

*In the opinion of Hawkins Delafield & Wood LLP, Bond Counsel to the Department of Water Resources of the State of California with respect to this financing, under existing statutes and court decisions and assuming continuing compliance with certain tax covenants described herein, (i) interest on the Series 2005 Bonds is excluded from gross income for federal income tax purposes pursuant to Section 103 of the Internal Revenue Code of 1986, as amended (the "Code"), and (ii) interest on the Series 2005 Bonds is not treated as a preference item in calculating the alternative minimum tax imposed on individuals and corporations under the Code; such interest, however, is included in the adjusted current earnings of certain corporations for purposes of calculating the alternative minimum tax imposed on such corporations. In addition, in the opinion of Bond Counsel, under existing statutes, interest on the Series 2005 Bonds is exempt from State of California personal income taxes. See "TAX MATTERS" herein.*

**\$2,594,000,000**

**State of California Department of Water Resources  
Power Supply Revenue Bonds (Variable Rate Demand Bonds)  
consisting of**

**\$759,400,000**

**Series 2005F (Daily Rate)**

**\$1,834,600,000**

**Series 2005G (Weekly Rate)**

**Dated: Date of Delivery**

**Price: 100%**

**Due: See inside cover**

The \$759,400,000 aggregate principal amount of Series 2005F Bonds consists of five separate subseries, designated Series 2005F-1 through Series 2005F-5. The \$1,834,600,000 aggregate principal amount of Series 2005G Bonds consists of 14 separate subseries, designated Series 2005G-1 through Series 2005G-14. Any Bond of any of such two Series or 19 subseries may be referred to herein as a "Series 2005 Bond" and all Bonds of such two Series and 19 subseries are collectively referred to herein as the "Series 2005 Bonds." Certain terms relating to each subseries of Series 2005 Bonds are described in the "Series Descriptions" following this cover page.

The Series 2005 Bonds will mature in the principal amounts and on the dates set forth in the Series Descriptions. Each subseries of Series 2005 Bonds may bear interest at Daily Rates, Weekly Rates, Flexible Rates, Term Rates, Auction Rates or Fixed Rates (each, an "Interest Rate Mode"), as described herein. During the "Initial Interest Period" set forth on the applicable Series Description, each subseries of Series 2005 Bonds will bear interest at the "Initial Rate" determined by the Underwriters prior to the delivery date. Following such Initial Interest Period, each subseries of Series 2005 Bonds will automatically convert, without a mandatory tender for purchase, to Daily Rates or Weekly Rates, as set forth in the Series Descriptions, subject to possible future adjustment to a different Interest Rate Mode. While bearing interest at Daily Rates or Weekly Rates, the interest rate on the Series 2005 Bonds will be periodically reset, as described herein. **THIS OFFICIAL STATEMENT IS NOT INTENDED TO DESCRIBE THE SERIES 2005 BONDS WHILE BEARING INTEREST AT AUCTION RATES, FLEXIBLE RATES, TERM RATES OR FIXED RATES.**

The Series 2005 Bonds are subject to optional and mandatory redemption prior to maturity as described herein. See "THE SERIES 2005 BONDS – Redemption."

The Series 2005 Bonds may be tendered for purchase at the option of the Owners thereof, subject to the terms and conditions set forth in the Indenture. The Series 2005 Bonds are also subject to mandatory tender for purchase in certain circumstances. See "THE SERIES 2005 BONDS – Optional and Mandatory Tender for Purchase." Subject to certain conditions precedent, Series 2005 Bonds that are tendered for purchase (optional or mandatory) but are not successfully remarketed will be purchased with funds provided pursuant to an Enhancement Facility. See the Series Descriptions and Appendices I and K for additional information concerning the Enhancement Facilities. See also "SECURITY FOR THE BONDS."

Payment of the principal of, interest on, and purchase price of, certain subseries of Series 2005 Bonds will be secured by direct-pay letters of credit issued by the providers identified in the applicable Series Descriptions, in each case subject to the terms thereof. See "SECURITY FOR THE BONDS – Initial Letters of Credit." The scheduled payment of the principal of and interest on each other subseries of Series 2005 Bonds when due will be insured by a financial guaranty insurance policy to be issued by the bond insurer identified in the applicable Series Descriptions simultaneously with the issuance of the Series 2005 Bonds. See "SECURITY FOR THE BONDS – Bond Insurance." Payment of the purchase price of each insured subseries of Series 2005 Bonds will be supported by a liquidity facility issued by the provider identified in the applicable Series Description. See "SECURITY FOR THE BONDS – Initial Liquidity Facilities."

Series 2005 Bonds may be purchased in book-entry form only, in the principal amount of \$100,000 or any integral multiple of \$5,000 in excess of \$100,000. See APPENDIX B – "BOOK-ENTRY SYSTEM."

The Bonds are being issued under a Trust Indenture, as amended and supplemented (the "Indenture") among the Department of Water Resources of the State of California ("DWR"), the Treasurer of the State of California, as trustee (the "Trustee") and U.S. Bank National Association, as co-trustee (the "Co-Trustee"). Net proceeds of the Series 2005 Bonds will be used by DWR to refund certain outstanding Bonds issued in 2002. See "PLAN OF REFUNDING."

The Bonds are payable primarily from charges ("Bond Charges") imposed by the California Public Utilities Commission (the "CPUC") upon customers in the service areas of the three major investor-owned electric utilities in California. The CPUC has covenanted in a rate agreement with DWR (the "Rate Agreement") to calculate, revise and impose Bond Charges sufficient to pay debt service on the Bonds and other Bond Related Costs when due, as explained under "SECURITY FOR THE BONDS – Bond Related Costs" and "– Rate Covenants," and under "CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES – Rate Agreement."

In the Indenture, DWR has pledged and assigned its revenues from Bond Charges for the payment of debt service on the Bonds and Parity Obligations when due, subject to the possible prior use of revenues from Bond Charges to pay amounts due under Priority Long-Term Power Contracts (as defined in the Indenture), as explained under "SECURITY FOR THE BONDS."

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

See "**RISK FACTORS**" concerning certain risks that should be considered by investors in deciding whether to purchase Series 2005 Bonds.

THE BONDS SHALL NOT BE OR BE DEEMED TO CONSTITUTE A DEBT OR LIABILITY OF THE STATE OF CALIFORNIA OR OF ANY POLITICAL SUBDIVISION THEREOF OR A PLEDGE OF THE FAITH AND CREDIT OF THE STATE OF CALIFORNIA OR OF ANY SUCH POLITICAL SUBDIVISION, OTHER THAN DWR TO THE EXTENT PROVIDED IN THE INDENTURE. THE BONDS SHALL BE PAYABLE SOLELY FROM THE FUNDS PLEDGED THEREFOR PURSUANT TO THE INDENTURE. THE BONDS SHALL NOT DIRECTLY OR INDIRECTLY OR CONTINGENTLY OBLIGATE THE STATE OF CALIFORNIA OR ANY POLITICAL SUBDIVISION THEREOF TO LEVY OR TO PLEDGE ANY FORM OF TAXATION WHATSOEVER THEREFOR OR TO MAKE ANY APPROPRIATION FOR THEIR PAYMENT.

*Certain legal matters incident to the authorization, sale and issuance of the Series 2005 Bonds are subject to the approval of The Honorable Bill Lockyer, Attorney General of the State of California, and of Hawkins Delafield & Wood LLP, Bond Counsel to DWR. Certain legal matters will be passed upon for DWR by Nancy Saracino, Chief Counsel to DWR, and Orrick, Herrington & Sutcliffe LLP, Disclosure and Special Counsel to DWR. Certain legal matters will be passed upon for the CPUC by Randolph L. Wu, General Counsel to the CPUC, and Paul, Weiss, Rifkind, Wharton & Garrison LLP, Special Counsel to the CPUC. Certain legal matters will be passed upon for the Underwriters by Nixon Peabody LLP, counsel to the Underwriters. Certain legal matters will be passed upon for the letter of credit and liquidity facility providers by White & Case LLP, counsel to such providers. It is expected that the Series 2005 Bonds will be available for delivery on or about December 1, 2005.*

**Honorable Philip Angelides  
Treasurer of the State of California**

**JPMorgan**

**Goldman, Sachs & Co.**

**Lehman Brothers**

**Banc of America Securities LLC**

**E. J. De La Rosa & Co., Inc.**

**UBS Financial Services Inc.**

**\$759,400,000 State of California Department of Water Resources Power Supply Revenue Bonds, Series 2005F (Daily Rate) <sup>(1)</sup>**

Series	Maturity Date (May 1)	Principal Amount	Last Day of Initial Interest Period	Remarketing Agent	Credit Enhancement <sup>(2) (4)</sup>	Liquidity Support <sup>(3) (4)</sup>
F-1	2019	\$59,400,000	1/11/06	UBS Financial Services Inc.	Lloyds (LOC)	Lloyds (LOC)
F-2	2020	200,000,000	1/11/06	Goldman, Sachs & Co.	JPMorgan (50%)/Société Générale (50%) (LOC)	JPMorgan (50%)/ Société Générale (50%) (LOC)
F-3	2021	150,000,000	1/11/06	JPMorgan	BNY (50%)/CalPERS (50%) (LOC)	BNY (50%)/CalPERS (50%) (LOC)
F-4	2022	150,000,000	1/11/06	JPMorgan	Bank of America (LOC)	Bank of America (LOC)
F-5	2022	200,000,000	1/11/06	Lehman Brothers	Citibank (LOC)	Citibank (LOC)

**\$1,834,600,000 State of California Department of Water Resources Power Supply Revenue Bonds, Series 2005G (Weekly Rate) <sup>(1)</sup>**

Series	Maturity Date (May 1)	Principal Amount	Last Day of Initial Interest Period	Remarketing Agent	Credit Enhancement <sup>(2) (4)</sup>	Liquidity Support <sup>(3) (4)</sup>
G-1	2011	\$100,000,000	2/1/06	JPMorgan	Scotiabank (LOC)	Scotiabank (LOC)
G-2	2011	36,600,000	2/1/06	Lehman Brothers	Lloyds (LOC)	Lloyds (LOC)
G-3	2016	100,000,000	2/1/06	E. J. De La Rosa & Co., Inc.	FSA (INS)	JPMorgan (LIQ)
G-4	2016	98,000,000	2/1/06	Lehman Brothers	FSA (INS)	Morgan Stanley (LIQ)
G-5	2016	200,000,000	2/1/06	Banc of America Securities LLC	FSA (INS)	Fortis (75%)/Scotiabank (25%) (LIQ)
G-6	2017	225,000,000	2/15/06	JPMorgan	FSA (INS)	Calyon (67%)/ Société Générale (33%) (LIQ)
G-7	2017	75,000,000	2/15/06	UBS Financial Services Inc.	FSA (INS)	Société Générale (LIQ)
G-8	2018	200,000,000	2/15/06	Goldman, Sachs & Co.	MBIA (INS)	JPMorgan (LIQ)
G-9	2018	50,000,000	2/15/06	JPMorgan	MBIA (INS)	Scotiabank (LIQ)
G-10	2018	300,000,000	2/15/06	JPMorgan	FGIC (INS)	Depfa (LIQ)
G-11	2018	75,000,000	3/1/06	UBS Financial Services Inc.	FSA (INS)	KBC (67%)/Morgan Stanley (33%) (LIQ)
G-12	2018	50,000,000	3/1/06	JPMorgan	FGIC (INS)	LBBW (LIQ)
G-13	2018	125,000,000	3/1/06	Goldman, Sachs & Co.	FGIC (INS)	Morgan Stanley (LIQ)
G-14	2018	200,000,000	3/1/06	Lehman Brothers	FGIC (INS)	Helaba (50%)/BLB (50%) (LIQ)

<sup>(1)</sup> Interest Rate Mode immediately following Initial Interest Period. See “THE SERIES 2005 BONDS – Initial Interest Periods.”

<sup>(2)</sup> “LOC” means a direct-pay letter of credit providing both credit enhancement and liquidity support. “INS” means a financial guaranty insurance policy providing credit enhancement only. For additional information, see “SECURITY FOR THE BONDS” and Appendices I, J and K.

<sup>(3)</sup> “LOC” means a direct-pay letter of credit providing both credit enhancement and liquidity support. “LIQ” means a standby bond purchase arrangement providing liquidity support only. For additional information, see “SECURITY FOR THE BONDS” and Appendices I and K.

<sup>(4)</sup> Percentages reflect the pro rata obligations of multiple fronting banks to make payments under a single Enhancement Facility. Such obligations are several and not joint, and multiple fronting banks are not liable for the obligations of the others. See “SECURITY FOR THE BONDS – Initial Letters of Credit – Initial Letters of Credit Issued by Multiple Banks” and “– Initial Liquidity Facilities – Initial Liquidity Facilities Issued by Multiple Banks.”

## SERIES 2005F SERIES DESCRIPTIONS

<b>\$59,400,000 Series 2005F-1 Bonds</b>	
CUSIP:	13066Y LA5
Maturity Date:	May 1, 2019
Initial Interest Period:	Date of delivery through and including January 11, 2006.
Interest Payment Date for Initial Interest Period:	January 12, 2006
Interest Rate Mode Following Initial Interest Period:	Daily Rate Mode
Rate Determination Dates (Daily Rate Mode):	Not later than 10:00 a.m. New York City time each Business Day.
Interest Payment Dates (Daily Rate Mode):	The first Business Day of each calendar month, commencing February 1, 2006.
Letter of Credit (5-Year Stated Term) Issued by:	Lloyds TSB Bank plc
Remarketing Agent:	UBS Financial Services Inc.
Expected Enhanced Ratings (Long-Term/Short-Term):	Moody's: Aaa/VMIG 1 S&P: AA/A-1+ Fitch Ratings: AA+/F1+ See "RATINGS" herein.

<b>\$200,000,000 Series 2005F-2 Bonds</b>	
CUSIP:	13066Y LB3
Maturity Date:	May 1, 2020
Initial Interest Period:	Date of delivery through and including January 11, 2006.
Interest Payment Date for Initial Interest Period:	January 12, 2006
Interest Rate Mode Following Initial Interest Period:	Daily Rate Mode
Rate Determination Dates (Daily Rate Mode):	Not later than 10:00 a.m. New York City time each Business Day.
Interest Payment Dates (Daily Rate Mode):	The first Business Day of each calendar month, commencing February 1, 2006.
Letter of Credit (5-Year Stated Term) Issued by:	JPMorgan Chase Bank, National Association (50%)* Société Générale (50%)*
Remarketing Agent:	Goldman, Sachs & Co.
Expected Enhanced Ratings (Long-Term/Short-Term):	Moody's: Aaa/VMIG 1 S&P: AA-/A-1+ Fitch Ratings: A+/F1+ See "RATINGS" herein.

\* Percentages reflect the pro rata obligations of multiple fronting banks to make payments under a single direct-pay letter of credit. Such obligations are several and not joint, and multiple fronting banks are not liable for the obligations of the others. See "SECURITY FOR THE BONDS – Initial Letters of Credit – *Initial Letters of Credit Issued by Multiple Banks.*"

<b>\$150,000,000 Series 2005F-3 Bonds</b>	
CUSIP:	13066Y LC1
Maturity Date:	May 1, 2021
Initial Interest Period:	Date of delivery through and including January 11, 2006.
Interest Payment Date for Initial Interest Period:	January 12, 2006
Interest Rate Mode Following Initial Interest Period:	Daily Rate Mode
Rate Determination Dates (Daily Rate Mode):	Not later than 10:00 a.m. New York City time each Business Day.
Interest Payment Dates (Daily Rate Mode):	The first Business Day of each calendar month, commencing February 1, 2006.
Letter of Credit (3-Year Stated Term) Issued by:	The Bank of New York (50%)* California Public Employees' Retirement System (50%)*
Remarketing Agent:	J.P. Morgan Securities Inc.
Expected Enhanced Ratings (Long-Term/Short-Term):	Moody's: Aaa/VMIG 1 Fitch Ratings: AA-/F1+ See "RATINGS" herein.

<b>\$150,000,000 Series 2005F-4 Bonds</b>	
CUSIP:	13066Y LD9
Maturity Date:	May 1, 2022
Initial Interest Period:	Date of delivery through and including January 11, 2006.
Interest Payment Date for Initial Interest Period:	January 12, 2006
Interest Rate Mode Following Initial Interest Period:	Daily Rate Mode
Rate Determination Dates (Daily Rate Mode):	Not later than 10:00 a.m. New York City time each Business Day.
Interest Payment Dates (Daily Rate Mode):	The first Business Day of each calendar month, commencing February 1, 2006.
Letter of Credit (3-Year Stated Term) Issued by:	Bank of America, N.A.
Remarketing Agent:	J.P. Morgan Securities Inc.
Expected Enhanced Ratings (Long-Term/Short-Term):	Moody's: Aaa/VMIG 1 S&P: AA/A-1+ Fitch Ratings: AA-/F1+ See "RATINGS" herein.

\* Percentages reflect the pro rata obligations of multiple fronting banks to make payments under a single direct-pay letter of credit. Such obligations are several and not joint, and multiple fronting banks are not liable for the obligations of the others. See "SECURITY FOR THE BONDS – Initial Letters of Credit – *Initial Letters of Credit Issued by Multiple Banks.*"

**\$200,000,000 Series 2005F-5 Bonds**

CUSIP:	13066Y LE7
Maturity Date:	May 1, 2022
Initial Interest Period:	Date of delivery through and including January 11, 2006.
Interest Payment Date for Initial Interest Period:	January 12, 2006
Interest Rate Mode Following Initial Interest Period:	Daily Rate Mode
Rate Determination Dates (Daily Rate Mode):	Not later than 10:00 a.m. New York City time each Business Day.
Interest Payment Dates (Daily Rate Mode):	The first Business Day of each calendar month, commencing February 1, 2006.
Letter of Credit (3-Year Stated Term) Issued by:	Citibank, N.A.
Remarketing Agent:	Lehman Brothers Inc.
Expected Enhanced Ratings (Long-Term/Short-Term):	Moody's: Aaa/VMIG 1 S&P: AA/A-1+ Fitch Ratings: AA+/F1+ See "RATINGS" herein.

## SERIES 2005G SERIES DESCRIPTIONS

<b>\$100,000,000 Series 2005G-1 Bonds</b>	
CUSIP:	13066Y LK3
Maturity Date:	May 1, 2011
Initial Interest Period:	Date of delivery through and including February 1, 2006.
Interest Payment Date for Initial Interest Period:	February 2, 2006
Interest Rate Mode Following Initial Interest Period:	Weekly Rate Mode
Rate Determination Dates (Weekly Rate Mode):	Wednesdays, or if not a Business Day, the next preceding Business Day, commencing February 1, 2006.
Interest Payment Dates (Weekly Rate Mode):	The first Business Day of each calendar month, commencing March 1, 2006.
Letter of Credit (5-Year Stated Term) Issued by:	Bank of Nova Scotia
Remarketing Agent:	J.P. Morgan Securities Inc.
Expected Enhanced Ratings (Long-Term/Short-Term):	Moody's: Aaa/VMIG 1 S&P: AA-/A-1+ Fitch Ratings: AA-/F1+ See "RATINGS" herein.

