

**CITY OF SANTA CLARA  
ELECTRIC UTILITY ENTERPRISE FUND  
(SILICON VALLEY POWER)  
FINANCIAL STATEMENTS**



**FOR THE YEARS ENDED JUNE 30, 2010 AND 2009  
CITY OF SANTA CLARA, CALIFORNIA  
1500 WARBURTON AVENUE  
SANTA CLARA, CA 95050-3796**

**PREPARED BY DEPARTMENT OF FINANCE**



**CITY OF SANTA CLARA ELECTRIC UTILITY ENTERPRISE FUND  
(SILICON VALLEY POWER)**

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**INDEPENDENT AUDITORS' REPORT**

Honorable Mayor and City Council  
City of Santa Clara  
Santa Clara, California

We have audited the accompanying statements of net assets of the City of Santa Clara, California, Electric Utility Enterprise Fund (Silicon Valley Power) as of and for the years ended June 30, 2010 and 2009, and the related statements of revenues, expenses, and changes in net assets, and cash flows for the years then ended, as listed in the table of contents, which collectively comprise the basic financial statements. These financial statements are the responsibility of the City's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free of material misstatement. An audit includes examining on a test basis evidence supporting the amounts and disclosures in the fund financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1, the financial statements of Silicon Valley Power are intended to present the financial position, and the changes in financial position and cash flows, of only that portion of the business-type activities of the City of Santa Clara that is attributable to the transactions of the Electric Utility Enterprise Fund. It does not purport to, and does not present fairly the financial position of the City as of June 30, 2010 and 2009, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America

In our opinion the financial statements referred to above present fairly in all material respects the financial position of Silicon Valley Power as of June 30, 2010 and 2009, and the results of its operations and its cash flows for the years then ended, in conformity with generally accepted accounting principles in the United States of America.

As described in Note 2B and Note 5E to the financial statements, Silicon Valley Power adopted the provisions of GASB Statement No. 53, *Accounting and Financial Reporting for Derivatives Instruments*, in fiscal year ended June 30, 2010.

Management's Discussion and Analysis is not a required part of the financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. 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.

*Vavrinek, Trine, Day & Co., LLP.*

Pleasanton, California  
December 28, 2010

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## **MANAGEMENT'S DISCUSSION AND ANALYSIS**

This section of the Silicon Valley Power financial statements presents a narrative overview and analysis of the financial activities for the fiscal year. Please read this document in conjunction with the accompanying Basic Financial Statements.

Silicon Valley Power is a separate enterprise fund of the City of Santa Clara, and was established to account for the electric power transactions of the City of Santa Clara. Silicon Valley Power owns power generation facilities, has investments in joint ventures that produce electric power, and trades power on the open market. These efforts are directed toward ensuring its retail customers—the citizens, organizations and businesses of the City of Santa Clara—have a reliable source of electric power at reasonable rates.

Silicon Valley Power has been affected by the deregulation of the electric power industry in California, as discussed in detail in Note 7 to its financial statements.

### **OVERVIEW OF SILICON VALLEY POWER'S BASIC FINANCIAL STATEMENTS**

The Basic Financial statements are in two parts:

- 1) Management's Discussion and Analysis (this part),
- 2) The Basic Financial Statements, which include the entity-wide Financial Statements, along with the Notes to these financial statements.

The Basic Financial Statements comprise the entity-wide Financial Statements. These financial statements provide both a short-term and a long-term view of Silicon Valley Power's financial activities and financial position.

The entity-wide Financial Statements are comprised of the Statement of Net Assets and the Statement of Revenues, Expenses and Changes in Net Assets. The Statement of Net Assets provides information about the financial position of Silicon Valley Power as a whole, including all its long-term liabilities on the full accrual basis. The Statement of Revenues, Expenses and Changes in Net Assets provides information about all Silicon Valley Power's revenues and all its expenses, also on the full accrual basis, with the emphasis on measuring net revenues or expenses of the program.

## FISCAL YEAR 2009-10 FINANCIAL HIGHLIGHTS—ENTITY-WIDE AND FUND BASIS

The following is summarized financial information from the Statements of Net Assets (Table 1) and the Statements of Revenues, Expenses and Changes in Net Assets (Table 2).

**Table 1**  
**Net Assets**  
**June 30, 2010 and 2009**  
**(in millions)**

<u>Description</u>			<u>Increase (Decrease)</u>		<u>2008</u>
	<u>2010</u>	<u>2009</u>	<u>Amount</u>	<u>%</u>	
Cash and investments	\$ 244.9	\$ 275.6	\$ (30.7)	-11.1%	\$ 345.4
Other assets	97.7	75.1	22.6	30.1%	93.1
Capital assets	487.4	483.6	3.8	0.8%	463.8
Total Assets	<u>830.0</u>	<u>834.3</u>	<u>(4.3)</u>	-0.5%	<u>902.3</u>
Long-term debt outstanding (including current portion)	229.4	227.6	1.8	0.8%	223.1
Other liabilities	<u>26.4</u>	<u>27.4</u>	<u>(1.0)</u>	-3.6%	<u>53.0</u>
Total Liabilities	<u>255.8</u>	<u>255.0</u>	<u>0.8</u>	0.3%	<u>276.1</u>
Net Assets:					
Invested in capital assets, net of debt	286.7	278.9	7.8	2.8%	250.3
Restricted for projects	-	-	-		11.3
Unrestricted	<u>287.5</u>	<u>300.4</u>	<u>(12.9)</u>	-4.3%	<u>364.6</u>
Total Net Assets	<u>\$ 574.2</u>	<u>\$ 579.3</u>	<u>\$ (5.1)</u>	-0.9%	<u>\$ 626.2</u>

**Table 2**  
**Revenues, Expenses and Changes in Net Assets**  
**For the years ended June 30, 2010 and 2009**  
**(in millions)**

<u>Description</u>			<u>Increase (Decrease)</u>		<u>2008</u>
	<u>2010</u>	<u>2009</u>	<u>Amount</u>	<u>%</u>	
Revenues:					
Retail	\$ 252.5	\$ 243.9	\$ 8.6	3.5%	\$ 240.1
Wholesale	67.8	102.5	(34.7)	-33.9%	172.4
Interest Revenue	7.8	10.2	(2.4)	-23.5%	15.6
Net increase (decrease) in fair value of investment	(0.2)	9.6	(9.8)	-102.1%	1.1
Rents and royalties	2.7	2.9	(0.2)	-6.9%	2.5
Other	<u>18.3</u>	<u>13.0</u>	<u>5.3</u>	40.8%	<u>9.0</u>
Total Revenues	<u>348.9</u>	<u>382.1</u>	<u>(33.2)</u>	-8.7%	<u>440.7</u>
Expenses:					
Retail	262.2	300.0	(37.8)	-12.6%	276.1
Wholesale	73.7	110.9	(37.2)	-33.5%	178.0
Interest on long term debt	8.5	9.9	(1.4)	-14.1%	11.8
Other	<u>8.9</u>	<u>7.5</u>	<u>1.4</u>	18.7%	<u>6.3</u>
Total Expenses	<u>353.3</u>	<u>428.3</u>	<u>(75.0)</u>	-17.5%	<u>472.2</u>
Increase (decrease) in net assets before transfers	(4.4)	(46.2)	41.8	90.5%	(31.5)
Transfers in (out)	<u>(0.7)</u>	<u>(0.7)</u>	<u>-</u>	0.0%	<u>(0.7)</u>
Increase (decrease) in net assets	<u>(5.1)</u>	<u>(46.9)</u>	<u>41.8</u>	89.1%	<u>(32.2)</u>
Net Assets - July 1	579.3	626.2	(46.9)	-7.5%	658.4
Net Assets - June 30	<u>\$ 574.2</u>	<u>\$ 579.3</u>	<u>\$ (5.1)</u>	-0.9%	<u>\$ 626.2</u>



Silicon Valley Power retail operating revenues were \$252.5 million in fiscal year 2009-10, \$243.9 million in fiscal year 2008-09, and \$240.1 million in fiscal year 2007-08, reflecting increases of approximately 3.5%, and 1.6% from fiscal years 2008-09 and 2007-08, respectively. The main reason for the increase in fiscal year 2009-10 was higher power consumption by the industrial sector combined with an increase in utility rates of 7% in January 2010.

In December 2008, the City Council adopted a 7% rate increase to be effective January 2010. The primary reason for this increase was a rise in cost and use of fuel for electric generation, combined with a significant reduction in energy available from Western Power Administration.

Retail operating expenses were \$262.2 million in fiscal year 2009-10, \$300.0 million in fiscal year 2008-09, and \$276.1 million in fiscal year 2007-08, a decrease of \$37.8 million or 12.6% and an increase of \$23.9 million or 8.7% from fiscal years 2008-09 and 2007-08, respectively. The operating expenses for fiscal year 2009-10 were lower primarily due to decreases in the price of purchased power.

Revenues from wholesale power sales of electricity were \$67.8 million in fiscal year 2009-10, \$102.5 million in fiscal year 2008-09, and \$172.4 million in fiscal year 2007-08. Concurrently, the cost of wholesale power purchases was \$73.7 million in current fiscal year, \$110.9 million in fiscal year 2008-09, and \$178.0 million in fiscal year 2007-08. The wholesale power market has stabilized in recent years compared to the peak years of the power crisis experienced by California in 2001, resulting in a lower level of wholesale power transactions.

