fiscal agency of the State of Washington, or any
26 successor bond registrar selected by the City, whose duties include the registration and

1 authentication of the Bonds, maintenance of the Bond Register, effecting transfer of ownership of
2 the Bonds, and paying the principal of and premium, if any, and interest on the Bonds.

3 "Bond Resolution" means the resolution or resolutions fixing certain provisions of the Bonds
4 and their sale as authorized by Section 3 of this ordinance.

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

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

14 "CIP" means the portion or portions relating to the Light System of the "2008-2013 Capital
15 Improvement Program" of the City as adopted by the City in Ordinance 122560, passed
16 November 19, 2007, as that CIP may be amended, updated, supplemented or replaced from time to
17 time.

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

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

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

24 "Conservation Plan" means the 1996 Energy Management Services Plan of the City with
25 respect to the Light System endorsed by the City in Resolution 29427, adopted September 16, 1996,
26

1 as that plan may be amended, updated, supplemented or replaced from time to time, to the extent that
2 funds are appropriated by the City therefor.

3 “Deferred Hydroelectric Project Relicensing Costs” means certain costs required by the
4 Federal Energy Regulatory Commission to be incurred as a condition of the renewal of licenses for
5 the Light System’s hydroelectric projects, which costs are treated in the same manner as capital
6 expenditures.

7 “DTC” means The Depository Trust Company, New York, New York, as initial Securities
8 Depository for the Bonds.

9 “Director of Finance” means the Director of Finance of the City, or any successor thereto.

10 “Future Parity Bonds” means any fixed or variable rate revenue bonds of the City (other than
11 the Bonds) issued hereafter having a charge or lien upon the Gross Revenues for payment of the
12 principal thereof and interest thereon equal in priority to the charge or lien upon the Gross Revenues
13 of the Light System for the payment of the principal of and interest on the Outstanding Parity Bonds
14 and the Bonds. Future Parity Bonds may include Parity Payment Agreements and any other
15 obligations issued in compliance with Section 15(g) or Section 15(h).

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

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

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

11 “High Ross Agreement” means the agreement dated as of March 30, 1984, between the City
12 and Her Majesty the Queen in Right of the Province of British Columbia relating to the City’s High
13 Ross Dam.

14 “High Ross Capital Payments” means the deferred portion of the annual capital payments
15 required to be made by the City under Section 5 of the High Ross Agreement, representing the
16 annual cost that would have been incurred by the City for the construction of the High Ross Dam.

17 “Letter of Representations” means the Blanket Issuer Letter of Representations between the
18 City and DTC dated October 4, 2006, as it may be amended from time to time.

19 “Light Fund” means the special fund of the City of that name heretofore created and
20 established by the City Council.

21 “Light System” means the municipal light and power plant and system now belonging to or
22 which may hereafter belong to the City.

23 “Mayor” means the Mayor of the City.

24 “Moody’s” means Moody’s Investors Service, Inc.

25 “Net Revenue” for any period has the meaning assigned to that term in Section 15(g)(ii).

26

1 "New Covenant Date" means the date on which no 1997 Bonds, 1998A Bonds, 1998B
2 Bonds, 1999 Bonds, or 2000 Bonds remain outstanding under the respective ordinances authorizing
3 the issuance of such bonds.
4 "Outstanding Parity Bonds" means, collectively, the outstanding 1997 Bonds, 1998A Bonds,
5 1998B Bonds, 1999 Bonds, 2000 Bonds, 2001 Bonds, 2002 Bonds, 2003 Bonds and 2004 Bonds, all
6 as described in Exhibit A.
7 "Parity Bond Fund" means the Seattle Municipal Light Revenue Parity Bond Fund
8 established pursuant to Ordinance 92938 for the purpose set forth in Section 15(a).
9 "Parity Bond Ordinance" means any ordinance or resolution passed or adopted by the City
10 Council providing for the issuance of Parity Bonds, and any other ordinance or resolution amending
11 or supplementing the provisions of any Parity Bond Ordinance as originally passed or adopted or as
12 theretofore amended or supplemented.
13 "Parity Bonds" means the Outstanding Parity Bonds, the Bonds and any Future Parity Bonds.
14 "Parity Payment Agreement" means a Payment Agreement under which the City's
15 obligations are expressly stated to constitute a charge and lien on the Net Revenue of the Light
16 System equal in rank with the charge and lien upon such Net Revenue required to be paid into the
17 Parity Bond Fund to pay and secure the payment of the principal of and interest on Parity Bonds.
18 "Payment Agreement" means a written contract entered into, for the purpose of managing or
19 reducing the City's exposure to fluctuations or levels of interest rates or for other interest rate,
20 investment, asset or liability management purposes, by the City and a Qualified Counterparty on
21 either a current or forward basis as authorized by any applicable laws of the State in connection with,
22 or incidental to, the issuance, incurring or carrying of particular bonds, notes, bond anticipation
23 notes, commercial paper or other obligations for borrowed money, or lease, installment purchase or
24 other similar financing agreements or certificates of participation therein, that provides for an
25 exchange of payments based on interest rates, ceilings or floors on such payments, options on such
26 payments, or any combination thereof or any similar device.

1 "Payment Agreement Payments" means the amounts, periodically required to be paid by the
2 City to the Qualified Counterparty pursuant to a Payment Agreement.
3 "Payment Agreement Receipts" means the amounts periodically required to be paid by the
4 Qualified Counterparty to the City pursuant to a Payment Agreement.
5 "Permitted Investments" means any investments or investment agreements permitted for the
6 investment of City funds under the laws of the State of Washington as amended from time to time.
7 "Plan of Additions" means, collectively, the CIP and the Conservation Plan, as they may be
8 modified hereafter by ordinance as described herein, the High Ross Capital Payments and the
9 Deferred Hydroelectric Project Relicensing Costs.
10 "Professional Utility Consultant" means the independent person(s) or firm(s) selected by the
11 City having a favorable reputation for skill and experience with electric systems of comparable size
12 and character to the Light System in such areas as are relevant to the purposes for which they were
13 retained.
14 "Qualified Counterparty" means a party (other than the City or a person related to the City)
15 who is the other party to a Payment Agreement and who is qualified to act as the other party to a
16 Payment Agreement under any applicable laws of the State.
17 "Qualified Insurance" means any municipal bond insurance policy or surety bond issued by
18 any insurance company licensed to conduct an insurance business in any state of the United States
19 (or by a service corporation acting on behalf of one or more such insurance companies) which
20 insurance company or companies, as of the time of issuance of such policy or surety bond, are rated
21 in one of the two highest rating categories by Moody's and S&P or their comparably recognized
22 business successors.
23 "Qualified Letter of Credit" means any letter of credit issued by a financial institution for the
24 account of the City on behalf of the owners of Parity Bonds, which institution maintains an office,
25 agency or branch in the United States and as of the time of issuance of such letter of credit is rated in
26

1 one of the two highest rating categories by Moody's and S&P or their comparably recognized
2 business successors.
3 "Rate Stabilization Account" means the fund of that name established in the Light Fund
4 pursuant to Ordinance 121637.
5 "RBI" means The Bond Buyer Revenue Bond Index or comparable index, or, if no
6 comparable index can be obtained, 80% of the interest rate for actively traded 30 year United States
7 Treasury obligations.
8 "Refunding Parity Bonds" means Parity Bonds issued pursuant to Section 15(h) of this
9 ordinance for the purpose of refunding bonds of any prior series of Parity Bonds.
10 "Reserve Fund" means the Municipal Light and Power Bond Reserve Fund established
11 pursuant to Ordinance 71917, as amended.
12 "Reserve Fund Requirement" means, at any time, the lesser of (a) the maximum Annual Debt
13 Service on all Parity Bonds then outstanding, and (b) the maximum amount permitted by the Code as
14 a "reasonably required reserve or replacement fund." *Notwithstanding the foregoing, on the New*
15 *Covenant Date, "Reserve Fund Requirement" shall mean, for any issue of Future Parity Bonds, the*
16 *Reserve Fund Requirement specified for that issue, and the Reserve Fund Requirement for all series*
17 *of Future Parity Bonds shall be the sum of the Reserve Fund Requirement for all such Future Parity*
18 *Bonds.*
19 "S&P" means Standard & Poor's Ratings Services, a Division of The McGraw-Hill
20 Companies, Inc.
21 "Securities Depository" means any one of the following registered securities depositories
22 which has been designated by the City: (i) DTC; (ii) Midwest Securities Trust Company, Chicago,
23 Illinois, (iii) Philadelphia Depository Trust Company, Philadelphia, Pennsylvania; or (iv) such other
24 securities depositories as the City may designate in a certificate of the City delivered to the Bond
25 Registrar.
26

1 "Serial Bonds" means Parity Bonds maturing in specified years, for which no Sinking Fund
2 Requirements are mandated.
3 "Sinking Fund Account" means any account created in the Parity Bond Fund to amortize the
4 principal or make mandatory redemptions of Term Bonds.
5 "Sinking Fund Requirement" means, for any calendar year, the principal amount and
6 premium, if any, of Term Bonds required to be purchased, redeemed, paid at maturity or paid into
7 any Sinking Fund Account for such calendar year as established by the Parity Bond Ordinance
8 authorizing the issuance of such Term Bonds.
9 "State" means the State of Washington.
10 "Subordinate Lien Bonds" means, collectively, the City's outstanding Municipal Light and
11 Power Adjustable Rate Revenue Bonds, 1990, Municipal Light and Power Adjustable Rate Revenue
12 Bonds, 1991, Series A and B, Municipal Light and Power Adjustable Rate Revenue Bonds, 1993,
13 and Municipal Light and Power Adjustable Rate Revenue Bonds, 1996, and any bonds issued
14 hereafter, having a charge or lien upon the Gross Revenues of the Light System on a parity with
15 those bonds.
16 "Term Bonds" means any Parity Bonds identified as such in the Parity Bond Ordinance
17 authorizing the issuance thereof, which Parity Bond Ordinance requires that all or a portion of such
18 bonds be purchased, redeemed or paid prior to maturity in a schedule established thereby.
19 "Valuation Date" means, with respect to any Capital Appreciation Bonds, the date or dates
20 set forth in any Parity Bond Ordinance authorizing such Parity Bonds on which specific Accreted
21 Values are assigned to the Capital Appreciation Bonds.
22 "Variable Interest Rate" means any variable interest rate or rates to be borne by any Parity
23 Bonds. The method of computing such a variable interest rate shall be as specified in the Parity
24 Bond Ordinance authorizing or specifying the terms of such Parity Bonds, which Parity Bond
25 Ordinance also shall specify either (i) the particular period or periods of time or manner of
26 determining such period or periods of time for which each value of such variable interest rate shall

1 remain in effect or (ii) the time or times upon which any change in such variable interest rate shall
2 become effective.

3 "Variable Interest Rate Bonds" means, for any period of time, any Parity Bonds that bear a
4 Variable Interest Rate during that period, except that Parity Bonds shall not be treated as Variable
5 Interest Rate Bonds if the net economic effect of interest rates on particular Parity Bonds of an issue
6 and interest rates on other Parity Bonds of the same issue, as set forth in the applicable Parity Bond
7 Ordinance, or the net economic effect of a Payment Agreement with respect to particular Parity
8 Bonds, in either case is to produce obligations that bear interest at a fixed interest rate; and Parity
9 Bonds with respect to which a Payment Agreement is in force shall be treated as Variable Interest
10 Rate Bonds if the net economic effect of the Payment Agreement is to produce obligations that bear
11 interest at a Variable Interest Rate.

12 Section 2. Adoption of System or Plan. The Plan of Additions constitutes a system or
13 plan of additions to and betterments and extensions of the Light System (each element thereof an
14 "Addition"). To the extent not previously specified, adopted and ordered by the City by ordinance,
15 the City specifies, adopts and orders to be carried out the Plan of Additions, and declares the
16 estimated cost of that system or plan to be \$1,700,000,000, of which \$200,000,000 is expected to be
17 financed from proceeds of the Bonds.

18 The Plan of Additions shall include any amendments, updates, supplements or replacements
19 to the CIP or the Conservation Plan determined by ordinance to constitute a system or plan of
20 additions to and betterments and extensions of the Light System, all of which automatically shall
21 constitute amendments to the Plan of Additions. The Plan of Additions also may be modified,
22 without amending the CIP or the Conservation Plan, to include other elements if the City determines
23 by ordinance that those other elements constitute a system or plan of additions to or betterments or
24 extensions of the Light System. The Plan of Additions includes the purchase and installation of all
25 materials, supplies, appliances, equipment (including but not limited to data processing hardware
26 and software and conservation equipment) and facilities, the acquisition of all permits, licenses,

1 franchises, property and property rights, other capital assets and all engineering, consulting and other
2 professional services and studies (whether performed by the City or by other public or private
3 entities) necessary or convenient to carry out the Plan of Additions.

4 Section 3. Authorization and Description of Bonds; Bond Resolution. For the purpose of
5 providing all or part of the funds with which to (1) pay part of the cost of carrying out the Plan of
6 Additions; (2) provide for the Reserve Fund Requirement; and (3) pay the costs of issuing and
7 selling the Bonds, the City shall issue and sell the Bonds in the aggregate principal amount of not to
8 exceed \$215,000,000. The Bonds may be issued in one or more series; may be combined with other
9 Parity Bonds authorized separately; shall be called "The City of Seattle, Washington, Municipal
10 Light and Power Improvement Revenue Bonds, 2008" (unless changed by resolution); may have
11 such different or further designation or designations as determined by the Director of Finance or as
12 the City Council may specify in a resolution or resolutions fixing the terms of and matters relating to
13 the Bonds (collectively, the "Bond Resolution"); shall be dated and shall mature on such date or
14 dates specified in the Bond Resolution, except that the final maturity date of the Bonds shall not
15 extend beyond 30 years from their respective dates of issuance; shall be issued in fully registered
16 form; shall be numbered separately in the manner and with any additional designation as the Bond
17 Registrar for the Bonds deems necessary for purposes of identification; shall bear interest at the rate
18 or rates (computed on the basis of a 360-day year of twelve 30-day months) specified in the Bond
19 Resolution, except that the true interest cost shall not exceed 8.0% per annum, payable at the times
20 specified in the Bond Resolution; and shall have such denominations, mature on such dates and be
21 subject to optional or mandatory redemption, open market purchase or defeasance on the terms and
22 at the times specified in the Bond Resolution. The Director of Finance may designate Term Bonds
23 with mandatory redemption amounts, all to be provided by the Bond Resolution.

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

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 4. 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
15 other action to be taken by registered owners of Bonds and for all other purposes whatsoever; and
16 the City and the Bond Registrar shall not be affected by any notice to the contrary. The City and the
17 Bond Registrar shall not have any responsibility or obligation to any direct or indirect DTC
18 participant, any person claiming a beneficial ownership interest in the Bonds under or through DTC
19 or any such direct or indirect participant, or any other person which is not shown on the Bond
20 Register as being a registered owner of Bonds, with respect to: (1) the Bonds; (2) any records
21 maintained by DTC or any such direct or indirect participant; (3) the payment by DTC or any such
22 direct or indirect participant of any principal of, premium, if any, or interest on the Bonds; (4) any
23 notice which is permitted or required to be given to registered owners of Bonds under this ordinance
24 or the Bond Resolution; (5) the selection by DTC or any direct or indirect participant of any person
25 to receive payment in the event of a partial redemption of the Bonds; or (6) any consent given or
26 other action taken by DTC as registered owner of 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 15
11 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
19 (or through a successor Securities Depository) is not in the best interests of the City. In each of such
20 events (unless, in the case described in clause (1) above, the City appoints a successor Securities
21 Depository), the Bonds shall be delivered in registered certificate form to such persons, and in such
22 maturities and principal amounts, as may be designated by DTC, but without any liability on the part
23 of the City or the Bond Registrar for the accuracy of such designation. Whenever DTC requests the
24 City and the Bond Registrar to do so, or whenever the City requests DTC and the Bond Registrar to
25 do so after the determination by the City to replace DTC with a successor Securities Depository, the
26 City and the Bond Registrar shall cooperate with DTC in taking appropriate action after reasonable

1 notice to arrange for another Securities Depository to maintain custody of certificates evidencing the
2 Bonds.

3 Section 5. 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 6. 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 \$1,000,000 or more in
21 aggregate principal amount of Bonds, by wire transfer to an account in the United States designated
22 in writing by such registered owner prior to the Record Date. Principal of and premium, if any, on
23 the Bonds shall be payable upon presentation and surrender of the Bonds by the registered owners at
24 either of the principal corporate trust office or offices of the Bond Registrar at the option of the
25 owners. Notwithstanding the foregoing, payment of any Bonds registered in the name of DTC or its
26 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 7. 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 \$5,000, may be
23 redeemed, unless otherwise provided in the Bond Resolution. If less than all of the principal amount
24 of any Bond is redeemed, upon surrender of that Bond at either of the principal offices of the Bond
25 Registrar, there shall be issued to the registered owner, without charge therefor, a new Bond (or
26 Bonds, at the option of the registered owner) of the same series, maturity and interest rate in any of

1 the denominations authorized by the Bond Resolution in the aggregate total principal amount
2 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 7 shall
7 be cancelled.

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

21 Section 9. 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 Section 10. Form and Execution of Bonds. The Bonds shall be typed, photocopied,
2 printed or lithographed on good bond paper in a form consistent with the provisions of this
3 ordinance, the Bond Resolution and State law; shall be signed by the Mayor and Director of Finance,
4 either or both of whose signatures may be manual or in facsimile; and the seal of the City or a
5 facsimile reproduction thereof shall be impressed or printed thereon.

6 Only Bonds bearing a Certificate of Authentication in substantially the following form,
7 manually signed by the Bond Registrar, shall be valid or obligatory for any purpose or entitled to the
8 benefits of this ordinance:

9 **CERTIFICATE OF AUTHENTICATION**

10 This Bond is one of the fully registered The City of Seattle, Washington,
11 Municipal Light and Power Improvement Revenue Bonds, 2008, described in the
12 Bond Ordinance.

13 Bond Registrar

14 By _____

15 Authorized Signer

16 The authorized signing of a Certificate of Authentication shall be conclusive evidence that the Bond
17 so authenticated has been duly executed, authenticated and delivered and is entitled to the benefits of
18 this ordinance.

19 If any officer whose facsimile signature appears on the Bonds ceases to be an officer of the
20 City authorized to sign bonds before the Bonds bearing his or her facsimile signature are
21 authenticated or delivered by the Bond Registrar or issued by the City, those Bonds nevertheless
22 may be authenticated, delivered and issued and, when authenticated, issued and delivered, shall be as
23 binding on the City as though that person had continued to be an officer of the City authorized to
24 sign bonds. Any Bond also may be signed on behalf of the City by any person who, on the actual
25 date of signing of the Bond, is an officer of the City authorized to sign bonds, although he or she did
26 not hold the required office on the date of issuance of the Bonds.

1 Section 11. Bond Registrar. The Bond Registrar shall keep, or cause to be kept, at its
2 principal corporate trust office, sufficient books for the registration and transfer of the Bonds which
3 shall be open to inspection by the City at all times. The Bond Registrar is authorized, on behalf of
4 the City, to authenticate and deliver Bonds transferred or exchanged in accordance with the
5 provisions of the Bonds and this ordinance, to serve as the City's paying agent for the Bonds and to
6 carry out all of the Bond Registrar's powers and duties under this ordinance and SMC Chapter 5.10
7 establishing a system of registration for the City's bonds and obligations, as that chapter now exists
8 or may hereafter be amended. The City reserves the right in its discretion to appoint special paying
9 agents, registrars or trustees in connection with the payment of some or all of the principal of or
10 interest on the Bonds. If a new Bond Registrar is appointed by the City, notice of the name and
11 address of the new Bond Registrar shall be mailed to the registered owners of the Bonds. The notice
12 may be mailed together with the next interest payment due on the Bonds, but, to the extent
13 practicable, shall be mailed not less than 15 days prior to a maturity date of the principal of any
14 Bond.

15 The Bond Registrar shall be responsible for its representations contained in the Bond
16 Registrar's Certificate of Authentication on the Bonds. The Bond Registrar may become the
17 registered owner of Bonds with the same rights it would have if it were not the Bond Registrar and,
18 to the extent permitted by law, may act as depository for and permit any of its officers or directors to
19 act as members of, or in any other capacity with respect to, any committee formed to protect the
20 rights of the registered owners of the Bonds.

21 Section 12. Parity With Other Bonds. The Bonds authorized herein shall be on a parity
22 with the Outstanding Parity Bonds and all bonds hereafter issued on a parity therewith, without
23 regard to date of issuance or authorization and without preference or priority of right or lien with
24 respect to participation of special funds in amounts from gross revenues for payment thereof.
25 Nothing contained herein shall prevent the City from issuing revenue bonds or other obligations
26

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 13. City Findings of Sufficiency of Revenues. The Bonds shall be issued only if
4 the City Council finds and determines by the Bond Resolution that the issuance and sale of the
5 Bonds is in the best interest of the City and in the public interest. In making such findings and
6 determinations, the City Council shall give due regard to the cost of operation and maintenance of
7 the Light System and to any portion of the Gross Revenues pledged for the payment of any bonds,
8 warrants or other indebtedness, and shall find and determine that the Gross Revenues, at the rates
9 established from time to time consistent with Section 15(d) of this ordinance, will be sufficient, in
10 the judgment of the City Council, to meet all expenses of operation and maintenance of the Light
11 System and to provide the amounts previously pledged for the payment of all outstanding obligations
12 payable out of the Gross Revenue and pledged herein for the payment of the Bonds.