<b>\$36,600,000 Series 2005G-2 Bonds</b>	
CUSIP:	13066Y LL1
Maturity Date:	May 1, 2011
Initial Interest Period:	Date of delivery through and including February 1, 2006.
Interest Payment Date for Initial Interest Period:	February 2, 2006
Interest Rate Mode Following Initial Interest Period:	Weekly Rate Mode
Rate Determination Dates (Weekly Rate Mode):	Wednesdays, or if not a Business Day, the next preceding Business Day, commencing February 1, 2006.
Interest Payment Dates (Weekly Rate Mode):	The first Business Day of each calendar month, commencing March 1, 2006.
Letter of Credit (5-Year Stated Term) Issued by:	Lloyds TSB Bank plc
Remarketing Agent:	Lehman Brothers Inc.
Expected Enhanced Ratings (Long-Term/Short-Term):	Moody's: Aaa/VMIG 1 S&P: AA/A-1+ Fitch Ratings: AA+/F1+ See "RATINGS" herein.

<b>\$100,000,000 Series 2005G-3 Bonds</b>	
CUSIP:	13066Y LM9
Maturity Date:	May 1, 2016
Initial Interest Period:	Date of delivery through and including February 1, 2006.
Interest Payment Date for Initial Interest Period:	February 2, 2006
Interest Rate Mode Following Initial Interest Period:	Weekly Rate Mode
Rate Determination Dates (Weekly Rate Mode):	Wednesdays, or if not a Business Day, the next preceding Business Day, commencing February 1, 2006.
Interest Payment Dates (Weekly Rate Mode):	The first Business Day of each calendar month, commencing March 1, 2006.
Bond Insurance:	Financial Security Assurance Inc.
Liquidity Facility (7-Year Stated Term) Issued by:	JPMorgan Chase Bank, National Association
Remarketing Agent:	E. J. De La Rosa & Co., Inc.
Expected Enhanced Ratings:	Moody's: Aaa/VMIG 1 S&P: AAA/A-1+ Fitch Ratings: AAA/F1+ See "RATINGS" herein.

<b>\$98,000,000 Series 2005G-4 Bonds</b>	
CUSIP:	13066Y LN7
Maturity Date:	May 1, 2016
Initial Interest Period:	Date of delivery through and including February 1, 2006.
Interest Payment Date for Initial Interest Period:	February 2, 2006
Interest Rate Mode Following Initial Interest Period:	Weekly Rate Mode
Rate Determination Dates (Weekly Rate Mode):	Wednesdays, or if not a Business Day, the next preceding Business Day, commencing February 1, 2006.
Interest Payment Dates (Weekly Rate Mode):	The first Business Day of each calendar month, commencing March 1, 2006.
Bond Insurance:	Financial Security Assurance Inc.
Liquidity Facility (5-Year Stated Term) Issued by:	Morgan Stanley Bank
Remarketing Agent:	Lehman Brothers Inc.
Expected Enhanced Ratings:	Moody's: Aaa/VMIG 1 S&P: AAA/A-1 Fitch Ratings: AAA/F1+ See "RATINGS" herein.

<b>\$200,000,000 Series 2005G-5 Bonds</b>	
CUSIP:	13066Y LP2
Maturity Date:	May 1, 2016
Initial Interest Period:	Date of delivery through and including February 1, 2006.
Interest Payment Date for Initial Interest Period:	February 2, 2006
Interest Rate Mode Following Initial Interest Period:	Weekly Rate Mode
Rate Determination Dates (Weekly Rate Mode):	Wednesdays, or if not a Business Day, the next preceding Business Day, commencing February 1, 2006.
Interest Payment Dates (Weekly Rate Mode):	The first Business Day of each calendar month, commencing March 1, 2006.
Bond Insurance:	Financial Security Assurance Inc.
Liquidity Facility (5-Year Stated Term) Issued by:	Fortis Bank S.A./N.V. (75%)* Bank of Nova Scotia (25%)*
Remarketing Agent:	Banc of America Securities LLC
Expected Enhanced Ratings:	Moody's: Aaa/VMIG 1 S&P: AAA/A-1+ Fitch Ratings: AAA/F1+ See "RATINGS" herein.

<b>\$225,000,000 Series 2005G-6 Bonds</b>	
CUSIP:	13066Y LF4
Maturity Date:	May 1, 2017
Initial Interest Period:	Date of delivery through and including February 15, 2006.
Interest Payment Date for Initial Interest Period:	February 16, 2006
Interest Rate Mode Following Initial Interest Period:	Weekly Rate Mode
Rate Determination Dates (Weekly Rate Mode):	Wednesdays, or if not a Business Day, the next preceding Business Day, commencing February 15, 2006.
Interest Payment Dates (Weekly Rate Mode):	The first Business Day of each calendar month, commencing March 1, 2006.
Bond Insurance:	Financial Security Assurance Inc.
Liquidity Facility (5-Year Stated Term) Issued by:	Calyon (67%)* Soci�t� G�n�rale (33%)*
Remarketing Agent:	J.P. Morgan Securities Inc.
Expected Enhanced Ratings:	Moody's: Aaa/VMIG 1 S&P: AAA/A-1+ Fitch Ratings: AAA/F1+ See "RATINGS" herein.

\* Percentages reflect the pro rata obligations of multiple fronting banks to make payments under a single liquidity facility. Such obligations are several and not joint, and multiple fronting banks are not liable for the obligations of the others. See "SECURITY FOR THE BONDS – Initial Liquidity Facilities – *Initial Liquidity Facilities Issued by Multiple Banks.*"

<b>\$75,000,000 Series 2005G-7 Bonds</b>	
CUSIP:	13066Y LG2
Maturity Date:	May 1, 2017
Initial Interest Period:	Date of delivery through and including February 15, 2006.
Interest Payment Date for Initial Interest Period:	February 16, 2006
Interest Rate Mode Following Initial Interest Period:	Weekly Rate Mode
Rate Determination Dates (Weekly Rate Mode):	Wednesdays, or if not a Business Day, the next preceding Business Day, commencing February 15, 2006.
Interest Payment Dates (Weekly Rate Mode):	The first Business Day of each calendar month, commencing March 1, 2006.
Bond Insurance:	Financial Security Assurance Inc.
Liquidity Facility (5-Year Stated Term) Issued by:	Société Générale
Remarketing Agent:	UBS Financial Services Inc.
Expected Enhanced Ratings:	Moody's: Aaa/VMIG 1 S&P: AAA/A-1+ Fitch Ratings: AAA/F1+ See "RATINGS" herein.

<b>\$200,000,000 Series 2005G-8 Bonds</b>	
CUSIP:	13066Y LH0
Maturity Date:	May 1, 2018
Initial Interest Period:	Date of delivery through and including February 15, 2006.
Interest Payment Date for Initial Interest Period:	February 16, 2006
Interest Rate Mode Following Initial Interest Period:	Weekly Rate Mode
Rate Determination Dates (Weekly Rate Mode):	Wednesdays, or if not a Business Day, the next preceding Business Day, commencing February 15, 2006.
Interest Payment Dates (Weekly Rate Mode):	The first Business Day of each calendar month, commencing March 1, 2006.
Bond Insurance:	MBIA Insurance Corporation
Liquidity Facility (7-Year Stated Term) Issued by:	JPMorgan Chase Bank, National Association
Remarketing Agent:	Goldman, Sachs & Co.
Expected Enhanced Ratings:	Moody's: Aaa/VMIG 1 S&P: AAA/A-1+ Fitch Ratings: AAA/F1+ See "RATINGS" herein.

<b>\$50,000,000 Series 2005G-9 Bonds</b>	
CUSIP:	13066Y LJ6
Maturity Date:	May 1, 2018
Initial Interest Period:	Date of delivery through and including February 15, 2006.
Interest Payment Date for Initial Interest Period:	February 16, 2006
Interest Rate Mode Following Initial Interest Period:	Weekly Rate Mode
Rate Determination Dates (Weekly Rate Mode):	Wednesdays, or if not a Business Day, the next preceding Business Day, commencing February 15, 2006.
Interest Payment Dates (Weekly Rate Mode):	The first Business Day of each calendar month, commencing March 1, 2006.
Bond Insurance:	MBIA Insurance Corporation
Liquidity Facility (5-Year Stated Term) Issued by:	Bank of Nova Scotia
Remarketing Agent:	J.P. Morgan Securities Inc.
Expected Enhanced Ratings:	Moody's: Aaa/VMIG 1 S&P: AAA/A-1+ Fitch Ratings: AAA/F1+ See "RATINGS" herein.

<b>\$300,000,000 Series 2005G-10 Bonds</b>	
CUSIP:	13066Y LQ0
Maturity Date:	May 1, 2018
Initial Interest Period:	Date of delivery through and including February 15, 2006
Interest Payment Date for Initial Interest Period:	February 16, 2006
Interest Rate Mode Following Initial Interest Period:	Weekly Rate Mode
Rate Determination Dates (Weekly Rate Mode):	Wednesdays, or if not a Business Day, the next preceding Business Day, commencing March 1, 2006
Interest Payment Dates (Weekly Rate Mode):	The first Business Day of each calendar month, commencing April 3, 2006.
Bond Insurance:	Financial Guaranty Insurance Company
Liquidity Facility (10-Year Stated Term) Issued by:	DEPFA BANK plc
Remarketing Agent:	J.P. Morgan Securities Inc.
Expected Enhanced Ratings:	Moody's: Aaa/VMIG 1 S&P: AAA/A-1+ Fitch Ratings: AAA/F1+ See "RATINGS" herein.

<b>\$75,000,000 Series 2005G-11 Bonds</b>	
CUSIP:	13066Y LR8
Maturity Date:	May 1, 2018
Initial Interest Period:	Date of delivery through and including March 1, 2006
Interest Payment Date for Initial Interest Period:	March 2, 2006
Interest Rate Mode Following Initial Interest Period:	Weekly Rate Mode
Rate Determination Dates (Weekly Rate Mode):	Wednesdays, or if not a Business Day, the next preceding Business Day, commencing March 1, 2006
Interest Payment Dates (Weekly Rate Mode):	The first Business Day of each calendar month, commencing April 3, 2006.
Bond Insurance:	Financial Security Assurance Inc.
Liquidity Facility (3-Year Stated Term) Issued by:	KBC Bank N.V. (67%)* Morgan Stanley Bank (33%)*
Remarketing Agent:	UBS Financial Services Inc.
Expected Enhanced Ratings:	Moody's: Aaa/VMIG 1 S&P: AAA/A-1 Fitch Ratings: AAA/F1+ See "RATINGS" herein.

<b>\$50,000,000 Series 2005G-12 Bonds</b>	
CUSIP:	13066Y LS6
Maturity Date:	May 1, 2018
Initial Interest Period:	Date of delivery through and including March 1, 2006
Interest Payment Date for Initial Interest Period:	March 2, 2006
Interest Rate Mode Following Initial Interest Period:	Weekly Rate Mode
Rate Determination Dates (Weekly Rate Mode):	Wednesdays, or if not a Business Day, the next preceding Business Day, commencing March 1, 2006
Interest Payment Dates (Weekly Rate Mode):	The first Business Day of each calendar month, commencing April 3, 2006.
Bond Insurance:	Financial Guaranty Insurance Company
Liquidity Facility (3-Year Stated Term) Issued by:	Landesbank Baden Württemberg
Remarketing Agent:	J.P. Morgan Securities Inc.
Expected Enhanced Ratings:	Moody's: Aaa/VMIG 1 S&P: AAA/A-1 Fitch Ratings: AAA/F1+ See "RATINGS" herein.

\* Percentages reflect the pro rata obligations of multiple fronting banks to make payments under a single liquidity facility. Such obligations are several and not joint, and multiple fronting banks are not liable for the obligations of the others. See "SECURITY FOR THE BONDS – Initial Liquidity Facilities – *Initial Liquidity Facilities Issued by Multiple Banks.*"

<b>\$125,000,000 Series 2005G-13 Bonds</b>	
CUSIP:	13066Y LT4
Maturity Date:	May 1, 2018
Initial Interest Period:	Date of delivery through and including March 1, 2006
Interest Payment Date for Initial Interest Period:	March 2, 2006
Interest Rate Mode Following Initial Interest Period:	Weekly Rate Mode
Rate Determination Dates (Weekly Rate Mode):	Wednesdays, or if not a Business Day, the next preceding Business Day, commencing March 1, 2006
Interest Payment Dates (Weekly Rate Mode):	The first Business Day of each calendar month, commencing April 3, 2006.
Bond Insurance:	Financial Guaranty Insurance Company
Liquidity Facility (3-Year Stated Term) Issued by:	Morgan Stanley Bank
Remarketing Agent:	Goldman, Sachs & Co.
Expected Enhanced Ratings:	Moody's: Aaa/VMIG 1 S&P: AAA/A-1 Fitch Ratings: AAA/F1+ See "RATINGS" herein.

<b>\$200,000,000 Series 2005G-14 Bonds</b>	
CUSIP:	13066Y LU1
Maturity Date:	May 1, 2018
Initial Interest Period:	Date of delivery through and including March 1, 2006
Interest Payment Date for Initial Interest Period:	March 2, 2006
Interest Rate Mode Following Initial Interest Period:	Weekly Rate Mode
Rate Determination Dates (Weekly Rate Mode):	Wednesdays, or if not a Business Day, the next preceding Business Day, commencing March 1, 2006
Interest Payment Dates (Weekly Rate Mode):	The first Business Day of each calendar month, commencing April 3, 2006.
Bond Insurance:	Financial Guaranty Insurance Company
Liquidity Facility (3-Year Stated Term) Issued by:	Landesbank Hessen-Thüringen Girozentrale (50%)* Bayerische Landesbank (50%)*
Remarketing Agent:	Lehman Brothers Inc.
Expected Enhanced Ratings:	Moody's: Aaa/VMIG 1 S&P: AAA/A-1 Fitch Ratings: AAA/F1+ See "RATINGS" herein.

\* Percentages reflect the pro rata obligations of multiple fronting banks to make payments under a single liquidity facility. Such obligations are several and not joint, and multiple fronting banks are not liable for the obligations of the others. See "SECURITY FOR THE BONDS – Initial Liquidity Facilities – *Initial Liquidity Facilities Issued by Multiple Banks.*"

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Copies of this Official Statement may be obtained from:

**HONORABLE PHILIP ANGELIDES**

Treasurer of the State of California

Agent for Sale

P.O. Box 942809

Sacramento, California 94209-0001

1-800-900-3873

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## GENERAL INFORMATION

For an index of defined terms used in this Official Statement, see APPENDIX G – “INDEX OF PRINCIPAL DEFINITIONS.” Capitalized terms used but not defined in this Official Statement have the meanings given in the Indenture. For definitions of certain terms used in the Indenture, see APPENDIX C – “SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE.”

Descriptions and summaries of CPUC orders, the Rate Agreement, the Indenture, the Series 2005 Bonds, the Master Credit, Liquidity and Participation Agreement (the “Master Bank Agreement”), DWR’s servicing arrangements, DWR’s power supply contracts (including the Priority Long-Term Power Contracts), Division 27 (commencing with Section 80000) of the California Water Code, as amended from time to time (the “Act”), and other documents, regulations and laws referred to in this Official Statement do not purport to be complete and reference is made to each of them for a complete statement of their provisions. A copy of the Rate Agreement is attached as Appendix D to this Official Statement. Copies of DWR’s power supply contracts are posted on DWR’s Internet site at [www.cers.water.ca.gov](http://www.cers.water.ca.gov). Copies of other DWR documents may be obtained by request to DWR at [cersforum@water.ca.gov](mailto:cersforum@water.ca.gov) or 3310 El Camino Avenue, Suite 120, Sacramento, California 95821, Attention: Chief, Financial Management Office, Power Supply Program, upon payment of a reproduction fee.

So far as any statements made in this Official Statement involve matters of opinion, assumptions, projections, anticipated events or estimates, whether or not expressly stated, they are set forth as such and not as representations of fact, and actual results may differ substantially from those set forth herein. Neither this Official Statement nor any statement which may have been made verbally or in writing is to be construed as a contract with the owners of the Series 2005 Bonds.

No person has been authorized to give information or to make any representations other than those 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 DWR or the State. This Official Statement does not constitute an offer to sell or a solicitation of an offer to buy, nor shall there be any sale of the Series 2005 Bonds offered hereby by any person in any jurisdiction in which it is unlawful for such person to make such offer, solicitation or sale. This Official Statement speaks only as of its date and any information, estimates and/or expressions of opinion herein are subject to change without notice; and neither the delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no material change in the affairs of DWR or the CPUC since the date hereof.

The information set forth herein has been obtained from official sources that are believed to be reliable, but it is not guaranteed as to accuracy or completeness. The presentation of information is intended to show recent historic information and is not intended to indicate future or continuing trends in the financial position or other affairs of DWR or the CPUC. No representation is made that past experience, as it might be shown by such financial and other information, will necessarily continue or be repeated in the future.

This Official Statement includes forward-looking statements that are based on DWR’s current expectations and projections about future events. These forward-looking statements are subject to risks and uncertainties, including risks and uncertainties outside the control of DWR. Such statements generally are identifiable by the terminology used, such as “plan,” “expect,” “estimate,” “budget,” “believes” or other similar words. Such forward-looking statements include but are not limited to certain statements contained under the captions “SUMMARY,” “PLAN OF REFUNDING,” “SECURITY FOR THE BONDS,” “THE DWR POWER SUPPLY PROGRAM,” “CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES,” “LITIGATION AND ADMINISTRATIVE PROCEEDINGS,” “RISK FACTORS” and “TAX MATTERS” in this Official Statement. The achievement of certain results or other expectations contained in such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause actual results, performance or achievements described to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. DWR does not plan to issue any updates or revisions to these forward-looking statements if or when expectations or events, conditions or circumstances on which such statements are based occur or fail to occur.

A wide variety of other information, including financial information, concerning DWR and the State is available from DWR, the State Treasurer, the State and publications and websites of DWR, the State Treasurer, the State and various State agencies and officials, including the CPUC. Except as expressly provided otherwise herein, no such information is a part of or incorporated into this Official Statement.

The CPUC makes no representation as to the accuracy or completeness of this Official Statement, including any forward-looking statements or projections contained in this Official Statement and any description in this Official Statement of litigation involving or affecting the CPUC. Any statements regarding such litigation do not necessarily represent the CPUC's view of such litigation or any position in such litigation. In addition, while CPUC staff may have assisted in the preparation of certain sections of this Official Statement, the CPUC can only take positions through formal action and has not taken any such action or approved this Official Statement. The CPUC is an independent five member body that must act by an affirmative vote of a majority of its members and, as a result, the CPUC can only indicate its views in formal decisions or other formal actions. In addition, the CPUC is an independent body not subject to the control of DWR and may take positions in the future different from DWR in litigation, or other matters described in this Official Statement. As a result, statements in this Official Statement regarding electricity markets and regulation, and DWR's views of the CPUC's role or DWR's role in such markets and regulation, do not necessarily represent the views, opinions or beliefs of the CPUC and should not be construed as such by any recipient of this Official Statement.