Interest revenues were \$7.8 million in fiscal year 2009-10, \$10.2 million in fiscal year 2008-09, and \$15.6 million in fiscal year 2007-08. The decrease in the current fiscal year is primarily due to lower cash reserves and a lower interest rate environment resulting from the severe decline in the stock market compared to the prior year. Interest expense was \$8.5 million in fiscal year 2009-10, \$9.9 million in fiscal year 2008-09, and \$11.8 million in fiscal year 2007-08.

The Electric Utility Fund is a participant in a number of joint ventures such as Northern California Power Agency (NCPA), the Transmission Agency of Northern California (TANC), M-S-R Public Power Agency (MSR PPA), and M-S-R Energy Authority (MSR EA). The Electric Utility Fund had \$574.2 million in net assets at June 30, 2010, a decrease of \$5.1 million from the prior fiscal year. Of this amount, \$286.7 million was invested in capital assets, net of related debt; \$287.5 million was unrestricted. At June 30, 2009, the Electric Utility Fund had \$579.3 million in net assets, a decrease of \$46.9 million from fiscal year 2007-08.

## **CAPITAL ASSETS**

At the end of fiscal year 2009-10, Silicon Valley Power had \$487.4 million, net of depreciation, invested in capital assets, with a significant amount in power generation facilities and the remainder in transmission and distribution assets. At June 30, 2010, Silicon Valley Power had various projects completed or under construction. In the fiscal year 2009-10, the Capital Improvement Projects Budget included appropriations for significant investments in substation improvements in the coming years.

Further detail may be found in Note 4 to the financial statements.

## **DEBT ADMINISTRATION**

Each of Silicon Valley Power's debt issues is discussed in detail in Note 5 to the financial statements. At June 30, 2010, Silicon Valley Power's debt is comprised of four issues of Revenue Bonds with outstanding principal balances of \$216.1 million at that date. These Bonds are secured by electric revenues earned by Silicon Valley Power, and mature in fiscal years 2010 through 2035. Details of each of these Bond issues may be found in Note 5 to the financial statements.

## **ECONOMIC OUTLOOK AND MAJOR INITIATIVES**

The economy of the City of Santa Clara and its major initiatives for the coming year are discussed in detail in the Letter of Transmittal Section of the City's Comprehensive Annual Financial Report for the year ended June 30, 2010.

## **CONTACTING SILICON VALLEY POWER'S FINANCIAL MANAGEMENT**

These Basic Financial Statements are intended to provide citizens, taxpayers, investors, and creditors with a general overview of the Silicon Valley Power's finances. Questions about these Statements should be directed to the City of Santa Clara Finance Department, at 1500 Warburton Avenue, Santa Clara, CA 95050-3796.

**CITY OF SANTA CLARA ELECTRIC UTILITY ENTERPRISE FUND**  
**(SILICON VALLEY POWER)**  
**STATEMENTS OF NET ASSETS**  
**June 30, 2010 and 2009**

<b>ASSETS</b>	<b>2010</b>	<b>2009</b>
Current Assets:		
Pooled cash and investments (Note 3)	\$ 229,346,225	\$ 260,440,115
Investments with fiscal agent (Note 3)	6,102,700	6,496,311
Receivables (net of allowances)		
Accounts	38,112,605	29,959,181
Interest	1,245,156	1,833,177
Due from other funds of the City of Santa Clara (Note 2D)	1,578,822	1,650,713
Inventory of material and supplies (Note 2E)	9,855,579	9,660,245
Total Current Assets	<u>286,241,087</u>	<u>310,039,742</u>
Noncurrent Assets:		
Capital assets (Note 4)		
Land	13,550,593	13,550,593
Buildings, improvements and infrastructure	716,023,620	705,679,096
Equipment	9,373,978	8,800,479
Construction in progress	33,055,642	23,477,266
Accumulated depreciation	<u>(284,605,185)</u>	<u>(267,898,076)</u>
Total Capital assets (Net of accumulated depreciation)	<u>487,398,648</u>	<u>483,609,358</u>
Other Noncurrent Assets:		
Investments in joint ventures (Note 6)	27,548,159	19,518,302
Investments with fiscal agent (Note 3)	9,363,860	8,688,289
Deposits	6,440,983	2,492,448
Deferred inflow of resources (Note 5)	10,867,835	7,714,294
Other assets	<u>2,147,509</u>	<u>2,261,735</u>
Total Other Noncurrent Assets	<u>56,368,346</u>	<u>40,675,068</u>
Total Noncurrent Assets	<u>543,766,994</u>	<u>524,284,426</u>
Total Assets	<u>830,008,081</u>	<u>834,324,168</u>
<b>LIABILITIES</b>		
Current Liabilities:		
Accrued liabilities	22,895,706	22,149,128
Interest payable	2,100,409	2,411,536
Deposit liability	230,073	258,531
Accrued compensated absences	321,972	295,119
Derivative instrument - power purchase hedge (Note 5)	850,112	-
Current portion of long-term debt (Note 5)	<u>4,425,000</u>	<u>4,220,000</u>
Total Current Liabilities	<u>30,823,272</u>	<u>29,334,314</u>
Noncurrent Liabilities:		
Long-term portion accrued compensated absences	2,417,460	2,265,952
Long-term debt (Note 5)	211,698,043	215,715,240
Derivative instrument - interest rate swap (Note 5)	<u>10,867,835</u>	<u>7,714,294</u>
Total Noncurrent Liabilities	<u>224,983,338</u>	<u>225,695,486</u>
Total Liabilities	<u>255,806,610</u>	<u>255,029,800</u>
<b>NET ASSETS</b>		
Invested in capital assets, net of related debt	286,742,165	278,858,718
Unrestricted net assets	<u>287,459,306</u>	<u>300,435,650</u>
Total Net Assets	<u>\$ 574,201,471</u>	<u>\$ 579,294,368</u>

See accompanying notes to the financial statements

**CITY OF SANTA CLARA ELECTRIC UTILITY ENTERPRISE FUND  
(SILICON VALLEY POWER)  
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS  
For the years ended June 30, 2010 and 2009**

	<u>2010</u>	<u>2009</u>
Operating Revenues:		
Residential sales	\$ 22,350,425	\$ 21,039,109
Commercial sales	13,112,366	12,547,952
Industrial sales	215,498,767	208,814,890
Other operating revenues	1,556,843	1,486,834
Total Operating Revenues	<u>252,518,401</u>	<u>243,888,785</u>
Operating Expenses:		
Operations	52,903,894	50,344,849
Maintenance	10,516,756	9,281,142
Purchased power	180,893,020	222,466,997
Amortization	877,997	1,180,342
Depreciation	16,985,674	16,686,160
Total Operating Expenses	<u>262,177,341</u>	<u>299,959,490</u>
Operating Income (Loss)	(9,658,940)	(56,070,705)
Nonoperating Revenues (Expenses):		
Interest revenue	7,775,597	10,169,358
Net increase (decrease) in the fair value of investments	(169,237)	9,558,379
Interest expense	(8,546,949)	(9,859,859)
Wholesale resources sales (Note 7)	67,839,812	102,480,126
Wholesale resources purchases (Note 7)	(73,727,274)	(110,879,043)
Equity in income (losses) of joint ventures	1,736,243	1,223,202
Rents and royalties	2,735,236	2,866,152
Mandated program receipts and other revenues	16,579,906	11,760,520
Loss on retirement of assets	(148)	(187)
Mandated program disbursements and other expenses	(8,907,300)	(7,518,113)
Total Nonoperating Revenues, net	<u>5,315,886</u>	<u>9,800,535</u>
Income (Loss) Before Transfers	<u>(4,343,054)</u>	<u>(46,270,170)</u>
Transfers Out	<u>(749,843)</u>	<u>(678,814)</u>
Net Income (Loss)	(5,092,897)	(46,948,984)
Net Assets, Beginning of Year	<u>579,294,368</u>	<u>626,243,352</u>
Net Assets, End of Year	<u>\$ 574,201,471</u>	<u>\$ 579,294,368</u>

See accompanying notes to the financial statements

**CITY OF SANTA CLARA ELECTRIC UTILITY ENTERPRISE FUND  
(SILICON VALLEY POWER)  
STATEMENTS OF CASH FLOWS  
For the years ended June 30, 2010 and 2009**

	<u>2010</u>	<u>2009</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Receipts from customers	\$ 252,627,125	\$ 242,563,001
Payments to suppliers	(238,347,133)	(265,800,387)
Payments to employees	(19,787,185)	(17,972,269)
Other receipts	9,709,169	4,107,900
Net Cash from Operating Activities	<u>4,201,976</u>	<u>(37,101,755)</u>
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES</b>		
Wholesale resources sales	67,839,812	102,480,126
Wholesale resources purchases	(73,727,274)	(110,879,043)
(Provision) reduction for disputed SCS charges	-	4,441,776
Increase (decrease) in due from other funds	71,891	69,292
Wholesale trading escrow	(1,532,968)	-
Transfers (out)	(749,843)	(678,814)
Cash Flows from Noncapital Financing Activities	<u>(8,098,382)</u>	<u>(4,566,663)</u>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>		
Acquisition and construction of capital assets, net	(22,627,879)	(33,788,545)
Principal payments on debt	(4,220,000)	(3,580,000)
Interest paid on debt	(8,272,213)	(9,089,498)
Cash Flows from Capital and Related Financing Activities	<u>(35,120,092)</u>	<u>(46,458,043)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Rents and royalties received	2,425,753	2,901,165
Interest and dividends	5,948,052	9,148,336
Net increase (decrease) in the fair value of investments	(169,237)	9,558,379
Payments made by fiscal agent	8,802,125	10,232,635
Deposits made with fiscal agent	(9,084,085)	(15,800,964)
Cash Flows from Investing Activities	<u>7,922,608</u>	<u>16,039,550</u>
Net Decrease in Cash and Cash Equivalents	(31,093,890)	(72,086,911)
Cash and cash equivalent at Beginning of Period	<u>260,440,115</u>	<u>332,527,026</u>
Cash and cash equivalent at End of Period	<u>\$ 229,346,225</u>	<u>\$ 260,440,115</u>
<b>Reconciliation of Operating Loss to Net Cash Provided (Used) by Operating activities:</b>		
Operating loss	\$ (9,658,940)	\$ (56,070,705)
Adjustments to reconcile operating income to net cash provided (used) by operating activities:		
Amortization	877,997	1,180,342
Depreciation	16,985,674	16,686,160
Change in assets and liabilities:		
Receivable, net	(14,167,876)	25,365,366
Inventory	(959,105)	155,068
Accrued liabilities	3,273,259	(29,004,714)
Compensated absences	178,361	344,321
Other receipts	16,579,906	11,760,520
Other expenses	(8,907,300)	(7,518,113)
Net Cash Provided (Used) by Operating Activities	<u>\$ 4,201,976</u>	<u>\$ (37,101,755)</u>
<b>NONCASH TRANSACTIONS:</b>		
Joint Ventures		
Nonoperating Income (Expense)	<u>\$ 1,736,243</u>	<u>\$ 1,223,202</u>