13 Section 14. Security for the Bonds. The Bonds shall be special limited obligations of the
14 City payable from and secured solely by the Gross Revenues and by money in the Parity Bond Fund
15 and the Reserve Fund. The Gross Revenues are pledged to make the payments into the Parity Bond
16 Fund and the Reserve Fund required by Section 15(a) and (b) of this ordinance, which pledge shall
17 constitute a charge upon such Gross Revenues prior and superior to all other charges whatsoever,
18 save and except reasonable charges for maintenance and operation of the Light System.

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

23 Section 15. Bond Covenants.

24 (a) Parity Bond Fund. A special fund of the City known as the "Seattle Municipal Light
25 Revenue Parity Bond Fund" (the "Parity Bond Fund") has heretofore been created by Ordinance
26 92938, and is now maintained as a separate account within the Light Fund, for the sole purpose of

1 paying the principal of and interest on the bonds therein authorized and future bonds issued on a
2 parity therewith as the same shall become due. The Bonds shall be payable, principal, premium, if
3 any, and interest, out of the Parity Bond Fund.
4 From and after the issuance of the Bonds, and so long thereafter as obligations are
5 outstanding against the Parity Bond Fund (including any Payment Agreement Payments required to
6 be made under any Parity Payment Agreements), the Director of Finance shall set aside and pay into
7 the Parity Bond Fund on or prior to the respective dates on which the interest on or principal of and
8 interest on the Bonds shall become due and payable certain fixed amounts out of the Gross Revenues
9 sufficient to pay such interest or principal and interest as the same shall become due.

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

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

19 In the Bond Resolution, the City will specify whether it will satisfy the Reserve Fund
20 Requirement with Qualified Insurance or a Qualified Letter of Credit or by depositing into the
21 Reserve Fund, out of any money legally available therefor, within 5 years from the date of issuance
22 of the Bonds, the amount required to fund the Reserve Fund to the Reserve Fund Requirement.

23 Money held in the Reserve Fund shall, to the fullest extent practicable and reasonable, be
24 invested and reinvested at the direction of the Director of Finance solely in, and obligations
25 deposited in such accounts shall consist of, Permitted Investments. Earnings on money and
26 investments in the Reserve Fund shall be deposited in that fund and credited against amounts

1 required to be deposited therein until the Reserve Fund is fully funded, and thereafter such earnings
2 shall be deposited in the Parity Bond Fund.

3 (i) Reserve Fund Requirement.

4 (A) The City shall provide in the Parity Bond Ordinance authorizing the
5 issuance of any Future Parity Bonds for deposit into the Reserve Fund out of the Gross Revenues (or
6 out of any other funds of the City on hand and legally available therefor, including the proceeds of
7 the Future Parity Bonds being issued or any other Future Parity Bonds) of periodic payments so that
8 by five years from the date of such Future Parity Bonds there will have been paid into the Reserve
9 Fund an amount which, together with the money already on deposit therein, will be at least equal to
10 the Reserve Fund Requirement for all Parity Bonds outstanding at the end of that five-year period.

11 (B) Notwithstanding the foregoing, any Parity Bond Ordinance may
12 provide for the City to obtain Qualified Insurance or a Qualified Letter of Credit for specific
13 amounts required to be paid into the Reserve Fund. The amount available to be drawn upon under
14 such Qualified Insurance or Qualified Letter of Credit shall be credited against the amounts required
15 to be maintained in the Reserve Fund by Section 15(b)(i)(A).

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

1 effective date of any cancellation of a Qualified Letter of Credit or Qualified Insurance to make up
2 the deficiency caused thereby.

3 (D) If the amount in the Reserve Fund shall be less than the Reserve Fund
4 Requirement (taking into account the five year period referred to in Section 15(b)(i)(A)), the City
5 shall transfer to the Reserve Fund money in an amount sufficient to restore the Reserve Fund to the
6 Reserve Fund Requirement within 12 months after the date of such deficiency. The City shall
7 transfer such amounts first from money in the Light Fund (after making provision for payment of
8 operating and maintenance expenses and for the required payments into the Parity Bond Fund) and
9 only thereafter from money in any construction fund or account established with respect to any issue
10 of Parity Bonds, first taking money from the unrestricted portion thereof, then taking money from
11 the restricted portion thereof. If the amount in the Reserve Fund shall be greater than the Reserve
12 Fund Requirement, then and only then may the City withdraw such excess from the Reserve Fund
13 and deposit such excess in the Light Fund.

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

20 (iii) Use of Reserve Fund for Payment of Debt Service. If the money in the Parity
21 Bond Fund is insufficient to meet maturing installments of either interest on or principal of and
22 interest on the Parity Bonds payable out of the Parity Bond Fund (including amounts payable under
23 any Parity Payment Agreements), such deficiency shall be made up from the Reserve Fund by the
24 withdrawal of money or proceeds of Qualified Insurance or Qualified Letters of Credit therefrom, as
25 the case may be. Any deficiency created in the Reserve Fund by reason of any such withdrawal or
26 claim against Qualified Insurance or a Qualified Letter of Credit shall then be made up out of the

1 Gross Revenues (or out of such other funds of the City on hand and legally available therefor), after
2 making necessary provision for the payments required to be made for operation and maintenance of
3 the Light System and debt service on any obligations payable from such Gross Revenues.

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

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

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

17 (c) Sale or Disposition of the Light System.

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

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

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

1 (B) provision is made for the payment, redemption or other retirement of a
2 principal amount of Parity Bonds equal to the greater of the following amounts:
3 (I) An amount which will be in the same proportion to the net
4 principal amount of Parity Bonds then outstanding (defined as the total principal amount of Parity
5 Bonds then outstanding less the amount of cash and investments in the Parity Bond Fund) that the
6 Gross Revenues for the 12 preceding months attributable to the part of the Light System sold or
7 disposed of bears to the total Gross Revenues for such period; or
8 (II) An amount which will be in the same proportion to the net
9 principal amount of Parity Bonds then outstanding that the book value of the part of the Light
10 System sold or disposed of bears to the book value of the entire Light System immediately prior to
11 such sale or disposition.
12 (iii) The City may dispose of any portion of the Light System that has become
13 unserviceable, inadequate, obsolete, worn out or unfit to be used or no longer necessary, material to
14 or useful in the operation of the Light System.
15 (iv) If the ownership of all or part of the Light System is transferred from the City
16 through the operation of law, the City shall reconstruct or replace the transferred portion using any
17 proceeds of the transfer unless the City Council determines that such reconstruction or replacement
18 is not in the best interests of the City and the owners of the Parity Bonds, in which case any proceeds
19 shall be used to retire Parity Bonds prior to maturity.

20 (d) Rates and Charges. The City will establish from time to time and maintain such rates
21 for electric energy as will maintain the Light System in sound financial condition and provide
22 sufficient revenues to permit the payment of sums into the special fund which the City has pledged
23 to be set aside for the payment of principal and interest, as herein provided, to be applied to the
24 payment of the principal of and interest on the Parity Bonds until the Parity Bonds shall have been
25 paid in full, and in addition thereto, will pay all costs of operation and maintenance, and all bonds,
26

1 warrants and indebtedness for which any revenues of the Light System shall have been heretofore
2 pledged.

3 (e) Maintenance and Operation of the Light System. The City will operate the properties
4 of the Light System in an efficient manner and at a reasonable cost; and will maintain, preserve and
5 keep, or cause to be maintained, preserved and kept, the properties of the Light System and every
6 part and parcel thereof in good repair, working order and condition; and from time to time will make
7 or cause to be made all necessary and proper repairs, renewals and replacements thereto so that at all
8 times the business carried on in connection therewith will be properly and advantageously
9 conducted.

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

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

1 (i) There is no deficiency in the Parity Bond Fund or in any of the accounts
2 therein and provision has been made to meet the Reserve Fund Requirement for all Parity Bonds
3 then outstanding plus such proposed series of Parity Bonds; and
4 (ii) There shall have been filed with the City either:
5 (A) a certificate of the Director of Finance stating that Net Revenue in any
6 12 consecutive months out of the most recent 24 months preceding the delivery of the Parity Bonds
7 then proposed to be issued (the "Base Period") was not less than 125% of maximum Annual Debt
8 Service in any future calendar year on all Parity Bonds then outstanding and the Parity Bonds then
9 proposed to be issued (except that if any adjustment in the rates, fees and charges for the services of
10 the Light System shall be effective at any time on or prior to the date of delivery of the Parity Bonds
11 then proposed to be issued or within six months after the delivery of such Parity Bonds, the Director
12 of Finance shall reflect in his or her certificate the Net Revenue he or she calculates would have been
13 collected in the Base Period if such new rates, fees and charges had been in effect for the entire Base
14 Period), or
15 (B) a certificate of the Professional Utility Consultant setting forth:
16 (I) the amount of the Adjusted Net Revenue computed as provided
17 in paragraph (C) below;
18 (II) the amount of maximum Annual Debt Service in any calendar
19 year thereafter on account of all Parity Bonds to be outstanding in such calendar year, including the
20 Parity Bonds proposed to be issued, and stating that the amount shown in paragraph (B)(I) above is
21 not less than 125% of the amount shown in this paragraph (B)(II).

22 "Net Revenue" as used in this Section 15(g) means that amount determined by deducting
23 from the Gross Revenues the expenses of operation, maintenance and repair of the Light System,
24 *except that on the New Covenant Date, "Net Revenue" as used in this Section 15(g) shall mean that*
25 *amount determined by deducting from the Gross Revenues the expenses of operation, maintenance*
26

1 *and repair of the Light System and further deducting any deposits into the Rate Stabilization*
2 *Account, and by adding to Gross Revenues any withdrawals from the Rate Stabilization Account.*

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

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

7 (A) If the Parity Bonds are being issued for the purpose of acquiring
8 operating electric utility properties having an earnings record, the Professional Utility Consultant
9 shall estimate the effect on the Net Revenue for the Base Period of the acquisition of such electric
10 utility properties and the integration thereof into the Light System, and shall adjust the Net Revenue
11 for the Base Period to give effect to such estimate. Any such estimate shall be based upon the
12 operating experience and records of the City and upon any available financial statements and records
13 relating to the earnings of such electric utility properties to be acquired.

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

22 (C) If the purpose for which the Parity Bonds are being issued is to acquire
23 or construct generation or transmission facilities required to furnish or make available to the Light
24 System additional power and energy, or transmission facilities required to enable the City to sell
25 additional power and energy, the Professional Utility Consultant may adjust the Net Revenue for the
26 Base Period by (a) deducting the amount of the estimated increase in operating and maintenance

1 expenses resulting from the acquisition or construction of such facilities in their first year of full
2 operation, (b) adding any additional revenues to be derived from the sale or transmission of such
3 additional power and energy pursuant to executed power sales contracts, and (c) adding an amount
4 equal to the estimated cost of the power and energy which would have been replaced or displaced by
5 such facilities had such additional power and energy in excess of the power and energy to be sold
6 pursuant to clause (b) above been used in the Light System during the Base Period.

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

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

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

23 (iv) In rendering any certificate under this Section 15(g), the Professional Utility
24 Consultant may rely upon, and such certificate shall have attached thereto, (A) financial statements
25 of the Light System, certified by the Director of Finance, showing income and expenses for the
26 period upon which the same are based and a balance sheet as of the end of such period, (B) similar

1 certified statements by the Division of Municipal Corporations of the Office of the State Auditor of
2 the State (or any successor thereto), or (C) similar certified statements by a Certified Public
3 Accountant for as much of such period as any examination by them has been made and completed.
4 If two or more of such statements are inconsistent with each other, the Professional Utility
5 Consultant shall rely on the statement described under clause (A) in this Section 15(g)(iv).

6 (h) Issuance of Refunding Parity Bonds.

7 (i) Without complying with the provisions of Section 15(g) of this ordinance, the
8 City may at any time and from time to time issue one or more series of Refunding Parity Bonds, but
9 only if there shall have been filed with the City a certificate of the Director of Finance stating that
10 Annual Debt Service immediately after the issuance of such Refunding Parity Bonds (calculated by
11 including debt service on the Refunding Parity Bonds but excluding debt service on the bonds to be
12 refunded with the proceeds thereof) does not exceed the Annual Debt Service immediately prior to
13 the issuance of the Refunding Parity Bonds (calculated by including debt service on the bonds to be
14 refunded but excluding debt service on the Refunding Parity Bonds) by more than \$5,000 in any
15 calendar year that any then-outstanding Parity Bonds are anticipated to be outstanding.

16 (ii) Parity Bonds of any one or more series or one or more maturities within a
17 series may be refunded by a single series of Refunding Parity Bonds, which Parity Bonds to be
18 refunded shall be specified in the Parity Bond Ordinance providing for the issuance of the Refunding
19 Parity Bonds, and the principal amount of such Refunding Parity Bonds may include amounts
20 necessary to pay the principal of the Parity Bonds to be refunded, interest thereon to the date of
21 payment or redemption thereof, any premium payable thereon upon such payment or redemption and
22 the costs of issuance of such Refunding Parity Bonds. The proceeds of the Refunding Parity Bonds
23 shall be held and applied in such manner as is provided in the Parity Bond Ordinance providing for
24 the issuance of such Refunding Parity Bonds, so that upon the delivery of such Refunding Parity
25 Bonds the Parity Bonds to be refunded thereby shall be deemed to be no longer outstanding in
26

1 accordance with the provisions of the Parity Bond Ordinance providing for the issuance of those
2 bonds.
3 (iii) Refunding Parity Bonds may also be issued upon compliance with the
4 provisions of Section 15(g) of this ordinance.

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

8 Section 16. Preservation of Tax Exemption for Interest on Bonds. The City covenants
9 that it will take all actions consistent with the terms of the Bonds, this ordinance and the Bond
10 Resolution, reasonably within its power and necessary to prevent interest on the Bonds from being
11 included in gross income for federal income tax purposes, and it will neither take any action nor
12 make or permit any use of proceeds of the Bonds or other funds of the City treated as proceeds of the
13 Bonds at any time during the term of the Bonds which will cause interest on the Bonds to be
14 included in gross income for federal income tax purposes.

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

17 Section 17. Advance Refunding or Defeasance of Bonds. For the purpose of enabling the
18 Bonds to be later refunded under the provisions of Ordinance 121941, the Bonds are hereby
19 designated "Refundable Bonds" for purposes of Ordinance 121941. The City may issue advance
20 refunding bonds pursuant to the laws of the State or use money available from any other lawful
21 source to pay when due the principal of and premium, if any, and interest on the Bonds, or any
22 portion thereof included in a refunding or defeasance plan, and to redeem and retire, release, refund
23 or defease those Bonds (the "Defeased Bonds") and to pay the costs of such refunding or defeasance.
24 If money and/or Government Obligations sufficient in amount, together with known earned income
25 from the investments thereof, to redeem and retire, release, refund or defease the Defeased Bonds in
26 accordance with their terms, are set aside in a special trust fund or escrow account irrevocably

1 pledged to that redemption, retirement or defeasance (the "Trust Account"), then all right and
2 interest of the owners of the Defeased Bonds in the covenants of this ordinance and in the Gross
3 Revenue and the funds and accounts pledged to the payment of the Defeased Bonds, other than the
4 right to receive the funds so set aside and pledged, thereafter shall cease and become void. Such
5 owners thereafter shall have the right to receive payment of the principal of and interest or
6 redemption price on the Defeased Bonds from the Trust Account. The City shall include in the
7 refunding or defeasance plan such provisions as the City deems necessary for the random selection
8 of any Defeased Bonds that constitute less than all of a particular maturity of the Bonds, for notice of
9 the defeasance to be given to the owners of the Defeased Bonds and to such other persons as the City
10 shall determine, and for any required replacement of Bond certificates for defeased Bonds.

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

15 If the refunding plan provides that the Defeased Bonds be secured by money and/or
16 Government Obligations pending the prior redemption of the Defeased Bonds and if such refunding
17 plan also provides that certain money and/or Government Obligations are pledged irrevocably for
18 the prior redemption of the Defeased Bonds included in that refunding plan, then only the debt
19 service on the Bonds which are not Defeased Bonds and the refunding bonds, the payment of which
20 is not so secured by the refunding plan, shall be included in the computation of the coverage
21 requirement for the issuance of Future Parity Bonds and for determining compliance with rate
22 covenants.

23 Section 18. Amendments.

24 (a) Amendments Without Bond Owners' Consent. The City Council from time to time
25 and at any time may pass a resolution or resolutions, or ordinance or ordinances, supplemental
26

1 hereto, which resolution or resolutions, ordinance or ordinances thereafter shall become a part of this
2 ordinance, for any one or more of the following purposes:

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

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

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

14 Any such supplemental resolution or ordinance of the City may be passed without the
15 consent of the owners of any Parity Bonds at any time outstanding, notwithstanding any of the
16 provisions of Section 18(b) of this ordinance, but only upon receipt by the City of an opinion of
17 Bond Counsel to the effect that the amendment is permitted by the terms of this ordinance. The City
18 shall deliver a copy of any such supplemental resolution or ordinance to Moody's, S&P or any other
19 rating agency then maintaining a rating on any Parity Bonds then outstanding prior to its passage by
20 the City.

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

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

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

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

11 It shall not be necessary for the consent of bond owners under this Section 18(b) to approve
12 the particular form of any proposed supplemental ordinance or resolution, but it shall be sufficient if
13 such consent shall approve the substance thereof.

14 (c) Effect of Amendment. Upon the passage of any supplemental resolution or ordinance
15 pursuant to the provisions of this section, this ordinance shall be deemed to be modified and
16 amended in accordance therewith, and the respective rights, duties and obligations of the City under
17 this ordinance shall thereafter be determined, exercised and enforced thereunder, subject in all
18 respects to such modification and amendments, and all the terms and conditions of any such
19 supplemental resolution or ordinance shall be deemed to be a part of the terms and conditions of this
20 ordinance for any and all purposes.

21 (d) Notation on Bonds. Parity Bonds executed and delivered after the execution of any
22 supplemental resolution or ordinance passed pursuant to the provisions of this Section 18 may have a
23 notation as to any matter provided for in such supplemental resolution or ordinance, and if such
24 supplemental resolution or ordinance shall so provide, new bonds modified to conform, in the
25 opinion of the City Council, to any modification of this ordinance contained in any such
26 supplemental resolution or ordinance may be prepared by the City and delivered without cost to the

1 owners of any affected Parity Bonds then outstanding, upon surrender for cancellation of such bonds
2 in equal aggregate principal amounts.

3 Section 19. Rate Stabilization Account. On and after the New Covenant Date, the City
4 may at any time deposit in the Rate Stabilization Account, Gross Revenue and any other money
5 received by the Light System and available to be used therefor. Thereafter, the City may withdraw
6 any or all of the money from the Rate Stabilization Account for inclusion in the Net Revenue for any
7 fiscal year of the City. Such deposits or withdrawals may be made up to and including the date 90
8 days after the end of the fiscal year for which the deposit or withdrawal will be included as Net
9 Revenue.

10 Section 20. Sale of Bonds. The Director of Finance may provide for the sale of the Bonds
11 by public sale or by a negotiated sale, limited offering or private placement, with the successful
12 underwriter, placement agent or purchaser, as applicable, chosen through a selection process
13 acceptable to the Director of Finance. The terms of that sale, which may include a forward or
14 delayed delivery of the Bonds, shall be consistent with this ordinance and the Bond Resolution, and
15 shall be confirmed by the Bond Resolution. The Bonds will be delivered to the purchasers as
16 provided in the Bond Resolution, immediately upon payment to the City of the purchase price plus
17 accrued interest to the date of closing in immediately available federal funds in Seattle, Washington,
18 at the City's expense or at another place upon which the Director of Finance and the purchaser may
19 mutually agree at the purchaser's expense.

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

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

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

10 Section 22. General Authorization. The Mayor of the City and the Director of Finance
11 and each of the other appropriate officers of the City are each authorized and directed to do
12 everything as in their judgment may be necessary, appropriate or desirable in order to carry out the
13 terms and provisions of, and complete the transactions contemplated by, this ordinance. In
14 particular, and without limitation, the Director of Finance may, in his or her discretion and without
15 further action by the City Council, (a) issue requests for proposals for underwriting or financing
16 facilities and execute engagement letters with underwriters, bond insurers or other financial
17 institutions based on responses to such requests, (b) deem final and approve the distribution of any
18 preliminary official statement or official statement relating to the Bonds, (c) comply with any
19 continuing disclosure requirements applicable to the Bonds and (d) change the Bond Registrar or any
20 securities depository appointed for the Bonds.

21 Section 23. Severability. The provisions of this ordinance are declared to be separate and
22 severable. If a court of competent jurisdiction, all appeals having been exhausted or all appeal
23 periods having run, finds any provision of this ordinance to be invalid or unenforceable as to any
24 person or circumstance, such offending provision shall, if feasible, be deemed to be modified to be
25 within the limits of enforceability or validity. However, if the offending provision cannot be so
26 modified, it shall be null and void with respect to the particular person or circumstance, and all other

1 provisions of this ordinance in all other respects, and the offending provision with respect to all other
 2 persons and all other circumstances, shall remain valid and enforceable.