Information in this Official Statement about the major investor-owned utilities in California, Pacific Gas & Electric Company, San Diego Gas & Electric Company and Southern California Edison (collectively, the "IOUs"), has been obtained from publicly available documents. Each of the IOUs and the parent companies of each of the IOUs named under "THE DWR POWER SUPPLY PROGRAM – Customer Base" file annual, quarterly and certain other reports with the Securities and Exchange Commission ("SEC"). Such reports are available on the SEC's website ([www.sec.gov](http://www.sec.gov)) and upon request from the Office of Public Reference of the SEC, 450 5th Street, NW, Room 1300, Washington, D.C. 20549-0102 (phone: (202) 942-8090; fax: (202) 628-9001; e-mail: [publicinfo@sec.gov](mailto:publicinfo@sec.gov)). No such report is a part of or incorporated into this Official Statement. Filings by each of the IOUs with the Federal Energy Regulatory Commission ("FERC") may be found on FERC's website ([www.ferc.gov](http://www.ferc.gov)). No such report on the SEC's website or report on the FERC website is a part of or incorporated into this Official Statement. The information referred to in this paragraph has not been independently verified and DWR and the Underwriters do not warrant that this information is accurate or complete.

Information about bond insurers, letter of credit providers and liquidity facility providers in this Official Statement has been obtained from such insurers and providers. Additional information concerning such insurers and providers may be found in other documents referenced in Appendix I and Appendix J. No such additional information or other document is a part of or incorporated into this Official Statement unless expressly stated otherwise. The information referred to in this paragraph has not been independently verified and DWR, the CPUC and the Underwriters do not warrant that such information is accurate or complete.

In connection with this offering the Underwriters may over-allot or effect transactions that stabilize or maintain the market prices of the Series 2005 Bonds offered hereby at levels above that which might otherwise prevail in the open market. Such stabilizing, if commenced, may be discontinued at any time.

The Underwriters have provided the following sentence for inclusion in this Official Statement: The Underwriters have reviewed the information in this Official Statement in accordance with, and as a part of, their responsibilities to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Underwriters do not guarantee the accuracy or completeness of such information.

Other than with respect to information concerning Financial Security Assurance Inc. contained under the caption "APPENDIX J – INFORMATION CONCERNING THE BOND INSURERS AND THE FORMS OF FINANCIAL GUARANTY INSURANCE POLICIES – FINANCIAL SECURITY ASSURANCE INC." and the specimen "Municipal Bond Insurance Policy" herein, none of the information in this Official Statement has been supplied or verified by Financial Security Assurance Inc. and Financial Security Assurance Inc. makes no representation or warranty, express or implied, as to (i) the accuracy or completeness of such information; (ii) the validity of the FSA-Insured Bonds; or (iii) the tax exempt status of the interest on the FSA-Insured Bonds.

OFFICIAL STATEMENT

\$2,594,000,000

State of California Department of Water Resources
Power Supply Revenue Bonds, Series 2005F and Series 2005G

SUMMARY

This summary is a brief description of the Series 2005 Bonds and this Official Statement. A full review should be made of the entire Official Statement, including the Appendices. The Index of Principal Definitions in Appendix G lists the pages on which the definitions of principal terms used in this Official Statement appear.

General ..... This Official Statement describes the Department of Water Resources ("DWR") of the State of California ("State"), DWR's Power Supply Program and DWR's Power Supply Revenue Bonds (the "Bonds"), including its \$759,400,000 Power Supply Revenue Bonds, Series 2005F (the "Series 2005F Bonds") and its \$1,834,600,000 Power Supply Revenue Bonds, Series 2005G (the "Series 2005G Bonds" and together with the Series 2005F Bonds, the "Series 2005 Bonds"), offered hereby. See "SECURITY FOR THE BONDS."

Outstanding Bonds; Plan of Refunding ..... In 2002, DWR issued Bonds in the aggregate principal amount of \$11,263,500,000 (the "Series 2002 Bonds") for the purpose of financing and refinancing costs of the Power Supply Program. DWR is issuing the Series 2005 Bonds to refund \$2,352,210,000 principal amount of Series 2002 Bonds, and to pay costs of issuance and certain costs of credit and liquidity enhancement of the Series 2005 Bonds. Upon the issuance of the Series 2005 Bonds, \$10,937,415,000 aggregate principal amount of Bonds will remain "Outstanding" (as defined in Appendix C). See "PLAN OF REFUNDING."

The Series 2002 Bonds, the Series 2005 Bonds and any Additional Bonds that are Outstanding from time to time will be secured by and payable from the Trust Estate on a parity basis. See "SECURITY FOR THE BONDS."

Bond Authorization ..... The Series 2005 Bonds are being issued under Division 27 (commencing with Section 80000) of the California Water Code, as amended from time to time (the "Act") and a Trust Indenture, as amended and supplemented (the "Indenture"), including, with respect to the Series 2005 Bonds, as supplemented by a Fourth Supplemental Trust Indenture (the "Fourth Supplemental Indenture") among DWR, the Treasurer of the State, as Trustee, and U.S. Bank National Association, as Co-Trustee (collectively, the "Trustees").

The Series 2005 Bonds ..... The Series 2005F Bonds will be issued in five separate subseries, designated Series 2005F-1 through Series 2005F-5. The Series 2005G Bonds will be issued in 14 separate subseries, designated Series 2005G-1 through Series 2005G-14. The Series Descriptions following the cover of this Official Statement contain, for each subseries of Series 2005 Bonds, summary descriptions of: the CUSIP number, the principal amount, the maturity date, the length of the Initial Interest Period, the Interest Rate Mode following the Initial Interest Period, the interest payment dates, the

interest rate determination dates, the Remarketing Agents, the providers of credit enhancement and liquidity support, and the expected enhanced ratings assigned to each such subseries. Series 2005 Bonds may be purchased in book-entry form only, in the principal amount of \$100,000 or any integral multiple of \$5,000 in excess thereof. The Series 2005 Bonds will be subject to redemption before their stated maturity, at the option of DWR, as described herein. Certain subseries of the Series 2005 Bonds will be term bonds, subject to mandatory redemption from Sinking Fund Installments. In certain circumstances, the owners of the Series 2005 Bonds will have the option of tendering their Bonds for purchase, and in certain circumstances the owners of the Series 2005 Bonds will be required to tender their Bonds for purchase, as described herein. See “THE SERIES 2005 BONDS.”

**Department of Water Resources.....**

DWR was established in 1956 under California law as a department of the State. The Director and Chief Deputy Director of DWR are appointed by the Governor and, as a part of the Executive Branch, report to the Governor through the Secretary of the Resources Agency. DWR has been operating the Power Supply Program since early 2001. See “THE DWR POWER SUPPLY PROGRAM.” Under the Power Supply Program, DWR has been purchasing power for sale to end use customers in the service areas of the three major investor-owned electric utilities in the State: Pacific Gas and Electric Company (“PG&E”), Southern California Edison (“SCE”), and San Diego Gas & Electric Company (“SDG&E”) (collectively, the “IOUs”).

**Power Supply Program.....**

DWR established the Power Supply Program in 2001, when Governor Gray Davis determined that the IOUs could not supply electric power sufficient to prevent widespread and prolonged disruption of electric service in California. Governor Davis proclaimed a state of emergency, and directed DWR to procure electric power for retail customers of the IOUs. During 2001 and 2002, DWR entered into both short-term and long-term contracts to purchase power from wholesale suppliers, and supplied the portion of the retail load that the IOUs could not provide (the “net short”). DWR continues to purchase wholesale power to satisfy the net short, but only through long-term wholesale power contracts that DWR entered into prior to December 31, 2002. On that date, DWR’s statutory authority to enter into new power purchase arrangements expired, and DWR has not made any spot market purchases and has not entered into any new power contracts since that date. As DWR’s existing power contracts expire, the IOUs are required to replace that power. See “THE DWR POWER SUPPLY PROGRAM.”

DWR recovers the costs of the Power Supply Program through “Bond Charges” and “Power Charges,” which are imposed by the CPUC on the approximately 11 million bundled customers and certain direct access customers. A “bundled customer” is a retail customer that purchases electrical energy and transmission and distribution services from an IOU. A “direct access” customer is a retail customer that purchases electrical energy from an electric service provider but purchases transmission and distribution services from an IOU. An “electric service provider” is a privately-owned retail seller of electrical energy, other than an IOU that

is regulated by the CPUC, as defined with more particularity in Appendix D.

Bond Charges are the primary source of money to pay debt service on the Bonds, and must be imposed by the CPUC whether or not DWR continues to purchase or sell electricity under the Power Supply Program. Power Charges are the primary source of money to procure wholesale power and pay other operating costs of the Power Supply Program. See “SECURITY FOR THE BONDS – Rate Covenants” and “CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES – Rate Agreement.”

**California Public Utilities**

**Commission.....**

Under California law and the Rate Agreement (described below), the CPUC sets Bond Charges and Power Charges to recover DWR’s statutorily defined revenue requirements and allocates such charges among service areas and electric customers. The CPUC has also adopted a number of decisions that implement other aspects of the Power Supply Program. See “CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES.”

The CPUC was established in 1911 under the California Constitution and the California Public Utilities Act enacted in 1912. The CPUC is an independent regulatory agency and is not controlled by DWR. The CPUC regulates the IOUs and other California entities, mostly investor-owned electric, telecommunications, natural gas, water, railroad and passenger transportation companies. See “CALIFORNIA PUBLIC UTILITIES COMMISSION.”

The CPUC makes no representation as to the accuracy or completeness of this Official Statement, including any forward-looking statements or projections contained in this Official Statement and any description in this Official Statement of litigation involving or affecting the CPUC. Any statements regarding such litigation do not necessarily represent the CPUC’s view of such litigation or any position in such litigation. In addition, while CPUC staff may have assisted in the preparation of certain sections of this Official Statement, the CPUC can only take positions through formal action and has not taken any such action or approved this Official Statement. The CPUC is an independent five member body that must act by an affirmative vote of a majority of its members and, as a result, the CPUC can only indicate its views in formal decisions or other formal actions. In addition, the CPUC is an independent body not subject to the control of DWR and may take positions in the future different from DWR in litigation, or other matters described in this Official Statement. As a result, statements in this Official Statement regarding electricity markets and regulation, and DWR’s views of the CPUC’s role or DWR’s role in such markets and regulation, do not necessarily represent the views, opinions or beliefs of the CPUC and should not be construed as such by any recipient of this Official Statement.

**Rate Covenants and Bond**

**Charges.....**

The Bonds are payable primarily from charges (“Bond Charges”) to be imposed by the CPUC upon the approximately 11 million bundled

customers and certain direct access customers in the service areas of the IOUs. In the Rate Agreement with DWR (the “Rate Agreement”), the CPUC has covenanted to calculate, revise and impose from time to time, Bond Charges sufficient to provide moneys so that amounts available for deposit in the Bond Charge Payment Account under the Indenture from time to time, together with amounts on deposit in the Bond Charge Payment Account, are at all times sufficient to pay or provide for the payment of debt service on the Bonds and other Bond Related Costs (as defined in the Rate Agreement) when due in accordance with the Indenture and other financing documents. See “SECURITY FOR THE BONDS – Rate Covenants” and “CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES – Rate Agreement.”

Under the Act and the Rate Agreement, DWR is responsible for notifying the CPUC of the amounts required to pay Bond Related Costs that are to be recovered from Bond Charges. “CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES – Rate Agreement.” Under the Rate Agreement, DWR is also responsible for notifying the CPUC of DWR’s “Retail Revenue Requirements” (defined in the Rate Agreement as the amounts required to pay DWR costs that are to be recovered from Power Charges imposed by the CPUC from time to time). Retail Revenue Requirements do not include Bond Related Costs recovered from Bond Charges.

In the Indenture, DWR has covenanted to cause to be established, fixed and revised from time to time, charges sufficient, together with any other available moneys and securities on deposit in DWR’s Electric Power Fund, to satisfy all of DWR’s revenue requirements at the times and in the amounts needed. The term “revenue requirement” means the amounts needed from time to time by DWR to satisfy its obligations under the Act and under proclamations and orders issued pursuant to the California Emergency Services Act that are identified in the Indenture. These obligations include, but are not limited to, making deposits to the Bond Charge Payment Account and Debt Service Reserve Account in the amounts and at the times required by the Indenture. See “CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES - DWR Actions to Establish Revenue Requirements.”

**Bond Related Costs .....**

Bond Related Costs that are payable from Bond Charges imposed by the CPUC under the Rate Agreement include, among other costs, debt service on the Bonds and payments required to be made: (i) under agreements with issuers of credit and liquidity facilities, including letters of credit, bond insurance, guarantees, debt service reserve fund surety bonds, lines of credit, reimbursement agreements, and standby bond purchase agreements, (ii) under agreements relating to other financial instruments entered into in connection with the Bonds, including but not limited to investment agreements, hedges, interest rate swaps, caps, options and forward purchase agreements, and (iii) under agreements relating to the remarketing of Bonds, including but not limited to remarketing agreements, dealer agreements and auction agent agreements. Such payments may cover fees, expenses, indemnification, or other obligations due the providers of any such facilities, and such agreements may be entered into at any time concurrently with or after the

issuance of Bonds. See “SECURITY FOR THE BONDS – Bond Related Costs.”

In connection with the issuance of the Series 2005 Bonds, DWR has entered into agreements with interest rate swap providers, and expects to enter into agreements with issuers of credit and liquidity facilities and agreements relating to the remarketing of the Series 2005 Bonds, each requiring the payment of certain Bond Related Costs on a parity with payment of debt service on the Bonds. See “PLAN OF REFUNDING” and “SECURITY FOR THE BONDS – Bond Related Costs.”

**Security for the Bonds;  
Bond Charge Revenues.....**

The primary source of moneys for the payment of debt service on the Bonds and other Bond Related Costs will be Bond Charge Revenues, which constitute part of the Trust Estate securing the Bonds, as described below.

The “Trust Estate” is assigned and pledged to the Trustees under the Indenture for the benefit of the Bonds and Parity Obligations, subject to the use of the Trust Estate in accordance with the Indenture. The “Trust Estate” is defined in the Indenture to include, among other things, “Revenues.” “Revenues” includes “Bond Charge Revenues,” “Power Charge Revenues” and “Direct Access Power Charge Revenues.” “Revenues” also includes revenues from a surcharge (referred to herein as the “Cost Responsibility Surcharge”) on direct access customers, various types of “departing load” and from other possible future sources as described under “THE DWR POWER SUPPLY PROGRAM – Direct Access, Departing Load and Community Choice Aggregation” and “CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES.”

- “Bond Charge Revenues” are Revenues received by DWR arising from Bond Charges imposed by the CPUC upon customers in the service areas of the IOUs as described under “SECURITY FOR THE BONDS – Rate Covenants.”
- “Power Charge Revenues” are Revenues received by DWR arising from Power Charges imposed by the CPUC upon customers for electric power deemed sold to customers by DWR as described under “CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES.”
- “Direct Access Power Charge Revenues” are Revenues received by DWR from Direct Access Power Charges imposed by the CPUC upon any person receiving power from an “Electric Service Provider” (as that term is defined in the Rate Agreement, attached as Appendix D).

The use of amounts on deposit in the Bond Charge Collection Account (including Bond Charge Revenues) for the payment of debt service on the Bonds and other Bond Related Costs when due is subject to the possible prior use of such amounts to pay amounts due under Priority Long-Term Power Contracts (“Priority Contract Costs”). See “SECURITY FOR THE BONDS” and “RISK FACTORS – Determination of Power

Charges and Bond Charges; Possible Use of Amounts in the Bond Charge Collection Account to Pay Priority Contract Costs.”

**Sources of Payment of Operating Expenses; Priority Long-Term**

**Power Contracts .....**

Power Supply Program operating expenses, including Priority Contract Costs, are expected to be paid from Power Charge Revenues, Direct Access Power Charge Revenues and other Revenues (other than Bond Charge Revenues). Each Priority Long-Term Power Contract (see “SECURITY FOR THE BONDS – Priority Long-Term Power Contracts”) contains a provision requiring that payments by DWR under the contract are to be paid or payable prior to payment of Bond Related Costs. Substantially all of the power to be purchased by DWR will be purchased under Priority Long-Term Power Contracts and for that reason substantially all of the operating expenses of the Power Supply Program will be Priority Contract Costs. The CPUC has covenanted to calculate, revise and impose Power Charges sufficient to satisfy the Retail Revenue Requirements, including Priority Contract Costs, as specified by DWR. See “SECURITY FOR THE BONDS – Rate Covenants” above. See also “RISK FACTORS – Determination of Power Charges and Bond Charges; Possible Use of Amounts in the Bond Charge Collection Account to Pay Priority Contract Costs.”

**Accounts and Flow of Funds under the Indenture.....**

The Indenture establishes within the Electric Power Fund two sets of accounts for Revenues. One set of accounts, the “Bond Charge Accounts,” is primarily for the deposit of Bond Charge Revenues and the payment of Bond Related Costs. Another set of accounts, the “Power Charge Accounts,” is primarily for the deposit of Power Charge Revenues and the payment of operating expenses (including Priority Contract Costs and other costs of the Power Supply Program). Bond Charge Accounts include the Bond Charge Collection Account, the Bond Charge Payment Account, and the Debt Service Reserve Account. Power Charge Accounts include the Operating Account, the Priority Contract Account and the Operating Reserve Account. See “SECURITY FOR THE BONDS – Accounts and Flow of Funds under the Indenture.”

**Bond Charge Accounts .....**

The Indenture requires the following deposits and transfers of Bond Charge Revenues:

- All Bond Charge Revenues are required to be deposited in the Bond Charge Collection Account. DWR is also required to deposit in the Bond Charge Collection Account any payments received from any counterparty to a “Qualified Swap” (as defined in Appendix C) relating to Bonds.
- On or before the last Business Day of each month, DWR is required to transfer from the Bond Charge Collection Account to the Bond Charge Payment Account such amount as is necessary to make the amount in the Bond Charge Payment Account sufficient to pay Bond Related Costs (including Debt Service on the Bonds) estimated to accrue or be payable during the next succeeding three calendar months. Each such transfer is subject to the prior transfer of amounts in the Bond Charge Collection

Account to the Priority Contract Account if and to the extent amounts in the Priority Contract Account, the Operating Account and the Operating Reserve Account are insufficient to pay Priority Contract Costs. See “RISK FACTORS – Determination of Power Charges and Bond Charges; Possible Use of Amounts in the Bond Charge Collection Account to Pay Priority Contract Costs.”