See accompanying notes to the financial statements

**CITY OF SANTA CLARA ELECTRIC UTILITY ENTERPRISE FUND  
(SILICON VALLEY POWER)  
NOTES TO FINANCIAL STATEMENTS**

**For the years ended June 30, 2010 and 2009**

**NOTE 1 – DEFINITION OF THE REPORTING ENTITY**

The City of Santa Clara, California's Electric Utility Enterprise Fund, which began operating as Silicon Valley Power (SVP) in 1999, commenced operations over 100 years ago in 1896. Originally, Silicon Valley Power constructed a lighting plant consisting of forty-six 2000 candlepower direct current lamps and a dynamo (a type of electric generator) which entered into service in October 1896. In late 1903, Silicon Valley Power invested \$5,000 to convert the system to alternating current and abandoned the small generating plant. Wholesale power was purchased from United Gas and Electric Company of San Jose.

Between 1903 and 1965, Silicon Valley Power purchased all of its electric power requirements from investor owned utilities. In 1965, it received an allocation of power from the Federal Central Valley Project and began to diversify its resources. Silicon Valley Power became a charter member of the Northern California Power Agency (NCPA) in June 1968. Throughout the 1970's, Silicon Valley Power and NCPA worked on behalf of all municipal electric utilities in Northern California to gain access to wholesale transmission markets and to jointly develop cost-effective electric generation resources.

In 1980, Silicon Valley Power became a generating utility for the first time in 73 years with the start of operations of the 6-Megawatt Cogen No. 1 power plant. In 1983, the 110 Megawatt NCPA Geothermal Project, the first municipally owned and operated geothermal power plant in the United States, entered service with Silicon Valley Power as lead partner holding a 55% participation share. Subsequently, Silicon Valley Power participated in further jointly owned power generation projects including hydroelectric, natural gas and coal fired generation. In 2005, SVP placed the 147 Megawatt Don Von Raesfeld Power Plant into service.

Today, Silicon Valley Power has grown to approximately 7,990 streetlights and serves approximately 52,364 electric customers. As Silicon Valley Power looks to the future, it is preparing for the new competitive electric market by further streamlining its operations, and working with its customers to enhance the value they receive from municipal ownership of their electric utility.

**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**A. Basis of Presentation**

Silicon Valley Power's Financial Statements are prepared in conformity with accounting principles generally accepted in the United States of America. The Government Accounting Standards Board (GASB) is the acknowledged standard setting body for establishing accounting and financial reporting standards followed by governmental entities in the United States of America. The electric enterprise fund is included in the City of Santa Clara's (the City) Comprehensive Annual Financial Report, and therefore, these financial statements do not purport to represent the financial position and changes in financial position of the City.

**CITY OF SANTA CLARA ELECTRIC UTILITY ENTERPRISE FUND  
(SILICON VALLEY POWER)  
NOTES TO FINANCIAL STATEMENTS**

**For the years ended June 30, 2010 and 2009**

**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**B. Basis of Accounting**

Silicon Valley Power reports its activities as a proprietary fund type (Enterprise Fund) which is maintained on the accrual basis of accounting wherein revenues are recognized in the accounting period in which they are earned regardless of whether they are received, and expenses are recognized in the period in which the related liabilities are incurred. Certain indirect costs are included in program expenses reported for individual functions and activities. Silicon Valley Power has elected under GASB Statement No. 20 Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting to apply all applicable GASB pronouncements, as well as any applicable pronouncements of the Financial Accounting Standards Board (FASB), the Accounting Principles Board, or any Accounting Research Bulletins issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

During fiscal year 2009-10 Silicon Valley Power implemented the following GASB Statements: Statements No. 51 “Accounting and Financial Reporting for Intangible Assets.” which requires that all intangible assets not specifically excluded by its scope provisions be classified as capital assets. This statement became effective July 1, 2009 for the City and did not result in a financial impact on the financial statements.

In FY 09-10, SVP implemented Statement No. 53 “Accounting and Financial Reporting for Derivative Instruments” which requires governments to measure and report most derivative instruments at fair value on the statement of net assets, and gains (losses) be reported on the statement of revenues, expenses and change in fund net assets. Under hedge accounting, gains (losses) are reported on the statement of net assets as deferred (inflows) outflows of resources until termination, at which time the deferred amounts are reported as an adjustment to the underlying hedged transaction. In accordance with approved risk management policies, SVP uses derivative instruments to manage its exposure to pricing fluctuations. SVP also uses derivative instruments to hedge its exposure to changing interest rates through the use of an interest rate swap. In FY09-10, all SVP hedges were deemed effective. The hedge contracts on power purchases are recognized as a reduction (increase) in the purchase power cost on the statement of revenues, expenses and change in fund net assets and are shown on the statement of net assets as short term derivative instrument. The interest rate hedges are shown as noncurrent deferred inflow of resources and long term derivative instruments (refer to Note 5).

The GASB issued Statement No. 57 “OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans” which related to the use of the alternative measurement method and the frequency and timing of measurement by employers that participate in agent multiple-employer other postemployment benefits plans. This statement becomes effective June 15, 2011.

**C. Measurement Focus**

Enterprise funds are accounted for on a cost of services or economic resources measurement focus, which means that all liabilities associated with the activity are included on their Statement of Net Assets. Enterprise fund type operating statements present increases (revenues) and decreases (expenses) in total net assets. Reported net assets are segregated into three categories – invested in capital assets net of related debt, restricted and unrestricted.

**CITY OF SANTA CLARA ELECTRIC UTILITY ENTERPRISE FUND  
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**For the years ended June 30, 2010 and 2009**

**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**D. Cash and Investments**

Silicon Valley Power's cash and investments pool is maintained by the City of Santa Clara except for fiscal agent cash and investments.

While maintaining safety and liquidity, the City maximizes investment return by pooling its available cash for investment purposes. Unless there are specific legal or contractual requirements to do otherwise, interest earnings are apportioned among funds according to average monthly cash and investment balances. It is generally the City's intention to hold investments until maturity. City investments are stated at fair value (see Note 3).

Cash and cash equivalents for purposes of the statement of cash flows include pooled cash and investments and cash designated for construction. Transactions with City-wide cash management pools are similar to those with external investment pools; therefore, since pooled cash and investments have the same characteristics as demand deposits in that the City's individual funds and component units may withdraw additional monies at any time without prior notice or penalty, pooled cash and investments are considered essentially demand deposit accounts.

Cash and investments with fiscal agent, a bond reserve investment pool, and amounts classified as deposits are not considered cash and cash equivalents.

**E. Due from City of Santa Clara**

During the course of operations, transactions occur between Silicon Valley Power and the City for goods provided or services rendered. The related receivables, net, are classified as "Due from other funds of the City of Santa Clara" on the accompanying statement of net assets.

**F. Inventory of Materials and Supplies**

Inventory of materials and supplies is accounted for using the consumption method and is stated at average cost. Inventory consists of expendable supplies held for consumption by the electric utility.

**G. Capital Assets**

All capital assets with a value of \$5,000 or more with useful lives exceeding two years, are capitalized. These assets are valued at historical cost or estimated historical cost if actual historical cost is not available. Contributed capital assets are valued at their estimated fair value on the date contributed. Depreciation is recorded on a straight-line basis over the estimated useful lives of the assets (buildings and improvements: 20 to 50 years; and equipment: 3 to 25 years) and is charged as an expense against operations. Accumulated depreciation is reported on the statement of net assets.

The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized. Improvements are capitalized and depreciated over the remaining useful lives of the related capital assets.



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**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

Capital assets and the related obligations under lease/purchase agreements are capitalized and accounted for in accordance with FASB's Statement of Financial Accounting Standards (SFAS) No. 13 Accounting for Leases. Interest is capitalized on construction in progress in accordance with SFAS No. 62, Capitalization of Interest Cost in Situations Involving Certain Tax-Exempt Borrowings, and Certain Gifts and Grants. Accordingly, interest capitalized is the total interest cost for the date of the borrowings net of any interest earned on temporary investments of the borrowed proceeds until the specified asset is ready for its intended use. There was no interest capitalized for the fiscal year ended June 30, 2010.