3 Section 24. Ratification of Prior Acts. Any action taken after passage of this ordinance
 4 but prior to its effective date that is consistent with the authority of this ordinance, is ratified,
 5 approved and confirmed.

6 Section 25. Headings. Section headings in this ordinance are used for convenience only
 7 and shall not constitute a substantive portion of this ordinance.

8 Section 26. Effective Date. This ordinance shall take effect and be in force 30 days from
 9 and after its approval by the Mayor, but if not approved and returned by the Mayor within ten days
 10 after presentation, it shall take effect as provided by Municipal Code Section 1.04.020.

11 Passed by the City Council the ___ day of ___, 2008, and signed by me in open
 12 session in authentication of its passage this ___ day of ___, 2008.

13
 14 Approved by me this ___ day of ___, 2008.
 15 _____
 16 President _____ of the City Council

17
 18 Filed by me this ___ day of ___, 2008.
 19 _____
 20 Gregory J. Nickels, Mayor

21
 22 _____
 23 City Clerk

24 (SEAL)

EXHIBIT A
OUTSTANDING PARITY BONDS

Issue Name	Dated Date	Original Par Amount	Outstanding Balance (as of 09/01/08)	Bond Legislation
Municipal Light and Power Revenue Bonds, 1997	12/1/1997	\$30,000,000	\$23,775,000	Ord 118745 Res 29686
Municipal Light and Power Refunding Revenue Bonds, 1998, Series A	1/1/1998	\$104,645,000	\$82,390,000	Ord 118744 Res 29687
Municipal Light and Power Refunding Revenue Bonds, 1998, Series B	10/1/1998	\$90,000,000	\$75,805,000	Ord 119141 Res 29851
Municipal Light and Power Revenue Bonds, 1999	10/1/1999	\$158,000,000	\$13,500,000	Ord 119638 Res 30065
Municipal Light and Power Revenue Bonds, 2000	12/1/2000	\$98,830,000	\$92,940,000	Ord 120131 Res 30274
Municipal Light and Power Improvement and Refunding Revenue Bonds, 2001	3/15/2001	\$503,700,000	\$464,270,000	Ord 120274 Res 30298
Municipal Light and Power Refunding Revenue Bonds, 2002	12/1/2002	\$87,835,000	\$49,220,000	Ord 120931 Res 30549
Municipal Light and Power Improvement and Refunding Revenue Bonds, 2003	8/20/2003	\$251,850,000	\$170,845,000	Ord 121198 Res 30618
Municipal Light and Power Improvement and Refunding Revenue Bonds, 2004	12/23/2004	\$284,855,000	\$260,535,000	Ord 121637 Res 30732

APPENDIX B
FORM OF BOND COUNSEL OPINION

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FOSTER PEPPER PLLC

[FORM OF APPROVING LEGAL OPINION]

The City of Seattle, Washington

Re: The City of Seattle, Washington, \$257,375,000
Municipal Light and Power Improvement and Refunding Revenue Bonds, 2008

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. As to matters of fact material to this opinion and of which attorneys within the firm involved with the issuance of the Bonds have no independent knowledge, we have relied upon representations contained in the certified proceedings and other certifications of public officials furnished to us.

The Bonds are issued pursuant to the laws of the State of Washington and Ordinance 121941, as amended by Ordinance 122838, Ordinance 122807, and Resolution 31105 of the City (collectively, the "Bond Legislation") to provide all or part of the funds to (i) finance certain capital improvements to and conservation program for the Light System of the City, (ii) refund certain of the City's outstanding Municipal Light and Power bonds, and (iii) pay the costs of issuance 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 special limited obligations of the City payable from and secured solely by the Gross Revenues of the Light System, by money in the Seattle Municipal Light Revenue Parity Bonds Fund (the "Parity Bond Fund") and by 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.

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 have been duly authorized and executed by the City and 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 and binding 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.

This opinion is given as of the date hereof, and we assume no obligation to revise or supplement this opinion to reflect any facts or circumstances that may hereafter come to our attention, or any changes in law that may hereafter occur.

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,

APPENDIX C

2007 AUDITED FINANCIAL STATEMENTS OF THE DEPARTMENT

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

Enterprise Fund of the City of Seattle

*Financial Statements as of and for the
Years Ended December 31, 2007 and 2006,
Required Supplementary Information, and
Independent Auditors' Report*

CITY OF SEATTLE—CITY LIGHT DEPARTMENT

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INDEPENDENT AUDITORS' REPORT

Energy and Technology Committee
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, 2007 and 2006, and the related statements of revenues, expenses, and changes in equity and cash flows for the years then ended. These financial statements are the responsibility of the Department's management. Our responsibility is to express an opinion on the financial statements based on our audits.

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

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Department as of December 31, 2007, and 2006, and the changes in its equity 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 8, the Department adopted the provision of Governmental Accounting Standards Board Opinion 45 - Accounting and Financial Reporting by Employers for Post-Employment Benefits other than Pensions, effective January 1 2007.

Energy and Technology Committee
City of Seattle—City Light Department

The management's discussion and analysis on pages 3 through 17 is not a required part of the basic financial statements, but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Virchow, Krause & Company, LLP

Madison, Wisconsin
May 6, 2008

CITY OF SEATTLE—CITY LIGHT DEPARTMENT

MANAGEMENT'S DISCUSSION AND ANALYSIS DECEMBER 31, 2007 AND 2006

The following discussion and analysis of the financial performance of the City of Seattle—City Light Department (the “Department”) provides a summary of the financial activities for the years ended December 31, 2007 and 2006. This discussion and analysis should be read in combination with the Department’s financial statements, which immediately follow this section.

ORGANIZATION

The Department is the public electric utility of the City of Seattle (the “City”). As an enterprise fund of the City, the Department owns and operates certain generating, transmission, and distribution facilities and supplies electricity to approximately 385,000 customers. The Department also supplies electrical energy to other City agencies at rates prescribed by City ordinances.

OVERVIEW OF THE FINANCIAL STATEMENTS

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

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

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

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

CONDENSED BALANCE SHEETS

	December 31		
	2007	2006	2005
Assets:			
Utility plant—net	\$1,591,294,242	\$1,516,974,608	\$1,458,734,681
Capitalized purchased power commitment	4,749,025	15,401,778	25,891,406
Restricted assets	31,109,383	31,502,946	35,815,079
Current assets	247,762,839	304,195,545	296,900,130
Other assets	<u>295,096,371</u>	<u>263,441,612</u>	<u>239,406,075</u>
Total assets	<u>\$2,170,011,860</u>	<u>\$2,131,516,489</u>	<u>\$2,056,747,371</u>
Liabilities:			
Long-term debt	\$1,263,273,902	\$1,332,589,712	\$1,401,815,402
Noncurrent liabilities	25,258,885	26,465,776	39,184,724
Current liabilities	185,237,520	185,799,064	193,070,831
Deferred credits	<u>35,170,995</u>	<u>39,101,262</u>	<u>36,878,664</u>
Total liabilities	1,508,941,302	1,583,955,814	1,670,949,621
Equity:			
Invested in capital assets—net of related debt	450,344,232	287,596,746	145,488,991
Restricted:	28,091,252	28,014,139	32,287,208
Unrestricted	<u>182,635,074</u>	<u>231,949,790</u>	<u>208,021,551</u>
Total equity	<u>661,070,558</u>	<u>547,560,675</u>	<u>385,797,750</u>
Total liabilities and equity	<u>\$2,170,011,860</u>	<u>\$2,131,516,489</u>	<u>\$2,056,747,371</u>

ASSETS

Utility Plant - Net

2007 Compared to 2006

Utility Plant Assets net of accumulated depreciation increased \$74.3 million to \$1,591.3 million for 2007. The increase consisted of the following:

- Additions and replacements in 2007 to *Utility plant-in-service net of retirements and adjustments* totaled \$121.6 million including:
 - a \$10.9 million increase in *Hydroelectric production plant* including \$5.2 million for the Ross Unit 43 generator and air circuit breaker; \$1.5 million for the elevator, security system and governor control upgrade and installation of fall protection at Boundary Powerhouse; \$0.9 million for the installation of irrigation system and backflow device at Newhalem; \$0.8 million for replacement of generator Unit 24 transformer at Gorge Powerhouse; and \$0.4 million for the improvement of Vista House road at Boundary; \$0.3 million for the

- improvement of access road at Ross; \$0.3 million for the purchases of equipment; \$0.6 million for other Hydroelectric plant assets;
- a \$5.6 million increase in *Transmission plant* including \$2.6 million for replacement of breakers and other station equipment; \$0.8 million for replacement of relays at University-Broad and Canal-Broad transmission lines; \$1.2 million in transmission towers; and \$0.2 million for transmission lines; \$0.5 million for construction of road for the Bothell-Maple Valley transmission lines; \$0.3 million for other Transmission plant assets;
 - a \$92.0 million increase in *Distribution plant* including \$1.6 million in substation equipment; \$10.7 million for poles; \$7.3 million for overhead conductors for capacity additions and relocations; \$17.9 million for underground conduit including \$4.8 million for Shoreline undergrounding and \$2.4 million for Laurelhurst 26-kV conversion; \$10.2 million for network underground conduit including \$4.4 million for South Lake Union Streetcar project; \$7.7 million for underground conductors; \$10.4 million for network underground conductors; \$4.8 million for meters including automated meter readers; \$8.3 million for transformers; \$8.7 million for overhead, underground, and network services; and \$3.1 million for streetlights including \$1.1 million for the streetlights at the Westlake area;
 - a \$13.2 million increase in *General plant* assets including \$7.6 million for purchases of vehicles and equipment; \$1.6 million for system developments and purchases of computer equipment; \$2.8 million for communication equipment; \$1.2 million for structure improvement including construction of the visitor center in Seattle Municipal Tower;

These additions to utility plant-in-service were offset by a corresponding increase in *Accumulated depreciation* of \$65.1 million which along with an increase in *Construction work-in-progress* of \$17.8 million contributed \$74.3 million to the net increase in Utility Plant-in-service.

- In addition, *Nonoperating property net of accumulated depreciation* decreased by a small amount, \$20 thousand due to a decrease of \$0.5 million in Utility Plant for Future Use for reclassification of a Network vault to Utility Plant-in-service and offsetting increases of \$0.3 million in the 1% for Art inventory and \$0.1 million for land purchase for future use for the remediation of the contaminated sediments in the lower Duwamish Waterway.
- *Land and land rights* increased \$1.2 million due to the land purchases at Skagit, amounting to \$0.9 million, for the wildlife habitat development projects and a \$0.3 million increase in Land Easements for Distribution plant assets.

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

2006 Compared to 2005

Utility Plant Assets net of accumulated depreciation increased \$58.2 million to \$1,517.0 million for 2006. The increase consisted of the following:

- Additions and replacements in 2006 to *Utility plant-in-service net of retirements and adjustments* totaled \$128.8 million including:
 - a \$16.4 million increase in *Hydroelectric production plant* including \$2.1 million for the North Cascades Environmental Learning Center; \$8.6 million for turbine overhaul,

- transformer bank replacement and electrical system upgrade at Gorge; \$3.6 million for the governor control, intake gate rock guard and network control system upgrade at Boundary; \$1.2 million for electrical system upgrade and generator air circuit breaker at Ross; and \$0.8 million for the spill gate control system installation at Diablo;
- a \$9.1 million increase in *Transmission plant* including \$4.0 million for station equipment replacement; \$3.4 million in transmission towers; and \$1.7 million for transmission lines;
 - a \$92.5 million increase in *Distribution plant* including \$4.7 million in substation structure and equipment; \$8.8 million for poles; \$6.3 million for overhead conductors for capacity additions and relocations; \$7.2 million for underground conduit; \$2.9 million for network underground conduit; \$12.6 million for underground conductors; \$9.9 million for network underground conductors and \$2.9 million for meters; \$7.7 million for transformers; and \$9.7 million due to overhead services, underground services, network underground services; \$1.2 million for streetlights; and a reclassification from Utility plant held for future use to Utility plant-in-service of \$18.8 million for the ductbanks and vaults installed for the undergrounding distribution system along Martin Luther King Way South related to the Sound Transit light rail project;
 - a \$10.8 million increase in *General plant* assets as a result of the addition of \$3.3 million for the customer billing system enhancement; other system developments and purchases of computer equipment amounting to \$3.4 million; \$1.4 million for communication equipment; \$2.0 million for transportation equipment including passenger cars; and \$0.7 million for other general plant assets;

These additions to utility plant-in-service were offset by a corresponding increase in *Accumulated depreciation* of \$62.4 million which along with an increase in *Construction work-in-progress* of \$9.5 million contributed \$75.8 million to the net increase in Utility plant-in-service.

- In addition, *Nonoperating property net of accumulated depreciation* decreased \$16.2 million due to the reclassification to utility plant-in-service of \$18.8 million for the ductbanks and vaults installed for the underground distribution system along Martin Luther King Way South related to the Sound Transit light rail project and a downward adjustment of \$0.3 million for the 1% for Art inventory. These decreases were offset by the \$2.5 million reclassification of the Interbay substation as Electrical Plant Held for Future Use; and
- *Land and land rights* decreased \$1.4 million due primarily to the reclassification of \$1.8 million for the Interbay substation land to Nonoperating property. This decrease is offset by a \$0.4 million net increase from the sale and acquisition of land for Hydraulic and Distribution plant sites.

Restricted Assets

2007 Compared to 2006

Restricted assets decreased by \$.4 million to \$31.1 million in 2007. Retainage deposits decreased in total by \$1.3 million for contractor completed projects during the year. These deposits were offset by an increase in customer advance payments received for customer electrical construction projects that will be scheduled for completion in the amount of \$.8 million. Other decreases in the amount of \$.1 million during the normal course of operations accounted for the balance.

The significant component of restricted assets remained the \$25.0 million Contingency Reserve Account established in 2005. The Contingency Reserve Account is restricted for extraordinary costs associated with the operation of the electric system. Other items within restricted assets were \$3.0 million for the debt service account, \$2.1 million for customer prepayments, and \$1.0 million for vendor retainage, escrow deposits, and other.

2006 Compared to 2005

Restricted assets decreased by \$4.3 million to \$31.5 million in 2006. The decrease was due primarily to the elimination of the \$3.8 million in restricted cash balance at the end of 2005 that was available to pay streetlight refund claims. All remaining claims were paid in 2006 and the \$3.5 million residual balance was transferred to operating cash. The Contingency Reserve Account in the amount of \$25.0 million established in 2005 accounts for the majority of restricted assets. In May 2005, the Seattle City Council passed Ordinance No. 121812 which authorized the purchase of a surety bond to meet the total reserve account requirements for the Department's first-lien bonds and eliminated the need for the previously held bond reserve account. Other items within restricted assets were \$2.9 million for the debt service account, and \$3.6 million for vendor retainage, escrow deposits, and other.

Current Assets

2007 Compared to 2006

Current assets decreased by \$56.4 million to \$247.8 million in 2007. *Operating cash* decreased \$39.4 million to \$87.7 million. One of the main reasons for the lower cash balance was the effect of the average system rate decrease of 8.4% implemented at the beginning of 2007. Other causes for the lower cash balance were due to higher operating costs, ongoing construction activity related to the Sound Transit light rail project, and increased construction for underground infrastructure projects in Shoreline, Aurora, and Burien; suburban areas or jurisdictions within the Department's service area.

Total *Accounts receivable* decreased \$9.0 million to \$71.7 million in 2007. Receivables for *electric sales* at \$41.2 million net of the allowance decreased slightly by \$.2 million from 2006. During 2007, \$14.6 million of electric accounts in arrears were written-off in the electric billing system. A corresponding adjustment was made to the allowance for electric accounts. Also in 2007, the \$7.7 million accrual for the Nucor billing for an Extraordinary Power Cost Adjustment (EPCA) allowed for in the most recent replacement interruptibility contracts was settled for nearly \$2.0 million. The unpaid balance of \$5.8 million for the Nucor receivable was written-off and the related allowance was adjusted accordingly. Accounts receivable for *wholesale power sales* net of allowance decreased \$2.6 million because of somewhat lower sales for December 2007 compared to December 2006. *Grants receivables* for capital grants decreased \$5.4 million as funds were received principally for the Sound Transit light rail project. However, \$3.3 million of grants receivable recorded at the end of 2006 was reversed in 2007 as a result of discussions initiated in 2007 and pending agreement between Sound Transit and the Department

regarding responsibility for cost overruns. *Other sundry receivables* decreased \$.8 million net from 2006 during the normal course of operations. More information on the Department's various accounts receivable balances can be found in Note 4 of the accompanying financial statements.

Other current assets decreased \$8.0 million in 2007 from 2006. *Unbilled revenues* decreased \$5.0 million due to the lower system rate decrease effective for 2007 and *Energy contracts* or short-term forward power contracts valued at fair market decreased \$5.8 million due to a combination of less forward power contracts outstanding and smaller variance between power contractual prices and forward market prices at the end of 2007 compared to 2006. Inventory for *Materials and supplies* increased \$2.8 million from 2006.

2006 Compared to 2005

Current assets increased \$7.3 million to \$304.2 million in 2006. *Operating cash* decreased \$14.7 million to \$127.1 million due primarily to increased construction activity related to the Sound Transit light rail, Shoreline infrastructure, and other distribution projects.

Total *Accounts receivable* increased \$10.8 million to \$80.7 million in 2006. Receivables for *electric sales* increased only \$0.6 million net of the allowance. Included in these receivables was \$7.7 million billed to Nucor for an Extraordinary Power Cost Adjustment which was offset by an increase of \$6.7 million in the allowance because of uncertainty surrounding the collectibility of this billing. Active accounts receivables in arrears over 90 days continued to decline with the continued focus on collection efforts in this area. Accounts receivable for *wholesale power sales* increased a net \$2.4 million on account of higher sales for December 2006 compared to December 2005, and recovery of monies from bankruptcy distributions during the year, which reduced the allowance for wholesale power sales by \$1.2 million. Related to power sales, valuation of the receivable for *exchanged energy* increased \$1.9 million as a result of valuing this transaction at market in compliance with a new accounting standard. *Interfund receivables* decreased \$1.7 million. *Due from other governments* increased \$6.2 million primarily for grants from Sound Transit as construction continued. *Standard connection* receivables were higher by \$2.5 million. *Miscellaneous sundry receivables* decreased by \$1.1 million from 2005 during the normal course of operations.

Other current assets increased \$11.2 million in 2006 from 2005. Increases included \$3.8 million for unbilled revenues due to the colder weather in December 2006; \$4.8 million for short-term forward power contracts valued at market with a favorable position at year end; and \$2.5 million for higher inventory.

Other Assets

2007 Compared to 2006

Statement of Financial Accounting Standards No. 71, *Accounting for the Effects of Certain Types of Regulation*, provides for the deferral of certain utility costs and related recognition in future years as the costs are recovered through future rates. Deferred costs are authorized by resolutions passed by the Seattle City Council and include capitalized energy management services, deferred power costs, deferral of payments to the Province of British Columbia under the High Ross Agreement, and other deferred charges.

Deferred assets increased \$31.6 million to \$295.1 million in 2007. The increase includes the following:

- \$3.5 million in *deferred conservation costs, net*. Conservation measures, funded in part by the BPA in exchange for decrements to Block power, are currently deferred and amortized over a 20-year period.

- \$12.1 million in *capitalized relicensing costs* incurred primarily in preparation for the application to FERC to relicense the Boundary hydro generation facility; the Department intends to submit an application for a new license by October 2009.
- \$8.9 million *annual deferral of payment due* to B. C. Hydro for the High Ross Agreement.
- \$17.8 million increase in long-term receivables for infrastructure improvements in the Department service areas of Shoreline, Aurora, and Burien. These improvements were recorded as contributions in aid of construction and will be repaid by the respective electric customers within these jurisdictions through electric rates over 25 years commencing in January 2008 for the Shoreline improvements. Billings will be made to Aurora beginning in June 2008 and Burien billings are anticipated in the latter part of 2008.
- \$10.9 million net decrease for *Bonneville Slice contract true-up payment*. The Department is subject to true-up payments for the Department's fixed 4.6676% of actual output and costs of Bonneville Slice power through September 30, 2011. In December 2006, Bonneville billed the Department \$10.9 million, which was recorded as an accounts payable and deferred asset in December 2006 to be paid and expensed in 2007. In December 2007, Bonneville issued a credit within the Bonneville monthly billing to the Department in the amount of \$1.6 million for the 2007 true-up cost adjustment with payment of the Bonneville bill due in January 2008. The true-up credit was recorded as a deferred credit in December 2007 and will be realized in 2008.
- \$.3 million net decrease in other deferred charges in the normal course of operations.