- Deficiencies in the Bond Charge Payment Account are required to be made up *first*, from the Operating Account and *second*, from the Debt Service Reserve Account (except for the payment of Fiduciary costs).
- The Debt Service Reserve Account is required by the Indenture to have a balance in the amount of maximum aggregate annual Debt Service on all outstanding Bonds, calculated in accordance with the Indenture (the “Debt Service Reserve Requirement”). Each month after the Bond Charge Payment Account is funded as described above, Revenues are to be transferred to the Debt Service Reserve Account and to any reserve established for Parity Obligations to the extent necessary to meet the respective requirements (including replenishment requirements) for such reserves. Amounts in the Debt Service Reserve Account may be used for the payment of Bond Related Costs (including debt service on the Bonds) except Fiduciary costs, but only if amounts in the Bond Charge Payment Account and Operating Account are insufficient for that purpose. See “SECURITY FOR THE BONDS – Accounts and Flow of Funds under the Indenture” and “– Debt Service Reserve Account.”

**Power Charge Accounts.....**

The Indenture requires the following deposits and transfers of all Revenues other than those required to be deposited in the Bond Charge Collection Account:

- All Revenues (including but not limited to Power Charge Revenues), other than Bond Charge Revenues and payments to DWR under Qualified Swaps relating to Bonds, are required to be deposited in the Operating Account.
- On or before the fifth Business Day of each month, DWR is required to transfer from the Operating Account to the Priority Contract Account such amount as is necessary to make the amount in the Priority Contract Account sufficient to pay Priority Contract Costs estimated to be due during the balance of such month and through the first five Business Days of the next succeeding calendar month. Amounts in the Priority Contract Account may be used solely to pay Priority Contract Costs. See “SECURITY FOR THE BONDS – Accounts and Flow of Funds under the Indenture.”
- Amounts in the Operating Account after the monthly transfer to the Priority Contract Account are to be used for the following purposes in the following order of priority: (i) for transfer to the Priority Contract Account if the estimated amount transferred to

that account (as described in the preceding paragraph) is insufficient to pay actual Priority Contract Costs then payable; (ii) for the payment of other operating expenses; (iii) to reimburse the Bond Charge Collection Account for amounts previously transferred from the Bond Charge Collection Account to the Priority Contract Account to pay Priority Contract Costs; (iv) to pay debt service on the Bonds and other Bond Related Costs (if amounts in the Bond Charge Payment Account are not sufficient for those purposes) and, in addition, prior to the time Bond Charge Revenues are received in amounts sufficient to make the transfers described in the second bullet point under “Bond Charge Accounts” above, to make those transfers as required; (v) for transfer to the Debt Service Reserve Account to the extent required by the Indenture as a result of the use of Bond Charge Revenues to pay Priority Contract Costs or a change in value of investments in such Account; (vi) to replenish the Operating Reserve Account to its requirement as provided by the Indenture; (vii) to pay any subordinated indebtedness and subordinated obligations and certain other amounts relating thereto; and (viii) for any other lawful purpose of the Power Supply Program. See “SECURITY FOR THE BONDS – Accounts and Flow of Funds under the Indenture,” “– Debt Service Reserve Account” and “– Operating Reserve Account.”

- The Operating Reserve Account is required by the Indenture to be funded in an amount equal to the Operating Reserve Account Requirement. Amounts in the Operating Reserve Account are to be transferred to the Operating Account if and to the extent that the amount in the Operating Account is insufficient for any of the purposes listed in clauses (i) through (v) of the preceding paragraph, unless the amount in the Operating Reserve Account is equal to or less than the “Priority Contract Contingency Reserve Amount” (an amount equal to the maximum amount projected by DWR to be payable under Priority Long-Term Power Contracts in any calendar month during the then-current revenue requirement period), in which event amounts in the Operating Reserve Account may only be used to make up any deficiency in the Priority Contract Account. See “SECURITY FOR THE BONDS – Accounts and Flow of Funds under the Indenture” and “– Operating Reserve Account.”

**Letters of Credit .....**

The payment when due of the principal of and interest on, and the payment of the purchase price upon tender of, all five subseries of the Series 2005F Bonds, the Series 2005G-1 Bonds and the Series 2005G-2 Bonds will be made from draws on direct-pay letters of credit with initial stated terms of three to five years each, as described in the Series Description following the cover of this Official Statement. In addition to the Series Descriptions, see “SECURITY FOR THE BONDS - Enhancement Facilities” and “– Initial Letters of Credit.” See also APPENDIX I – “INFORMATION CONCERNING INITIAL LETTER OF CREDIT PROVIDERS AND INITIAL LIQUIDITY FACILITY PROVIDERS.”

**Bond Insurance with Liquidity .....** The payment when due of the principal of and interest on each subseries of Series 2005G Bonds (other than the Series 2005G-1 and the Series 2005G-2 Bonds), is guaranteed by a financial guaranty insurance policy, and the payment of the purchase price upon tender of each such subseries is supported by a liquidity facility, all as described in the Series Descriptions following the cover of this Official Statement. All such financial guaranty insurance policies are irrevocable, and all such liquidity facilities are for initial stated terms of three to ten years each, as indicated in the applicable Series Descriptions. In addition to the Series Descriptions, see “SECURITY FOR THE BONDS – Bond Insurance” and “- Initial Liquidity Facilities,” APPENDIX J – “INFORMATION CONCERNING BOND INSURERS AND FORMS OF FINANCIAL GUARANTY INSURANCE POLICIES” and APPENDIX I – “INFORMATION CONCERNING INITIAL LETTER OF CREDIT PROVIDERS AND INITIAL LIQUIDITY FACILITY PROVIDERS.”

**Collection of Revenues;  
Servicing Arrangements .....** Pursuant to the Act, the CPUC has issued orders approving servicing agreements or orders for the IOUs to provide transmission and distribution services, bill and collect Bond Charges and Power Charges, and perform other services on behalf of DWR in connection with the Power Supply Program (collectively, the “Servicing Arrangements”). Under such Servicing Arrangements, the IOUs collect DWR’s Bond Charges and Power Charges solely as the agents of DWR. See “THE DWR POWER SUPPLY PROGRAM – Collection of Revenues.”

**The IOUs .....** The three major investor-owned electric utilities in California are PG&E, SCE and SDG&E. Their combined service areas cover approximately three-fourths of California’s land area and their combined approximately 11 million bundled customer accounts represent approximately three-quarters of all retail connections in California. DWR sells power to the same bundled customers served by the three IOUs. See “THE DWR POWER SUPPLY PROGRAM – Customer Base.”

**Litigation and Administrative  
Proceedings .....** Litigation and administrative proceedings involving DWR or affecting DWR’s Power Supply Program are summarized under “LITIGATION AND ADMINISTRATIVE PROCEEDINGS.”

**Risks.....** Investment in the Series 2005 Bonds is subject to certain risks, including the events and circumstances identified under “RISK FACTORS.” Cross-references below are to subsections of “RISK FACTORS.”

The occurrence of one or more of such events or circumstances could materially and adversely affect the ability of DWR to pay debt service on the Bonds.

Such risks relate to the following events or circumstances, among others:

- Failure of DWR’s assumptions and projections in calculating its revenue requirements and a delay or failure in appropriations required for certain of DWR’s administrative expenses (see

“Certain Risks Associated with DWR’s Power Supply Program”);

- The insufficiency of Power Charge Revenues to pay amounts due under DWR’s Priority Long-Term Power Contracts (including any termination payments), resulting in the use of Bond Charge Revenues for such purpose (see “Certain Risks Associated with DWR’s Power Supply Program”);
- Administrative or legal challenges to DWR’s proceedings for establishing its revenue requirements or the CPUC’s proceedings for calculating, revising and imposing Bond Charges and Power Charges, including particularly challenges to the inclusion of Priority Contract Costs in revenue requirement determinations (see “Determination of Power Charges and Bond Charges; Possible Use of Amounts in the Bond Charge Collection Account to Pay Priority Contract Costs”);
- A court declining to give effect to the Rate Agreement in accordance with its literal terms, including the CPUC’s Bond Charge Rate Covenant, if the effect of so doing would be to permit the recovery by DWR of power or bond costs that had been determined previously (in a legal challenge against DWR) not to be “just and reasonable” (see “Determination of Power Charges and Bond Charges; Possible Use of Amounts in the Bond Charge Collection Account to Pay Priority Contract Costs”);
- The failure or refusal of one or more IOUs to perform under the Servicing Arrangements, including action or inaction by a bankrupt IOU (see “Collection of Bond Charges and Power Charges” and “Bankruptcy Risks”);
- Uncertainties concerning changes in the electric industry and markets in the western states region (see “Uncertainties Relating to Electric Industry and Markets”);
- Uncertainties concerning possible legislative, regulatory or other action affecting the Power Supply Program (see “Uncertainties Relating to Government Action”); and
- Actual results materially differing from the projections and assumptions contained in this Official Statement or contained in DWR’s revenue requirements (see “Uncertainty of Projections and Assumptions”).

## THE SERIES 2005 BONDS

This section summarizes certain provisions of the Indenture and the Series 2005 Bonds. See APPENDIX C – “SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE” for the definitions of certain capitalized terms and a description of other provisions of the Indenture and the Series 2005 Bonds. See also “SECURITY FOR THE BONDS – Bond Insurance,” “– Enhancement Facilities,” “– Initial Letters of Credit,” “– Initial Liquidity Facilities” and APPENDIX K – “SUMMARY OF CERTAIN PROVISIONS OF THE MASTER BANK AGREEMENT” for additional information concerning credit enhancement and liquidity support for the Series 2005 Bonds.

### General

The Series 2005 Bonds may be purchased in book-entry form only, in the principal amount of \$100,000 or any integral multiple of \$5,000 in excess of \$100,000. See APPENDIX B – “BOOK-ENTRY SYSTEM.” The Series 2005 Bonds will be dated and will bear interest from the date of issuance and delivery, and will mature on the dates set forth on the inside cover. The Series 2005 Bonds may bear interest (or may be adjusted to bear interest) at Daily Rates, Weekly Rates, Flexible Rates, Term Rates, Auction Rates or Fixed Rates (each, an “Interest Rate Mode”). Initially, each subseries of Series 2005 Bonds will bear interest for the “Initial Interest Period” set forth in the applicable Series Description at an “Initial Rate” determined by the Underwriters prior to the delivery date. See also “THE SERIES 2005 BONDS – Initial Interest Periods.”

Following the applicable Initial Interest Periods, each subseries of the Series 2005F Bonds will bear interest at Daily Rates and each subseries of the Series 2005G Bonds will bear interest at Weekly Rates, until DWR changes the Interest Rate Mode for such subseries or until such subseries of Series 2005 Bonds matures or is redeemed. Certain terms of the Series 2005 Bonds while bearing interest at Daily Rates or Weekly Rates are summarized in the following sections. This Official Statement is not intended to describe the terms of the Series 2005 Bonds after any adjustment to Auction Rates, Flexible Rates, Term Rates or Fixed Rates. DWR anticipates that if it elects to change any subseries of Series 2005 Bonds to any of such other Interest Rate Modes, an offering document will be distributed describing such subseries of Series 2005 Bonds and such new Interest Rate Mode.

Interest at the rate determined for any particular Interest Period shall accrue from and including the commencement date of such Interest Period through and including the last day thereof, and shall be payable on each Interest Payment Date to the Owner of record on the Record Date. See the following sections for a description of the Interest Periods, Interest Payment Dates and Record Dates in Daily Rate Mode and in Weekly Rate Mode. Interest on overdue principal of and, to the extent lawful, on overdue premium and interest on the Series 2005 Bonds will be payable at the rate on such Bonds on the day immediately preceding the default in the payment thereof. Payment of defaulted interest will be made to the Owners of record as of the fifth day (or if such day is not a Business Day, then the next preceding Business Day) preceding the payment thereof. The Co-Trustee shall make interest rates available to any Owner requesting the same. The interest rate determined by the Remarketing Agent or otherwise determined as provided in the Indenture and contained in the records of the Co-Trustee will be conclusive and binding on DWR, the Trustees, the Remarketing Agent and the Owners of such Bonds, absent manifest error.

Interest on the Series 2005 Bonds shall be payable on each Interest Payment Date to the Owner of record on the applicable Record Date (i) by check mailed by the Paying Agent to the registered Owner at such Owner’s address as it appears on the books of registry required to be kept by the Registrar pursuant to the Indenture or (ii) by wire transfer to the account specified by the Owner of at least \$1,000,000 in aggregate principal amount of Series 2005 Bonds in a written direction received by the Paying Agent at its office designated for such purpose on or prior to a Record Date; provided, however, that upon redemption of any Series 2005 Bond on a date other than a Redemption Date, the accrued interest payable upon redemption shall be payable at the office of the Paying Agent designated for such purpose, upon presentation and surrender of such Bond, unless the Redemption Date is an Interest Payment Date, in which event the interest on such Bond so redeemed shall be paid by the Paying

Agent as described above. Any such direction or request shall remain in effect until revoked or revised by such Owner by an instrument in writing delivered to the Paying Agent.

Payments by wire transfer shall be in immediately available funds, unless the Remarketing Agent designates another type of funds in connection with a change in Interest Rate Modes.

**So long as any Series 2005 Bond is registered in the name of Cede & Co., as nominee of DTC, procedures with respect to the transfer of ownership, redemption, optional or mandatory tender for purchase, and the payment of principal, Purchase Price, Redemption Price, premium, if any, and interest on such Bond shall be in accordance with arrangements among DWR, the Trustee, the Co-Trustee, the Paying Agent and DTC. See APPENDIX B – “BOOK-ENTRY SYSTEM.”**

### **Initial Interest Periods**

This section summarizes certain terms of the Indenture and the Series 2005 Bonds applicable to the Initial Interest Periods (defined below).

Initially, each subseries of Series 2005 Bonds will bear interest at an Initial Rate. The Initial Rate for each subseries will apply for an Initial Interest Period, as set forth in the applicable Series Description. The Underwriter shall determine the Initial Rate for each subseries by determining in its judgment the minimum interest rate necessary to be borne by such subseries for the applicable Initial Interest Period to enable the Underwriter to sell the Bonds of such subseries on the date of issuance at a price equal to the principal amount thereof; provided, however, that in no event shall any rate so determined cause the amount of interest to accrue on such subseries during the Initial Interest Period to exceed the “Interest Portion” or the “Interest Commitment” of the applicable Enhancement Facility. See “SECURITY FOR THE BONDS - Initial Letters of Credit” and “- Initial Liquidity Facilities” for a description of such terms. Interest on each subseries of Series 2005 Bonds will be paid, with respect to the applicable Initial Interest Period, on the first Business Day following such Initial Interest Period.

On the day following the last day of the Initial Interest Period, each subseries of Series 2005F Bonds will begin to accrue interest at a Daily Rate and each subseries of Series 2005G Bonds will begin to accrue interest at a Weekly Rate. Such change to a Daily Rate Mode or a Weekly Rate Mode will occur automatically, without notice, consent, opinion or action of any kind. Notwithstanding any other description of redemption or tenders for purchase in this Official Statement, (1) the Series 2005 Bonds will not be subject to redemption during the applicable Initial Interest Period, (2) except as set forth in the following sentence, no Series 2005 Bond may be tendered for purchase at the option of the owner thereof during the applicable Initial Interest Period and (3) no mandatory tender for purchase will occur upon the change to Daily Rate Mode or Weekly Rate Mode on the day following the last day of the applicable Initial Interest Period. Upon notice given pursuant to the Indenture during the Initial Interest Period (see “Optional and Mandatory Tender for Purchase – Optional Tender for Purchase in Daily Rate Mode” and “—Optional Tender for Purchase in Weekly Rate Mode”) (i) not later than 11:00 a.m. New York City time on the last day of the applicable Initial Interest Period with respect to the Series 2005F Bonds, or (ii) not later than seven days prior to the last day of the applicable Initial Interest Period with respect to the Series 2005G Bonds, each Series 2005 Bond shall be subject to tender at the option of the owner thereof on the day immediately following the last day of the applicable Initial Interest Period.

Interest on Series 2005 Bonds during the Initial Interest Period shall be calculated on the basis of a 365-day year for the actual number of days elapsed. The Record Date for Series 2005 Bonds during the Initial Interest Period is the Business Day preceding the Interest Payment Date therefor.

### **Daily Rate Mode**

This section summarizes certain terms of the Indenture and the Series 2005 Bonds applicable to the Daily Rate Mode. Following the Initial Interest Periods (described in the Series Descriptions following the front cover

of this Official Statement), all subseries of the Series 2005F Bonds will bear interest at Daily Rates until such time as the Interest Rate Mode is changed by DWR or such Bonds are retired.

#### *Daily Periods*

While in a Daily Rate Mode, each Daily Rate will apply to an Interest Period commencing on a Business Day and ending on the day preceding the next succeeding Business Day (a “Daily Period”). After the Initial Interest Period, all subseries of the Series 2005F Bonds automatically will change to the Daily Rate Mode. Series 2005 Bonds in a Daily Rate Mode will continue to bear interest at Daily Rates for consecutive Daily Periods until DWR changes the Interest Rate Mode of such Bonds, or until redemption or maturity. See “THE SERIES 2005 BONDS – Changes in Interest Rate Mode.”

#### *Daily Rate Determination Method*

By 10:00 a.m., New York City time, on each Business Day for the Remarketing Agent, the Remarketing Agent shall determine the Daily Rate for the Series 2005 Bonds in a Daily Rate Mode by determining the Market Rate therefor on such day, which Daily Rate shall be effective for the Interest Period beginning on such Business Day and ending on the day preceding the next succeeding Business Day. The Remarketing Agent shall determine the Market Rate for any Series 2005 Bond in a Daily Rate Mode by determining in its judgment the minimum interest rate necessary to be borne by such Bond for the Daily Period to enable the Remarketing Agent to remarket such Bond on the date such Bonds are changed to a different Interest Rate Mode or continued in successive Daily Periods, at a price (without regard to accrued interest) equal to the principal amount thereof; provided, however, that in no event shall any rate so determined exceed the Maximum Rate. If for any reason the Remarketing Agent fails to determine the Market Rate for any such Bond on a rate determination date, or any Market Rate for any such Bond determined by the Remarketing Agent on a rate determination date is determined by a court of competent jurisdiction to be invalid or unenforceable, then, effective on the first day of the Interest Period following such rate determination date or the date with respect to which such court’s determination shall be effective, as the case may be, the Daily Rate Mode shall be automatically changed to a Weekly Rate Mode without a mandatory tender for purchase. “Maximum Rate” means, with respect to any Series 2005 Bonds other than Bonds purchased with funds obtained under a “Liquidity Facility” (as defined in Appendix C), the lesser of (a) the maximum rate, if any, permitted by State law, (b) the rate used by the provider of any applicable “Credit Facility” (as defined in Appendix C) to calculate the amount of the applicable principal and interest coverage thereunder (as required to maintain the ratings on such Bonds) (the “Applicable Principal and Interest Coverage”), or (c) the rate used by the provider of any applicable Liquidity Facility to calculate the amount of the Applicable Principal and Interest Coverage. Under existing State law, there is no maximum rate for obligations such as the Bonds. Accordingly, based on the interest rate used by the providers of the initial Credit Facilities and Liquidity Facilities to calculate the Applicable Principal and Interest Coverage, the Maximum Rate is currently 11%.