**H. Joint Ventures**

Silicon Valley Power participates in several joint ventures, and in accordance with GASB Statement No. 14, The Financial Reporting Entity, investments in these joint ventures are accounted for using the equity method, when appropriate. If Silicon Valley Power's equity in net losses of a joint venture exceeds its investments, use of the equity method is suspended except to the extent that Silicon Valley Power is obligated to provide further support or has guaranteed obligations of the joint venture.

Silicon Valley Power advances funds to certain of its joint ventures in the form of refundable advances, project advances, and operating and maintenance advances. Refundable advances accrue interest at rates stated in the related agreements. Operating, maintenance, and project advances are charged to operations when incurred.

Capitalized project costs are charged to operations in the event that a project is determined to be not economically feasible.

**I. Compensated Absences**

Vested or accumulated vacation leave and benefits are recorded as an expense and liability as the benefits accrue to the employees. Vacation pay accruals generally do not exceed the amount earned for one year, however, an employee may accumulate vacation pay earned, but not for more than two years.

In accordance with the provisions of GASB Statement No. 16, Accounting for Compensated Absences, a liability for sick leave and benefits is accrued using the vesting method. The vesting method provides that a governmental entity estimate its accrued sick leave liability based on the sick leave accumulated at the statement of net assets date by those employees who currently are eligible to receive termination payments as well as other employees who are expected to become eligible in the future to receive such payments. Estimated sick leave payments are recorded as an expense and liability by Silicon Valley Power.

**J. Risk Management**

Silicon Valley Power is covered under the City's self-insurance programs. Additional information with respect to the City's self-insurance programs can be found in the City's Comprehensive Annual Financial Report (CAFR).

**CITY OF SANTA CLARA ELECTRIC UTILITY ENTERPRISE FUND  
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**For the years ended June 30, 2010 and 2009**

**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**K. Electric Power Purchased**

Silicon Valley Power purchases power from various suppliers and agencies (including joint powers agencies) for resale to its customers (see Note 8). Silicon Valley Power also engages in numerous wholesale power transactions with the objective of reducing its overall cost of purchased power. Gross wholesale power sales and wholesale power purchases are recorded as nonoperating revenue and expense, respectively (see Note 7).

**L. Bond Discounts/Issuance Costs**

Bond discounts are presented as a reduction of the face amount of bonds payable, whereas issuance costs are recorded as deferred charges.

**M. Revenue Recognition**

Operating revenues are recognized based on cycle billings periodically rendered to customers. Operating revenues for services provided, but not billed at the end of the fiscal year, are recognized and accrued based on estimated consumption. Operating revenues primarily include the sales of electric power to residential, commercial, industrial, and municipal customers.

Non-operating revenues primarily represents wholesale resources sales, interest income, public benefit charge revenues, grants, rents, and other non-recurring miscellaneous income.

**N. Taxes on Income**

As an agency of the City, Silicon Valley Power falls under the review of the Internal Revenue Code Section 115 and corresponding California Revenue and Taxation Code provisions. As such, it is not subject to federal income or state franchise taxes.

**O. Net Assets and Fund Equity**

Silicon Valley Power may fund certain programs with a combination of restricted and unrestricted net assets. The policy is to first apply restricted net assets followed by unrestricted net assets if necessary.

**P. Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

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**NOTE 3 – CASH AND INVESTMENTS**

Silicon Valley Power's cash and investments pool is maintained by the City of Santa Clara except for fiscal agent cash and investments.

**A. Investments Authorized by the California Government Code and the City's Investment Policy**

The City's Investment Policy and the California Government Code allow the City to invest in certain types of investments, provided the credit ratings of the issuers are acceptable to the City. The table below also identifies certain provisions of the City's Investment Policy and the California Government Code that address interest rate risk, credit risk, and concentration of credit risk.

<u>Authorized Investment Type</u>	<u>Maximum Maturity</u>	<u>Minimum Credit Quality</u>	<u>Maximum Percentage or Portfolio</u>	<u>Maximum Investment In One Issuer</u>
U.S. Treasury Obligations	5 years	Top three ratings categories	None	None
U.S. Agency Securities (A)	5 years	Top three ratings categories	None	None
Negotiable Certificates of Deposit	5 years	N/A	30%	None
Bankers Acceptances	180 days	N/A	40%	30%
Commercial Paper	270 days	A1 / P1	25%	10%
California Local Agency Investment Fund	N/A	N/A	None	\$50M Per A/C
Repurchase Agreements	1 year	N/A	None	None
Reverse Repurchase Agreements (requires City Council approval)	92 days	N/A	None	None
Tax Exempt Municipal Bonds (for yield restriction purposes)	5 years	N/A	None	None
Medium Term Corporate Notes	5 years	Top three ratings categories	15%	None
Mutual Funds	N/A	Top rating category	20%	10%
Investment Pools	N/A	Top rating category	20%	10%

(A) Securities issued by the Federal Farm Credit Bank (FFCB), the Federal Home Loan Bank (FHLB), the Federal National Mortgage Association (FNMA), and the Federal Home Loan Mortgage Corporation (FHLMC)

**CITY OF SANTA CLARA ELECTRIC UTILITY ENTERPRISE FUND  
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**NOTE 3 – CASH AND INVESTMENTS (continued)**

**B. Investments Authorized by Debt Agreements**

The City invests bond proceeds designated for construction in instruments that are stated in the Investment Policy and in various return-guaranteed investment agreements. These investments are invested in accordance with bond indentures and the maturities of each investment should not exceed the final maturity of each bond. Bond proceed investments are reported monthly to the City Council.

Silicon Valley Power also maintains required amounts of cash and investments with trustees or fiscal agents under the terms of certain debt issues. These funds are unexpended bond proceeds or are pledged reserves to be used if the City fails to meet its obligations under these debt issues. The California Government Code 53601 (L) allows these funds to be invested in accordance with the statutory provisions governing the issuance of those bonds, indebtedness, other agreements, or certificates of participation in accordance with the ordinance, resolution, indenture, or agreement of the local agency providing for the issuance.

**C. Credit and Interest Rate Risk**

Credit risk is the risk that an issuer of an investment will not fulfill its obligations to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization.

Interest rate risk is the risk that changes in market interest rate will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates.

Information about the sensitivity of the fair values of Silicon Valley Power's investments to market interest rate fluctuations is provided by the following table that shows the distribution to Silicon Valley Power's investment by maturity.

	<b>Credit Rating</b>	<b>Carrying Amount</b>	<b>Maturity Date</b>
Investment held by fiscal agent:			
Mutual funds	AAA	<u>\$ 15,466,560</u>	12 months or less
Total Investments held by fiscal agent		15,466,560	
Investments not rated:			
Pooled Cash and Investments		<u>229,346,225</u>	12 months or less
Total Cash and Investments		<u><u>\$ 244,812,785</u></u>	

The City is a participant in the Local Agency Investment Fund (LAIF) that is regulated by California Government Code Section 16429 under the oversight of the Treasurer of the State of California.

**CITY OF SANTA CLARA ELECTRIC UTILITY ENTERPRISE FUND  
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**For the years ended June 30, 2010 and 2009**

**NOTE 3 – CASH AND INVESTMENTS (continued)**

The City reports its investment in LAIF at the fair value amount provided by LAIF, which is the same as the value of the pool share. The balance is available for withdrawal on demand, and is based on the accounting records maintained by LAIF, which are recorded on an amortized cost basis. Included in LAIF's investment portfolio are collateralized mortgage obligations, mortgage-backed securities, other asset-backed securities, loans to certain state funds, floating rate securities issued by federal agencies, government-sponsored enterprises, United States Treasury Notes and Bills, and corporations.

Mutual funds are available for withdrawal on demand.

**D. Concentration of Credit Risk**

Investments in the securities of any individual issuers that represent 5% or more of total SVP investments are shown in the table below:

<u>Issuer</u>	<u>Bond-rating</u>	<u>Fair Value</u>	<u>Expiration</u>	<u>% of Holding</u>
Federal Farm Credit Banks	AAA	\$ 27,110,585	N/A	11.07%
Federal Home Loan Banks	AAA	\$ 110,021,094	N/A	44.94%
Local Agency Investment Fund	N/A	\$ 20,039,547	N/A	8.19%

**E. Custodial Credit Risk**

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, the City will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. Under California Government Code Section 53651, depending on specific types of eligible securities, a bank must deposit eligible securities posted as collateral with its Agent having a fair value of 105% to 150% of the City's cash on deposit. All of the City's deposits are either insured by the Federal Depository Insurance Corporation (FDIC) or collateralized with pledged securities held in the trust department of the financial institutions.

The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty (e.g. broker-dealer) to a transaction, the City will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The City's Investment Policy limits its exposure to custodial credit risk by requiring that all security transactions entered into by the City, including collateral for repurchase agreements, be conducted on a delivery-versus-payment basis. Securities are to be held by a third party custodian.