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

2006 Compared to 2005

Deferred assets increased \$24.0 million to \$263.4 million in 2006. The increase includes the following:

- \$7.4 million in *deferred conservation costs, net*.
- \$4.7 million in *capitalized relicensing costs* incurred primarily in preparation for the application to FERC to relicense the Boundary hydro generation facility.
- \$8.9 million *annual deferral of payment due* to B. C. Hydro for the High Ross Agreement.
- \$3.5 million increase in long-term receivables, principally for the receivable from the City of Shoreline for infrastructure improvements, recorded as contributions in aid of construction for 2006, that will be repaid by Shoreline electric customers through rates over 25 years commencing in January 2008.
- \$1.8 million net increase for *Bonneville Slice contract true-up payment*. The Department is subject to true-up payments for the Department's fixed 4.6676% of actual output and costs of Bonneville Slice power through September 30, 2011. In December 2005, Bonneville billed the Department \$9.1 million for the 2005 true-up cost adjustment with payment due in January 2006. In December 2006, Bonneville billed the Department \$10.9 million, which was recorded as an accounts payable and deferred asset in December 2006 to be paid and expensed in 2007.

- \$1.3 million decrease due to *unrealized losses* from fair market valuations of short-term forward power contracts being incurred at the end of 2005 which did not recur at the end of 2006. The Department had a net overall favorable position of \$6.5 million for short-term forward contracts at the end of 2006, recorded in deferred credits.

LIABILITIES

Long-Term Debt

2007 Compared to 2006

Long-term debt decreased by \$69.3 million to \$1,263.3 million during 2007. No additional revenue bonds were issued in 2007. The Department continued making progress on debt reduction with a goal of a debt to capitalization ratio of 60.0% by 2010. The debt to capitalization ratio at the end of 2007 was 67.0%, a reduction from the 2006 ratio of 72.0%. The long-term note payable to Sound Transit for the new light rail line in progress was paid in full during 2007. Installment payments for the note payable with the State of Washington, negotiated in 2006 for the purchase of Microsoft Office 2003, were made on schedule. The principal amount paid during 2007 was \$270.2 thousand leaving a balance of \$284.9 thousand at the end of 2007. Net revenues available to pay debt service were equal to 1.88 times principal and interest on all bonds for 2007.

During 2007, Moody's Investors Service affirmed the credit rating of Aa3 for the Department's revenue bonds. Moody's also changed the outlook from stable to positive noting the improved financial trend and stronger focus on resource planning. Standard and Poor's credit rating was also affirmed at A+.

Note 6 of the accompanying financial statements provides additional information related to the Department's long-term debt.

2006 Compared to 2005

Long-term debt decreased by \$69.2 million to \$1,332.6 million during 2006. There were no new revenue bonds issued during 2006 as the focus continued to be on debt reduction with a goal of a debt to capitalization ratio of 60.0% by 2010. The debt to capitalization ratio at the end of 2006 was 72.0%. The long-term note payable to Sound Transit for the new light rail line in progress was repaid ahead of schedule during the year leaving a balance of \$4.0 million at the end of 2006. A new note payable was negotiated with the State of Washington during 2006 for the purchase of Microsoft Office 2003, which was installed on the local area network. The balance of this note at the end of the year was \$0.6 million. After payment of cash operating expenses, net revenues available to pay debt service were equal to 2.37 times principal and interest on all bonds.

Environmental Liabilities

Environmental liabilities totaled \$17.6 million, \$10.8 million and \$9.1 million at December 31, 2007, 2006 and 2005, respectively. The liabilities are primarily attributable to the estimated cost of remediating contaminated sediments in the lower Duwamish Waterway, which was designated a federal Superfund site by the Environmental Protection Agency in 2001. The Department is considered a potentially responsible party for contamination in the Duwamish River due to land ownership or use of property located along the river.

RESULTS OF OPERATIONS

While the balance sheets show changes in assets, liabilities, and fund equity, the statements of revenues, expenses, and changes in fund equity provide insight into the source of these changes.

Condensed Revenues and Expenses

	Year Ended December 31		
	2007	2006	2005
Operating revenues	\$ 832,524,784	\$ 831,810,233	\$ 748,552,561
Nonoperating revenues	<u>10,747,418</u>	<u>11,947,367</u>	<u>5,417,494</u>
Total revenues	843,272,202	843,757,600	753,970,055
Operating expenses	702,176,110	642,041,903	624,592,061
Nonoperating expenses	<u>73,698,789</u>	<u>71,780,961</u>	<u>73,646,463</u>
Total expenses	775,874,899	713,822,864	698,238,524
Capital contributions	37,736,620	21,538,722	18,944,222
Grants	<u>8,375,960</u>	<u>10,289,467</u>	<u>7,234,823</u>
Net income	<u>\$ 113,509,883</u>	<u>\$ 161,762,925</u>	<u>\$ 81,910,576</u>

SUMMARY

2007 Compared to 2006

Net income for 2007 at \$113.5 million was another robust year, even though it was a decrease of \$48.3 million or 33%, from last year's record net income. \$40.7 million of the decrease was due in large part to the overall 2007 system rate decrease implemented in January 2007. Within operating expenses, administrative and general costs were higher by \$17.7 million due in part to higher costs in the areas of pensions, benefits, rents, and environmental pertaining to clean-up of the Duwamish superfund sites. Other power costs increased by nearly \$1.0 million. Offsetting the lower revenues and higher operating expenses was an increase in *Other deductions, net* by \$11.1 million from 2006, attributable mainly to higher capital fees recorded for underground infrastructure improvements to suburban areas within the Department's service area.

2006 Compared to 2005

Net income for 2006 was a record \$161.8 million, an increase of \$79.9 million for the year, and nearly twice the \$81.9 million net income earned in 2005. As a result of improved precipitation in the Northwest region, net revenue from short-term wholesale power sales was \$128.9 million compared to \$87.4 million in 2005, an increase of \$41.5 million. Operating revenues, outside of short-term wholesale power sales, increased \$56.7 million. The increase in operating revenues was offset by a \$32.3 million increase in operating expenses other than the cost of wholesale purchases. Also contributing to the higher net income in 2006 were higher non-operating revenues of \$6.6 million, higher capital contributions and fees of \$5.6 million, and slightly lower non-operating expenses of \$1.8 million over 2005.

REVENUES

2007 Compared to 2006

Retail—Revenues from sales of energy to retail customers decreased significantly by \$40.7 million to \$542.4 million in 2007. An average system rate decrease of 8.4% was in effect at the beginning of the year and hence, accounting for the decrease from 2006 revenues. Even with the lower rates, *residential retail* revenues only decreased by \$1.58 million or .8% from 2006 in part due to billed consumption to *residential retail* customers being higher by 2.4%. *Nonresidential revenues* experienced the largest decrease in retail revenues declining \$30.4 million or 8.0%, with megawatt hours billed increasing slightly by 1.9%. Also contributing to the lower *nonresidential revenues* was the fact that there was no Nucor ECPA adjustment in 2007 compared to the adjustment of \$7.7 million for 2006. The net *unbilled revenue* adjustment for 2007 was an unfavorable variance of \$8.7 million from 2006, also attributable essentially to the lower rates in effect.

Wholesale—*Sales* of surplus power in the wholesale market yielded \$161.1 million in revenue in 2007, a decrease of \$15.1 million from 2006. There was less overall power generation from the Department's facilities, especially at the Boundary plant that experienced lower stream flows than normal because of lower precipitation in the eastern Washington region. Sales of energy were lower by 16.6 % to 3,822,098 MWh for 2007 compared to 4,580,325 MWh in 2006. The lower sales of energy were offset in part by a 6.0 % increase in average year-to-date power sales price of \$47.72 per MWh in 2007 compared to \$45.03 per MWh in 2006.

Purchases of wholesale energy decreased by \$13.9 million in 2007. Energy purchased in 2007 was 947,937 MWh, a decrease of 386,042 MWh or 28.9% from 2006. Average year-to-date power purchase prices decreased to \$47.56 per MWh in 2007 from \$49.54 per MWh in 2006.

Energy sales were 4.03 times the amount of energy purchased during 2007. The higher ratio of sales to purchases along with higher average power prices during 2007 resulted in net revenues totaling \$127.7 million for 2007, an incremental decrease of \$1.2 million or .9% from net revenues of \$128.9 million in 2006. Net revenues include the effect of recording long-term purchased power bookouts (net financial settlement for power without physical delivery) that are a result of executing short-term wholesale power transactions. These bookouts totaled \$9.6 million for 2007 and \$11.3 million for 2006. The bookouts had the effect of lowering net revenues from wholesale energy sales for both years. Similarly, long-term power purchases also declined by equal amounts with no net effect to net income. This change was first implemented in 2006.

Other Power-Related—This category of revenue consists of other power-related transactions and products sold by the Department such as revenue from Bonneville conservation programs, sales of reserve capacity, wheeling, power exchanges, and other. Revenue in this category increased \$56.6 million to \$109.3 million in 2007. Effective in 2006, *power exchanges* derived from certain power contracts were valued at fair market in accordance with a new accounting standard. During 2007, valuations for power exchanges increased considerably as the Department expanded into additional ancillary services that included power exchange components. Additional power contracts with power exchange valuations at fair market totaled \$22.0 million. Of this amount, \$20.5 million had a corresponding purchased power exchange with no effect on net income. Wholesale power basis revenues (simultaneous sale/purchase of energy at one location and corresponding energy sale/purchase at another location) increased \$26.6 million from 2006, as more of these transactions were executed, with valuation at full contractual prices, compared to 2006. As a side note, net revenues from basis transactions increased only \$1.6 million from 2006. The balance of the \$8.0 million net increase in *other power-related revenues* was due primarily to

receiving contractual payments from the sale of energy generated at the Lucky Peak Project that also constituted a power exchange element.

Other—Revenues from a variety of other sources remained unchanged from 2006 at \$19.7 million. In 2007, there was an increase of \$3.2 million in non-utility operations for reimbursement of environmental mitigation costs from the City of Seattle in accordance with a court order judgment and \$1.2 million for insurance recoveries from previous claims. In 2006, \$3.5 million was realized for the balance of residual cash for unclaimed streetlight refunds by customers, as allowed by the streetlight court settlement and with no activity in this area in 2007. The remaining activity included increases and decreases during the normal course of operations.

2006 Compared to 2005

Retail—Revenues from sales of energy to retail customers increased by \$20.6 million to \$583.1 million in 2006. There were no rate adjustments during 2006 and accordingly, the downward Bonneville pass-through rate adjustment of November 2005 was still in effect. Energy consumption billed to *residential retail* customers was higher by 2.7% which accounted in part for the increase in revenues of \$2.6 million compared to 2005. *Nonresidential revenues* increased by \$13.1 million or 3.6%. Nonresidential consumption was up 2.8% over 2005. At the end of 2006, Nucor was billed \$7.7 million for the EPAC computed in accordance with the recent interruptible power contracts that expired on January 1, 2007, with the implementation of new system rates for the Department. The net *unbilled revenue* adjustment of \$3.8 million for 2006 resulted in a favorable swing of \$4.8 million between years on account of colder weather during the latter part of 2006.

Wholesale—*Sales* of surplus power in the wholesale market generated \$176.2 million in revenue in 2006, an increase of nearly \$27.0 million from 2005. Improved water conditions during 2006 contributed positively to the sales of surplus energy sold on the wholesale market. Sales of energy increased by 60.9% to 4,580,352 MWh for 2006 compared to 2,846,599 MWh in 2005. The higher sales of energy were offset in part by a 16.5% decrease in average year-to-date power sales price of \$45.03 per MWh in 2006 compared to \$53.93 per MWh in 2005.

Purchases of wholesale energy decreased by \$14.9 million in 2006 as a result of more power generated from improved precipitation in the region used for managing system load and meeting contractual obligations. Energy purchased in 2006 was 1,333,979 MWh, an increase of 300 MWh or 29.0% from 2005. Average year-to-date power purchase prices decreased to \$49.54 per MWh in 2006 from \$63.89 per MWh in 2005.

The net effect of higher energy sales at 3.43 times the amount of energy purchased combined with the impact of lower average power prices produced net revenues totaling \$128.9 million for 2006, an increase of \$41.5 million or 47.4% from net revenues of \$87.4 million in 2005. In addition, recording of long-term purchased power bookouts (net financial settlement for power without physical delivery) in the amount of \$11.3 million attributable to short-term wholesale power sales had the effect of lowering net revenues from wholesale energy sales for 2006. Conversely, long-term power purchases also declined by the same amount and consequently, there was no net effect to net income. This change was implemented in 2006 because of improved availability of power transaction data and to comply with accounting standards.

Other Power-Related—Revenue in this category increased \$29.4 million to \$52.7 million in 2006. Effective in 2006, *power exchanges* from certain power transactions were valued at fair market in accordance with a new accounting standard. These power exchanges totaled \$22.0 million. Of this amount, \$20.5 million had a corresponding purchased power exchange with no effect on net income. The balance of the \$7.4 million net increase in *other power-related revenues* was due primarily to receiving a

full year of power revenues from a contract with Grant County Public Utility District executed in November 2005, increasing revenues by \$7.1 million.

Other—Revenues from a variety of other sources increased \$6.7 million to \$19.7 million in 2006 from \$13.0 million in 2005. \$3.2 million of the increase was for the balance of residual cash for unclaimed streetlight refunds by customers, as allowed by the streetlight court settlement. In 2004, a Washington State Supreme Court decision required the City of Seattle reimburse the Department for \$23.9 million in streetlight costs that would have been billed to the City from December 29, 1999 to November 13, 2003. The Department was required to refund to its customers in the City the amount collected for streetlight costs over that period and to refund to its customers in the city of Tukwila the amount collected from December 24, 1999 through April 30, 2003. The balance in increased revenues in the amount of \$3.5 million was from other operations including \$2.6 million for salvage sales of surplus wire.

EXPENSES

2007 Compared to 2006

Total operating expenses were \$702.1 million, an increase of \$60.1 million from \$642.0 million in 2006.

Power related expenses totaled \$400.6 million, a \$45.9 million increase from 2006. *Bonneville power expenses* were higher by \$21.1 million. Bonneville power contractual costs increased \$13.6 million primarily for the block or fixed portion of the contract as a result of contractual changes that significantly increased power purchases for the Department over the remaining life of the contract effective in October 2006. Annual true-up for the slice or variable portion of the contract was a net increase of \$7.5 million from 2006. The annual true-up for 2006 expensed in 2007 resulted in a net increase of \$2.0 million for 2007. In addition, the Department benefited in 2006 from a one-time settlement with Bonneville in favor of the slice participants for the first five years of slice true-ups in the amount of \$5.4 million.

Power related wholesale purchases increased a total of \$45.3 million from 2006, of which \$20.5 million was for recording additional power exchanges at fair value corresponding to the related power exchange revenues noted above with no effect to net income. The balance of the increase of \$24.8 million from 2006 related in part to wholesale power basis transactions valued at contractual prices, also previously mentioned for associated basis revenues. In addition, fair market valuations were assigned to bookouts for basis transactions beginning in 2007 as system enhancements were developed that produced improved data.

Long-term purchased power – other and *short-term power expenses* decreased a combined \$25.1 million from 2006. Decreased purchases of short-term wholesale energy accounted for nearly \$14.0 million, as discussed above under *Wholesale* revenues. *Long-term purchased power – other* declined \$11.1 million from 2006, primarily due to the purchase power contract with the City of Klamath Falls that expired at the end of July 2006.

The balance net increase of \$4.6 million in *power related expenses* was basically the effect of higher fair market valuations of NCPA exchanged power delivered during 2007 (\$2.8 million) and a lower valuation of long-term purchased power bookouts resulting from short-term wholesale transactions (\$1.7 million).

Non-power operating expenses increased \$15.8 million to \$165.3 million in 2007 from \$149.5 million in 2006. Distribution expenses increased \$3.5 million due in part to higher labor expenses incurred for a variety of projects, including work related to the December 2006 Storm. Administrative and general costs incurred grew by \$17.7 million totaling \$66.7 million in 2007 due in large part to higher costs for administrative systems enhancements, pensions, benefits, rents, and environmental clean-up of various

Duwamish superfund sites. Offsetting the increases were *Customer Service* expenses declining by \$6.8 million from 2006; the majority due to the one-time Nucor EPAC bad debt expense of \$6.7 million incurred in 2006. Finally, higher amortization of deferred conservation costs in the amount of \$1.4 million made up the balance of the increase for this category of expenses.

Taxes decreased \$4.4 million from 2006 on account of the lower revenue base. *Depreciation expense* increased \$2.8 million in 2007, generally the result of new plant additions.

2006 Compared to 2005

Total operating expenses were \$642.0 million, an increase of \$17.4 million from \$624.6 million in 2005.

Power related expenses totaled \$354.7 million, a \$2.1 million increase from 2005. Bonneville power expenses were higher by \$23.2 million. Bonneville power contractual costs increased \$21.8 million primarily for the block or fixed portion of the contract as a result of contractual changes that significantly increased power purchases for the Department over the remaining life of the contract effective in October 2006. Annual true-up for the slice or variable portion of the contract was a net increase of \$1.4 million from 2005. The Department benefited from settlement with Bonneville in favor of the slice participants for the first five years of slice true-ups in the amount of \$5.4 million.

Power related wholesale purchases increased a total of \$22.3 million from 2005, of which \$20.5 million was for recording certain power exchanges at fair value corresponding to the related power exchange revenues noted above with no effect to net income.

Long-term purchased power –other and short-term power expenses decreased a combined \$53.0 million from 2005. Decreased purchases of short term wholesale energy accounted for \$14.9 million, as discussed above under Wholesale revenues. Long-term purchased power – other declined \$38.1 million from 2005. The purchase power contract with the City of Klamath Falls expired at the end of July 2006 accounting for \$31.8 million. In addition, \$11.3 million of lower long term purchased power costs pertain to recording bookouts assigned to short-term sales of surplus energy effective for 2006 as noted in Wholesale revenues above. The balance net increase of \$5.0 million is the result of higher costs incurred for several other long term purchase power contracts.

Non-power operating expenses increased \$12.7 million to \$149.5 million in 2006 from \$136.8 million in 2005. Distribution expenses included higher storm costs, specifically \$3.2 million for the December 14 Storm. Incorporated within customer service expenses was a \$6.7 million increase in bad debt expense tied directly to the revenue recorded for the Nucor EPAC due to uncertainty surrounding collectibility of the EPAC. Risk management liabilities were higher by \$1.0 million during 2006 due in part to higher judgment claims and ongoing remediation costs incurred for the Duwamish superfund site. Employee benefit expenses also increased by \$1.8 million from 2005 mainly due to higher health care costs.

OTHER NONOPERATING INCOME AND EXPENSE

2007 Compared to 2006

Nonoperating Revenues (Expenses)—Nonoperating (expenses) increased \$11.1 million to \$16.9 million in 2007 from \$28.0 million in 2006 due to the following:

Nonoperating income decreased \$6.4 million to \$5.6 million from 2006. *Investment income* increased incrementally \$.2 million to \$10.2 million from 2006. Other deductions were \$4.6 million in 2007, a \$6.6 million unfavorable variance from 2006. A significant portion of the variance is due to reversal of costs

that had been recorded as grant revenues in 2006. \$3.3 million of grants from Sound Transit was recorded as other deductions in 2007 because of pending discussion and agreement between Sound Transit and the Department regarding responsibility for cost overruns. Additionally, \$1.2 million of costs from the Spokane Bridge expansion project in Seattle were determined to be unrecoverable. The balance of \$2.1 million was mostly the result of minimal property sales in 2007 compared to 2006.

Nonoperating expense decreased \$3.2 million from \$71.8 million in 2006 to \$68.6 million in 2007. The decrease is due primarily due to lower interest expense on outstanding bonds as bonds continued to be repaid and with no additional bonds issued in 2007. Interest expense for parity bonds decreased \$2.8 million while interest expense for variable rate bonds remained virtually unchanged at \$2.9 million.

Fees and Grants—Fees and grants increased by \$14.3 million in 2007. The largest increase of \$12.4 million was the result of completed underground infrastructure improvements for the areas of Aurora and Burien; suburban areas or jurisdictions within the Department’s service territory. In 2006, infrastructure improvements were \$3.7 million for Shoreline. The respective customers from these jurisdictions will pay for these improvements over a 25 year period through their electric billings commencing January 2008 for Shoreline, and later in 2008 for the other areas. In-kind contributions were also higher in 2007 by \$5.3 million, of which \$2.4 million was for contributions relating to a new streetcar trolley serving Seattle’s north downtown area, and the balance was for on-going customer requested improvements. The balance of the increase of \$3.4 million for *fees and grants* were for other projects that had increases and decreases in the normal course of operations, and included \$6.0 million of federal and state grants recognized for the December 2006 storm.

2006 Compared to 2005

Nonoperating Revenues (Expenses)—Nonoperating revenues (expenses) increased \$8.4 million in 2006 as a result of the following:

Nonoperating income increased \$6.6 million to \$12.0 million in 2006. *Investment income* was higher by \$4.3 million compared to 2005 because of higher average operating cash balances during the year and because the City’s cash pool portfolio was turned over to higher yielding investments. The Department’s share of fair market value gains on investments in the City’s cash pool was a positive swing between years of \$2.6 million. Gains from the sale of surplus property and gains from bankruptcy distributions for delivered wholesale power in prior years combined added \$1.8 million more in 2006 than in 2005.