#### *Interest Calculation Method*

Interest on the Series 2005 Bonds during a Daily Rate Mode will be calculated on the basis of a 365-day or 366-day year, as applicable, for the actual number of days elapsed.

#### *Interest Payment Dates; Record Date*

Interest on Series 2005 Bonds in a Daily Rate Mode is payable on the first Business Day of each calendar month. The “Record Date” for Series 2005 Bonds bearing interest at Daily Rates is the close of business on the Business Day immediately preceding the applicable Interest Payment Date.

### **Weekly Rate Mode**

This section summarizes certain terms of the Indenture and the Series 2005 Bonds applicable to a Weekly Rate Mode. Following the Initial Interest Periods described in the Series Descriptions following the front cover

of this Official Statement, and until such time as the Interest Rate Mode is changed by DWR, all subseries of the Series 2005G Bonds will bear interest at Weekly Rates.

#### *Weekly Periods*

While in a Weekly Rate Mode, each Weekly Rate will apply to an Interest Period of seven calendar days commencing on the calendar day determined by DWR of a calendar week and ending on the next preceding calendar day of the next succeeding calendar week, provided that the first Weekly Period following the Initial Interest Period, or a change in the Interest Rate Mode to a Weekly Rate Mode, shall commence on the Business Day immediately following the last day of the Initial Interest Period or the end of the preceding Interest Period, as the case may be, may be less than seven calendar days and shall end on the day before the next Weekly Period Commencement Date. After the Initial Interest Period, all subseries of the Series 2005G Bonds automatically will change to the Weekly Rate Mode. During such Weekly Rate Mode, each Weekly Period shall start on a Thursday and end on the following Wednesday. Series 2005 Bonds in a Weekly Period will continue to bear interest at Weekly Rates until DWR changes such Bonds to a different Interest Rate Mode, or until redemption or maturity. See “THE SERIES 2005 BONDS – Changes in Interest Rate Mode.”

#### *Weekly Rate Determination Method*

By 4:00 p.m., New York City time, on the Business Day immediately preceding the first day of each Weekly Period (or such other day as may be specified by the Remarketing Agent) the Remarketing Agent shall determine the Weekly Rate for a subseries of Series 2005 Bonds by determining the Market Rate therefor on such day, which Weekly Rate shall be effective for such Weekly Period. The Remarketing Agent shall determine the Market Rate for any Bond in a Weekly Rate Mode by determining in its judgment the minimum interest rate necessary to be borne by such Bond for the Weekly Period to enable the Remarketing Agent to remarket such Bond on the date such Bonds are changed to a different Interest Rate Mode, or continued in successive Weekly Periods at a price (without regard to accrued interest) equal to the principal amount thereof; provided, however, that in no event shall any rate so determined exceed the Maximum Rate. If for any reason the Remarketing Agent fails to determine the Market Rate for any such Bond on a rate determination date, or any Market Rate for any such Bond determined by the Remarketing Agent on a rate determination date is determined by a court of competent jurisdiction to be invalid or unenforceable, then, effective on the first day of the Interest Period following such rate determination date or the date with respect to which such court’s determination shall be effective, as the case may be, such Bond shall bear interest at a rate equal to the Alternate Rate until the Market Rate is determined or redetermined, as the case may be.

#### *Interest Calculation Method*

Interest on the Series 2005 Bonds during a Weekly Rate Mode shall be calculated on the basis of a 365-day or 366-day year, as applicable, for the actual number of days elapsed.

#### *Interest Payment Dates; Record Date*

Interest on Series 2005 Bonds during a Weekly Rate Mode is payable on the first Business Day of each calendar month. The “Record Date” during a Weekly Rate Mode is the close of business on the Business Day immediately preceding the applicable Interest Payment Date.

#### **Term Rate Mode, Flexible Rate Mode, Auction Rate Mode and Fixed Rate Mode**

Pursuant to the Indenture, the Interest Rate Mode of Series 2005 Bonds may be changed to Term Rate Mode, Flexible Rate Mode, Auction Rate Mode or Fixed Rate Mode upon a mandatory tender for purchase. This Official Statement is not intended to describe the Series 2005 Bonds at any time during a Term Rate Mode, a Flexible Rate Mode, an Auction Rate Mode or a Fixed Rate Mode.

## Changes in Interest Rate Mode

This section summarizes certain provisions of the Indenture applicable to a change in Interest Rate Mode, other than the initial change in Interest Rate Mode following the last day of each Initial Interest Period. See “THE SERIES 2005 BONDS – Initial Interest Period.”

### *Change at the Option of DWR*

At any time, DWR may elect to change the Interest Rate Mode applicable to all or any portion of the Series 2005 Bonds to a Daily Rate Mode, a Weekly Rate Mode, a Flexible Rate Mode, a Term Rate Mode, an Auction Rate Mode, or a Fixed Rate Mode. DWR anticipates that if it elects to change the Interest Rate Mode of any subseries of Series 2005 Bonds, a remarketing memorandum will be distributed describing such subseries of Series 2005 Bonds and such new Interest Rate Mode. See APPENDIX C – “SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE.”

### *Notice to Bondholders*

The Paying Agent will send a notice of a proposed change in the Interest Rate Mode for a subseries of Bonds to the Bondowners of such subseries at least 15 days, but not more than 60 days, before the effective date of the change.

### *Mandatory Tender for Purchase*

If DWR changes the Interest Rate Mode for any Series 2005 Bonds (except for the automatic change from the Initial Interest Period, changes on an Interest Payment Date from Daily Rate Mode to Weekly Rate Mode, and changes on an Interest Payment Date from Weekly Rate Mode to Daily Rate Mode), such Bonds will be subject to mandatory tender for purchase on the effective date of the new Interest Rate Mode. Bondowners will have no right to retain their Series 2005 Bonds upon a mandatory tender for purchase. See “THE SERIES 2005 BONDS – Optional and Mandatory Tender for Purchase.”

### *Conditions Precedent to Changes in Interest Rate Modes*

The Interest Rate Mode for a subseries of Series 2005 Bonds shall not be changed unless: (i) the Liquidity Facility, if any, then in effect for such subseries permits a draw thereunder in an amount up to the Applicable Principal and Interest Coverage applicable to the new Interest Rate Mode, or (ii) the Credit Facility, if any, then in effect for the Bonds of such subseries permits a draw, borrowing or payment thereunder in an amount up to the Applicable Principal and Interest Coverage applicable to the new Interest Rate Mode.

In addition, no change shall be made from one Interest Rate Mode to another Interest Rate Mode if (1) DWR, the Trustee, the Co-Trustee and the Paying Agent shall receive written notice prior to such change that the opinion of Nationally Recognized Bond Counsel relating to the change (as described below) has been rescinded or will not be delivered or (2) any other condition to any such change required under the Fourth Supplemental Indenture has not been satisfied or (3) less than all of the Series 2005 Bonds of a subseries subject to mandatory tender for purchase upon such change shall have been remarketed or (4) interest due on all of the Series 2005 Bonds of a subseries has not been paid or (5) the premium applicable to certain adjustments from a Term Rate Mode or a Fixed Rate Mode has not been paid.

The Interest Rate Mode of a subseries of Series 2005 Bonds shall not be changed to an alternate Interest Rate Mode unless DWR obtains an opinion of Nationally Recognized Bond Counsel to the effect that the change in the Interest Rate Mode (1) is lawful under the Act and is authorized or permitted by the Indenture, and (2) will not, in and of itself, adversely affect the exclusion of interest on such Bonds from gross income for federal income tax purposes, nor adversely affect the validity of the Series 2005 Bonds of such subseries.

### *Failed Interest Rate Mode Changes*

If any condition to a change in the Interest Rate Mode has not been satisfied, the Paying Agent shall promptly send a notice to all Owners of Series 2005 Bonds to whom the Paying Agent had sent notice of the proposed change in the Interest Rate Mode stating that the proposed change in the Interest Rate Mode will not become effective, and that the Daily Rate Mode or the Weekly Rate Mode, as applicable, will remain in effect.

### *Change of a Portion of a Subseries to a Different Interest Rate Mode*

Less than all of the Bonds of a subseries then subject to a particular Interest Rate Mode may be converted to another Interest Rate Mode; provided, however, that in such event (a) such subseries shall be re-designated into one or more subseries for each separate Interest Rate Mode with a new CUSIP number for each subseries, and (b) the particular Series 2005 Bonds of a subseries or portions thereof which are to be converted to a new Interest Rate Mode shall be selected by the Registrar in such manner in its discretion as it shall deem appropriate and fair, subject to the provisions of the Indenture regarding authorized denominations. All Series 2005 Bonds of any such subseries shall be subject to the same Interest Rate Mode. Except as provided above, all Bonds of a subseries shall be subject to the same Interest Rate Mode.

## **Optional and Mandatory Tender for Purchase**

### *Optional Tender for Purchase in Daily Rate Mode*

The Owners of Series 2005 Bonds in a Daily Rate Mode may irrevocably tender such Bonds for purchase by giving telephonic notice to the Remarketing Agent, confirmed in writing to the Remarketing Agent and the Tender Agent, or notice in writing or by Electronic Means to the Remarketing Agent and the Tender Agent, by 11:00 a.m., New York City time, on any Business Day stating the principal amount of each such Bond, the Bond number, the CUSIP number, and the date (which must be a Business Day) on which such Bond is to be purchased. The Tender Agent shall promptly inform the Paying Agent of such notice. In the case of a Series 2005 Bond in a Daily Rate Mode to be purchased prior to an Interest Payment Date and after the Record Date in respect thereof, if the Owner is other than a Securities Depository or its nominee, the Owner shall deliver a due bill, in form satisfactory to the Paying Agent, for interest due on such Purchase Date. The Purchase Price for a Series 2005 Bond in a Daily Rate Mode and tendered to the Tender Agent for purchase will be paid in immediately available funds by 4:00 p.m., New York City time, on the Purchase Date (as defined in Appendix C). All Series 2005 Bonds in a Daily Rate Mode and tendered for purchase must be accompanied by an instrument of transfer satisfactory to the Tender Agent, executed in blank by the registered owner with the signature guaranteed.

### *Optional Tender for Purchase in Weekly Rate Mode*

The Owners of Series 2005 Bonds in a Weekly Rate Mode may irrevocably tender such Bonds for purchase by giving telephonic notice to the Remarketing Agent, confirmed in writing to the Remarketing Agent and the Tender Agent, or notice in writing or by Electronic Means to the Remarketing Agent and the Tender Agent, by 4:00 p.m., New York City time, on any Business Day stating the principal amount of each such Bond, the Bond number, the CUSIP number, and the date (which must be a Business Day at least seven (7) days after the notice is given) on which such Bond is to be purchased. The Tender Agent shall promptly inform the Paying Agent of such notice. In the case of a Series 2005 Bond in a Weekly Rate Mode to be purchased prior to an Interest Payment Date and after the Record Date in respect thereof, if the Owner is other than a Securities Depository or its nominee, the Owner shall deliver a due bill, in form satisfactory to the Paying Agent, for interest due on such Purchase Date. The Purchase Price for a Series 2005 Bond in a Weekly Rate Mode and tendered to the Tender Agent for purchase will be paid in immediately available funds by 4:00 p.m., New York City time, on the Purchase Date. All Series 2005 Bonds in a Weekly Rate Mode and tendered for purchase must be accompanied by an instrument of transfer satisfactory to the Tender Agent, executed in blank by the registered owner with the signature guaranteed.

### *Mandatory Tender for Purchase*

Except as provided in numbered paragraph 1, below, the Paying Agent will send a Notice of Mandatory Tender to the Owners of Series 2005 Bonds subject to mandatory tender for purchase, not more than forty-five nor less than fifteen days before the date on which such Bonds shall be subject to mandatory tender for purchase (or such lesser notice as may be permitted in numbered paragraphs 3, 4 and 5 below).

The following events will give rise to the mandatory tender for purchase of Series 2005 Bonds while in a Daily Rate Mode or a Weekly Rate Mode:

1. Upon a Change in the Interest Rate Mode. Except in the case of a change from a Daily Rate Mode to a Weekly Rate Mode on an Interest Payment Date, from a Weekly Rate Mode to a Daily Rate Mode on an Interest Payment Date, and from the Initial Interest Period to a Daily Rate Mode or a Weekly Rate Mode, upon any change in the Interest Rate Mode for a subseries of Series 2005 Bonds, such subseries shall be subject to mandatory tender for purchase on the effective date of such change, at a purchase price equal to the principal amount thereof, plus interest to the purchase date.

2. Upon Expiration, Termination, Substitution or Assignment of a Credit Facility or Liquidity Facility. All Series 2005 Bonds of a subseries secured or supported by a Credit Facility or Liquidity Facility shall be subject to mandatory tender for purchase on the earlier of (a) the fifth Business Day immediately prior to the Expiration thereof, (b) the fifth Business Day immediately prior to the Termination thereof, (c) the effective date of a Substitute Credit Facility (other than a Substitute Credit Facility delivered in substitution for or replacement of a bond insurance policy) or Substitute Liquidity Facility, as the case may be, or (d) the fifth (5th) Business Day immediately prior to the effective date of the assignment of the obligation of the Credit Facility Provider or the Liquidity Facility Provider under such Credit Facility or Liquidity Facility, as the case may be; provided, however, that such Bonds shall not be subject to mandatory tender for purchase if (x) in the case of termination, such Credit Facility or Liquidity Facility does not permit a draw or borrowing thereunder in connection with such Termination, (y) in the case of the delivery of a Substitute Credit Facility or Substitute Liquidity Facility, the Paying Agent shall have received at least fifteen (15) days prior to the effective date of such Substitute Credit Facility or Substitute Liquidity Facility a written confirmation from each Rating Agency then rating the Bonds of such Series to the effect that such substitution will not, by itself, result in a reduction or withdrawal of the short-term rating or the long-term rating, if any, of such Bonds below the rating of such Rating Agency then in effect with respect to such Bonds, and (z) in the case of the assignment of the obligation of the Credit Facility Provider or Liquidity Facility Provider under such Credit Facility or Liquidity Facility, as the case may be, the Paying Agent shall have received at least fifteen (15) days prior to the fifth (5th) Business Day immediately prior to the effective date of such assignment a written confirmation from each Rating Agency then rating the Bonds of such Series to the effect that such assignment will not, by itself, result in a reduction or withdrawal of the short-term rating or the long-term rating, if any, of such Bonds below the rating of such Rating Agency then in effect with respect to such Bonds. If such mandatory tender for purchase is required, the Paying Agent shall immediately prepare and send a notice to all Owners of such Bonds by first class mail, postage prepaid, which notice shall (i) state the effective date of the Expiration, Termination, substitution or assignment and the Purchase Date, (ii) state that upon such Purchase Date all such Bonds shall be purchased in whole at a Purchase Price equal to the principal amount thereof, without premium, plus accrued interest, if any, to the Purchase Date, and (iii) state that Owners of such Bonds shall have no right to retain their Bonds after the Purchase Date so specified.

To the extent that the Series 2005 Bonds of a subseries supported by a Credit Facility or a Liquidity Facility are not subject to mandatory tender for purchase as a result of a substitution or assignment, the Paying Agent is required to give the applicable Owners written notice of such substitution or assignment at least 15 days prior to the effective date of the Substitute Credit Facility or Substitute Liquidity Facility or assignment.

3. Upon an Event of Default under a Credit Facility or Liquidity Facility. A subseries of Series 2005 Bonds supported by a Liquidity Facility or Credit Facility, as the case may be, shall be subject to mandatory tender for purchase on the 15th Business Day immediately following the receipt by the Paying Agent of a written direction by or on behalf of the Liquidity Facility provider or Credit Facility provider, as the case may be, in accordance with the terms of such Liquidity Facility or Credit Facility, to cause the mandatory tender for purchase of such subseries of Series 2005 Bonds as a result of the occurrence of an event of default under the Credit Facility or Liquidity Facility, as the case may be. Upon the receipt of such written direction, the Paying Agent will immediately prepare and send a notice to all Owners of such subseries of Series 2005 Bonds and certain other parties by first class mail, postage prepaid, that such mandatory tender will occur on the 15th Business Day following the receipt by the Paying Agent of a written notice described in the preceding sentence, that Owners of such subseries of Series 2005 shall have no right to retain their Bonds after such mandatory tender date and upon such date all Series 2005 Bonds of such subseries shall be purchased in whole at a Purchase Price equal to the principal amount thereof, without premium, plus accrued interest, if any, to the Purchase Date. The Series 2005 Bonds of such subseries shall remain subject to mandatory tender for purchase as provided above notwithstanding the receipt by the Paying Agent of a subsequent notice from the issuer of a Credit Facility or Liquidity Facility, as the case may be, to the effect that the event of default thereunder has been cured.

4. Upon Non-Reinstatement of Interest Component under a Direct-Pay Credit Facility. A subseries of Series 2005 Bonds secured by a Direct-Pay Credit Facility shall be subject to mandatory tender for purchase on the first Business Day following the receipt by the Paying Agent of a written notice from the issuer of the Direct-Pay Credit Facility that such Direct-Pay Credit Facility will not be reinstated (in respect of interest) to an amount equal to the interest component of the Applicable Principal and Interest Coverage required with respect to such subseries. Upon the receipt of such written notice, the Paying Agent will immediately prepare and send a notice to the registered owners of such Bonds to the effect that such mandatory tender will occur on the first Business Day following the receipt by the Paying Agent of such written notice, with no right to retain. Such Bonds shall remain subject to mandatory tender for purchase as described above notwithstanding the receipt by the Paying Agent of a subsequent notice from the issuer of the Direct-Pay Credit Facility to the effect that such Direct-Pay Credit Facility has been reinstated to an amount equal to the Applicable Principal and Interest Coverage.

#### *Payment of Purchase Price*

Except as otherwise required or permitted by the book-entry system of the Securities Depository (initially, DTC), all purchases pursuant to an optional or mandatory tender of Series 2005 Bonds will be made by the Tender Agent in funds immediately available on the Purchase Date and will be at a Purchase Price of 100% of the principal amount of the Series 2005 Bond being purchased plus interest accrued to, but excluding, the Purchase Date. The Tender Agent shall pay the Purchase Price for each tendered Series 2005 Bond at or prior to 4:00 p.m., New York City time, on a Purchase Date only if the Owner thereof shall have delivered such Bond on such Purchase Date, as described below, properly endorsed in blank, and funds are available therefor. If an Owner of a tendered Series 2005 Bond shall have delivered such Bond to the Tender Agent after 12:00 noon, New York City time, the Tender Agent shall pay the Purchase Price of such Bond at or prior to 4:00 p.m., New York City time, on the Business Day immediately following the date on which such Bond was delivered to the Tender Agent. No optional or mandatory purchase of Series 2005 Bonds of a subseries shall be deemed to be a payment or redemption of the Series 2005 Bonds or of any portion thereof, and such purchase will not operate to extinguish or discharge the indebtedness evidenced by such Bonds, unless DWR otherwise directs the Co-Trustee in writing.