**CITY OF SANTA CLARA ELECTRIC UTILITY ENTERPRISE FUND  
(SILICON VALLEY POWER)  
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**For the years ended June 30, 2010 and 2009**

**NOTE 4 – CAPITAL ASSETS**

**A. Capital Assets Summary**

	<b>Balance</b>				<b>Balance</b>
	<b>June 30, 2009</b>	<b>Additions</b>	<b>Retirements</b>	<b>Transfers</b>	<b>June 30, 2010</b>
Non Depreciable Assets:					
Land	\$ 13,550,593	\$ -	\$ -	\$ -	\$ 13,550,593
Construction In Progress	23,477,266	20,547,462	-	(10,969,086)	33,055,642
Total Non Depreciable Assets	<u>37,027,859</u>	<u>20,547,462</u>	<u>-</u>	<u>(10,969,086)</u>	<u>46,606,235</u>
Capital assets being depreciated:					
Buildings and Improvements	705,679,096	-	-	10,344,524	716,023,620
Machinery & Equipment	8,798,872	227,650	(193,507)	539,356	9,372,371
Total capital assets being depreciated	<u>714,477,968</u>	<u>227,650</u>	<u>(193,507)</u>	<u>10,883,880</u>	<u>725,395,991</u>
Less accumulated depreciation for:					
Buildings and Improvements	(261,403,568)	(16,244,299)	-	-	(277,647,867)
Machinery & Equipment	(6,492,901)	(741,375)	193,359	85,206	(6,955,711)
Total accumulated depreciation	<u>(267,896,469)</u>	<u>(16,985,674)</u>	<u>193,359</u>	<u>85,206</u>	<u>(284,603,578)</u>
Net Depreciable Assets	446,581,499	(16,758,024)	(148)	10,969,086	440,792,413
Enterprise Activity Capital Assets, Net	<u>\$ 483,609,358</u>	<u>\$ 3,789,438</u>	<u>\$ (148)</u>	<u>\$ -</u>	<u>\$ 487,398,648</u>

Construction in progress as of June 30, 2010 consisted of \$33,055,642 in Electric Projects.

**CITY OF SANTA CLARA ELECTRIC UTILITY ENTERPRISE FUND  
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**For the years ended June 30, 2010 and 2009**

**NOTE 5 – LONG-TERM DEBT AND DERIVATIVE INSTRUMENTS**

Changes in long-term debt for the year ended June 30, 2010, consisted of the following:

<b>Type of Indebtedness</b>	<b>Issue Date</b>	<b>Final Maturity</b>	<b>Range of Interest Rates</b>	<b>Balance as of June 30, 2009</b>	<b>Debt Retired</b>	<b>Additions and Amortization of Discounts</b>	<b>Outstanding as of June 30, 2010</b>	<b>Current Portion</b>
Business Type Activity Debt								
Enterprise Long-term Debt								
Electric Utility:								
1998 Series A Subordinate Refunding Revenue Bonds	3/1/1998	7/1/2027	5%	\$ 1,860,000	\$ 880,000	\$ -	\$ 980,000	\$ 980,000
2003 Series A Subordinate Revenue Bonds	10/9/2003	7/1/2028	2.50% - 5.25%	89,275,000	2,900,000	-	86,375,000	2,985,000
2008 Series A Subordinate Revenue Bonds	4/23/2008	7/1/2034	Adj.	49,655,000	-	-	49,655,000	-
2008 Series B Subordinate Revenue Bonds	5/29/2008	7/1/2027	Adj.	86,600,000	440,000	-	86,160,000	460,000
Unamortized Discount/Premium				(7,454,760)	-	407,803	(7,046,957)	-
Total of Electric Utility Revenue Bonds				<u>\$ 219,935,240</u>	<u>\$ 4,220,000</u>	<u>\$ 407,803</u>	<u>\$ 216,123,043</u>	<u>\$ 4,425,000</u>

**A. Subordinated Electric Revenue Refunding Bonds, 1998 Series A**

On March 1, 1998, the City issued \$89.28 million of the 1998 Subordinated Electric Revenue Refunding Series A Bonds (Electric 1998A Bonds). The Bonds mature annually in serial amounts from July 1, 1998 to July 1, 2027 and bear a coupon rate of 5.00%. Debt service payment is secured by a pledge of net revenues of the Electric Utility Enterprise Fund. On July 1, 2008 \$80.53 million of the Electric 1998A Bonds were redeemed using proceeds from Subordinated Electric Revenue Refunding Bonds, 2008 Series B. The Balance of \$2.64 million of the Electric 1998A Bonds will be redeemed according to its original schedule.

**B. Subordinated Electric Revenue Refunding Bonds, 2003 Series A**

On October 9, 2003, Silicon Valley Power issued \$100 million of the Subordinated Electric Revenue Bonds, Series 2003A (Electric 2003A Bonds) to finance a portion of the Donald Von Raesfeld Power Plant. The Electric 2003A Bonds mature annually in serial amounts from July 1, 2005 to July 1, 2025 with the final Term Bond maturity of July 1, 2028 and bear coupon rates ranging from 2.50% to 5.25%. Debt service on the 2003A Bonds is secured by a pledge of net revenues of the Electric Utility Enterprise Fund.

**C. Subordinated Electric Revenue Refunding Bonds, 2008 Series A**

On April 23, 2008, Silicon Valley Power issued \$49.66 million of the Subordinated Electric Revenue Bonds, Series 2008A (Electric 2008A Bonds) to refinance the Electric 2003B Bonds on April 28, 2008. The Electric 2008A Bonds mature annually in serial amounts from July 1, 2028 to July 1, 2034. The Electric 2008A Bonds are multi-modal bonds that are authorized to be issued in variable mode. Initially, the Electric 2008A Bonds were issued in the Daily Mode. Payment of the principal of, interest on, and purchase price of the Electric 2008A Bonds are made from proceeds of draws on a Letter of Credit provided by Bank of America. Debt service on the 2008A Bonds is secured by a pledge of net revenues of the Electric Utility Enterprise Fund.

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**NOTE 5 – LONG-TERM DEBT AND DERIVATIVE INSTRUMENTS (continued)**

**D. Subordinated Electric Revenue Refunding Bonds, 2008 Series B**

On May 29, 2008, Silicon Valley Power issued \$86.6 million of the Subordinated Electric Revenue Bonds, Series 2008B (Electric 2008B Bonds) to refinance \$80.53 million of the Electric 1998A Bonds on July 1, 2008. The Electric 2008B Bonds mature annually in serial amounts from July 1, 2009 to July 1, 2027. The Electric 2008B Bonds are multi-modal bonds that are authorized to be issued in variable mode. Initially, the Electric 2008B Bonds were issued in the Weekly Mode. Payment of the principal of and interest on, and purchase price of, the Electric 2008B Bonds are made from proceeds of draws on the Letter of Credit provided by Dexia Credit Local. Debt service on the 2008B Bonds is secured by a pledge of net revenues of the Electric Utility Enterprise Fund.

**E. Derivative Instruments**

In FY 09-10, SVP implemented GASB Statement No. 53, which addresses recognition, measurement and disclosures related to derivative instruments to determine whether they meet the definition of derivative instruments, and if so, whether they effectively hedge the expected cash flows associated with the interest rate and energy exposures. Under hedge accounting, the increase (decrease) in the fair value of a hedge is reported as a deferred cash flow hedge on the statement of net assets. For the reporting period, all of SVP's derivatives meet the hedge effectiveness tests under GASB Statement No. 53.

Interest Rate Swap Agreements-2008 Series B Bonds

Pursuant to the Interest Rate Hedging Policy adopted by the City Council in 2006, as a means to lower the borrowing costs, the City has a variable-to-fixed interest rate Swap Agreement with JPMorgan related to the 2008 Series B bonds. Under the Swap Agreement, Santa Clara is obligated to make payments to the Swap Provider calculated on the basis of a fixed rate of 3.47% and receives from the Swap Provider payments equal to 65% of the one month London InterBank Offering Rate (LIBOR). Santa Clara's obligation to make any net regularly scheduled payments due to the Swap Provider under the Swap Agreement is payable from subordinated net revenues of the electric system on a parity with its other outstanding subordinated electric bonds. The effective date of the swap was May 29, 2008 and the scheduled termination date is July 1, 2027.

	Notional Amount (000's)	City Pays Fixed Rate to Counterparty	City Receives Floating Rate From Counterparty 6/30/2010	City Pays Variable Rate on Bond 6/30/2010
2008 Series B	\$83,015	3.47%	Weekly Mode - 65% of LIBOR=0.22694%	Weekly Mode - SIFMA=0.25%

The swap is classified as a debt instrument and had negative fair values of \$10,867,835 as of June 30, 2010 and \$7,714,294 as of June 30, 2009, resulting in a deferred inflow change of \$3,153,541 from June 30, 2009. The swap is classified as a deferred inflow of resources and derivative financial instrument on the statement of net assets. The fair values were based on MID-MARKET LEVELS as of the close of business date on June 30, 2010 and June 30, 2009, respectively. The



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**For the years ended June 30, 2010 and 2009**

**NOTE 5 – LONG-TERM DEBT AND DERIVATIVE INSTRUMENTS (continued)**

values were estimated from proprietary models based upon well recognized financial principles and reasonable estimates about relevant future market conditions.

**Rollover Risk**

SVP is exposed to rollover risk on hedging derivative instruments that are hedges of debt because SVP can terminate the interest rate swap prior to the maturity of the bond. The risk if the swap is terminated will be to re-expose SVP to the risks being hedged by the interest rate swap. SVP currently has no plans to terminate the swap prior to maturity in 2027.

**Interest Rate/Basis Risk**

SVP is exposed to interest rate risk on its swap agreement. The SVP's net payment on the swap increases as the LIBOR swap index decreases. With respect to basis risk, under the swap, the City receives 65% of LIBOR and pays the Securities Industry and Financial Markets Association (SIFMA) rate to bondholders of the City's 2008B bonds. The basis risk is the difference between the two rates. As of June 30, 2010, 65% of LIBOR was 0.22694% and the SIFMA rate was 0.25%.

Using rates as of June 30, 2010, debt service requirements of the variable-rate debt and net swap payments, assuming current interest rates remain the same for their term, were as follows. As rates vary, variable-rate bond interest payments and net swap payments will vary.