Nonoperating expense decreased \$1.8 million from \$73.6 million in 2005 to \$71.8 million in 2006. The decrease is due primarily due to lower interest expense on outstanding bonds as bonds continued to be repaid and with no new bonds issued during 2006. Interest expense for parity bonds decreased \$2.5 million while interest expense for variable rate bonds increased \$.8 million due to higher short-term interest rates.

Fees and Grants—Fees and grants increased by \$5.6 million in 2006. All *capital contributions* were higher by \$2.6 million for various new and ongoing projects within the Department’s service area. Completed in 2006 were underground improvements to a portion of the Shoreline infrastructure totaling \$3.7 million. Shoreline customers will pay for these improvements over a 25 year period through their electric billings commencing in mid-2007. In-kind contributions decreased \$7.0 million primarily from Sound Transit in connection with the construction of the regional light rail system received in 2005. *Grants* during 2006 were higher by \$3.0 million principally on behalf of Sound Transit construction at Tukwila.

RISK MANAGEMENT

The Department's exposure to market risk is managed by the Power Management Executive under the guidance of a Risk Oversight Council made up of the Chief Financial Officer, Power Supply and Environmental Affairs Officer, Director of Risk Oversight, and Power Management Executive (non-voting member). The Department engages in market transactions to meet its load obligations and to realize earnings from surplus energy resources. Except for limited intraday and interday trading to take advantage of owned hydro storage, the Department does not take market positions in anticipation of generating revenue.

With a significant portion of the Department's revenue expected from wholesale energy market sales, great emphasis is placed on the management of risks associated with this activity. Policies, procedures, and processes designed to manage, control and monitor these risks are in place. A formal front, middle, and back office structure is in place to ensure proper segregation of duties. The Risk Oversight Division performs the middle office functions which include independent reporting of market positions and energy risk management policy compliance.

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

The Department mitigates credit risk by trading only with pre-approved, qualified counterparties. The Risk Oversight Council establishes the methodology for determining the maximum credit limit available to any counterparty. The CFO is responsible for establishing the actual, limit, not to exceed the maximum.

CITY OF SEATTLE—CITY LIGHT DEPARTMENT

BALANCE SHEETS

AS OF DECEMBER 31, 2007 AND 2006

ASSETS	2007	2006
UTILITY PLANT—At original cost:		
Plant-in-service—excluding land	\$ 2,605,862,005	\$ 2,485,488,981
Less accumulated depreciation	<u>(1,174,568,383)</u>	<u>(1,109,485,544)</u>
Total utility plant	1,431,293,622	1,376,003,437
Construction work-in-progress	104,241,116	86,410,907
Nonoperating property—net of accumulated depreciation	4,552,932	4,092,665
Assets held for future use	10,155,422	10,636,532
Land and land rights	<u>41,051,150</u>	<u>39,831,067</u>
Utility plant—net	<u>1,591,294,242</u>	<u>1,516,974,608</u>
CAPITALIZED PURCHASED POWER COMMITMENT	<u>4,749,025</u>	<u>15,401,778</u>
RESTRICTED ASSETS:		
Contingency Reserve Account	25,000,000	25,000,000
Debt Service Account	2,997,408	2,939,423
Special deposits and other	<u>3,111,975</u>	<u>3,563,523</u>
Total restricted assets	<u>31,109,383</u>	<u>31,502,946</u>
CURRENT ASSETS:		
Cash and equity in pooled investments	87,723,933	127,148,120
Accounts receivable, net of allowance of \$6,024,068 and \$23,321,762	71,680,393	80,672,388
Unbilled revenues	59,515,576	64,484,955
Energy contracts	854,726	6,680,264
Materials and supplies at average cost	26,935,722	24,156,843
Prepayments, interest receivable, and other	<u>1,052,489</u>	<u>1,052,975</u>
Total current assets	<u>247,762,839</u>	<u>304,195,545</u>
OTHER ASSETS:		
Deferred conservation costs—net	141,583,364	138,077,119
Capitalized relicensing costs—net	40,916,887	28,852,177
Deferred costs—High Ross Agreement—net	75,815,265	66,941,824
Other deferred charges and assets—net	<u>36,780,855</u>	<u>29,570,492</u>
Total other assets	<u>295,096,371</u>	<u>263,441,612</u>
TOTAL	<u>\$ 2,170,011,860</u>	<u>\$ 2,131,516,489</u>

See notes to financial statements.

	2007	2006
LIABILITIES		
LONG-TERM DEBT:		
Revenue bonds	\$ 1,342,460,000	\$ 1,409,215,000
Plus bond premium	29,031,729	32,807,763
Less bond discount	(480,702)	(560,841)
Less deferred charges on advanced refunding	(37,277,125)	(42,402,063)
Less revenue bonds—current portion	(70,460,000)	(66,755,000)
Notes payable	284,853	4,511,597
Less notes payable—current portion	<u>(284,853)</u>	<u>(4,226,744)</u>
Total long-term debt	<u>1,263,273,902</u>	<u>1,332,589,712</u>
NONCURRENT LIABILITIES:		
Accumulated provision for injuries and damages	19,684,951	12,260,522
Compensated absences	11,343,185	10,387,612
Long-term purchased power obligation	4,749,025	15,401,778
Less purchased power obligation—current portion	(11,970,000)	(11,770,000)
Other	<u>1,451,724</u>	<u>185,864</u>
Total noncurrent liabilities	<u>25,258,885</u>	<u>26,465,776</u>
CURRENT LIABILITIES:		
Accounts payable and other	72,887,909	72,463,514
Accrued payroll and related taxes	8,303,782	8,965,594
Compensated absences	1,222,813	1,005,628
Accrued interest	19,444,629	20,421,541
Notes payable—current portion	284,853	4,226,731
Long-term debt—current portion	70,460,000	66,755,000
Purchased power obligation	11,970,000	11,770,000
Energy contracts	<u>663,534</u>	<u>191,056</u>
Total current liabilities	<u>185,237,520</u>	<u>185,799,064</u>
DEFERRED CREDITS	<u>35,170,995</u>	<u>39,101,262</u>
Total liabilities	<u>1,508,941,302</u>	<u>1,583,955,814</u>
COMMITMENTS AND CONTINGENCIES (Note 14)		
EQUITY		
Invested in capital assets, net of related debt	450,344,232	287,596,746
Restricted net assets	28,091,252	28,014,139
Unrestricted—net	<u>182,635,074</u>	<u>231,949,790</u>
Total equity	<u>661,070,558</u>	<u>547,560,675</u>
TOTAL	<u>\$ 2,170,011,860</u>	<u>\$ 2,131,516,489</u>

CITY OF SEATTLE—CITY LIGHT DEPARTMENT

STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN EQUITY FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006

	2007	2006
OPERATING REVENUES:		
Retail power revenues	\$ 542,363,033	\$ 583,114,102
Short-term wholesale power revenues	161,154,295	176,243,887
Other power-related revenues	109,305,208	52,720,212
Other	<u>19,702,248</u>	<u>19,732,032</u>
Total operating revenues	<u>832,524,784</u>	<u>831,810,233</u>
OPERATING EXPENSES:		
Long-term purchased power—Bonneville	175,791,029	154,718,362
Long-term purchased power—other	44,403,554	55,521,124
Short-term wholesale power purchases	33,430,904	47,360,729
Other power expenses	76,982,940	30,710,604
Generation	24,973,789	19,563,515
Transmission	45,137,975	46,825,069
Distribution	53,753,779	50,337,958
Customer service	31,241,759	37,986,487
Conservation	13,557,643	12,216,759
Administrative and general	66,729,457	48,961,846
City of Seattle occupation tax	33,396,036	35,591,206
Other taxes	25,711,410	27,977,012
Depreciation	<u>77,065,835</u>	<u>74,271,232</u>
Total operating expenses	<u>702,176,110</u>	<u>642,041,903</u>
NET OPERATING INCOME	<u>130,348,674</u>	<u>189,768,330</u>
NONOPERATING REVENUES (EXPENSES):		
Investment income	10,217,061	9,994,035
Interest expense	(66,386,174)	(69,444,742)
Amortization of refunding loss	(5,124,938)	(5,441,816)
Amortization of bond premium	3,776,034	3,966,297
Amortization of bond discount and issue costs	(827,253)	(860,699)
Gain on sale of property	530,357	2,126,043
Other income (expense)—net	<u>(5,136,458)</u>	<u>(172,712)</u>
Total nonoperating expenses	<u>(62,951,371)</u>	<u>(59,833,594)</u>
NET INCOME BEFORE FEES AND GRANTS	<u>67,397,303</u>	<u>129,934,736</u>
FEES AND GRANTS:		
Capital contributions	37,736,620	21,538,722
Grants	<u>8,375,960</u>	<u>10,289,467</u>
Total fees and grants	<u>46,112,580</u>	<u>31,828,189</u>
NET INCOME	113,509,883	161,762,925
EQUITY:		
Beginning of year	<u>547,560,675</u>	<u>385,797,750</u>
End of year	<u>\$ 661,070,558</u>	<u>\$ 547,560,675</u>

See notes to financial statements.

CITY OF SEATTLE—CITY LIGHT DEPARTMENT

STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006

	2007	2006
OPERATING ACTIVITIES:		
Cash received from customers and counterparties	\$ 763,542,564	\$ 778,970,245
Cash paid to suppliers, employees, and counterparties	(486,298,742)	(472,629,484)
Taxes paid	(59,143,482)	(62,606,379)
Net cash provided by operating activities	<u>218,100,340</u>	<u>243,734,382</u>
NONCAPITAL FINANCING ACTIVITIES:		
Principal paid on State of Washington note	(269,157)	(276,494)
Interest paid on State of Washington note	(21,014)	(13,677)
Non-capital grants received	3,894,150	1,471,879
Gains from bankruptcy distributions	525,233	681,254
Bonneville receipts for conservation	1,917,215	4,010,862
Payment to vendors on behalf of customers for conservation augmentation	(13,693,237)	(17,647,501)
Net cash used in noncapital financing activities	<u>(7,646,810)</u>	<u>(11,773,677)</u>
CAPITAL AND RELATED FINANCING ACTIVITIES:		
Principal paid on long-term debt	(66,755,000)	(63,435,000)
Interest paid on long-term debt	(69,859,722)	(72,597,427)
Proceeds from Sound Transit note	956,793	956,793
Principal paid on Sound Transit note	(4,294,210)	(6,256,410)
Interest paid on Sound Transit note	(95,835)	(67,317)
Acquisition and construction of capital assets	(137,836,056)	(131,079,148)
Capital contributions	30,988,314	21,137,926
Capital grants received	6,467,849	3,533,213
Proceeds from sale of utility plant	5,124	1,507,840
(Increase) in other deferred assets and charges	(19,142,835)	(14,560,660)
Net cash used in capital and related financing activities	<u>(260,522,371)</u>	<u>(260,860,190)</u>
INVESTING ACTIVITIES:		
Interest received on investments and on cash and equity in pooled investments	<u>10,251,091</u>	<u>9,837,914</u>
Net cash provided by investing activities	<u>10,251,091</u>	<u>9,837,914</u>
NET INCREASE/(DECREASE) IN CASH AND EQUITY IN POOLED INVESTMENTS	(39,817,750)	(19,061,571)
CASH AND EQUITY IN POOLED INVESTMENTS:		
Beginning of year	<u>158,651,066</u>	<u>177,712,637</u>
End of year	<u>\$ 118,833,316</u>	<u>\$ 158,651,066</u>

	2007	2006
RECONCILIATION OF NET OPERATING INCOME TO		
NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Net operating income	\$ 130,348,674	\$ 189,768,330
Adjustments to reconcile operating income to net cash provided by operating activities:		
Non-cash items included in operating income:		
Depreciation	78,519,585	76,229,612
Amortization of deferred credits	(5,687,800)	(5,277,747)
Amortization of other deferred charges	12,288,798	11,850,756
Bad debt expense	4,061,778	11,436,243
Power revenues	(106,476,981)	(61,154,891)
Power expenses	106,364,389	61,236,376
Other	7,491,690	2,806,146
Change in:		
Accounts receivable	5,077,326	(17,852,150)
Unbilled revenues	4,969,379	(3,753,620)
Materials and supplies	(6,578,566)	(2,705,761)
Prepayments, interest receivable, and other	(656,769)	(1,552,705)
Other deferred assets and charges	(8,726,703)	(6,151,201)
Provision for injuries and damages and claims payable	1,565,970	(2,010,234)
Accounts payable, accrued payroll, and other	(4,460,430)	(9,134,772)
Total adjustments	<u>87,751,666</u>	<u>53,966,052</u>
Net cash provided by operating activities	<u>\$ 218,100,340</u>	<u>\$ 243,734,382</u>
SUPPLEMENTAL DISCLOSURES OF NONCASH ACTIVITIES:		
In-kind capital contributions	\$ 5,768,343	\$ 504,288
Amortization of debt related costs—net	(2,176,157)	(2,336,219)
Change in valuation of derivative financial instruments	(6,298,016)	5,930,269
Change in valuation of deferred gain on power exchange	(22,692)	(1,003,353)
Allowance for funds used during construction	2,690,637	2,575,745
Power exchange revenues	50,546,267	22,320,487
Power exchange expenses	(50,401,511)	(20,879,703)
Change in capitalized purchased power commitment/obligation	(10,652,753)	(10,489,628)
Note assumed for software agreement		831,598
Power revenue netting activity	12,443,673	38,834,404
Power expense netting activity	(43,171,799)	(40,356,674)

See notes to financial statements.

CITY OF SEATTLE—CITY LIGHT DEPARTMENT

NOTES TO FINANCIAL STATEMENTS

AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006

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 385,000 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 Seattle City Council. A requirement of Washington State law provides that rates must be fair, nondiscriminatory, and fixed to produce revenue adequate to pay for operation and maintenance expenses and to meet all debt service requirements payable from such revenue. The Department pays occupation taxes to the City based on total revenues.

The Department’s revenues were \$16.9 million and \$12.8 million for electrical energy and \$2.3 million and \$2.2 million for nonenergy services provided to other City departments in 2007 and 2006, respectively.

The Department receives certain services from other City departments and paid approximately \$39.8 million and \$32.9 million, respectively, in 2007 and 2006 for such services. Amounts paid include central cost allocations from the City for services received including treasury services, risk financing, purchasing, data processing systems, vehicle maintenance, personnel, payroll, legal, other administrative, and building rentals, including for the Department’s administrative offices.

The Department’s due from other City departments totaled \$.7 million and \$1.4 million at December 31, 2007 and 2006. The Department’s due to other City departments totaled \$11.5 million and \$6.2 million at December 31, 2007 and 2006. The balances due from and to are the result of transactions incurred in the normal course of operations.

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 and is current through 2007 with all applicable GASB pronouncements as well as Statements and Interpretations of the Financial Accounting Standards Board (“FASB”), Accounting Principles Board (“APB”) Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedures, except for those that conflict with or contradict GASB pronouncements.

Effective January 1, 2006, the Department adopted SFAS No. 153, *Exchanges of Nonmonetary Assets— an amendment of APB Opinion No. 29*. This Statement amends Opinion 29 to eliminate the exception for nonmonetary exchanges of similar productive assets and replaces it with a general exception for exchanges of nonmonetary assets that do not have commercial substance. These nonmonetary exchanges are to be measured at fair value. Accounting for power exchanges under short-term and long-term contracts is affected by this statement. Previously, these transactions were recognized by the Department

at the blended weighted-average cost of power in accordance with APB Opinion No. 29. The effect of implementing SFAS No. 153 on January 1, 2006 is noted in Note 10.

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

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

Restricted and Unrestricted Equity—The Department’s policy is to use restricted equity for their intended purpose and to use unrestricted equity for operating expenses. The Department does not currently incur expenses for which both restricted and unrestricted equity is available.

In September 2005, the bond reserve account was liquidated and a portion of these funds was used to establish a Contingency Reserve Account in the amount of \$25.0 million in accordance with City of Seattle Ordinance No. 121812. This account is restricted for extraordinary costs associated with the operation of the electrical system. There was no associated liability for the Contingency Reserve Account as of December 31, 2007.

Assets Held for Future Use—These assets include property acquired but never used by the Department in electrical service and therefore, held for future service under a definitive plan. Also included is property previously used in service but retired and held pending its reuse in the future under a definitive plan. As of December 31, 2007 and 2006, assets held for future use included the following electrical plan assets: substations, ducts and vaults, and transmission lines totaling \$10.2 million and \$10.6 million, respectively.

Fair Value of Financial Instruments—The Department’s financial instruments include cash and cash equivalents, short-term investments, receivables, payables, and long-term debt. The carrying value of these financial instruments other than long-term debt approximates fair value because of their short maturity or because they are based on year-end quoted market prices. Accordingly, the Department’s financial instruments other than long-term debt are reported at fair value on the accompanying balance sheets at December 31, 2007 and 2006. In addition, certain forward power contracts that are considered derivative instruments along with certain power exchange transactions are valued at fair value and related gains and losses resulting from fair valuation are deferred pursuant to SFAS No. 71.

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

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

The Department's customer base accounted for electric energy sales at December 31, 2007 and 2006, as follows:

	2007	2006
Residential	36.1 %	34.3 %
Nonresidential	<u>63.9</u>	<u>65.7</u>
Total	<u>100.0 %</u>	<u>100.0 %</u>

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

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

Administrative and General Overhead Costs Applied—Administrative and general costs are allocated to construction work-in-progress, major data processing systems development, programmatic conservation, relicensing mitigation projects, and billable operations and maintenance activities based on rates established by cost studies. Pension and benefit costs are fully allocated to capital and operations and maintenance activities based on a percentage of labor dollars. The administrative and general overhead costs applied totaled \$23.7 million and \$25.4 million in 2007 and 2006, respectively. Pension and benefit costs were \$28.9 million and \$26.1 million in 2007 and 2006, respectively. Administrative and general expenses, net of total applied overhead, were \$66.6 million and \$49.0 million in 2007 and 2006, respectively.

Interest Charged to Construction—Interest is charged for funds used during construction of plant assets and to nonbillable construction work-in-progress. Interest charged represents the estimated costs of financing construction projects and is computed using the Department's weighted-average interest rate for all bonds outstanding at the end of the year. Interest charged to construction totaled \$2.7 million and \$2.6 million in 2007 and 2006, respectively, and is reflected as a reduction of interest expense in the statements of revenues, expenses, and changes in equity.

Nonexchange Transactions—Capital contributions and grants in the amount of \$46.1 million and \$31.8 million are reported for 2007 and 2006, respectively, on the statements of revenues, expenses, and changes in equity as nonoperating revenues from nonexchange transactions. Capital contributions and grants revenues are recognized based on the accrual basis of accounting. In-kind capital contributions are recognized in the period when all eligibility requirements have been met as described in GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, and are recognized at fair market value. The determination of the fair market value is based on either the internal engineer's estimate of the current cost of comparable plant-in-service or the donor's actual cost. Federal and state grant revenues are recognized as earned and are subject to contract and other compliance audits.

Compensated Absences—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 or effective 2006 may elect tax-free conversion of 35% of their sick leave balance to a health reimbursement account (HRA). The HRA program is administered by Rehn & Associates; HRA investments are managed by HRA VEBA Trust Operations. The Department accrues all costs associated with compensated absences, including payroll taxes.

Use of Estimates—The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect amounts reported in the financial statements. The Department used significant estimates in determining reported allowance for doubtful accounts, unbilled revenues, energy contract assets and liabilities, accumulated provision for injuries and damages, 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 markets for short-term power transactions; 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 (“EPA”) regulations; federal government regulations or orders concerning the operations, maintenance, and/or licensing of hydroelectric facilities; other governmental regulations; restructuring of the electrical utility industry; and the costs of constructing transmission facilities that may be incurred as part of a northwest regional transmission system, and related effects of this system on transmission rights, transmission sales, the value of surplus energy, and governance.

Reclassifications—Certain 2006 account balances have been reclassified to conform to the 2007 presentation.

2. UTILITY PLANT

Utility Plant—Utility plant is recorded at original cost, which includes both direct costs of construction or acquisition and indirect costs, including an allowance for funds used during construction. The capitalization threshold was \$5,000 in 2007 and 2006. Property constructed with capital fees received from customers is included in utility plant. Capital fees totaled \$37.7 million in 2007 and \$21.4 million in 2006. Provision for depreciation is made using the straight-line method based upon estimated economic lives, which range from 3 to 50 years, of related operating assets. The Department uses a half-year convention method on the assumption that additions and replacements are placed in service at mid-year. The composite depreciation rate was approximately 3.0% in 2007 and 3.0 % in 2006. 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. The Department periodically reviews long-lived assets for impairment to determine whether any events or circumstances indicate the carrying value of the assets may not be recoverable. No impairment was identified in 2007 or 2006.