#### *Sources of Funds to Pay Purchase Price*

Funds for the payment of the Purchase Price of tendered Series 2005 Bonds shall be derived from the following sources and in the following order of priority:

1. immediately available funds transferred by the Remarketing Agent to the Tender Agent derived from the remarketing of such Bonds; and
2. immediately available funds drawn by the Paying Agent under the Liquidity Facility (including, in some cases, a Letter of Credit) applicable to such Bonds.

The Purchase Price of tendered Series 2005 Bonds is payable solely out of the above-described sources. Neither DWR, the Trustees, the Paying Agent, the Tender Agent nor the Remarketing Agent shall have any liability or, except from the sources identified above, obligation to pay or make available such Purchase Price, including under circumstances where the applicable Liquidity Facility (including, in some cases, a Letter of Credit) terminates and does not permit a draw thereunder in connection with such termination or where such Liquidity Facility provider is in default under such Liquidity Facility. The failure to pay any such Purchase Price for Series 2005 Bonds that have been tendered or deemed tendered for purchase from any of the sources identified above does not constitute an “Event of Default” under the Indenture, as defined in Appendix C. For a description of the termination provisions and the remedies of a Liquidity Provider, see “SECURITY FOR THE BONDS – Master Bank Agreement” and APPENDIX K – “SUMMARY OF CERTAIN PROVISIONS OF THE MASTER BANK AGREEMENT.” For a description of the initial Liquidity Providers with respect to Series 2005 Bonds, see the Series Descriptions following the cover of this Official Statement and APPENDIX I – “INFORMATION CONCERNING INITIAL LETTER OF CREDIT PROVIDERS AND INITIAL LIQUIDITY FACILITY PROVIDERS.”

#### *Purchase and Reimbursement Account*

The Tender Agent will hold a “Purchase and Reimbursement Account” in trust for the purpose of depositing money obtained from (i) the remarketing of Series 2005 Bonds of a subseries or (ii) draws under a Liquidity Facility (including, in some cases, a Letter of Credit), and such deposited moneys shall be used solely to pay the Purchase Price of Series 2005 Bonds of a subseries or to reimburse a provider of a Liquidity Facility (including, in some cases, a Letter of Credit). The Purchase and Reimbursement Account does not constitute part of the Trust Estate and will be held uninvested.

#### *Delivery of Tendered Series 2005 Bonds*

All Series 2005 Bonds subject to optional or mandatory tender for purchase must be physically delivered to the Tender Agent at its office designated for such purpose, by 12:00 noon, New York City time, on the Purchase Date, accompanied by an instrument of transfer thereof in a form satisfactory to the Tender Agent, executed in blank by the Owner thereof with the signature of such Owner guaranteed in accordance with the guidelines set forth by one of the nationally recognized medallion signature programs.

#### *Effect of Failure to Deliver Purchased Series 2005 Bonds*

If the Purchase Price with respect to each tendered Series 2005 Bond of a subseries has been delivered to the Tender Agent, Series 2005 Bonds of such subseries that have not been delivered to the Tender Agent shall be deemed tendered, interest thereon shall cease to accrue on the Purchase Date, and the Tender Agent shall hold the Purchase Price thereof in the Purchase and Reimbursement Account for the benefit of such registered Owner pending such delivery for a period of 30 days after the Purchase Date, after which time any such moneys still held by the Tender Agent shall be transferred to the Paying Agent and held by the Paying Agent for the benefit of such former Owner without liability for interest thereon, and the former Owner of such Bond shall look solely to such amounts held by the Paying Agent as an unsecured creditor for payment therefor. Any moneys so held by the Tender Agent or by the Paying Agent shall be held in trust for the Owners of the Bonds entitled thereto, and shall not be invested. If a Bond of a subseries is subject to tender on a Purchase Date, and if such Bond is not delivered to the Tender Agent for purchase, a new Series 2005 Bond of such subseries in replacement thereof will be authenticated and delivered to the new registered Owner, and the undelivered Series 2005 Bond will cease to bear interest and will be deemed to be no longer Outstanding, and, from that date, the registered Owner thereof will be

entitled only to the payment of the Purchase Price, including interest accrued to, but excluding, such Purchase Date.

*Possible Limitations of Book-Entry System*

No representation is made herein as to the timely exercise by DTC or any of its Participants of any direction with respect to an election to tender beneficial interests in Series 2005 Bonds, nor is any representation made herein as to the timely payment of principal and interest upon a tender of beneficial interests in Series 2005 Bonds under the book-entry system. Tenders of beneficial interests in Series 2005 Bonds under the book-entry system will be governed by the procedures of DTC and its Participants in effect from time to time. See APPENDIX B – “BOOK-ENTRY SYSTEM.”

**Redemption**

*Optional Redemption*

At the option of DWR, Series 2005 Bonds in a Daily Rate Mode or a Weekly Rate Mode may be redeemed at a Redemption Price equal to the principal amount thereof with interest accrued to, but excluding, the Redemption Date, in whole or in part, on any Business Day.

*Mandatory Redemption from Sinking Fund Installments*

The Series 2005F-2 Bonds, the Series 2005F-3 Bonds, the Series 2005F-4 Bonds, the Series 2005G-1 Bonds, the Series 2005G-2 Bonds, the Series 2005G-6 Bonds, the Series 2005G-8 Bonds, the Series 2005G-9 Bonds and the Series 2005G-10 Bonds have been designated as “Term Bonds.” The Series 2005 Bonds that are Term Bonds are subject to redemption in part, by lot, on the dates and in the amounts set forth in the tables below, at the Redemption Price equal to the principal amount to be redeemed, plus accrued interest to the Redemption Date, from Sinking Fund Installments established under the Indenture.

**SINKING FUND INSTALLMENTS**

<b>Redemption Date (May 1)</b>	<b>Series</b>								
	<u>2005F-2</u>	<u>2005F-3</u>	<u>2005F-4</u>	<u>2005G-1</u>	<u>2005G-2</u>	<u>2005G-6</u>	<u>2005G-8</u>	<u>2005G-9</u>	<u>2005G-10</u>
2006	--	--	--	19,200,000	7,000,000	--	--	--	--
2007	--	--	--	15,200,000	5,500,000	--	--	--	--
2008	--	--	--	15,700,000	5,700,000	--	--	--	--
2009	--	--	--	16,300,000	6,000,000	--	--	--	--
2010	--	--	--	16,800,000	6,200,000	--	--	--	--
2011	--	--	--	16,800,000*	6,200,000*	--	--	800,000	--
2012	--	--	--	--	--	--	--	24,700,000	--
2013	--	--	--	--	--	--	25,600,000	--	--
2014	--	--	--	--	--	--	26,500,000	--	--
2015	--	--	--	--	--	--	140,900,000	--	--
2016	--	--	--	--	--	87,300,000	--	--	--
2017	--	--	--	--	--	137,700,000*	--	--	267,300,000
2018	--	--	--	--	--	--	7,000,000*	24,500,000*	32,700,000*
2019	107,000,000	--	--	--	--	--	--	--	--
2020	93,000,000*	46,800,000	--	--	--	--	--	--	--
2021	--	103,200,000*	50,800,000	--	--	--	--	--	--
2022	--	--	99,200,000*	--	--	--	--	--	--

\* Payment at maturity.

### *Selection of Bonds for Redemption*

If less than an entire maturity of a subseries of Series 2005 Bonds is to be redeemed, the Registrar shall select the particular Bonds or portions thereof to be redeemed in such manner in its discretion as it shall deem appropriate and fair. **However, if Series 2005 Bonds of a particular subseries have been purchased with funds derived from a Liquidity Facility, the Registrar is required to select such Bonds for redemption prior to selecting any other Bonds of the same subseries.**

### *Notice of Redemption*

The Registrar is to give notice of redemption by mailing copies of such notice (only to The Depository Trust Company (“DTC”) rather than the beneficial owners of the Series 2005 Bonds so long as DTC is the securities depository for the Series 2005 Bonds). The Registrar shall give such notice not more than 25 days nor less than 15 days prior to the Redemption Date, in the case of Series 2005 Bonds in a Daily Rate Mode or a Weekly Rate Mode. Notices of redemption given as described above are effective whether the notice is actually received, and whether any DTC procedures for giving notice are complied with. See APPENDIX B – “BOOK-ENTRY SYSTEM.”

Any notice of optional redemption may be made conditional upon the availability of moneys sufficient to pay the redemption price or the satisfaction of any other condition, including the receipt by the Paying Agent of moneys sufficient to pay the redemption price, and it may be rescinded at any time before the payment of the redemption price if any such condition is not satisfied or if any other specified event occurs. Notice of rescission of any conditional redemption will be given in the same manner as the notice of redemption, as promptly as practicable upon the failure of such condition or the occurrence of such event.

### *Effect of Redemption*

If, on the redemption date, moneys for the redemption of all Series 2005 Bonds to be redeemed, together with interest to the redemption date, are held by the Paying Agent and are available therefor, and if notice of redemption shall have been mailed as described above, then, from and after the redemption date, interest on the Series 2005 Bonds called for redemption shall cease to accrue. If said moneys shall not be so available on the redemption date, unless, in the case of any conditional notice, the conditions thereof are not satisfied or such notice is rescinded, the Series 2005 Bonds called for redemption shall continue to bear interest until paid at the same rate as they would have borne had they not been called for redemption.

## PLAN OF REFUNDING

### Refunding of Prior Bonds

DWR will apply a portion of the proceeds of the Series 2005 Bonds, together with other available monies (the “Refunding Proceeds”), to advance refund certain maturities of the Bonds designated as Series 2002A (the “Series 2002A Bonds”), as described in the following table (the “Refunded Bonds”). The Refunded Bonds will be redeemed on May 1, 2012 at a redemption price equal to 101% of the principal amount thereof, plus accrued interest thereon.

<u>Refunded Bonds</u>		
<u>Maturity Date (May 1)</u>	<u>Outstanding Principal Amount</u>	<u>Interest Rate</u>
2015	\$115,000,000	6.000%
2016	139,950,000	5.875%
2016	325,000,000	5.500%
2017	163,550,000	5.750%
2017	305,345,000	5.375%
2018	170,575,000	5.125%
2018	341,415,000	5.375%
2019	170,000,000	5.125%
2020	146,000,000	5.250%
2021	163,000,000	5.375%
2022	312,375,000	5.375%

DWR will use the Refunding Proceeds to purchase Defeasance Securities (as defined in Appendix C) which will be deposited, together with certain uninvested cash, in an irrevocable trust (the “Escrow Fund”) held by the State Treasurer, as Trustee and escrow agent, as security solely for the Refunded Bonds. The Defeasance Securities in the Escrow Fund will be scheduled to mature at such times and in such amounts, and will bear interest payable at such times and in such amounts, that together with the uninvested cash on deposit in the Escrow Fund, will provide sufficient moneys to pay, when due or called for redemption, the redemption price of and interest on the Refunded Bonds. See “VERIFICATION.” Upon the issuance of the Series 2005 Bonds, irrevocable instructions will be given to the Treasurer, as Trustee for the Refunded Bonds, to mail a timely notice of redemption of such Refunded Bonds. Accordingly, upon issuance of the Series 2005 Bonds, adequate and complete provision will be made for the full and timely payment of the redemption price of and interest on the Refunded Bonds, and the Refunded Bonds will be payable solely from the Defeasance Securities and uninvested cash on deposit in the Escrow Fund and will no longer be deemed to be Outstanding under the Indenture. The maturing principal of, and the investment income to be derived from, the Defeasance Securities and uninvested cash on deposit in the Escrow Fund will not be available to pay principal of, premium, if any, or interest on the Series 2005 Bonds or any bonds other than the Refunded Bonds.

## Estimated Sources and Uses of Funds

The estimated sources and uses of the proceeds of the Series 2005 Bonds and certain amounts available in the Electric Power Fund at the time of issuance of the Series 2005 Bonds are as follows:

### Estimated Sources of Funds

Principal Amount of Bonds	\$2,594,000,000
Release from Debt Service Reserve Account	16,644,115
Release from Bond Charge Payment Account	<u>42,611,804</u>
Total Sources of Funds	<u>\$2,653,255,919</u>

### Estimated Uses of Funds

Deposit in Escrow Fund for Refunded Bonds	\$2,628,321,405
Costs of Issuance	2,844,400
Underwriters' Discount	2,495,387
Credit Enhancement Fees and Charges <sup>1</sup>	<u>19,594,727</u>
Total Uses of Funds	\$2,653,255,919

<sup>1</sup> Includes bond insurance premiums and initial bank fees and expenses.

## Interest Rate Hedges

On October 11, 2005, DWR entered into a total of six fixed payer interest rate swap transactions with five counterparties in an aggregate notional amount of \$2,594,000,000 in order to place the aggregate carrying charges, including bond interest and net swap payments, with respect to the Series 2005 Bonds on an effectively fixed rate basis. See "THE DWR POWER SUPPLY PROGRAM – Financing of the Power Supply Program – *Interest Rate Hedges*" for a further description of such interest rate swap transactions.

## SECURITY FOR THE BONDS

### Introduction

The primary source of moneys for the payment of the Bonds and Bond Related Costs is Bond Charge Revenues, which constitutes part of the Trust Estate securing the Bonds, as described below. Bond Charges are imposed by the CPUC pursuant to the Rate Agreement and the Act upon customers in the service areas of the three IOUs.

The "Trust Estate" is assigned and pledged to the Trustees under the Indenture for the benefit of the Bonds and Parity Obligations, subject to the use of the Trust Estate in accordance with the Indenture. The "Trust Estate" is defined in the Indenture to include, among other things, "Revenues." "Revenues" includes both "Bond Charge Revenues" and "Power Charge Revenues." "Revenues" also includes revenues received by DWR from charges on customers of electric service providers, as described in "THE DWR POWER SUPPLY PROGRAM – Direct Access, Departing Load and Community Choice Aggregation." For a further description of the terms "Trust Estate" and "Revenues," see APPENDIX C – "SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE – Definitions."

- "Bond Charge Revenues" are Revenues received by DWR arising from Bond Charges imposed by the CPUC upon customers in the service areas of the IOUs, including the Bond Charge component of the Cost Responsibility Surcharge imposed upon certain direct access customers and certain

departing load, as described in “THE DWR POWER SUPPLY PROGRAM – Direct Access, Departing Load and Community Choice Aggregation.”

- “Power Charge Revenues” are Revenues received by DWR arising from Power Charges imposed by the CPUC upon customers in the service areas of the IOUs, including the Power Charge component of the Cost Responsibility Surcharge imposed upon certain direct access customers and certain departing load, as described in “THE DWR POWER SUPPLY PROGRAM – Direct Access, Departing Load and Community Choice Aggregation.”

The use of amounts on deposit in the Bond Charge Collection Account (including Bond Charge Revenues) for the payment of debt service on the Bonds and other Bond Related Costs when due is subject to the possible prior use of such amounts to pay “Priority Contract Costs” (defined to include costs and expenses under the Priority Long-Term Power Contracts described under “SECURITY FOR THE BONDS – Priority Long-Term Power Contracts”) and under certain circumstances, expenses of the Trustees (see APPENDIX C – “SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE – Events of Default and Remedies”). See also “SECURITY FOR THE BONDS – Accounts and Flow of Funds Under the Indenture,” “SECURITY FOR THE BONDS – Priority Long-Term Power Contracts,” and “RISK FACTORS – Determination of Power Charges and Bond Charges; Possible Use of Amounts in the Bond Charge Collection Account to Pay Priority Contract Costs.”

The accounts created under the Indenture and the flow of funds under the Indenture provide for the allocation of Revenues among different uses and are discussed below. See APPENDIX C – “SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE” for a detailed discussion of security provisions for the Bonds.

THE BONDS SHALL NOT BE OR BE DEEMED TO CONSTITUTE A DEBT OR LIABILITY OF THE STATE OR OF ANY POLITICAL SUBDIVISION THEREOF OR A PLEDGE OF THE FAITH AND CREDIT OF THE STATE OR OF ANY SUCH POLITICAL SUBDIVISION, OTHER THAN DWR TO THE EXTENT PROVIDED IN THE INDENTURE. THE BONDS SHALL BE PAYABLE SOLELY FROM THE FUNDS PLEDGED THEREFOR PURSUANT TO THE INDENTURE. THE BONDS SHALL NOT DIRECTLY OR INDIRECTLY OR CONTINGENTLY OBLIGATE THE STATE OR ANY POLITICAL SUBDIVISION THEREOF TO LEVY OR TO PLEDGE ANY FORM OF TAXATION WHATEVER THEREFOR OR TO MAKE ANY APPROPRIATION FOR THEIR PAYMENT.

#### **Accounts and Flow of Funds under the Indenture**

Revenues are held in and accounted for in the Electric Power Fund established under the Act for DWR. The Indenture establishes two sets of accounts for Revenues within the Electric Power Fund.

One set of accounts is primarily for the deposit of Bond Charge Revenues and the payment of Bond Related Costs (collectively, the “Bond Charge Accounts”):

- the Bond Charge Collection Account,
- the Bond Charge Payment Account, and
- the Debt Service Reserve Account.

The other set of accounts is primarily for the deposit of Power Charge Revenues and the payment of operating expenses (including payments of Priority Contract Costs and other power purchase costs and other costs of the Power Supply Program) (collectively, the “Power Charge Accounts”):

- the Operating Account,
- the Priority Contract Account, and

- the Operating Reserve Account.

In addition, an Administrative Cost Account facilitates accounting for certain DWR administrative costs that are subject to appropriation, but this account has no effect on the use of Revenues.

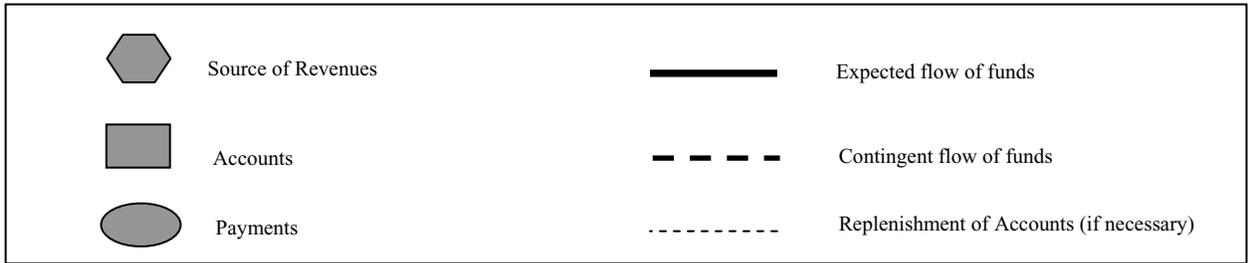
The Indenture requires all Bond Charge Revenues and any payments received from any counterparty to a Qualified Swap relating to Bonds to be deposited in the Bond Charge Collection Account, and all Power Charge Revenues and all other Revenues to be deposited in the Operating Account.