<b>Year Ending June 30</b>	<b>Variable-Rate Bond</b>		<b>Interest Rate Swaps, Net</b>	<b>Total</b>
	<b>Principal</b>	<b>Interest</b>		
2011	\$ 460,000	\$ 214,250	\$ 2,677,957	\$ 3,332,207
2012	3,160,000	206,350	2,576,287	3,242,637
2013	3,350,000	197,975	2,468,617	5,826,592
2014	3,550,000	189,100	2,355,110	5,894,210
2015	3,760,000	179,700	2,235,117	5,964,817
2016-2020	22,245,000	737,725	9,141,538	30,939,263
2021-2025	29,025,000	410,288	5,047,661	33,007,948
2026-2028	20,610,000	52,913	646,828	27,729,741
	<u>\$ 86,160,000</u>	<u>\$ 2,188,300</u>	<u>\$ 27,149,115</u>	<u>\$ 115,937,415</u>

**Notional Amounts and Fair Values**

SVP maintains a Market Risk Management Policy, which among other things, sets forth the guidelines for the purchase and sale of certain financial instruments defined as hedge instruments in support of market power purchase transactions. The primary goal of these guidelines is to provide a framework for the operation of an energy price hedging program to better manage SVP's risk exposure in order to stabilize pricing and costs for the benefit of SVP and its customers.

Consistent with hedge accounting treatment meeting effectiveness tests, changes in fair value are reported as deferred flows of resources on the statement of net assets until the contract expiration that occurs in conjunction with the hedged expected energy purchase transaction. When hedging

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**NOTE 5 – LONG-TERM DEBT AND DERIVATIVE INSTRUMENTS (continued)**

contracts expire, at the time the purchase transactions occur, the deferred balance is recorded as a component of Purchased Power. For energy derivatives, fair values are estimated by comparing contract prices to forward market prices quoted by third party market participants.

SVP had the following future derivative instruments outstanding at June 30, 2010 with Bache Commodities to hedge cash flows on CAISO NP15 power purchases:

Objective	Notional Amount (MWh)	Trade Date	Effective Date	Maturity Date	Terms	Classification	Fair Value		Change in Fair Value	
							Amount	Classification	Amount	Amount
Hedge cash flows on NP15 power purchases	61,600	Apr-10	Jul-10	Sep-10	Pay \$50.00/Mwh; settle on CAISO NP15	Derivative Instrument	\$ (455,256)	Purchased Power Expense	\$	(455,256)
Hedge cash flows on NP15 power purchases	30,800	May-10	Jul-10	Sep-10	Pay \$49.75/Mwh; settle on CAISO NP15	Derivative Instrument	(144,052)	Purchased Power Expense		(144,052)
Hedge cash flows on NP15 power purchases	30,800	May-10	Oct-10	Dec-10	Pay \$49.00/Mwh; settle on CAISO NP15	Derivative Instrument	(70,400)	Purchased Power Expense		(70,400)
Hedge cash flows on NP15 power purchases	30,800	May-10	Oct-10	Dec-10	Pay \$49.25/Mwh; settle on CAISO NP15	Derivative Instrument	(75,500)	Purchased Power Expense		(75,500)
Hedge cash flows on NP15 power purchases	10,400	Jun-10	Jul-10	Jul-10	Pay \$48.00/Mwh; settle on CAISO NP15	Derivative Instrument	(45,552)	Purchased Power Expense		(45,552)
Hedge cash flows on NP15 power purchases	30,800	Jun-10	Jul-10	Sep-10	Pay \$47.00/Mwh; settle on CAISO NP15	Derivative Instrument	(59,352)	Purchased Power Expense		(59,352)
					Total		<u>\$ (850,112)</u>			<u>\$ (850,112)</u>

SVP had no future derivative instruments outstanding at June 30, 2009.

**Credit Risk**

Credit risk is the risk of loss due to a counterparty defaulting on its obligations. SVP is exposed to credit risk if hedging instruments are in asset positions. As of June 30, 2010, SVP was not exposed to credit risk because the swap and all open derivative contracts had a negative fair value. However, should interest rates change and the fair market value of the swap become positive, the City would be exposed to credit risk in the amount of the fair market values. The swap and open contract counterparties were rated A+ and A, respectively, by S&P at June 30, 2010.

SVP's policy for requiring collateral on hedging instruments varies based on individual contracts and counterparty credit ratings. Under the interest rate swap agreement, collateral is required based on the counterparty rating and dollar threshold on the mark-to-market value of the swap. Under the trading agreements with Merrill Lynch, Pierce, Fenner & Smith, Inc. and Bache Commodities, the trading accounts are prefunded by SVP. If the account value falls below zero, margin calls are invoked. At June 30, 2010 SVP had posted collateral of \$4,908,014 on the

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**For the years ended June 30, 2010 and 2009**

**NOTE 5 – LONG-TERM DEBT AND DERIVATIVE INSTRUMENTS (continued)**

interest rate swap and \$1,532,968 was deposited with Merrill Lynch, Pierce, Fenner & Smith, Inc. and Bache Commodities for wholesale trading. At June 30, 2010, no margin calls were paid to Bache Commodities on the outstanding future derivative instruments.

It is also SVP's policy to negotiate netting arrangements whenever it has entered into more than one derivative instrument transaction with a counterparty. Under the terms of these arrangements, should one party become insolvent or otherwise default on its obligations, the non-defaulting party may accelerate and terminate all outstanding transactions and net their fair values so that a single amount will be owed by (or to) the non-defaulting party. At June 30, 2010 SVP had various derivative instrument purchase contracts with Bache Commodities.

Termination Risk

The swap may be terminated by the City at any time. If the swap is terminated, the City may be required to make a termination payment to the Swap Provider if the swap had a negative fair market value. The cost to terminate would be the fair value of the swap at the time of termination. Any such termination payment owed by Santa Clara would be payable from net revenues of the electric system subordinate to Santa Clara's outstanding electric revenue bonds. If the swap had a positive fair market value, the Swap Provider would be required to make a termination payment to the City. Futures contracts are traded over the counter and have no termination risks.

Price Risk

With respect to price risk under these future contracts, SVP receives the CAISO NP15 average daily rate at settlement and pays the fixed contracted rate entered into on the trade date. SVP is exposed to risk because the commodity purchase price being hedged is different from the price on settlement.

**F. Other**

Various debt agreements governing Silicon Valley Power's revenue bonds contain a number of covenants including those that require Silicon Valley Power to maintain and preserve the enterprise in good repair and working order, to maintain certain levels of insurance, and to fix and collect rates, fees, and charges so as to maintain certain debt coverage ratios. Silicon Valley Power is in compliance with these specific covenants and all other material covenants governing the particular revenue bond issues. No event of default as defined in the bond indentures has occurred or was occurring as of the date of this report.

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**NOTE 5 – LONG-TERM DEBT AND DERIVATIVE INSTRUMENTS (continued)**

**G. Repayment Requirements**

As of June 30, 2010, the debt service requirements to maturity for Silicon Valley Power's long-term debt are as follows:

<u>Year Ending June 30</u>	<b>Long-term Debt Future Debt Service Requirements</b>		
	<u>Principal</u>	<u>Interest*</u>	<u>Total</u>
2011	\$ 4,425,000	\$ 4,404,357	\$ 8,829,357
2012	6,255,000	4,289,782	10,544,782
2013	6,560,000	4,163,332	10,723,332
2014	6,885,000	4,031,582	10,916,582
2015	7,250,000	3,868,232	11,118,232
2016-2020	42,250,000	16,610,885	58,860,885
2021-2025	54,660,000	10,510,413	65,170,413
2026-2030	53,515,000	3,105,788	56,620,788
2031-2035	41,370,000	215,950	41,585,950
	<u>\$ 223,170,000</u>	<u>\$ 51,200,318</u>	<u>\$ 274,370,318</u>

\* Interest on the 2008 Series A and B Bonds is estimated using current rate at June 30, 2010.

**Reconciliation of Long-term Debt:**

Principal Outstanding As Reported Above	\$ 223,170,000
Deduct Unamortized Discount - Electric Revenue Bonds	<u>(7,046,957)</u>
Total Long-term Debt	<u>\$ 216,123,043</u>

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**NOTE 6 – PARTICIPATION IN JOINT VENTURES**

**A. Investment in Joint Ventures**

Silicon Valley Power (through the City) participates in significant joint ventures: Northern California Power Agency (NCPA), Transmission Agency of Northern California (TANC), M-S-R Public Power Agency (MSR PPA), M-S-R Energy Authority (MSR EA).

The separately issued financial statements of these joint ventures (as noted below) are available on request.

	NCPA	TANC	MSR PPA	MSR EA
Date of latest audited financial statement	6/30/2009	6/30/2009	12/31/2009	12/31/2009
Participant's address	651 Commerce Dr. Roseville, CA 95678	P.O. Box 15129 Sacramento, CA 95851	P.O. Box 4060 Modesto, CA 95352	P.O. Box 4060 Modesto, CA 95352

As described in paragraph (D) below, the carrying value of Silicon Valley Power's investment in MSR PPA is \$0. Silicon Valley Power's financial statements reflect the following investments in joint ventures as of June 30, 2010:

	NCPA			TANC	MSR EA	MSR PPA
	Geothermal	Hydroelectric	Combustion Turbine			
Participation percentage	44.39%	37.02%	25.00%	20.47%	33.40%	35.00%
Investment		\$26,796,234		\$ 751,925	\$ -	\$ -
Method of accounting		Equity		Equity	Equity	Equity

**B. Northern California Power Agency (NCPA)**

NCPA was formed in 1968 as a joint powers agency in the State of California. Its membership consists of eleven cities with publicly owned electric utility distribution systems, one irrigation district, one public utility district, one port authority, one transit district, and two other associate member entities. NCPA is generally empowered to purchase, generate, transmit, distribute and sell electrical energy. Members participate in the projects of NCPA on an elective basis. Therefore, the participation percentage varies for each project in which it participates.