Utility plant-in-service at original cost, excluding land, at December 31, 2007 and 2006, was:

2007	Hydraulic Production	Transmission	Distribution	General	Total
Original cost:					
Beginning balance	\$ 624,274,271	\$ 158,732,010	\$ 1,346,854,631	\$ 355,628,069	\$ 2,485,488,981
Capital acquisitions	11,634,127	5,756,508	85,014,964	15,350,827	117,756,426
Dispositions	(2,480,053)	(190,004)	(3,959,070)	(2,241,092)	(8,870,219)
Transfers and adjustments	804,896		10,626,761	55,160	11,486,817
Total original cost	634,233,241	164,298,514	1,438,537,286	368,792,964	2,605,862,005
Accumulated depreciation:					
Beginning balance	307,075,915	70,279,113	499,148,271	232,982,245	1,109,485,544
Increase in accumulated depreciation	12,537,792	3,535,103	41,857,793	21,480,028	79,410,716
Retirements	(3,019,809)	(501,688)	(8,125,799)	(2,371,925)	(14,019,221)
Retirement work-in-process	(51,369)	(1,963)	(255,715)	391	(308,656)
Total accumulated depreciation	316,542,529	73,310,565	532,624,550	252,090,739	1,174,568,383
Ending balance	\$ 317,690,712	\$ 90,987,949	\$ 905,912,736	\$ 116,702,225	\$ 1,431,293,622
2006	Hydraulic Production	Transmission	Distribution	General	Total
Original cost:					
Beginning balance	\$ 607,845,610	\$ 149,637,146	\$ 1,254,331,982	\$ 344,904,112	\$ 2,356,718,850
Capital acquisitions	18,179,093	9,292,426	77,534,616	11,888,491	116,894,626
Dispositions	(1,750,432)	(491,993)	(3,915,545)	(1,105,515)	(7,263,485)
Transfers and adjustments		294,430	18,903,578	(59,018)	19,138,990
Total original cost	624,274,271	158,732,009	1,346,854,631	355,628,070	2,485,488,981
Accumulated depreciation:					
Beginning balance	297,675,624	67,645,115	469,069,141	212,665,550	1,047,055,430
Increase in accumulated depreciation	12,367,505	3,270,096	38,904,274	21,536,670	76,078,545
Retirements	(2,918,189)	(645,383)	(8,272,612)	(1,226,397)	(13,062,581)
Retirement work-in-process	(49,025)	9,285	(552,532)	6,422	(585,850)
Total accumulated depreciation	307,075,915	70,279,113	499,148,271	232,982,245	1,109,485,544
Ending balance	\$ 317,198,356	\$ 88,452,896	\$ 847,706,360	\$ 122,645,825	\$ 1,376,003,437

3. CASH AND EQUITY IN POOLED INVESTMENTS

Cash and Equity in Pooled Investments—Cash resources of the Department are combined with cash resources of the City to form a pool of cash that is managed by the City’s Department of Executive Administration (“DEA”). Under the City’s investment policy, DEA invests and manages all temporary cash surpluses in the pool. The Department’s share of the pool is included in the balance sheets under the caption “cash and equity in pooled investments” or accounts within restricted cash. The pool operates like a demand deposit account in that all agencies, including the Department, may deposit cash at any time and can also withdraw cash out of the pool without prior notice or penalty. Accordingly, the statements of cash flows reconcile to cash and equity in pooled investments. The city considers investments in financial instruments having a maturity of 90 days or less as a cash equivalent.

Custodial Credit Risk—Deposits—As of December 31, 2007 and 2006, the City’s pool contained cash on deposit with the City’s custodial banks in the amounts of \$14,487,958 and \$20,542,798 respectively. Custodial credit risk is the risk that the deposits may not be returned to the City in the event of a bank failure. The Federal Deposit Insurance Corporation (“FDIC”) insures the City’s deposits up to \$100,000. All deposits not covered by FDIC insurance are covered by the Public Deposit Protection Commission (“PDPC”) of the State of Washington. The PDPC is a statutory authority established under the Revised

Code of Washington (RCW) 39.58. It constitutes a multiple financial institution collateral pool. In the case of a loss by any public depository in the state, each public depository is liable for an amount up to 11% of its public deposits. Provisions of RCW 39.58.060 authorize the PDPC to make pro-rata assessments in proportion to the maximum liability of each such depository as it existed on the date of loss. Therefore, PDPC protection is that of collateral, not of insurance.

Investments—The Department’s cash resources may be invested by DEA separate from the cash and investments pool. Investments are managed in accordance with the City’s investment policy, with limits and restrictions applied at the City-wide level rather than to specific investments of the Department. The city considers an investment held for more than one year as a long-term investment.

As of December 31, 2007 and 2006, the Department’s dedicated investments and the City’s pool and other investments were as follows:

2007	Fair Value				Weighted-Average Maturity (Days)
	Dedicated Investments of the Department	City Pool	Other City Dedicated Investments	Total	
U.S. government agencies	\$ -	\$ 563,723,234	\$ 5,554,398	\$ 569,277,632	804
Municipal bonds taxable		34,927,394	13,578,497	48,505,891	288
Commercial paper		219,776,326		219,776,326	12
U.S. government obligations		15,370,313		15,370,313	517
Repurchase agreements		92,283,483		92,283,483	2
Total	\$ -	\$ 926,080,750	\$ 19,132,895	\$ 945,213,645	

Portfolio weighted-average maturity 507

2006	Fair Value				Weighted-Average Maturity (Days)
	Dedicated Investments of the Department	City Pool	Other City Dedicated Investments	Total	
U.S. government agencies	\$ -	\$ 487,816,597	\$ 61,903,104	\$ 549,719,701	325
Municipal bonds taxable		7,928,395		7,928,395	182
Commercial paper		200,814,310	28,656,174	229,470,484	18
U.S. government obligations		24,914,063		24,914,063	46
Repurchase agreements		112,044,546		112,044,546	2
Total	\$ -	\$ 833,517,911	\$ 90,559,278	\$ 924,077,189	

Portfolio weighted-average maturity 201

As of December 31, 2007 and 2006, the Department's share of the City pool was as follows:

	2007	2006
Cash and equity in pooled investments:		
Restricted assets	\$ 31,109,383	\$ 31,502,946
Current assets	<u>87,723,934</u>	<u>127,148,120</u>
Total	<u>\$ 118,833,317</u>	<u>\$ 158,651,066</u>
Balance as a percentage of City pool	12.8 %	19.0 %

Interest Rate Risk—Interest rate risk is the risk that changes in interest rates over time will adversely affect the fair value of an investment. In accordance with its investment policy, the City manages its exposure to declines in fair values by limiting the weighted-average maturity of its investment portfolio to no longer than five years. Furthermore, to achieve its financial objective of maintaining liquidity to meet its operating cash flow needs, the City typically selects investments that have much shorter average maturities.

Credit Risk—Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. In accordance with its investment policy, the City manages its exposure to credit risk by limiting its investments in commercial paper purchased on the secondary market to those with maturities not longer than 180 days from purchase and with the highest rating by at least two nationally recognized statistical rating organizations (“NRSRO”). As of December 31, 2007 and 2006, the City's investments in commercial paper were rated P-1 by Moody's Investors Service, A-1 or A-1+ by Standard & Poor's, or F-1 by Fitch Ratings.

The City also purchases obligations of government-sponsored enterprises, which are eligible as collateral for advances to member banks as determined by the Board of Governors of the Federal Reserve System. These include, but are not limited to, debt securities of Federal Home Loan Bank, Federal Home Loan Mortgage Corporation, Federal Farm Credit Bank, and Federal National Mortgage Association. As of December 31, 2007 and 2006, these investments were rated Aaa by Moody's Investors Service and AAA by Standard & Poor's.

The City's investments in repurchase agreements require a master repurchase agreement executed with the counterparty and may only be conducted with primary dealers, the City's bank of record, or master custodial bank. Securities delivered as collateral must be priced at a minimum of 102% of their market value for U.S. Treasuries and at higher margins of 103% to 105% for debentures of U.S. federal government-sponsored enterprises, mortgage-backed pass-throughs, banker's acceptances, and commercial paper. In addition, collateral securities must have the highest credit ratings of at least two NRSROs. Repurchase agreements themselves do not carry a credit rating as of December 31, 2007 and 2006, the securities underlying the City's investment in repurchase agreements included collateral other than U.S. Treasuries.

Concentration of Credit Risk—Concentration of credit risk is the risk of loss attributed to the magnitude of a government’s investment in a single issuer. In accordance with its investment policy, the City manages its exposure to concentration of credit risk for the City’s investments portfolio as a whole. The City limits its investments in any one issuer to no more than 20% of its portfolio, except for investments in U.S. government obligations or U.S. government agency securities, which may comprise up to 100% of the portfolio. The City’s investments in which 5% or more is invested in any single issuer as of December 31, 2007 and 2006, were as follows:

Issuer	2007		2006	
	Fair Value	Percent of Total Investments	Fair Value	Percent of Total Investments
Bank of America	\$ 91,600,000	10 %	\$ 111,000,000	12 %
Federal Home Loan Mortgage Corporation	168,023,684	18	177,957,324	19
Federal National Mortgage Corporation	198,573,365	21	166,586,419	18
Federal Home Loan Bank	<u>182,696,219</u>	<u>19</u>	<u>185,438,458</u>	<u>20</u>
Total	<u>\$ 640,893,268</u>	<u>68 %</u>	<u>\$ 640,982,201</u>	<u>69 %</u>

The Department did not have any dedicated investments and therefore, did not have investments in which 5% or more is invested in any single issuer as of December 31, 2007 and 2006.

Custodial Credit Risk—Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty, the City will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. In accordance with its investment policy, the City maintains a list of security dealers and financial institutions authorized to provide investment services to the City. The security dealers and financial institutions may include primary dealers or regional dealers that qualify under Securities and Exchange Commission Rule 15C3-1 (uniform net capital rule) and investment departments of local banks which passed evaluation of their financial condition, strength, and capability to fulfill commitments; overall reputation with other dealers and investors; regulatory status; and background and expertise on their individual representative.

Foreign Currency Risk—The City treasury investments pool and securities held for dedicated funds do not have any exposure to foreign currency risk.

Securities Lending Transactions—The City is authorized to engage in securities lending transactions similar to that instituted by the Washington State Treasurer’s Office and other municipal corporations in the State of Washington. There were no securities lending transactions outstanding as of December 31, 2007 and 2006.

Reverse Repurchase Agreements—The City may enter into reverse repurchase agreements as part of its investment policies. These agreements are sales of securities with a simultaneous agreement to repurchase the securities at a future date at the same prices plus contracted rates of interest. The fair value of the securities underlying the agreements normally exceeds the cash received, providing the dealers a margin against a decline in the fair value of the securities. If the dealers default on their obligations to resell these securities to the City, or provide securities or cash of equal value, the City would suffer an economic loss equal to the difference between the fair value plus accrued interest of the underlying securities and the agreement obligation, including accrued interest. There were no outstanding reverse repurchase agreements as of December 31, 2007 and 2006.

4. ACCOUNTS RECEIVABLE

Accounts receivable at December 31, 2007 and 2006, consist of:

	Retail Electric	Wholesale Power	Other Operating	Operating Subtotal	Nonoperating Subtotal	Total
2007						
Accounts receivable	\$ 44,802,691	\$ 17,764,875	\$ 3,216,278	\$ 65,783,844	\$ 11,920,617	\$ 77,704,461
Less allowance for doubtful accounts	<u>(3,650,000)</u>	<u>(885,068)</u>	<u>(1,489,000)</u>	<u>(6,024,068)</u>		<u>(6,024,068)</u>
	<u>\$ 41,152,691</u>	<u>\$ 16,879,807</u>	<u>\$ 1,727,278</u>	<u>\$ 59,759,776</u>	<u>\$ 11,920,617</u>	<u>\$ 71,680,393</u>
2006						
Accounts receivable	\$ 62,334,650	\$ 20,400,149	\$ 8,981,303	\$ 91,716,102	\$ 12,278,048	\$ 103,994,150
Less allowance for doubtful accounts	<u>(20,971,000)</u>	<u>(885,762)</u>	<u>(1,465,000)</u>	<u>(23,321,762)</u>		<u>(23,321,762)</u>
	<u>\$ 41,363,650</u>	<u>\$ 19,514,387</u>	<u>\$ 7,516,303</u>	<u>\$ 68,394,340</u>	<u>\$ 12,278,048</u>	<u>\$ 80,672,388</u>

5. SHORT-TERM POWER CONTRACTS AND DERIVATIVE INSTRUMENTS

The Department enters into short-term forward contracts to purchase or sell energy. Under these forward contracts, the Department commits to purchase or sell a specified amount of energy at a specified time, or during a specified time in the future. Certain of the forward contracts are considered derivative instruments as they may be net-settled without physical delivery. These derivative instruments, along with other short-term power transactions, are entered into for the purpose of managing the Department's resources to meet load requirements and to realize earnings from surplus energy resources. Except for limited intraday and interday trading to take advantage of owned hydro storage, the Department does not take market positions in anticipation of generating revenue. Power transactions in response to forecasted seasonal resource and demand variations require approval by the Department's Risk Oversight Council. Fluctuations in annual precipitation levels and other weather conditions materially affect the energy output from the Department's hydroelectric facilities and some of its long-term purchased hydroelectric power agreements. Demand fluctuates with weather and local economic conditions. Accordingly, short-term power transactions required to manage resources to meet the Department's load and dispose of surplus energy may vary from year to year.

The fair value of the Department's derivative financial instruments at December 31 as follows:

	2007	2006
Derivative financial instrument - current assets:		
Forward electric energy sales	<u>\$ 854,726</u>	<u>\$ 6,680,264</u>
Derivative financial instrument - current liabilities:		
Forward electric energy sales	\$ 663,534	\$ 191,056
Regulatory deferred gain - deferred credits:	<u>191,192</u>	<u>6,489,208</u>
	<u>\$ 854,726</u>	<u>\$ 6,680,264</u>

The Seattle City Council has deferred recognition of the effects of reporting the fair value of derivative financial instruments for rate-making purposes, and maintains regulatory accounts to defer the accounting impact of these accounting adjustments in accordance with SFAS No. 71 (see also Notes 11 and 12).

6. LONG-TERM DEBT

At December 31, 2007 and 2006, the Department's long-term debt consisted of the following:

LONG-TERM			2007	2006
Prior Lien Bonds:	Fixed Rate	Year Due		
2004 ML&P Improvement and Refunding Revenue Bonds	3.000%–5.250%	2029	\$ 266,785,000	\$ 272,785,000
2003 ML&P Improvement and Refunding Revenue Bonds	4.000%–6.000%	2028	170,845,000	194,665,000
2002 ML&P Refunding Revenue Bonds	3.000%–4.500%	2014	49,220,000	58,475,000
2001 ML&P Improvements and Refunding Revenue Bonds	5.000%–5.500%	2026	480,560,000	487,550,000
2000 ML&P Revenue Bonds	4.500%–5.625%	2025	92,940,000	95,955,000
1999 ML&P Revenue Bonds	5.000%–6.000%	2024	13,500,000	16,750,000
1998B ML&P Revenue Bonds	4.750%–5.000%	2024	78,885,000	81,835,000
1998A ML&P Refunding Revenue Bonds	4.500%–5.000%	2020	86,980,000	92,045,000
1997 ML&P Revenue Bonds	5.000%–5.125%	2022	24,930,000	26,035,000
Total prior lien bonds			<u>1,264,645,000</u>	<u>1,326,095,000</u>
Subordinate Lien Bonds:				
1996 ML&P Adjustable Rate Revenue Bonds	variable rates	2021	15,415,000	16,220,000
1993 ML&P Adjustable Rate Revenue Bonds	variable rates	2018	13,900,000	14,900,000
1991B ML&P Adjustable Rate Revenue Bonds	variable rates	2016	9,500,000	11,700,000
1991A ML&P Adjustable Rate Revenue Bonds	variable rates	2016	25,000,000	25,000,000
1990 ML&P Adjustable Rate Revenue Bonds	variable rates	2015	14,000,000	15,300,000
Total subordinate lien bonds			<u>77,815,000</u>	<u>83,120,000</u>
Notes Payable—				
2006 Note Payable—State of Washington	5.000%	2008	284,853	3,956,493
2005 Note Payable—Sound Transit	variable rates	2007	-	555,104
			<u>284,853</u>	<u>4,511,597</u>
Total long-term debt			<u>\$1,342,744,853</u>	<u>\$1,413,726,597</u>

The Department had the following activity in long-term debt during 2007 and 2006:

	Balance at December 31, 2006	Additions	Reductions	Balance at December 31, 2007	Current Portion
2007					
Prior Lien Bonds	\$ 1,326,095,000	\$ -	\$(61,450,000)	\$ 1,264,645,000	\$64,620,000
Subordinate Lien Bonds	83,120,000		(5,305,000)	77,815,000	5,840,000
Note payable—Sound Transit	3,956,493		(3,956,493)		
Note payable—State of Washington	555,104		(270,251)	284,853	284,853
Total	<u>\$ 1,413,726,597</u>	<u>\$ -</u>	<u>\$(70,981,744)</u>	<u>\$ 1,342,744,853</u>	<u>\$70,744,853</u>
2006					
Prior Lien Bonds	\$ 1,384,755,000	\$ -	\$(58,660,000)	\$ 1,326,095,000	\$61,450,000
Subordinate Lien Bonds	87,895,000		(4,775,000)	83,120,000	5,305,000
Note payable—Sound Transit	9,593,840	956,793	(6,594,140)	3,956,493	3,956,493
Note payable—State of Washington		831,598	(276,494)	555,104	270,251
Total	<u>\$ 1,482,243,840</u>	<u>\$ 1,788,391</u>	<u>\$(70,305,634)</u>	<u>\$ 1,413,726,597</u>	<u>\$70,981,744</u>

Prior Lien Bonds—In December 2004, the Department issued \$284.9 million in ML&P Improvement and Refunding Revenue Bonds that bear interest at rates ranging from 3.00% to 5.25% and mature serially from August 1, 2005 through 2025. Proceeds were used to finance certain capital improvements and conservation programs and to defease certain outstanding 1995A, 1996, and 1999 series prior lien bonds. There were no additional bonds issued during 2007 and 2006.

Debt service requirements for prior lien bonds are as follows:

Years Ending December 31	Principal Redemptions	Interest Requirements	Total
2008	\$ 64,620,000	\$ 63,596,351	\$ 128,216,351
2009	67,990,000	60,235,645	128,225,645
2010	71,525,000	56,698,740	128,223,740
2011	66,995,000	53,286,445	120,281,445
2012	66,850,000	50,253,820	117,103,820
2013–2017	352,820,000	196,663,556	549,483,556
2018–2022	329,845,000	107,080,694	436,925,694
2023–2027	227,265,000	29,407,572	256,672,572
2028–2029	<u>16,735,000</u>	<u>984,231</u>	<u>17,719,231</u>
Total	<u>\$1,264,645,000</u>	<u>\$618,207,054</u>	<u>\$1,882,852,054</u>

The Department was 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 2004 bonds, the maximum annual debt service on prior lien bonds was \$128.2 million due and paid in 2006. The maximum amount of the reserve permitted by the IRC was \$113.3 million. At December 31, 2004, the balance in the reserve account was \$87.0 million at fair value. In September 2005, the Department purchased a Municipal Bond (Surety Bond) to replace the reserve account authorized by Ordinance No. 121812. Accordingly, the funds in the reserve account of \$87.4 million, were used to fund a new \$25.0 million Contingency Reserve Account, also authorized by Ordinance No. 121812. The balance of \$62.4 million was used for additional long-term debt reduction by transferring these funds to the Construction Account for authorized capital expenditures.

A portion of the proceeds from the 2004 refunding bonds were placed in a separate irrevocable trust to provide for all future debt service payments on the bonds defeased. The balance outstanding in the irrevocable trust during 2007 and 2006 was for the 2004 series. Neither the assets of the trust account nor the liabilities for the defeased bonds are reflected in the Department’s financial statements. The bonds defeased in 2004 had an outstanding principal balance of \$138.3 million as of December 31, 2007 and 2006, respectively. Funds held in the 2004 trust account on December 31, 2007, are 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 claims on revenues. Subordinate lien bonds may be issued to the extent that the new bonds will not cause the aggregate principal amount of such bonds then outstanding to exceed the greater of \$70.0 million or 15% of the aggregate principal amount of prior lien bonds then outstanding. 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. The subordinate lien bonds are supported by a letter of credit issued by JP Morgan Chase Bank that provides credit and liquidity support for the principal amounts and accrued interest then outstanding in the event that the subordinate lien bonds are not able to be remarketed. The letter of credit expires on January 31, 2010.

Future debt service requirements on the subordinate lien bonds, based on 2007 end of year actual interest rates ranging from 3.27% to 3.42% through year 2021, are as follows:

Years Ending December 31	Principal Redemptions	Interest Requirements	Total
2008	\$ 5,840,000	\$ 2,510,779	\$ 8,350,779
2009	6,270,000	2,312,471	8,582,471
2010	6,705,000	2,100,042	8,805,042
2011	7,345,000	1,871,142	9,216,142
2012	7,785,000	1,623,434	9,408,434
2013–2017	37,055,000	3,988,567	41,043,567
2018–2022	<u>6,815,000</u>	<u>493,396</u>	<u>7,308,396</u>
Total	<u>\$77,815,000</u>	<u>\$14,899,831</u>	<u>\$ 92,714,831</u>

Fair Value—The fair value of the Department’s bonds 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 (net of premiums and discounts) and fair values at December 31, 2007 and 2006, are as follows:

	2007		2006	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Long-term debt:				
Prior lien bonds	\$ 1,293,365,796	\$ 1,310,243,325	\$ 1,358,529,557	\$ 1,397,098,567
Subordinate lien bonds	<u>77,645,231</u>	<u>77,815,000</u>	<u>82,932,366</u>	<u>83,120,000</u>
Total	<u>\$ 1,371,011,027</u>	<u>\$ 1,388,058,325</u>	<u>\$ 1,441,461,923</u>	<u>\$ 1,480,218,567</u>

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

The excess of costs incurred over the carrying value of bonds refunded on early extinguishment of debt is amortized as a component of interest expense using both the straight-line and effective interest methods over the terms of the issues to which they pertain. Deferred refunding costs amortized to interest expense totaled \$5.1 million in 2007 and \$5.4 million in 2006. Deferred refunding costs in the amount of \$37.3 million and \$42.4 million are reported as a component of long-term debt in the 2007 and 2006 balance sheets, respectively.