The Indenture requires the following transfers of Revenues to and from the Bond Charge Accounts:

- On or before the last Business Day of each month, DWR is required to transfer from the Bond Charge Collection Account to the Bond Charge Payment Account such amount as is necessary to make the amount in the Bond Charge Payment Account sufficient to pay Bond Related Costs (including “Debt Service” on the Bonds) estimated to accrue or be payable during the next succeeding three calendar months. For the definition of Debt Service, see APPENDIX C – “SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE – Definitions.” Each such transfer is subject to the prior transfer of amounts in the Bond Charge Collection Account to the Priority Contract Account if and to the extent amounts in the Priority Contract Account, the Operating Account and the Operating Reserve Account are insufficient to pay Priority Contract Costs then due under Priority Long-Term Power Contracts. See “SECURITY FOR THE BONDS – Priority Long-Term Power Contracts.” Amounts in the Bond Charge Payment Account may be used solely to pay debt service on the Bonds and other Bond Related Costs.
- Deficiencies in the Bond Charge Payment Account are required to be made up *first*, from the Operating Account and *second*, from the Debt Service Reserve Account (except for Fiduciary costs).

On the following page is a simplified schematic representation of the flow of funds within the two sets of accounts (excluding the Administrative Cost Account).

## Flow of Revenues under the Indenture\*



\*Simplified for graphic presentation purposes.

- Each month after the Bond Charge Payment Account is funded as described above, Revenues are required to be transferred to the Debt Service Reserve Account, on a parity with payments for any reserve established for Parity Obligations, to the extent necessary to meet the respective requirements for such reserves. In the case of the Debt Service Reserve Account: (i) to the extent such transfer is required as a result of the use of Bond Charge Revenues for the payment of Priority Contract Costs or change in investment value, such transfers shall be made *first*, from the Operating Account and *second*, to the extent necessary, from the Bond Charge Collection Account, and (ii) if any other transfer is required, it shall be made from the Bond Charge Collection Account. Deficiencies in the Debt Service Reserve Account may be cured by monthly deposits during the period commencing no later than seven months following the determination of the deficiency, such that the deficiency is cured by no later than 12 months following the determination of the deficiency.

The Indenture requires the following transfers of Revenues to and from the Power Charge Accounts:

- On or before the fifth Business Day of each month, DWR is required to transfer from the Operating Account to the Priority Contract Account such amount as is necessary to make the amount in the Priority Contract Account sufficient to pay Priority Contract Costs estimated to be due during the balance of such month and through the first five Business Days of the next succeeding calendar month. Amounts in the Priority Contract Account may be used solely to pay Priority Contract Costs.
- Amounts in the Operating Account after the above transfer to the Priority Contract Account are to be used for the following purposes in the following order of priority:
  - (i) for transfer to the Priority Contract Account if the amount therein is insufficient to pay Priority Contract Costs then due (that is, if the estimated amount previously transferred to that account turns out to be insufficient to pay actual Priority Contract Costs);
  - (ii) for the payment of other Operating Expenses;
  - (iii) to reimburse the Bond Charge Collection Account for any amounts previously transferred from the Bond Charge Collection Account to the Priority Contract Account to pay Priority Contract Costs;
  - (iv) to pay debt service on the Bonds and other Bond Related Costs (if amounts in the Bond Charge Payment Account are not sufficient for those purposes) and, in addition, prior to the time Bond Charge Revenues are received in amounts sufficient to make the required transfers described above from the Bond Charge Collection Account to the Bond Charge Payment Account with respect to Bond Related Costs, amounts to make those transfers as required;
  - (v) for transfer to the Debt Service Reserve Account to the extent required by the Indenture as a result of the use of Bond Charge Revenues to pay Priority Contract Costs or a change in value of investments in the Debt Service Reserve Account;
  - (vi) to replenish the Operating Reserve Account to its requirement as provided by the Indenture;
  - (vii) to pay Subordinated Indebtedness and Subordinated Obligations and certain other amounts relating thereto; and
  - (viii) for any other lawful purpose of the Power Supply Program.
- The Operating Reserve Account may be drawn upon to make up any deficiency in the Operating Account for any of the purposes listed in clauses (i) through (v) of the preceding list, provided, however, that if and to the extent that the amount in the Operating Reserve Account is or would be

less than or equal to the Priority Contract Contingency Reserve Amount, amounts in the Operating Reserve Account may be used only to make up any deficiency in the Priority Contract Account. See “SECURITY FOR THE BONDS - Operating Reserve Account” below.

The Indenture prescribes an application of Revenues that may be different than as described above in the event of a default thereunder. See APPENDIX C – “SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE – Events of Defaults and Remedies.”

### **Debt Service Reserve Account**

The “Debt Service Reserve Requirement” is an amount equal to maximum aggregate annual Debt Service on all outstanding Bonds, determined in accordance with the Indenture. The Debt Service Reserve Account was initially funded with proceeds of the Series 2002 Bonds and is required to be maintained in the amount of the Debt Service Reserve Requirement. The Debt Service Reserve Account is required to be replenished, if necessary, from Power Charge Revenues or Bond Charge Revenues in the manner and at the times (which may extend over a period of one year commencing seven months following the determination of the deficiency) described under APPENDIX C – “SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE – Application and Flow of Funds – *Debt Service Reserve Account*.”

For an explanation of assumptions to be used in calculating the Debt Service Reserve Requirement for variable rate and hedged bonds and under other circumstances, see the definitions of Debt Service and Debt Service Reserve Account in APPENDIX C – “SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE – Definitions.”

Alternate Debt Service Reserve Account Deposits may be made to the Debt Service Reserve Account in lieu of cash and/or securities. Such Deposits may consist of irrevocable surety bonds, insurance policies, letters of credit or similar obligations.

Whenever the amount in the Debt Service Reserve Account exceeds the Debt Service Reserve Requirement, after giving effect to any Alternate Debt Service Reserve Account Deposit, the excess shall, at least annually, be transferred to the Bond Charge Collection Account.

Amounts in the Debt Service Reserve Account may be used for the payment of Bond Related Costs (including debt service on the Bonds, payments under Enhancement Facilities and scheduled and termination payments under Qualified Swaps) except Fiduciary costs, and in each case only if amounts in the Bond Charge Payment Account and Operating Account are insufficient for that purpose. See APPENDIX C – “SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE—Application and Flow of Funds – *Debt Service Reserve Account*.”

### **Operating Account**

DWR has covenanted in the Indenture to include in its revenue requirements amounts estimated to be sufficient, among other things, to cause the amount on deposit in the Operating Account (excluding any reserves established for any Subordinated Indebtedness or Subordinated Obligations), at all times during any calendar month, to equal the Minimum Operating Expense Available Balance. “Minimum Operating Expense Available Balance” means, at the time revenue requirements are submitted to the CPUC, the maximum amount projected by DWR by which Operating Expenses exceed Power Charge Revenues during any one calendar month during that revenue requirement period, based on such assumptions as DWR deems to be appropriate after consultation with the CPUC and taking into account a range of possible future outcomes.

## **Operating Reserve Account**

The Operating Reserve Account has been established in case the amount in the Operating Account is insufficient to pay certain expenses, including any Priority Long-Term Power Contract termination payments, any other Priority Contract Costs and any of the other expenses listed in clauses (i) through (v) of the list of monthly Operating Account transfers set forth above under “SECURITY FOR THE BONDS - Accounts and Flow of Funds under the Indenture.” If the amount in the Operating Account is insufficient to pay Priority Contract Costs of any kind, the Operating Reserve Account is required to be exhausted before the Bond Charge Collection Account is utilized for such purpose. If the amount in the Operating Reserve Account is less than or equal to the Priority Contract Contingency Reserve Amount, amounts in the Operating Reserve Account may only be used to make up any deficiency in the Priority Contract Account. The “Priority Contract Contingency Reserve Amount” is to be calculated at the beginning of each revenue requirement period and is the maximum monthly amount of Priority Contract Costs projected by DWR to be payable under Priority Long-Term Power Contracts during that revenue requirement period, based on such assumptions as DWR deems to be appropriate, taking into account a range of possible future outcomes.

The “Operating Reserve Account Requirement” is an amount, during each revenue requirement period, equal to the greater of (1) the largest aggregate amount, as projected by DWR, by which Operating Expenses exceed Power Charge Revenues during any seven calendar month period commencing in that revenue requirement period, and (2) 12 percent of DWR’s projected annual operating expenses; provided, however, that solely for purposes of (2) above, the projected amount shall not be less than the applicable percentage of DWR’s operating expenses for the most recent 12 calendar month period for which DWR determines that reasonably full and complete operating expense information is available, adjusted for reductions in DWR financial responsibility for power supply contracts. Projections may be based on such assumptions as DWR deems to be appropriate and, in the case of clause (1) above, may take into account a range of possible future outcomes. Whenever the Indenture requires DWR to consult with the CPUC with respect to assumptions made by DWR, DWR is required to involve the CPUC in the development of those assumptions by conferring regularly in a manner consistent with DWR’s obligations under Article 4 of the Rate Agreement. The Operating Reserve Account is required to be replenished, if necessary, from Power Charge Revenues in the manner and at the times (which may extend over a period of one year commencing seven months following the determination of the deficiency) described in APPENDIX C – “SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE – Application and Flow of Funds – *Operating Reserve Account.*”

Whenever the Operating Reserve Account Requirement is reduced pursuant to the Indenture, any excess amounts in the Operating Reserve Account (“Excess Amounts”) will be used at such time to satisfy any deficiencies existing at such time in the transfers, applications and withdrawals described in clauses (i) through (v) of the list under “SECURITY FOR THE BONDS - Accounts and Flow of Funds under the Indenture” above. Unless otherwise agreed by both DWR and the CPUC, each acting in its own discretion, any Excess Amounts remaining after application to the uses described in the preceding sentence shall be used, at the direction of the CPUC after consultation with DWR, to (i) adjust DWR charges or (ii) with the agreement of DWR, to reduce debt outstanding under the Indenture, in all instances upon consideration of the interests of the customers of the IOUs and of DWR and, if applicable, electric service provider retail customers. If and when DWR no longer is responsible for the payment of costs under any Power Supply Contract, the balance, if any, in the Operating Reserve Account is required to be applied as described in the preceding two sentences.

## **Bond Related Costs**

Bond Related Costs that are payable from Bond Charges imposed by the CPUC under the Rate Agreement consist of payments or deposits or other provision to be made by DWR under the Indenture or other financing documents or the Act, for the following components of DWR’s revenue requirements under the Act:

- (i) principal of, premium, if any, and interest on Bonds and any additional amount required under the Indenture or other financing documents to be deposited into the Bond Charge Collection Account to provide debt service coverage of the Bonds;
- (ii) payments required to be made (A) under agreements with issuers of credit and liquidity facilities and their participants, including letters of credit, bond insurance, guarantees, debt service reserve fund surety bonds, lines of credit, reimbursement agreements, and standby bond purchase agreements, (B) under agreements relating to other financial instruments entered into in connection with the Bonds, including but not limited to investment agreements, hedges, interest rate swaps, caps, options and forward purchase agreements, and (C) under agreements relating to the remarketing of Bonds, including but not limited to remarketing agreements, dealer agreements and auction agent agreements;
- (iii) deposits to the Debt Service Reserve Account established under the Indenture to the extent necessary to provide therein an amount equal to the requirement for such account under the Indenture and other financing documents if not otherwise replenished from Power Charges;
- (iv) the costs of the Trustees and the Registrars and Paying Agents associated with the issuance and administration of the Bonds; and
- (v) when and if DWR no longer sells Power under the Act and Bonds remain outstanding, DWR's Bond Charge servicing costs, costs of preparing and providing the information and reports required under the Indenture and other financing documents, the Rate Agreement and the Act, related audit, legal and consulting costs, related administrative costs, and costs of complying with arbitrage restrictions and rebate requirements.

The amount payable under Parity Obligations is not limited by the Indenture or the Rate Agreement. However, not all costs that constitute Bond Related Costs under the Rate Agreement are payable on a parity with the Bonds. "Parity Obligation" is defined in the Indenture to include only "Reimbursement Obligations" and the amounts payable under Qualified Swaps. The criteria for determining whether an agreement is a Reimbursement Obligation or a Qualified Swap are explained in APPENDIX C – "SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE – Special Provisions Relating to Enhancement Facilities, Qualified Swaps, Other Similar Arrangements and Interim Financing Notes."

In connection with the issuance of the Series 2002 Bonds, DWR entered into agreements with issuers of credit and liquidity facilities and agreements with interest rate swap providers, which constitute Parity Obligations. In connection with the issuance of the Series 2005 Bonds, DWR has entered into agreements with interest rate swap providers, and expects to enter into additional agreements with issuers of credit and liquidity facilities and agreements, which constitute Parity Obligations. See "THE DWR POWER SUPPLY PROGRAM – Financing of the Power Supply Program."

### **Rate Covenants**

The CPUC has irrevocably covenanted in the Rate Agreement, for the benefit of Bondholders (and all other persons to whom DWR is obligated to pay Bond Related Costs), to calculate, revise and impose from time to time, Bond Charges sufficient to provide moneys so that amounts available for deposit in the Bond Charge Payment Account under the Indenture from time to time, together with amounts on deposit in the Bond Charge Payment Account, are at all times sufficient to pay or provide for the payment of debt service on the Bonds and all other Bond Related Costs (as defined in the Rate Agreement) when due in accordance with the Indenture and other financing documents. See "CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES – Rate Agreement." The Rate Agreement provides that this covenant shall have the force and effect of a "financing order" under the California Public Utilities Code and shall be irrevocable and enforceable in accordance with its terms, including, without limitation, in circumstances in which DWR has breached its

obligations under the Rate Agreement or in respect of the Financing Documents. Under the California Public Utilities Code, a “financing order” is binding upon the CPUC as it may be constituted from time to time, and the CPUC shall have no authority to rescind, alter or amend its obligations thereunder. Under the Act, the rights, powers and duties of the CPUC may not be diminished or impaired in a manner that would adversely affect the interests or rights of Bondholders. See “SECURITY FOR THE BONDS – Bond Related Costs.” See also, however, “RISK FACTORS – Determination of Power Charges and Bond Charges; Possible Use of Amounts in the Bond Charge Collection Account to Pay Priority Contract Costs.”

DWR has covenanted in the Indenture to cause to be established, fixed and revised from time to time, charges sufficient, together with any other available moneys and securities on deposit in DWR’s Electric Power Fund, to satisfy all of DWR’s revenue requirements at the times and in the amounts needed. The term “revenue requirements” means the amounts needed from time to time by DWR to satisfy its obligations under the Act and under proclamations and orders issued pursuant to the California Emergency Services Act. These obligations include, but are not limited to, making deposits to the Bond Charge Payment Account and Debt Service Reserve Account in the amounts and at the times required by the Indenture. See APPENDIX C – “SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE.”

### **Priority Long-Term Power Contracts**

#### *General*

The Priority Long-Term Power Contracts each provide, in effect, that payments by DWR under the contracts are to be paid or are payable prior to bonds, notes, or other indebtedness of DWR secured by a pledge or assignment of the revenues of DWR under the Act and other amounts in the Electric Power Fund established by the Act. Substantially all of the power purchased by DWR under the Act will be purchased under Priority Long-Term Power Contracts and for that reason substantially all operating expenses will be Priority Contract Costs. See also “THE DWR POWER SUPPLY PROGRAM – Power Purchase Contracts.”

Under the Rate Agreement, the term “Priority Long Term Power Contracts” is defined as (i) those long-term electric power contracts identified in the appendix to the Rate Agreement and not including any electric power contracts entered into after August 14, 2001, provided, however, that such term includes any priority long-term electric power contract entered into after such date as an amendment or novation of any Priority Long-Term Power Contract, and (ii) any contracts entered into for the purpose of securing fuel for use at generating facilities being operated pursuant to such Priority Long-Term Power Contracts, if that fuel supply contract contains a provision to the general effect that payments by DWR under the contract are to be paid or payable prior to bonds, notes or other indebtedness of DWR secured by a pledge or assignment of the revenues of DWR under the Act and other amounts in the Electric Power Fund. The Indenture incorporates by reference the Rate Agreement’s definition of that term.

The Priority Long-Term Power Contracts obligate DWR to purchase power from various suppliers. The Priority Long-Term Power Contracts currently have varying terms through 2013. The total amount of energy purchased by DWR through the Priority Long-Term Power Contracts has been in excess of its customers’ needs; such excess circumstance is expected to recur from time to time. In these periods, DWR has sought and will continue to seek to sell the excess energy to other users. DWR expects that from time to time the price it receives for excess energy will be less than its cost for that energy. If any such losses are substantially greater than projected by DWR in its then-current revenue requirement calculation, the submission of a revised revenue requirement and the imposition of increased Power Charges could be required. See “CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES.

If a counterparty under a Priority Long-Term Power Contract fails to deliver power to DWR, whether such counterparty is contractually permitted to do so, financially unable to perform its obligations thereunder or unable to deliver power for any other reason, one or more IOUs would have to purchase replacement power because DWR is no longer authorized to enter into new power purchase contracts. If the failed deliveries occur

under a contract providing for power at a cost lower than DWR's cumulative average cost (and sufficient mark-to-market termination payments are not owed, are not paid or are delayed for any reason), DWR could experience significant cash flow deterioration during the period required for DWR to submit a revised revenue requirement and for the CPUC to raise Power Charges.

#### *Payment Priority*

The use of amounts on deposit in the Bond Charge Collection Account (including Bond Charge Revenues) for the payment of debt service on the Bonds and other Bond Related Costs when due is subject to the possible prior use of such amounts to pay Priority Contract Costs. See "SECURITY FOR THE BONDS - Accounts and Flow of Funds Under the Indenture." To date, it has not been necessary to use Bond Charge Revenues to pay Priority Contract Costs because Power Charge Revenues have been adequate to pay all Priority Contract Costs as and when due. Although no assurances can be given, DWR expects the calculation, imposition and collection of Power Charge Revenues to continue to be adequate to pay all Priority Contract Costs as and when due and does not expect to use Bond Charge Revenues to pay Priority Contract Costs. See "SECURITY FOR THE BONDS - Recovery of Amounts Used to Pay Priority Contract Costs." See also "RISK FACTORS – Determination of Power Charges and Bond Charges; Possible Use of Amounts in the Bond Charge Collection Account to Pay Priority Contract Costs."

If Bond Charge Revenues and other amounts on deposit in the Bond Charge Collection Account are used to pay Priority Contract Costs, the Rate Agreement provides that DWR shall take such actions as are required under the Rate Agreement so that the amounts applied from the Bond Charge Collection Account for such purpose shall be replenished from Power Charges. See "SECURITY FOR THE BONDS - Recovery of Amounts Used to Pay Priority Contract Costs."