A Commission comprised of one representative from each joint venture member governs NCPA. The Commission is responsible for the general management of the affairs, property, and business of NCPA. Under the direction of the General Manager, the staff of NCPA is responsible for providing various administrative, operating and planning services for NCPA and its associated power corporations.

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**NOTE 6 – PARTICIPATION IN JOINT VENTURES (continued)**

**Project Financing and Construction**

NCPA's project construction and development programs have been individually financed by project revenue bonds collateralized by NCPA's assignment of all payments, revenues and proceeds associated with its interest in each project. Each project participant has agreed to pay its proportionate share of debt service and other costs of the related project, notwithstanding the suspension, interruption, interference, reduction or curtailment of output from the project for any reason. Certain of the revenue bonds are additionally supported by municipal bond insurance credit enhancements.

**Hydroelectric Project**

NCPA contracted to finance, manage, construct, and operate Hydroelectric Project Number One for the licensed owner, Calaveras County Water District (CCWD). In exchange, NCPA has the right to the electric output of the project for 50 years from February 1982. NCPA also has an option to purchase power from the project in excess of the CCWD's requirements for the subsequent 50 years, subject to regulatory approval.

**Geothermal Project**

The NCPA Geothermal Plants have historically experienced greater than anticipated declines in steam production from the existing geothermal wells. Although initially operated as baseload generation projects at full capability (238MW), by 1988 NCPA changed its steam field production from baseload to load-following and reduced average annual steam production. Along with other steam field operators in the area, the Agency began implementing various operating strategies to further reduce the rate of decline in steam production. The Agency has modified both steam turbine units and the associated steam collection system to enable generation with lower pressure steam at higher mass-flow rates to optimize the utilization of the available steam resource.

Based upon current operation protocols and forecasted operations, NCPA expects average annual generation and peak capacity to decrease further, reaching approximately 72 MW by the year 2031.

**Combustion Turbine Project No. 1**

NCPA owns five dual (natural gas and fuel oil) combustion turbine units, each of which is nominally rated at 25 MW, which are collectively known as the Combustion Turbine Project No. 1. These units were completed in 1986 and are designed to provide peak power and reserve requirements and emergency support. Each purchaser is responsible under its power sales contract for paying entitlement share in Combustion Turbine Project No. 1 of all NCPA's costs of such project.

**Lodi Energy Center**

On May 24, 2010, Santa Clara entered into an agreement with NCPA for a 25.75% interest in the 280 MW combined cycle natural gas fired power plant, to be located in Lodi, California. The project received approval from the California Energy Commission in April 2010 and is expected to be operational around June 2012.

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**NOTE 6 – PARTICIPATION IN JOINT VENTURES (continued)**

**C. Transmission Agency of Northern California (TANC)**

TANC was organized under the California Government Code pursuant to a joint powers agreement entered into by 15 Northern California utilities. The purpose of TANC is to provide electric transmission or other facilities for the use of its members through its authority to plan, acquire, construct, finance, operate and maintain facilities for electric power transmission. The joint powers agreement provides that the costs of TANC's activities can be financed or recovered through assessment of its members or from user charges through transmission contracts with its members. Each TANC member has agreed to pay a pro-rata share of the costs to operate TANC and for payment of debt service, and has the right to participate in future project agreements.

The joint powers agreement remains in effect until all debt obligations and interest thereon have been paid, unless otherwise extended by the members.

**California-Oregon Transmission Project**

TANC is a participant and also the Project Manager of the California-Oregon Transmission Project (Project), a 339 mile long, 500 kilovolt alternating current transmission project between Southern Oregon and Central California. As Project Manager, TANC is responsible for the overall direction and coordination of all Project operations and maintenance, additions and betterments, and for general and administrative support.

The Project was declared commercially operable on March 24, 1993, with a rated transfer capability of 1,600 megawatts and provides a third transmission path between the electric systems of the Pacific Northwest and those in California. The Project has successfully met and completed all major environmental requirements. As of June 30, 2009, the most recent data available, TANC's investment in the Project was \$507.9 million, less accumulated depreciation and amortization of \$168.0 million.

In connection with its participation in the Project, TANC has an entitlement balance of the Project's transfer capability of approximately 1,362 megawatts and is obligated to pay an average of approximately 80 percent of the operating costs associated with the Project. TANC incurred and initially capitalized all costs for project construction since they were expected to be recovered through reimbursement from Project participants and from the successful operations of the Project transmission lines. The Project agreement among the participating members provides that each member agrees to make payments, from its revenues, to TANC for project costs incurred and for payment of debt service.

**D. M-S-R Public Power Agency (MSR PPA)**

MSR PPA is a joint power agency formed in 1980 by the Modesto Irrigation District, the City, and the City of Redding, California, to develop or acquire and manage electric power resources for the benefit of the members. The personnel of its members and contract professional staff perform other administrative and management functions of MSR PPA. The member's income and expenses sharing ratio is as follows: Modesto Irrigation District – 50 percent, City of Santa Clara – 35 percent, and City of Redding – 15 percent.

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**NOTE 6 – PARTICIPATION IN JOINT VENTURES (continued)**

Silicon Valley Power's equity in MSR PPA's net losses exceeds its investments and, therefore, the equity method of accounting for the investment has been suspended. As of December 31, 2009, the date of the latest available audited financial statements, Silicon Valley Power's unrecognized share of member's deficit of MSR PPA was \$55.9 million. Under the joint exercise of power agreement, which formed MSR PPA, Silicon Valley Power is responsible for funding up to 35 percent of MSR PPA's operating cost, to the extent such funding is necessary. During the year ended June 30, 2009, Silicon Valley Power made no contributions to fund its share of operating deficits. If there were such contributions, they would be included in the Electric Utility Enterprise Fund expenses.

MSR PPA's principal activity is a 28.8 percent ownership interest in a 507-megawatt unit of a coal-fired electricity generating plant located in New Mexico (San Juan Plant). The acquisition of such ownership interest was funded through the issuance of revenue bonds, secured by a pledge and assignment of the net electric revenues of MSR PPA and supported by take-or-pay commitments of the equity participants. MSR PPA is also a participant in the Southwest Transmission Project, a 500-kilovolt alternating current transmission project between Central Arizona and Southern California that provides a firm transmission path for the electric power from the San Juan Plant to the MSR PPA members. The southwest Transmission Project was completed and placed in service in April 1996.

In accordance with an agreement with the Tucson Electric Power Company (TEP), MSR PPA has the right to certain levels of power transmission without charge and without transmission losses between the San Juan Plant in New Mexico and Palo Verde, Arizona through 2025. These rights are being utilized in connection with the delivery of power from the San Juan Plant to the members or to third party purchasers.

On June 1, 2005, MSR PPA entered into a series of agreements with PPM Energy (as amended in October 2005 and restated effective February 1, 2006; PPM Energy is now Iberdrola Renewable Holdings, Inc.) to purchase wind power energy from Big Horn I with nominal installed capacity of approximately 199.5 MW and an expected annual capacity factor of about 35%, as firmed, shaped, and delivered to the California-Oregon Border for a twenty-year period. The deliveries for the wind power began in 2006. The participation in this project is as follows:

Modesto Irrigation District	12.5%
City of Santa Clara	52.5%
City of Redding	35.0%

On December 9, 2009, MSR PPA entered into a series of agreements with Iberdrola Renewables Inc. to purchase additional wind power energy from the same site, called Big Horn II, with a nominal installed capacity of 50 MW and an expected capacity factor of about 35%, as firmed, shaped, and delivered to the California-Oregon Border (COB) for a twenty-year period. Deliveries of energy under this project are scheduled to begin on November 1, 2010. The participation in this project is as follows: Modesto Irrigation District – 65%; City of Santa Clara – 35%.



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**For the years ended June 30, 2010 and 2009**

**NOTE 6 – PARTICIPATION IN JOINT VENTURES (continued)**

**E. M-S-R Energy Authority (M-S-R EA)**

MSR EA is a joint power agency formed in 2008 by the Modesto Irrigation District, the City of Santa Clara, and the City of Redding, California, to develop or acquire and manage electric power resources for the benefit of the members. The personnel of its members and contract professional staff perform other administrative and management functions of MSR PPA. The member's income and expense sharing ratio is as follows: Modesto Irrigation District – 33.3%; City of Santa Clara – 33.4%; and City of Redding – 33.3%.

The City's equity in MSR EA's net losses exceeds its investment and, therefore, the equity method of accounting for the investment has been suspended. As of December 31, 2009, the date of the latest available audited financial statements, the City's unrecognized share of member's deficit of MSR EA was \$6.6 million. Under the joint exercise of power agreement, which formed MSR EA, the City is responsible for funding up to 33.4% of MSR EA's operating cost, to the extent such funding is necessary. During the year ended June 30, 2009, the City made no contributions to fund its share of operating deficits. If there were such contributions, they would be included in the Electric Utility Enterprise Fund expenses.