Note Payable—Sound Transit—In 2003, the Department negotiated an agreement with Sound Transit, the regional transit authority, to perform electrical work pertaining to the undergrounding of utilities along Martin Luther King Way for the new light rail line under construction. There were two major components of this work. The first component consisted of installing an underground ductbank along Martin Luther King Way in South Seattle. The second element was to perform the necessary underground electrical work within the ductbank. Financial terms of this agreement were finalized during 2005 that resulted in a note payable to Sound Transit. Sound Transit completed the underground ductbank at a cost of \$18.7 million, of which the Department was responsible for \$11.8 million, payable to Sound Transit. The completed underground electrical work was financed in part by Sound Transit and the total amount due Sound Transit was \$3.1 million. In 2006, the note payable was increased by nearly

\$1.0 million for additional electrical work performed. The entire note payable was repaid in full by the end of 2007. The note payable had an interest rate of 3.9%, plus an inflation component.

Note Payable—State of Washington—In 2007, the Department negotiated a note payable with the State of Washington for the purchase of software installed in 2006 department-wide. The total amount of the note payable was \$.8 million, maturing in 2008 at an imputed interest rate of 5%. During 2007, \$.3 million was repaid leaving a balance of \$.3 million at the end of the year. Debt service requirements are:

Years Ending December 31	Principal Redemptions	Interest Requirements	Total
2008	\$ 284,853	\$ 7,196	\$ 292,049
Total	\$ 284,853	\$ 7,196	\$ 292,049

Noncurrent Liabilities—The Department had the following activities during 2007 and 2006:

2007	Balance at 12/31/06	Additions	Reductions	Balance at 12/31/07	Current Portion
Compensated absences	\$ 11,393,239	\$ 16,247,317	\$ (15,074,557)	\$ 12,565,999	\$ 1,222,813
Long-term purchased power obligation	15,401,778	-	(10,652,753)	4,749,025	11,970,000
Other	185,864	1,273,023	(7,163)	1,451,724	-
Total	\$ 26,980,881	\$ 17,520,340	\$ (25,734,473)	\$ 18,766,748	\$ 13,192,813

2006	Balance at 12/31/05	Additions	Reductions	Balance at 12/31/06	Current Portion
Compensated absences	\$ 10,990,644	\$ 13,798,752	\$ (13,396,157)	\$ 11,393,239	\$ 1,005,628
Long-term purchased power obligation	25,891,406	-	(10,489,628)	15,401,778	11,770,000
Other	192,473	4,702	(11,311)	185,864	-
Total	\$ 37,074,523	\$ 13,803,454	\$ (23,897,096)	\$ 26,980,881	\$ 12,775,628

7. ACCOUNTS PAYABLE

Accounts Payable and Other—The composition of accounts payable and other at December 31, 2007 and 2006, is as follows:

	2007	2006
Vouchers payable	\$ 19,285,347	\$ 13,355,570
Power accounts payable	23,838,333	30,788,258
Interfund payable	11,451,789	6,159,676
Taxes payable	8,987,501	9,511,145
Claims payable—current	8,096,900	9,936,774
Guarantee deposit and contract retainer	957,659	2,246,526
Other accounts payable	<u>270,380</u>	<u>465,565</u>
Total	<u>\$ 72,887,909</u>	<u>\$ 72,463,514</u>

8. SEATTLE CITY EMPLOYEES' RETIREMENT SYSTEM

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

All employees of the City are eligible for membership in SCERS with the exception of uniformed police and fire personnel who are covered under a retirement system administered by the State of Washington. Employees of Metro and the King County Health Department who established membership in SCERS when these organizations were City departments were allowed to continue their SCERS membership. As of December 31, 2007, there were 5,201 retirees and beneficiaries receiving benefits and 8,842 active members of SCERS. In addition, 2,050 vested terminated employees were entitled to 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 as 2% multiplied by years of creditable service, multiplied by average salary, based on the highest 24 consecutive months, excluding overtime. The benefit is actuarially reduced for early retirement. Future increases in the cost-of-living adjustments are available to current and future retired members only if SCERS attains at least a 95% funding level. SCERS does not provide termination benefits.

Actuarially recommended contribution rates both for members and for the employer were 8.03% of covered payroll during 2007 and 2006.

Under the authority of the state and City, SCERS operates a securities lending program, and there were transactions during 2007 and 2006. SCERS has had no losses resulting from a default, and SCERS did not have negative credit exposure at December 31, 2007 or 2006.

SCERS issues stand-alone financial statements that may be obtained by writing to the Seattle City Employees' Retirement System, 720 Third Avenue, Suite 1000, Seattle, WA 98104; telephone: (206) 386-1293.

Employer contributions for the City were \$40.2 million and \$38.1 million in 2007 and 2006. Department contributions were \$8.4 million and \$8.0 million in 2007 and 2006. The annual required contributions were made in full.

Actuarial Data

Valuation date	January 1, 2006
Actuarial cost method	Entry age
Amortization method	Level percent
Remaining amortization period	18.0 years, open
Amortization period	Maximum of 40 years
Asset valuation method	Market

Actuarial Assumptions*

Percentage

Investment rate of return	7.75%
Projected general wage increases	4.00
Cost-of-living year-end bonus dividend	0.67

* Includes price inflation at 3.5% and 0.5% of payroll growth.
 Note: There are no post-retirement benefit increases assumed.

Annual Pension Cost and Net Pension Obligation
for Fiscal Year Ending December 31, 2005
Based on January 1, 2004 Valuation
(latest information available)

Years Ending December 31	2004	2005
1a Total normal cost rate	13.05 %	13.05 %
1b Employee contribution rate	8.03 %	8.03 %
1c Employer normal cost rate (1a-1b)	5.02 %	5.02 %
2a Total employer contribution rate	8.03 %	8.03 %
2b Amortization payment rate (2a-1c)	3.01 %	3.01 %
2c Amortization period *	30.20 %	30.20 %
2d GASB 27 amortization rate	3.01 %	3.01 %
3 Total annual required contribution (ARC) rate (1c+2d)	8.03 %	8.03 %
4 Covered employee payroll **	\$ 456,808,182	\$ 447,040,411
5a ARC (3x4)	\$ 36,681,697	\$ 35,897,345
5b Interest on net pension obligation (NPO)	(5,773,805)	(5,910,271)
5c ARC adjustment	4,012,944	4,107,791
5d Annual pension cost (APC) (5a+5b+5c)	<u>\$ 34,920,836</u>	<u>\$ 34,094,865</u>
6 Employer contribution	\$ 36,681,697	\$ 35,897,345
7a Change in NPO (5d-6)	(1,760,861)	(1,802,480)
7b NPO at beginning of year	(74,500,706)	(76,261,567)
7c NPO at end of year (7a+7b)	<u>\$ 76,261,567</u>	<u>\$ 78,064,047</u>

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

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

Schedule of funding progress for SCERS (dollar amounts in millions):

Actuarial Valuation Date January 1,	Actuarial Value of Assets (a)	Actuarial Accrued Liabilities ("AAL")⁽¹⁾ (b)	Unfunded AAL ("UAAL")⁽²⁾ (b-a)	Funding Ratio (a/b)	Covered Payroll⁽³⁾ (c)	UAAL or (Excess) as a Percentage of Covered Payroll ((b-a)/c)
2002	\$ 1,383.7	\$ 1,581.4	\$ 197.7	87.5 %	\$ 405.1	48.8 %
2004	1,527.5	1,778.9	251.4	85.9	424.7	59.2
2006	1,791.8	2,017.5	225.8	88.8	447.0	50.5

(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.

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

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

The Seattle City Council authorizes the obligations of the plan members and the City as employer by passing ordinances and amendments regarding contributions to the plans. Eligible retirees up to age 65 self-pay 100% of the premium based on blended rates which were established by including the experience of retirees with the experience of active employees for underwriting purposes. The plan is financed on a pay-as-you-go basis, and the City was required to contribute \$1.4 million in 2007.

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

Actuarial data and assumptions

Valuation date	January 1, 2006
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	30 years, closed
Discount rate	5.125%
Health care cost trend rates—medical:	12%, decreasing by 0.5% for each year for 12 years to an ultimate rate of 6%.
Participation	45% of Active Employees who retire participate
Mortality	General Service Actives and Retirees based on the Group Annuity Mortality (GAM) 1994 Static Table (Final) with ages set forward one year.
Marital status	60% of members electing coverage: married or have a registered domestic partner. Male spouses two years older than their female spouses.
Morbidity factors	Morbidity rate ranges for ages 50 through 64: 94.6% to 166.5% for male retirees, 106.9% to 134.3% for female retirees, 104.5% to 183.9% for male spouses, and 118.1% to 148.4% for female spouses. Retirees' spouses pay a lower premium than retirees.
Other considerations	Active employees with current spouse and/or dependent coverage elect same plan and coverage.

Based on the actuarial valuation date of January 1, 2006, the City’s annual cost for fiscal year ended December 31, 2007, the amount of expected contribution to the plan, and changes in net obligation are as follows:

	2007
Annual required contribution	\$ 9,328,990
Interest on net OPEB obligation	-
Adjustment to annual required contribution	-
Annual OPEB cost (expense)	9,328,990
Expected contribution (employer-paid benefits)	<u>(1,354,268)</u>
Increase in net OPEB obligation	7,974,722
Net OPEB Obligation - beginning of the year	-
Net OPEB obligation - end of year	<u>\$ 7,974,722</u>

Schedules of funding progress are as follows (dollars in millions):

Actuarial Valuation Date January 1,	Actuarial Value of Assets (a)	Actuarial Accrued Liabilities ("AAL") Entry Age (b)	Unfunded AAL ("UAAL") (b-a)	Funding Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
2006	\$ 0.0	\$ 84.3	\$ 84.3	0.0 %	N/A	N/A

The Health Care Subfund of the General Fund is reported in the City's Comprehensive Annual Financial Report that can be obtained by writing the Department of Finance, City of Seattle, PO Box 94747, Seattle, WA 98124-4747.

9. DEFERRED COMPENSATION

The Department's employees may contribute to the City'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 Plan administrator is Prudential Retirement. 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 a low risk of liability for investment losses under the Plan. Participants direct the investment of their money into one or more options provided by the Plan and may change their selection from time to time. By enrolling in the Plan, participants accept and assume all risks inherent in the Plan and its administration.

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

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

In 2006, the Department and BPA amended the Block agreement to enable the Department to participate in the BPA Flexible Priority Firm (PF) Program. Under the provisions of this program, the Block product is subject to a Flexible PF Charge on a power bill increasing the amount payable by the Department for power service in a given month followed by reductions in the amount payable for power service in subsequent months until the charge is recovered. Participation in the program provides the Department with a monthly discount on its Block bill whether or not the Flexible PF Charge is applied. In order to participate, the Department was required to enter into an irrevocable standby letter of credit

for \$16.5 million issued by the Bank of America with a term from October 1, 2006 through September 30, 2009. The Flexible PF Charge was not applied in 2007 or 2006.

The terms of the Slice product specify that the Department will receive a fixed percentage (4.6676%) of the actual output of the Federal Columbia River Power System. The cost of Slice power is based on the Department's same percentage (4.6676%) of the expected costs of the system and is subject to true-up adjustments based on actual costs with specified exceptions. Subsequent amendments to the contract provide that Bonneville will pay the Department for qualified energy savings realized through specified programs and decrement Block purchases accordingly.

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 that began commercial operation in 1988 at the existing Army Corps of Engineers Lucky Peak Dam on the Boise River near Boise, Idaho. The irrigation districts are owners and license holders of the project, and the FERC license expires in 2030. The agreement, which expires in 2038, obligates the Department to pay all ownership and operating costs, including debt service, over the term of the contract, whether or not the plant is operating or operable. 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. The project's debt matures in July 2008.

British Columbia—High Ross Agreement—In 1984, an agreement was reached between the Province of British Columbia and the City under which British Columbia will provide the Department with power equivalent to that which would result from an addition to the height of Ross Dam. The power is to be received for 80 years, and delivery of power began in 1986. In addition to the direct costs of power under the agreement, the Department incurred costs of approximately \$8.0 million in prior years related to the proposed addition and was obligated to help fund the Skagit Environmental Endowment Commission through four annual \$1 million payments. These costs were deferred and are being amortized to purchase power expense over 35 years through 2035.

Power received and expenses under these and other long-term purchased power agreements at December 31, 2007 and 2006, are as follows:

	2007 Expense	2006 Expense	2007 Average Megawatts	2006
Bonneville Block	\$ 59,277,987	\$ 45,061,622	242.2	174.4
Bonneville Slice	116,513,042	109,656,740	411.3	451.1
	<u>175,791,029</u>	<u>154,718,362</u>	653.5	625.5
Lucky Peak	15,473,269	16,438,418	31.2	46.5
British Columbia - High Ross Agreement	13,395,061	13,386,727	35.8	36.1
City of Klamath Falls	-	12,006,483	-	11.4
State Line Wind	20,447,943	20,334,594	44.0	43.9
Grant County Public Utility District	1,360,686	1,348,433	2.9	2.8
Grand Coulee Project Hydro Authority	3,531,066	5,963,960	29.1	27.6
Bonneville South Fork Tolt billing credit	(3,411,408)	(3,078,065)	-	-
British Columbia - Boundary Encroachment	-	-	1.9	2.6
Exchange energy - NCPA	3,188,694	381,652	6.3	0.7
Long-term purchased power booked out	(9,581,757)	(11,261,078)	(22.5)	(26.2)
	<u>\$ 220,194,583</u>	<u>\$ 210,239,486</u>	<u>782.2</u>	<u>770.9</u>

Power Exchanges—Northern California Power Agency (“NCPA”) and the Department executed a long-term Capacity and Energy Exchange Agreement in March 1993. The Department delivers a total of 90,580 MWh of exchange power to NCPA from June through October 15. NCPA returns a total of 91,584 MWh, or an option of 108,696 MWh under conditions specified in the contract at a 1.2:1 ratio of exchange power, from December through April. The agreement, which includes a financial settlement option, may be terminated beginning May 31, 2014 or annually on the same date thereafter with seven years’ advance written notice by either party. The effect of implementing SFAS No. 153, *Exchanges of Nonmonetary Assets - an amendment of APB Opinion No. 29*, on January 1, 2006, was to increase accounts receivable by \$3.7 million, revenues by \$2.4 million, and expense by \$0.2 million and to recognize deferred unrealized gain of \$1.5 million.

Estimated Future Payments Under Purchased Power and Transmission Contracts—The Department’s estimated payments under its contracts with Bonneville, the public utility districts, irrigation districts, Lucky Peak Project, British Columbia—High Ross Agreement, PacifiCorp Power Marketing, Inc. (now PPM Energy) and PacifiCorp for wind energy and net integration and exchange services, and for transmission with Bonneville, ColumbiaGrid, and others for the period from 2008 through 2065, undiscounted, are:

Years Ending December 31	Estimated Payments
2008	\$ 245,567,142
2009	259,813,091
2010	261,996,849
2011 ⁽¹⁾	217,720,792
2012	93,204,910
2013–2017	485,795,077
2018–2022	451,692,200
2023–2027 ⁽²⁾	213,507,254
2028–2032	33,138,332
2033–2037	33,556,166
2038–2042	9,535,584
2043–2065	<u>20,458,113</u>
Total	<u>\$2,325,985,510</u>

(1) Bonneville Block and Slice contract expires September 30, 2011.

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

The effects of changes that could occur to transmission as a result of FERC’s implementation of the Federal Power Act as amended August 8, 2005, are not known and are not reflected in the estimated future payments except for inclusion of costs associated with ColumbiaGrid. The Department executed an agreement in January 2007 with ColumbiaGrid, a non-profit membership corporation formed to improve the operational efficiency, reliability, and planned expansion of the Northwest transmission grid.

Payments under these long-term power contracts totaled \$230.8 million and \$231.2 million in 2007 and 2006, respectively. Payments under these transmission contracts totaled \$37.1 million and \$37.5 million in 2007 and 2006, respectively.

11. OTHER ASSETS

Seattle City Council passed resolutions authorizing the debt financing and/or deferral of certain costs in accordance with SFAS No. 71, *Accounting for the Effects of Certain Types of Regulation*. Unamortized charges for the deferral of contractual payments pursuant to the High Ross Agreement are being amortized to expense over 35 years through 2035 (see Note 10). Bonneville Slice contract true-up payments are deferred in the year invoiced and recognized as expense in the following year (See Note 10). Endangered Species Act costs are deferred and amortized to expense over the remaining license period (see Note 14).

Seattle City Council affirmed the Department's practice of deferring recognition of the effects of reporting the fair value of exchange contracts for rate making purposes and maintaining regulatory accounts to defer the accounting impact of these accounting adjustments, in Resolution 30942 adopted January 16, 2007 (see Note 10).

Underground electrical infrastructure costs for suburban jurisdictions will be recovered through rates from customers within the respective jurisdictions for a period of approximately 25 years after approval by the Seattle City Council. Programmatic conservation costs incurred by the Department and not funded by third parties are amortized to expense over 20 years. Capitalized relicensing and mitigation costs are deferred and amortized to expense over the remaining license period; or unamortized if incurred for future relicensing (see Note 14). The remaining components of other assets, excluding billable work in progress and real estate and conservation loans receivable, are being amortized to expense over 4 to 36 years.

Regulatory deferred charges and other assets net at December 31, 2007 and 2006, consisted of the following:

	2007	2006
Regulatory deferred charges:		
Deferred conservation costs—net	\$ 141,583,364	\$ 138,077,119
British Columbia - High Ross Agreement—net	75,815,265	66,941,824
Power exchange - regulatory deferred loss ⁽¹⁾	762,634	-
Bonneville Slice contract true-up payment ⁽¹⁾	-	10,895,754
Endangered Species Act—net ⁽¹⁾	2,128,461	2,194,463
	<u>2,891,095</u>	<u>13,090,217</u>
	<u>220,289,724</u>	<u>218,109,160</u>
Other deferred charges and assets—net:		
Regulatory deferred charges—net	2,891,095	13,090,217
Suburban infrastructure long-term receivables	21,559,438	3,494,000
Puget Sound Energy interconnection and substation	1,290,717	1,433,629
Studies, surveys, and investigations	675,269	967,578
Skagit Environmental Endowment	1,527,663	1,645,176
South Fork Tolt mitigation—net	372,716	263,827
Real estate and conservation loans receivable	34,129	280,540
Unamortized debt expense	6,497,250	7,244,364
General work-in-process to be billed	1,681,461	970,509
Other	251,117	180,652
	<u>36,780,855</u>	<u>29,570,492</u>
Capitalized relicensing costs:		
Skagit—net	19,301,824	19,051,042
Boundary—net	21,615,063	9,801,135
	<u>40,916,887</u>	<u>28,852,177</u>
Less: Regulatory deferred charges—net	<u>(2,891,095)</u>	<u>(13,090,217)</u>
Total Other Assets	<u>\$ 295,096,371</u>	<u>\$ 263,441,612</u>

(1) Amounts comprise regulatory deferred charges, net in other assets.

12. DEFERRED CREDITS

Seattle City Council passed resolutions authorizing deferral of certain credits in accordance with SFAS No. 71. Payments received from Bonneville for qualified conservation augmentation programs are amortized to revenues over the life of the 10-year contract that expires September 30, 2011. Other deferred credits are amortized to revenues as earned, except unrealized or deferred gains from fair valuations that expire at contract completion and deposits that are returned to customers.

Regulatory deferred credits and other credits at December 31, 2007 and 2006, consisted of the following:

	2007	2006
Regulatory deferred credits:		
Bonneville conservation augmentation	\$21,298,593	\$25,069,178
Deferred Bonneville Slice true-up credit	1,612,698	-
Unrealized gains from fair valuations of short-term forward electric energy transactions	191,192	6,489,208
Exchange energy: regulatory deferred gain	<u>438,162</u>	<u>460,854</u>
	<u>23,540,645</u>	<u>32,019,240</u>
Other credits:		
Deferred capital fees	8,423,428	4,642,695
Deferred revenues in lieu of rent for in-kind capital	566,551	551,599
Customer deposits—sundry sales	2,060,472	1,242,282
Deferred operations and maintenance revenues	491,065	463,880
Deferred revenues—other	<u>88,834</u>	<u>181,566</u>
	<u>11,630,350</u>	<u>7,082,022</u>
Total	<u>\$35,170,995</u>	<u>\$39,101,262</u>

13. PROVISION FOR INJURIES AND DAMAGES

The Department is self-insured for casualty losses to its property, including for terrorism, environmental cleanup, and 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 economic and social factors. Liabilities for lawsuits, claims, and workers' compensation were discounted over a period of 15 to 16 years in 2007 and 2006 at the City's average annual rate of return on investments, which was 5.075% in 2007 and 3.966% in 2006. Liabilities for environmental cleanup and for casualty losses to the Department's property do not include claims that have been incurred but not reported and are not discounted due to uncertainty with respect to regulatory requirements and settlement dates.