In 2009, the City of Santa Clara, along with the Cities of Modesto and Redding participated in the M-S-R Energy Authority Gas Prepay Project. The Gas Prepay Project provides the City of Santa Clara, through a Gas Supply Agreement with M-S-R EA dated September 10, 2009, a secure and long-term supply of natural gas of 7,500 MM Btu (Million British thermal unit) daily or 2,730,500 MM Btu annually through December 31, 2012, and 12,500 MM Btu daily, or 4,562,500 MM Btu annually thereafter until September 30, 2039. The agreement provides this supply at a discounted price below the spot market price (the Pacific Gas & Electric City gate index) over the next 30 years. As of June 30, 2010, bonds issued by MSR EA to finance the City's share of the Gas Prepay Project were outstanding in the principal amount of \$500,200,000. These bonds were initially sold on August 27, 2009. Under the Gas Supply Agreement, MSR EA will bill the City for actual quantities of natural gas delivered each month on a "take-and-pay" basis. MSR EA has contracted with Citigroup Energy, Inc. ("CEI") to use the proceeds of the Gas Prepay bond issue to prepay CEI for natural gas. CEI has guaranteed repayment of the bonds, and responsibility for bond repayment is non-recourse to the City of Santa Clara. Moreover, any default by the other Gas Prepay Project participants is also non-recourse to the City.

**F. Contingent Liability**

Under the terms of the various joint venture agreements, Silicon Valley Power is contingently liable for a portion of the long-term debt of the entities under take-or-pay agreements, letters of credit, guarantees or other similar agreements. Based on the most recent audited financial statements of the individual joint ventures, Silicon Valley Power was contingently liable for long-term debt as follows:

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**NOTE 6 – PARTICIPATION IN JOINT VENTURES (continued)**

<u>Agreements</u>	<u>Total Debt</u>	<u>Silicon Valley Power's Debt Share</u>	<u>Silicon Valley Power's Contingent Liability</u>
NCPA 06/30/09	\$ 628,895,000	37.57%	\$ 236,275,852
TANC 06/30/09	435,790,000	20.84%	90,818,636
MSR PPA 12/31/09	380,580,000	35.00%	133,203,000
MSR EA 12/31/09	901,620,000	55.48%	500,200,000
TOTAL	<u>\$ 2,346,885,000</u>		<u>\$ 960,497,488</u>

In addition, Silicon Valley Power would be, under certain conditions, liable to pay a portion of costs associated with the operations of the entities. Under certain circumstances, such as default or bankruptcy of the other participants, Silicon Valley Power may also be liable to pay a portion of the debt of these joint ventures on behalf of those participants and seek reimbursement from those participants.

**NOTE 7 – RESTRUCTURING OF THE CALIFORNIA ELECTRIC INDUSTRY**

**A. Long-term Power Purchase Contracts**

Silicon Valley Power purchases wholesale electric power from various participants of the Western Systems Power Pool (WSPP), NCPA, MSR Public Power Agency (Note 6), Western Area Power Administration, and other sources to supply the power requirements of Silicon Valley Power's electric utility customers. Silicon Valley Power actively manages the financial risks inherent in these long-term contracts, including the risks arising from the changing spot market prices that move above and below the contract prices and from contract disputes that may arise from time to time. The cost of power is included in enterprise fund materials, services and supplies expense.

**B. Restructuring of the California Electric Industry**

**Deregulation Legislation and Direct Access**

The passage of AB1890 in 1998 triggered fundamental changes in the structure of the electric industry in California. The essential feature of AB1890 was to allow individual consumers the opportunity to buy energy directly from power producers and marketers, rather than from their local investor owned utility. This was called direct access. Generally, AB1890 provided for creation of the California Power Exchange (Cal PX), which was to be a clearinghouse for energy transactions among investor owned utilities, independent generators and power marketers, who in turn would serve direct access customers. AB1890 also created the California Independent System Operator (CAISO), which was to manage the state's bulk transmission grid. In addition, investor owned utilities were encouraged to sell a substantial portion of their generating facilities to third parties, which they did. AB1890 further provided for a four-year freeze of investor-owned utility rates and recovery by investor and publicly owned utilities during this four-year period of so-called "stranded costs" arising from what were thought at the time to be uncompetitive generation investments.

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**NOTE 7 – RESTRUCTURING OF THE CALIFORNIA ELECTRIC INDUSTRY (continued)**

AB1890 also encouraged, but did not require, municipal utilities to establish direct access programs.

In 1999, the City Council adopted a direct access program that provided for a stranded cost charge, or Competition Transition Charge, subject to legal validation of the City's and Silicon Valley Power's right to collect such a charge. That validation was secured in 2000, and Silicon Valley Power's direct access program was to commence in April 2001.

However, in 2000 and 2001, the price of electricity at the Cal PX became extremely high, and investor-owned utilities were unable to pay for the energy that they needed from the Cal PX. These conditions caused the passage of AB1X by the California legislature, pursuant to which investor owned utilities' energy procurement function was assigned to the California Department of Water Resources. AB1X also suspended direct access for investor-owned utilities, essentially until 2013. Based on this development, Silicon Valley Power has deferred implementation of its direct access program.

**Other Effects of Restructuring**

The restructuring of the electric industry has created a substantially changed market for electricity. Compared to the prior market structure, this market has exhibited increased uncertainty and volatility. In anticipation of this restructured market, Silicon Valley Power developed a strategic plan to guide its electric utility's transition efforts into the new environment. As part of the Strategic Plan, the Cost Reduction Account (also called Cost Reduction Fund) was established to protect ratepayers from rate volatility in future years due to revenue shortfalls or unexpected costs. As of June 30, 2010, the balance of the Cost Reduction Account is \$84.2 million.

The strategic plan is a multi-pronged strategic initiative to address electric generation, transmission and distribution business issues given both the initially anticipated operating environment, and the operating environment that has actually evolved. The City's management believes that the strategic plan has been an effective tool for the electric utility as it has transitioned into the new environment.

**Energy Wholesale Trading and Risk Management**

Silicon Valley Power participates in the wholesale gas and power market and the California Independent System Operator's centralized market. Silicon Valley Power engages in the trading of commodity forward contracts (gas and electric energy contracts). Activities during the fiscal year were substantially considered hedging transactions and, as such, have been accounted for using the settlement method of accounting. Accordingly, related gross purchases and sales totaling \$73.7 million and \$67.8 million, respectively, for fiscal year ended June 30, 2010, have been separately reported on the statement of revenues, expenses and changes in net assets. Associated receivables representing delivered but unbilled energy, and corresponding payable amounts totaling \$6.80 million and \$6.92 million, respectively, have been reported in the proprietary funds statement of net assets.

The restructured electric wholesale market exposes Silicon Valley Power to various risks including market, credit and operational risks. Active and effective management of these risks associated

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**NOTE 7 – RESTRUCTURING OF THE CALIFORNIA ELECTRIC INDUSTRY (continued)**

with the power trading activity is critical to its continued success and contribution to the entire utility. A Risk Management Committee, separate from the units that create the risk exposures, overseen by a Risk Oversight Committee that reports ultimately to the City Council, administers and monitors compliance with the risk policies and procedures on a regular basis. The City and Silicon Valley Power believe that it has the resource commitment, effective policies and procedures, and is continuing to improve the control structure and oversight for evaluating and controlling the market and credit risks to which it is exposed.

**Credit Arrangements**

The City of Santa Clara (The City) maintains credit policies, procedures, and systems for Silicon Valley Power that help mitigate credit risk and minimize overall credit risk exposure. The policies include transacting only with investment grade counterparties, and evaluation of potential counterparties' financial condition and an assignment of credit limits as applicable. These credit limits are established based on risk and return considerations under terms customarily available in the industry. Additionally, The City is a signatory to the WSPP netting agreement supplement and otherwise, enters into master netting arrangements whenever possible and, where appropriate, obtains collateral prior to trade execution. Master netting agreements incorporate rights of setoff that provide for the net settlement of subject contracts with the same counterparty in the event of default.

**C. Electric Rate Increase**

In December 2009, the City Council adopted a 7% rate increase on January 1, 2010 and 7% rate increase on January 1, 2011. The primary reasons for the increase were the increased cost and use of fuel for electric generation, combined with a significant reduction in energy available from Western Area Power Administration. City staff continues to monitor costs and revenues to assess future rate increase recommendations.

**NOTE 8 – MAJOR SUPPLIERS**

Silicon Valley Power purchases wholesale electric energy from various participants of the Western System Power Pool, NCPA, M-S-R Public Power Agency, Western Area Power Administration, and other sources to supply its retail electric utility customers.

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**NOTE 9 – COMMITMENTS AND CONTINGENCIES**

Commitments and contingencies, undeterminable in amount, include normal recurring pending claims and litigation. In the opinion of management, based upon discussion with legal counsel, there is no pending litigation, which is likely to have a material adverse affect on the financial position of the fund.

Silicon Valley Power has future commitments under construction projects as follows:

	Authorized	Expended Through June 30, 2010	Remaining Commitments
Electric Projects	\$ 68,578,700	\$ 33,055,642	\$ 35,523,058

**NOTE 10 – SUBSEQUENT EVENT**

SVP and Pacific Gas and Electric Company (“PG&E”) were engaged in certain disputes in the proceedings associated with the voluntary petition in bankruptcy under Chapter 11 of the Bankruptcy Code filed by PG&E on April 6, 2001, in the United States Bankruptcy Court for the Northern District of California, San Francisco Division, designated as Case No. 01-30923 DM (“PG&E Bankruptcy Proceedings”).

A tentative agreement was reached that is reflected in the binding term sheet executed by the Parties dated October 21, 2010; The intent of the agreement is to accomplish a global settlement, resolving all claims between the Parties relating to transactions in Western Energy Markets.

It is probable that SVP will pay approximately \$7.6 million in 2011 to settle this claim.