The Lower Duwamish Waterway was designated a federal Superfund site by the EPA in 2001 for contaminated sediments. The City is one of four parties who signed an Administrative Order on Consent with the EPA and State Department of Ecology to conduct a remedial investigation/feasibility study to prepare a site remedy. The Department is considered a potentially responsible party for contamination in the Duwamish River due to land ownership or use of property located along the river. The liability for the Lower Duwamish Waterway site was estimated at \$14.9 million and \$8.9 million for 2007 and 2006, respectively.

The changes in the provision for injuries and damages at December 31, 2007 and 2006, are as follows:

	2007	2006
Unpaid claims at January 1	\$22,197,296	\$ 18,387,556
Payments	(6,930,388)	(3,834,006)
Incurred claims	<u>12,514,943</u>	<u>7,643,746</u>
Unpaid claims at December 31	<u>\$27,781,851</u>	<u>\$ 22,197,296</u>

The provision for injuries and damages included in current and noncurrent liabilities at December 31, 2007 and 2006, is as follows:

	2007	2006
Noncurrent liabilities	\$19,684,951	\$ 12,260,522
Accounts payable and other	<u>8,096,900</u>	<u>9,936,774</u>
Total	<u>\$27,781,851</u>	<u>\$ 22,197,296</u>

14. 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. This lease was extended through December 2006. Beginning in 2007, the Department made monthly lease payments to the City through the central cost allocation process, similar to all other payments for tenancy of city property. The Department also leases office equipment and smaller facilities for various purposes through long-term operating lease agreements. Expense under all leases totaled \$6.9 million and \$4.4 million in 2007 and 2006, respectively.

Minimum payments under the operating leases are:

Year Ending December 31	Minimum Payments
2008	\$ 396,986
2009	170,185
2010	6,202
2011	<u>68</u>
Total	<u>\$ 573,441</u>

2008 Capital Program—The estimated financial requirement for the Department's 2008 program for capital improvement, conservation, and deferred operations and maintenance including required expenditures on assets owned by others is \$247.7 million. The Department has substantial contractual commitments relating thereto.

Application Process for New Boundary License—The Department's FERC license for the Boundary Project expires on September 30, 2011. The Department intends to submit an application for a new license by October 2009. Application process costs are estimated at \$57.6 million; as of December 31,

2007, \$23.0 million had been expended and deferred. A new license may require additional mitigation efforts for endangered species, including water quality standards, the full extent of which is not known at this time. Cost projections for new license requirements are not included in the forecast.

Skagit and South Fork Tolt Licensing Mitigation and Compliance—In 1995, the FERC issued a license for operation of the Skagit hydroelectric facilities through April 30, 2025. On July 20, 1989, the FERC license for operation of the South Fork Tolt hydroelectric facilities through July 19, 2029, became effective. As a condition for both of these licenses, the Department has taken and will continue to take required mitigating and compliance measures. Total Skagit mitigation costs, excluding Endangered Species Act (ESA) costs, from the effective date until expiration of the federal operating license were estimated at December 31, 2007, to be \$92.8 million, of which \$62.9 million had been expended. South Fork Tolt costs were estimated at \$4.2 million and \$1.1 million was expended through 2007. Capital improvement, other deferred costs, and operations and maintenance costs are included in the estimates for both licenses.

Endangered Species—Several fish species that inhabit waters where hydroelectric projects are owned by the Department, or where the Department purchases power, have been listed under the Endangered Species Act (ESA) as threatened or endangered. On the Columbia River System, the National Oceanographic Atmospheric Administration (NOAA) Fisheries has developed a broad species recovery plan for listed salmon and steelhead, including recommendations for upstream and downstream fish passage requirements. These requirements include minimum flow targets for the entire Columbia Basin designed to maximize the survival of migrating salmon and steelhead. As a result, the Department's power generation at its Boundary Project is reduced in the fall and winter when the region experiences its highest sustained energy demand. The Boundary Project's firm capability is also reduced.

In Puget Sound, bull trout and Chinook salmon were listed as threatened species in 1999 by U.S. Fish and Wildlife Service (USFWS) and NOAA Fisheries, respectively. In 2007, NOAA Fisheries also listed steelhead as threatened in the Puget Sound. These ESA listings affect City Light's Skagit, Tolt, and Cedar Falls hydroelectric projects. Bull trout are present in the waters of Skagit and Cedar River projects including the reservoirs, and are present in the Tolt River downstream of Tolt Reservoir. Chinook salmon and steelhead are present downstream of all these projects. A draft recovery plan and proposed critical habitat for Puget Sound bull trout was issued by the U.S. Fish and Wildlife Service in July 2004. The Puget Sound bull trout recovery plan is expected to be finalized by the USFWS in 2008. Critical habitat was designated for bull trout by the USFWS, and includes the Skagit, Tolt, and Cedar Rivers downstream of the City Light's projects. The City of Seattle's reservoirs (Ross, Diablo, Gorge, Tolt, and Chester Morse) were not designated as critical habitat for bull trout. The final recovery plan for Puget Sound Chinook salmon was developed by regional stakeholders under the authority of NOAA Fisheries and was adopted by NOAA Fisheries in January 2007. Critical habitat has been designated for Puget Sound Chinook salmon, and includes that mainstream rivers downstream of the City's hydroelectric projects. The recovery planning process for Puget Sound steelhead will be initiated by NOAA Fisheries in 2008. While it is unknown how other listings will affect the Department's hydroelectric projects and operations, the Department is carrying out an ESA Early Action program in cooperation with agencies, tribes, local governments, and salmon groups for bull trout, Chinook salmon, and steelhead. The Department has been participating in the implementation of the Chinook salmon recovery plan on both regional and watershed levels. On the Cedar, the Department's activities are covered by a Habitat Conservation Plan that authorizes operations with regard to all listed species. In addition to the ESA, hydroelectric projects must also satisfy the requirements of the Clean Water Act in order to obtain a FERC license. Total costs through 2011, estimated at December 31, 2007, for the ESA were \$34.7 million, of which \$30.1 million had been expended.

Project Impact Payments—Effective November 1999, the Department committed to pay a total of \$11.6 million and \$7.8 million over 10 years ending in 2008 to Pend Oreille County and Whatcom County, respectively, for impacts on county governments from the operations of the Department’s hydroelectric projects. The payments compensate the counties, and certain school districts and towns located in these counties, for loss of revenues and additional financial burdens associated with the projects. The Boundary Project located on the Pend Oreille River affects Pend Oreille County, and Skagit River hydroelectric projects affect Whatcom County. The combined impact compensation, including annual inflation factor of 3.1%, and retroactive payments totaled \$1.3 million and \$1.2 million to Pend Oreille County, and \$0.9 million and \$0.8 million to Whatcom County in 2007 and 2006, respectively.

Streetlight Litigation—In November 2003, the Washington Supreme Court invalidated a 1999 ordinance that included streetlight costs in the Department’s general rate base for Seattle and Tukwila customers. As a result, the Department resumed billing the City for streetlight costs. In May 2004, further proceedings resulted in a ruling that required the Department to refund the amount collected from ratepayers since December 1999 attributable to streetlight costs. The ruling also required the City of Seattle general fund to repay the Department for the streetlight costs that should have been billed over the same period. The judgment was entered in October 2004, and required the City’s general fund to pay approximately \$23.9 million to the Department, an amount representing billings for streetlight services that should have been made to the City from late December 1999 through November 2003. In addition, the judgment required the City’s general fund to pay approximately \$222,000 to the Department for “loss of use” of funds, calculated as a percentage of the difference between the amount that should have been billed to the City and the amount paid by ratepayers for streetlight services. Payments were due on an installment schedule and received accordingly.

The Department was to refund to ratepayers in Seattle and Tukwila the amount of streetlight costs billed to them from January 2000 through November 2003. Gross refunds were estimated to be \$21.5 million, plus \$2.6 million to compensate ratepayers for “loss of use” of funds. Plaintiffs’ attorney fees totaling \$3.3 million and \$0.7 million in administrative costs related to the refunds were deducted from the gross refund amount, leaving \$20.0 million to be refunded to ratepayers. All refunds to ratepayers were paid by December 2006, and in December 2006, \$3.5 million of remaining funds representing unclaimed streetlight refunds, was transferred to operations in accordance with the streetlight judgment.

Also in this partial judgment, the City’s One Percent for Art Ordinance was declared invalid as applied to the Department. The City appealed this ruling. On December 19, 2005, the Washington Court of Appeals reversed the trial court’s ruling that had declared the ordinance invalid as applied to the Department, but affirmed the trial court’s ruling that art funded by the Department must have a “sufficiently close nexus” to the Department’s purpose of providing electricity. Consequently in 2005, the Department recorded a reduction of \$1.0 million in the One Percent for Art assets to comply with the court’s ruling. During 2006, \$1.1 million plus interest was received from the City’s general fund.

In 2006, the State Supreme Court also has ruled that certain greenhouse gas offset contracts must be paid for by the City’s general fund, although the Court reconsidered that decision.

In 2007, the streetlight litigation ended with (a) the State Supreme Court’s denial of a motion for reconsideration of its decision that certain greenhouse gas offset contracts must be paid for by the City’s general fund, rather than the Department and (b) the Court of Appeals award of approximately \$1.3 million in attorney fees for causing the Department to change its ordinance governing certain utilities relocation expenses related to Sound Transit construction. The Department paid just over \$1.0 million of the award and another city of Seattle department the remainder.

Burns versus Seattle—In July 2005, a class action lawsuit, *Burns v. Seattle*, was filed against the City and five suburban cities (Shoreline, Tukwila, Burien, SeaTac, and Lake Forest Park) that have franchise agreements with the Department for the provision of retail electric service. In each franchise, the Department agreed to make a payment in exchange for the suburban city’s agreement not to establish its own municipal electric utility. The plaintiffs claimed that these payments were illegal “franchise fees” under RCW 35.21.860(1). In August 2007, the State Supreme Court upheld the payments, ending litigation.

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

- ***California refund case, appeals and related litigation***—In the proceeding before the Federal Energy Regulatory Commission (“FERC”), various public and private California entities (the “California Parties”) sought refunds in markets that had been created by the State of California. The Department had sold energy in one of these markets. The Department faced potential liability of approximately \$6.5 million, subject to offsets. In 2001, FERC ordered refunds to the extent that actual energy prices exceeded rates that FERC determined to be “just and reasonable.” On appeal, the Court of Appeals for the Ninth Circuit held that FERC has no authority to order governmental entities such as the Department to pay refunds. Following this ruling, the three major California investor-owned utilities sought refunds from the Department and other governmental entities in federal district court on a breach of contract theory. In March 2007, the court dismissed all claims. In April 2007, the three major California investor-owned utilities refilled their claims in state court. In December 2007, the trial court denied a request to dismiss the case.
- ***Pacific Northwest refund case and appeal***—In the proceeding before FERC, various sellers of energy, including the Department, sought refunds on energy sales in the Pacific Northwest between May 2000 and June 2001. The Department’s claims currently are in excess of \$100.0 million. In 2003, FERC declined to grant refunds on the grounds that there was no equitable way to do so. In August 2007, the Ninth Circuit held that FERC had abused its discretion in denying all refund relief in the Pacific Northwest, and remanded the case to FERC for further proceedings. In December 2007, various sellers of energy filed petitions for rehearing in the Ninth Circuit. The Ninth Circuit has yet to rule on those petitions.
- ***Grand Coulee Project Hydro Authority (GCPHA) Litigation***—The Department and the City of Tacoma (the “Cities”) are in an ongoing contract dispute with the GCPHA over the amount of incentive payments due to the GCPHA under five identical long-term power purchase contracts. The Cities each are responsible for half of the incentive payments.

The paid but disputed amount for contract years 2002 and 2003 (approximately \$5.4 million) was submitted to an arbitrator in May 2006. Thereafter, the GCPHA claimed approximately \$2.0 million for the 2004 contract year. The court prevented the GCPHA from collecting on that invoice while the arbitration proceeded, but required the Cities to deposit the 2004 disputed amount with the court. The GCPHA then claimed \$3.4 million in incentive payments for the 2005 contract year, and the Cities again were ordered to deposit that amount with the court. The arbitrator ultimately decided against the Cities on the 2002 and 2003 contract years, and the court denied the Cities request for refunds. Based on this decision, the court released the disputed \$5.4 million for contract years 2004 and 2005 to the GCPHA. The Cities have appealed the trial court’s decision to confirm the arbitrator’s decision.

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

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

15. SUBSEQUENT EVENTS

Global financial markets have endured extensive volatility over the first quarter of 2008 in response to the decline in the U.S. housing market since the summer of 2007. The result has been to the benefit of the City's cash pool, of which the Department has an equity in the pooled investments. The City's pool has strategically invested in internally researched and approved Asset Backed Commercial Paper (ABCP) programs that have provided above average yield to the pool and its participants. Given the short duration of the City's pool, the market's volatility has not had a significant impact on the market valuation of the City's investment holdings.

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APPENDIX D
DEMOGRAPHIC AND ECONOMIC INFORMATION

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DEMOGRAPHIC AND ECONOMIC INFORMATION

Seattle is the largest city in the Pacific Northwest and, as the County seat, is the center of King County's economic activity. King County is the largest county in the State in population, number of cities and employment, and the twelfth most populated county in the United States. Of the State's population, nearly 30 percent reside in King County, and of the County's population, 32 percent live in the City of Seattle.

Population

Historical and current population figures for the State of Washington, the County and the City are given below.

POPULATION

<u>Year</u>	<u>Washington</u>	<u>King County</u>	<u>Seattle</u>
1980 ⁽²⁾	4,130,163	1,269,749	493,846
1990 ⁽²⁾	4,866,692	1,507,319	516,259
2000 ⁽²⁾	5,894,121	1,737,034	563,374
2001 ⁽¹⁾	5,974,900	1,758,300	568,100
2002 ⁽¹⁾	6,041,700	1,774,300	570,800
2003 ⁽¹⁾	6,098,300	1,779,300	571,900
2004 ⁽¹⁾	6,167,800	1,788,300	572,600
2005 ⁽¹⁾	6,256,400	1,808,300	573,000
2006 ⁽¹⁾	6,375,600	1,835,300	578,700
2007 ⁽¹⁾	6,488,000	1,861,300	586,200
2008 ⁽¹⁾	6,587,600	1,884,200	592,800

(1) Source: State of Washington, Office of Financial Management

(2) Source: U.S. Department of Commerce, Bureau of Census

Per Capita Income

The following table presents per capita personal income for the Seattle Primary Metropolitan Statistical Area ("PMSA"), the County and the State.

	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>
Seattle PMSA	\$ 38,189	\$ 39,699	\$ 42,030	\$ 42,356	45,369
King County	44,153	44,704	49,533	48,789	52,655
State of Washington	32,573	33,166	35,289	35,838	38,212

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

Construction

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

BUILDING PERMIT VALUES

Year	New Single Family Units		New Multi Family Units		Total Value(\$)
	Number	Value(\$)	Number	Value(\$)	
2003	914	158,176,828	1,691	155,791,094	313,967,922
2004	754	129,729,132	2,790	227,540,589	357,269,721
2005	533	94,398,888	3,185	278,146,082	372,544,970
2006	482	90,534,640	5,538	597,085,138	687,619,778
2007	775	153,268,586	5,939	681,283,338	834,551,924

Source: U.S. Bureau of the Census

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)

<u>Year</u>	<u>The City of Seattle</u>	<u>King County</u>
2003	\$ 12,522,830	\$ 35,370,831
2004	12,868,301	37,253,104
2005	14,236,200	40,498,329
2006	15,564,363	43,993,479
2007	17,030,512	47,766,339
2008*	8,399,721	22,761,952

* Through second quarter only.

Source: Washington State Department of Revenue

Industry and Employment

**KING COUNTY
RESIDENT CIVILIAN LABOR FORCE AND EMPLOYMENT
AND NONAGRICULTURAL WAGE AND SALARY EMPLOYMENT***

	Annual Average				
	2003	2004	2005	2006	2007
Civilian Labor Force	992,400	994,800	1,012,940	1,047,740	1,070,870
Total Employment	930,500	943,420	965,940	1,005,240	1,031,700
Total Unemployment	61,900	51,380	47,000	42,500	39,170
Percent of Labor Force	6.2	5.2	4.6	4.1	3.7
NAICS INDUSTRY	2003	2004	2005	2006	2007
Total Nonfarm	1,111,641	1,119,167	1,143,675	1,176,683	1,198,392
Total Private	949,057	957,008	982,475	1,014,800	1,035,483
Goods Producing	164,228	163,667	170,850	183,108	188,125
Natural Resources and Mining	844	825	658	658	675
Construction	57,537	58,992	62,808	70,075	74,467
Manufacturing	105,858	103,392	106,900	112,367	113,000
Services Providing	947,413	955,950	973,300	993,583	1,010,258
Trade, Transportation and Utilities	222,110	222,700	222,858	224,283	224,125
Information	68,351	67,717	69,283	72,500	75,642
Financial Activities	78,468	77,242	76,467	77,567	76,908
Professional and Business Services	160,218	163,708	173,225	182,233	189,917
Employment Services	25,061	27,850	31,458	33,708	34,150
Educational and Health Services	114,908	118,142	122,750	124,717	127,300
Leisure and Hospitality	100,894	103,783	106,092	108,575	111,617
Other Services	39,888	40,533	41,392	41,808	41,842
Government	162,584	162,150	161,208	161,892	162,917
Workers in Labor/Management Disputes	67	83	850	8	0

* Columns may not add to totals due to rounding.

Source: Washington State Employment Security Department

The following table presents employment data for major employers in 2007 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**

Employer	Employees
The Boeing Company	71,400
Microsoft	33,100
University of Washington	24,400
Wal-Mart Stores	16,600
Naval Base Kitsap	15,300
Providence Health	14,800
King County	13,600
City of Seattle	12,000
Fred Meyer Stores	11,800
Alaska Air	8,000
Costco Wholesale Corp.	7,400
Weyerhaeuser	7,100
Washington Mutual	7,000
Group Health Cooperative	5,700
Bank of America	5,500
Macy's Northwest	5,400
Nordstrom	5,400
Quality Food Centers	5,400
Home Depot	5,200
Seattle School District	5,000

Sources: Puget Sound Book of Lists, 2008, and individual employers.

Other Issues

A variety of additional issues may have an effect on the Puget Sound area's economy, including but not limited to transportation infrastructure, endangered species listings, the commercial real estate market, and limits on residential development and resulting housing costs. 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. 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 bonds, 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, each in the aggregate principal amount of such maturity, and will be deposited with DTC.

DTC, the world’s largest securities 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 3.5 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments (from over 100 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 is the holding company for DTC, National Securities Clearing Corporation and Fixed Income Clearing Corporation, all of which are registered clearing agencies. DTCC is owned by the users of its regulated subsidiaries. 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 and www.dtc.org.

Purchases of Bonds under the DTC system 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.

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 within a maturity are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such maturity to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to Bonds unless authorized by a Direct Participant in accordance with DTC's MMI 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).

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, the Bond Registrar or the City, subject to any statutory or regulatory requirements as may be in effect from time to time. Payments to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) are 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 securities depository with respect to the Bonds at any time by giving reasonable notice to the City or the Bond Registrar. Under such circumstances, in the event that a successor depository is not obtained, Bond certificates are required to be printed and delivered.

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

The information in this appendix 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.

The Bond Registrar shall not be obligated to exchange or transfer any Bond during the 15 days preceding any principal or interest payment or redemption date.

The City and the Bond Registrar may treat DTC (or its nominee) as the sole and exclusive Registered Owner of the Bonds registered in such name for the purposes of payment of the principal of, premium, if any, or interest with respect to those Bonds, selecting Bonds or portions thereof to be redeemed, giving any notice permitted or required to be given to Registered Owners of Bonds under this ordinance or the Bond Resolution, registering the transfer of Bonds, obtaining any consent or other action to be taken by Registered Owners of Bonds, and for all other purposes whatsoever; and the City and the Bond Registrar shall not be affected by any notice to the contrary. The City and the Bond Registrar shall not have any responsibility or obligation to any direct or indirect DTC participant, any person claiming a beneficial ownership interest in the Bonds under or through DTC or any such participant, or any other person which is not shown on the Bond Register as being a Registered Owner of Bonds, with respect to: (i) the Bonds; (ii) any records maintained by DTC or any such participant; (iii) the payment by DTC or such participant of any amount in respect of the principal of, premium, if any, or interest with respect to the Bonds; (iv) any notice which is permitted or required to be given to Registered Owners of Bonds under this ordinance or the Bond Resolution; (v) the

selection by DTC or any such participant of any person to receive payment in the event of a partial redemption of the Bonds; or (vi) any consent given or other action taken by DTC as Registered Owner of the Bonds.