In the absence of material change in the net per unit cost of energy derived from Priority Long-Term Power Contracts and provided to DWR's retail customers and in the absence of material termination payments on Priority Long-Term Power Contracts, Power Charge Revenues are expected to increase and decrease approximately in proportion to increases and decreases in Priority Contract Costs. Furthermore, the timing of monthly payments of Priority Contract Costs (an average lag of about 35 days from provision of energy) is comparable to the timing of receipt by DWR of Power Charge Revenues (an average lag of about 45 days from consumption of energy).

However, a number of factors affect the variability of net per unit Priority Contract Costs from time to time, and, as a result, the sufficiency of the monthly amount of Power Charge Revenues in relation to the monthly amount of Priority Contract Costs. These factors include, but are not limited to, the cost from time to time of natural gas costs, the amount of surplus power from Priority Long-Term Power Contracts (energy DWR is required to take) sold at prices below the price paid for such power, and the amount of power dispatched from time to time under contracts with fixed capacity payments or with adjustment rights on block quantities. In the course of preparing its revenue requirement determinations, DWR evaluates several cash flow scenarios that make varying assumptions concerning these factors. See "CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES – Substantive Considerations in Establishing Revenue Requirements."

#### *Termination Payments*

In addition, most of the Priority Long-Term Power Contracts provide for the payment of termination liquidated damages by DWR upon the occurrence of an event of default by DWR and termination of the Priority Long-Term Power Contract by the seller. The principal risk of termination is the failure of DWR to pay for purchased power, a Priority Contract Cost which is payable in the short term from the Operating Account, the Operating Reserve Account and, if necessary, the Bond Charge Collection Account, and payable in the longer term from increased Power Charges. See "CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES."

The termination liquidated damages are generally equal to the net present value of the difference between the price for power pursuant to the Priority Long-Term Power Contract and the then-current market price for power, for the entire remaining term of the Priority Long-Term Power Contract (referred to herein as the “mark-to-market value”). A portion of DWR’s Priority Long-Term Power Contracts currently have a positive mark-to-market value, while others have a negative mark-to-market value. The mark-to-market values of the Priority Long-Term Power Contracts change daily with wholesale power prices, and no assurance can be given that DWR will not have substantial contingent mark-to-market liabilities with respect to its Priority Long-Term Power Contracts in the future. Upon a DWR default under one or more Priority Long-Term Power Contracts with a negative mark-to-market value, DWR could incur termination payment liabilities in the hundreds of millions of dollars or greater. Under most of the Priority Long-Term Power Contracts, termination payments are due within 180 days of any termination and would constitute Priority Contract Costs recoverable from Power Charges. DWR revenue requirements and projected Power Charge Account balances are not established to specifically address contract terminations. If a termination were to occur, DWR might need to submit a revised revenue requirement to address the change in expected costs and energy deliveries, and the CPUC would need to act to set Power Charges that reflect the revised revenue requirement. See “SECURITY FOR THE BONDS” and “CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES.”

#### *Operating Reserve Account*

The Indenture requires the Operating Reserve Account to be established and maintained by DWR at an amount equal to the Operating Reserve Account Requirement, which may be based on such assumptions as DWR deems to be appropriate, after consultation with the CPUC, and taking into account a range of possible future outcomes. See “SECURITY FOR THE BONDS—Operating Reserve Account.” When establishing the Operating Reserve Requirement from time to time, DWR intends to utilize assumptions and take into account possible future outcomes that include a range of variation in the circumstances that affect the factors described in the foregoing paragraph.

#### *Certain Litigation*

Litigation is pending between DWR and one of its long-term power suppliers. See “THE DWR POWER SUPPLY PROGRAM – Power Purchase Contracts – *Dispute with Power Supplier.*”

#### **Recovery of Amounts Used to Pay Priority Contract Costs**

The Indenture and the Rate Agreement permit Bond Charge Revenues to be used to pay Priority Contract Costs if other funds under the Indenture, such as Power Charge Revenues, are insufficient. The flow of funds required by the Indenture provides that Priority Contract Costs are to be paid each month from Power Charge Revenues before any payment or funding of any other Department Costs. See “SECURITY FOR THE BONDS – Accounts and Flow of Funds under the Indenture.” The CPUC has covenanted in the Rate Agreement to calculate, revise and impose, from time to time, Power Charges sufficient to provide moneys in the amounts and at the times necessary to satisfy the Retail Revenue Requirements submitted by DWR to the CPUC in accordance with the Rate Agreement. The Rate Agreement provides that in the event Priority Contract Costs are funded out of the Bond Charge Collection Account, DWR shall take such actions as are required under the Rate Agreement so that the amounts applied from the Bond Charge Collection Account for such purpose shall be replenished from Power Charges. See “CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES – Rate Agreement” and “RISK FACTORS – Determination of Power Charges and Bond Charges; Possible Use of Amounts in the Bond Charge Collection Account to Pay Priority Contract Costs.”

#### **Enhancement Facilities**

DWR has elected to deliver either (a) a bond insurance policy and a Liquidity Facility or (b) a letter of credit with respect to each subseries of Series 2005 Bonds upon their issuance and delivery, as provided in the Series Descriptions following the cover of this Official Statement and in “SECURITY FOR THE BONDS –

Initial Letters of Credit,” “– Initial Liquidity Facilities” and “– Bond Insurance.” This section summarizes certain provisions of the Indenture concerning Credit Facilities and Liquidity Facilities. See “SECURITY FOR THE BONDS – Initial Liquidity Facilities – *Cautionary Statements*,” “– *Liquidity Termination Event*,” “– *Liquidity Suspension Event*,” “– *Bond Insurer Approved Events of Default*” and “– *Termination of Initial Liquidity Facility*” for a description of certain circumstances under which a Liquidity Facility might be suspended or terminated.

Each Credit Facility for a subseries of Series 2005 Bonds shall provide for draws thereon or borrowings therefrom, in the aggregate, in an amount at least equal to the Applicable Principal and Interest Coverage for all of the Series 2005 Bonds of such subseries. Each Liquidity Facility for a subseries of Series 2005 Bonds shall provide for draws thereon or borrowings therefrom, in the aggregate, in an amount at least equal to the Applicable Principal and Interest Coverage for the Series 2005 Bonds of such subseries.

If a Direct-Pay Credit Facility is in place with respect to a subseries of Series 2005 Bonds, the Paying Agent shall draw under such Direct-Pay Credit Facility by no later than the time provided in the Direct-Pay Credit Facility for presentation of documents in order to receive payment in immediately available funds by 2:30 p.m., New York City time, on each Principal Installment due date, Redemption Date and Interest Payment Date, as the case may be, an amount sufficient to pay the principal or Redemption Price of and interest due on such Principal Installment due date, Redemption Date and Interest Payment Date, as the case may be, and shall immediately deposit the proceeds of such draw in the related subaccount in the Credit Facility Drawings Account.

Although the Indenture provides that Standby Credit Facilities may be used as Credit Facilities in support of a subseries of Series 2005 Bonds, the Master Bank Agreement entered into by DWR in connection with the issuance of the Bonds provides that all letters of credit issued in accordance therewith will be Direct-Pay Credit Facilities

At any time, DWR may deliver a Substitute Credit Facility or Substitute Liquidity Facility with respect to any subseries of Series 2005 Bonds, or may elect, following a mandatory tender for purchase, to have no Credit Facility or Liquidity Facility supporting such subseries. DWR may not deliver a Liquidity Facility for a subseries of Series 2005 Bonds without the prior consent of the Credit Facility Provider, if any, for such subseries and DWR may not deliver a Substitute Credit Facility for a subseries of Series 2005 Bonds without the prior consent of the Liquidity Facility Provider (unless such Substitute Credit Facility is also a Substitute Liquidity Facility), if any, for such subseries. If DWR elects to substitute any Enhancement Facility, to the extent that the Series 2005 Bonds supported by such Enhancement Facility are not subject to mandatory tender for purchase as a result of substitution, the Paying Agent will send notice to the Owners of the affected Series 2005 Bonds of such proposed substitution at least 15 days prior to the effective date of the substitution.

The Paying Agent will release any then-existing Credit Facility or Liquidity Facility only upon (i) the effective date of the Credit Facility or Liquidity Facility delivered in substitution therefor and, if a mandatory tender is required under the Indenture, following the honor of draws on such then-existing Credit Facility or Liquidity Facility upon the mandatory tender for purchase of such Series 2005 Bonds, (ii) the effective date of a change in the Interest Rate Mode to an Auction Rate Mode or a Fixed Rate Mode, or (iii) the Series 2005 Bonds secured thereby cease to be “Outstanding” in accordance with the Indenture (i.e., they are defeased, paid or otherwise cancelled); provided, however, that if a mandatory tender for purchase shall be required pursuant to the Indenture upon any substitution for a then existing Liquidity Facility, such then existing Liquidity Facility shall not be released or surrendered until the Paying Agent shall have made a drawing thereon (and the Liquidity Facility Provider has honored the draw) in an amount sufficient to effect the purchase of such Series 2005 Bonds on the applicable Purchase Date.

In the event that the principal, sinking fund installments, if any, Purchase Price and Redemption Price, if applicable, or interest due on any Outstanding Series 2005 Bonds shall be paid from draws made under an Enhancement Facility (including bond insurance, Letters of Credit and Liquidity Facilities), all covenants, agreements and other obligations of DWR to the Owners of such Series 2005 Bonds shall continue to exist, and the issuer of such Enhancement Facility shall be subrogated to the rights of such Owners.

## **Bond Insurance**

The scheduled payment of the principal of and interest on the Series 2005G Bonds (other than the Series 2005G-1 Bonds and the Series 2005G-2 Bonds) (collectively, the “Insured Bonds”), when due, will be insured by a financial guaranty insurance policy (each, a “Policy”) to be issued by the applicable bond insurer (a “Bond Insurer”) identified on the inside cover of this Official Statement. Debt service on all subseries of the Series 2005F Bonds, the Series 2005G-1 Bonds and the Series 2005G-2 Bonds is supported by direct-pay letters of credit but is not insured. See APPENDIX J – “INFORMATION CONCERNING BOND INSURERS AND FORMS OF FINANCIAL GUARANTY INSURANCE POLICIES.”

It is a condition to the issuance of the Series 2005 Bonds that the Bond Insurers issue the Policies. A specimen of each such Policy is included in Appendix J. Certain other information concerning each Bond Insurer and its Policy, which has been supplied by the Bond Insurer, is also set forth in Appendix J. No representation is made by DWR or the Underwriters as to the accuracy, completeness or adequacy of such information, or as to any additional documents referred to in Appendix J, or as to the absence of material adverse changes in such information subsequent to the date hereof. Neither DWR nor the Underwriters have made any independent investigation of the Bond Insurers or the Policies, and reference should be made to the information set forth below and in Appendix J hereto for a description thereof. Any additional documents referred to in Appendix J are not a part of this Official Statement. Except for payment of the premiums for the Policies, DWR has no responsibility whatsoever with respect to the Policies, including the collection of amounts payable thereunder.

The Indenture provides that so long as a Policy is in full force and effect, and payment on such Policy is not in default, then the applicable Bond Insurer shall be deemed to be the sole Owner of the outstanding Insured Bonds covered by such Policy when the approval, consent or action of the Owners thereof is required or may be exercised under the Indenture, except as provided by the provisions of the Indenture permitting modifications and amendments only with the consent of a particular Owner (see APPENDIX C – “SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE – Supplemental Indentures and Amendments”). With respect to such modifications and amendments, the consent of such Bond Insurer shall be required in addition to the consent of such Owner. Certain Bond Insurers may also have the right to consent to certain amendments to the Indenture, the Rate Agreement or the Master Bank Agreement, even if the approval of Owners is required, and to give notices of default under the Indenture.

## **Initial Letters of Credit**

### *General*

The payment of the principal of, interest on, Redemption Price of, and Purchase Price of, all five subseries of the Series 2005F Bonds, the Series 2005G-1 Bonds and the Series 2005G-2 Bonds will initially be paid from proceeds drawn under Letters of Credit (each, an “Initial Letter of Credit”). This section describes certain terms of the Initial Letters of Credit. The identities of the issuers of the Initial Letters of Credit (each, a “Credit Facility Provider”) are set forth in the Series Descriptions following the cover of this Official Statement. The Initial Letters of Credit will be direct-pay letters of credit issued under a Master Credit, Liquidity and Participation Agreement (the “Master Bank Agreement”), entered into among DWR, the various “banks” described therein and JPMorgan Chase Bank in its capacity as administrative agent for such banks (together with its successors and assigns in such capacity, the “Administrative Agent”). See “SECURITY FOR THE BONDS – Master Bank Agreement,” below and APPENDIX K – “SUMMARY OF CERTAIN PROVISIONS OF THE MASTER BANK AGREEMENT,” for additional provisions relevant to the Master Bank Agreement and the Initial Letters of Credit.

**Each Initial Letter of Credit secures only the subseries of Series 2005 Bonds for which it is issued, as described below, and funds available under such Initial Letter of Credit are not available for the payment of any other subseries of Series 2005 Bonds. The Series 2005G Bonds (other than the Series**

**2005G-1 Bonds and the Series 2005G-2 Bonds) are not secured by a Letter of Credit, but are secured by bond insurance and Liquidity Facilities, as described herein.**

*Stated Amount; Term*

Each Initial Letter of Credit will have an initial stated amount equal to the aggregate principal amount of the subseries of Series 2005 Bonds secured by such Initial Letter of Credit (the “Principal Portion”) plus a notional dollar amount of interest thereon (the “Interest Portion”) equal to approximately \$12,054 per \$1,000,000 of Principal Portion. This amount is determined by assuming a rate of 11% per annum on the Principal Portion for 40 days, calculated on the basis of a 365-day year and actual days elapsed (such method of calculating interest on any principal amount of Series 2005 Bonds, other than Insured Bonds, being referred to herein as the “Interest Coverage Amount”). The Interest Portion of each Initial Letter of Credit is greater than the amount of interest that will accrue on the Series 2005 Bonds secured thereby during the Initial Interest Period. The scheduled expiration date of each Initial Letter of Credit is three or five years after the issuance date of the Series 2005 Bonds, as set forth on the Series Description for each subseries. Each Initial Letter of Credit will be issued on the date the subseries of Series 2005 Bonds that it secures are issued. Each Initial Letter of Credit will support the applicable subseries of Series 2005 Bonds during the Initial Interest Period and thereafter, during a Daily Rate Mode or a Weekly Rate Mode. The Paying Agent will be the beneficiary of each Initial Letter of Credit. No person other than the Paying Agent shall be permitted to present drawings under any Initial Letter of Credit. Each Initial Letter of Credit may be transferred to a successor Paying Agent.

*Source of Payment*

Each Credit Facility Provider of an Initial Letter of Credit agrees that it will pay from its own funds its pro rata share of all drawings made under such Initial Letter of Credit.

*Initial Letters of Credit Issued by Multiple Banks*

The Initial Letters of Credit supporting the Series 2005F-2 Bonds and the Series 2005F-3 Bonds, respectively, are to be issued by more than one Credit Facility Provider. Where an Initial Letter of Credit is issued by more than one Credit Facility Provider, the obligations of each Credit Facility Provider thereof are several and not joint based upon the relative commitments of such Credit Facility Providers, which relative commitments are expressed as percentages in the Series Descriptions following the front cover of this Official Statement.

*Termination*

Each Initial Letter of Credit shall terminate on the earliest to occur of the following: (1) three or five years after the issuance date of the Series 2005 Bonds, as set forth on the Series Description for each subseries, or such later date or dates as the Credit Facility Provider of such Initial Letter of Credit shall specify from time to time in a written notice to the Paying Agent (the “Stated Expiration Date”); (2) the date on which the Credit Facility Provider honors payment of a drawing in respect of the payment of the principal of the Series 2005 Bonds of the subseries supported by such Initial Letter of Credit in which the Paying Agent certifies that no such Series 2005 Bonds will remain outstanding after the application of the proceeds of such drawing; (3) the date on which the Credit Facility Provider honors payment of a drawing in respect of the payment of the Redemption Price of the Series 2005 Bonds of the subseries supported by such Initial Letter of Credit in which the Paying Agent certifies that no such Series 2005 Bonds will remain outstanding after the application of the proceeds of such drawing; (4) 15 days after the Paying Agent receives written notice from the Credit Facility Provider (a) of the occurrence of a “Series Event of Default” under the Master Bank Agreement (see APPENDIX K – “SUMMARY OF CERTAIN PROVISIONS OF THE MASTER BANK AGREEMENT” for a description of these events), and (b) instructing the Paying Agent to cause a mandatory tender of the applicable Series 2005 Bonds and to make its final drawing under such Initial Letter of Credit (a “Default Notice”); (5) the date on which the Credit Facility Provider of such Initial Letter of Credit honors payment of a mandatory tender drawing in

connection with (a) the substitution of the Initial Letter of Credit with a substitute Credit Facility or a substitute Liquidity Facility (if a mandatory tender is required under the Indenture), (b) a conversion of all of the Series 2005 Bonds of the subseries supported by such Initial Letter of Credit to an Interest Rate Mode other than an Interest Rate Mode supported by such Initial Letter of Credit (e.g., a conversion of all of the Series 2005 Bonds of a subseries to a Fixed Rate Mode), (c) the occurrence of the Stated Expiration Date or (d) the receipt by the Paying Agent of a Default Notice; or (6) the date on which such Initial Letter of Credit is surrendered by the Paying Agent to the Credit Facility Provider thereof accompanied by a certificate in the form prescribed by the Initial Letter of Credit (for a description of the circumstances in which the Paying Agent may release a Credit Facility, see “SECURITY FOR THE BONDS – Enhancement Facilities”). Following the termination of its Initial Letter of Credit, the Credit Facility Provider thereof shall have no further obligation to honor drawings made (or attempted to be made) thereunder by the Paying Agent.

*Mandatory Purchase following Notice of Series Event of Default – No Termination*

As an alternate remedy to delivering a Default Notice to the Paying Agent following the occurrence of “Series Event of Default” under the Master Bank Agreement (see APPENDIX K – “SUMMARY OF CERTAIN PROVISIONS OF THE MASTER BANK AGREEMENT” for a description of these events), the Credit Facility Provider may deliver (1) a written notice to the Paying Agent requiring the Paying Agent to (a) cause a mandatory purchase of all outstanding Series 2005 Bonds of the subseries supported by such Initial Letter of Credit and (b) submit a mandatory tender drawing under such Initial Letter of Credit to pay the Purchase Price of such Series 2005 Bonds upon their mandatory purchase; and (2) a written notice to the Remarketing Agent(s) for the Series 2005 Bonds of such subseries instructing such Remarketing Agent(s) to cease remarketing such Bonds following their purchase from the proceeds of a mandatory tender drawing under such Initial Letter of Credit until such time, if any, as such Remarketing Agent(s) shall have received written notice from the Credit Facility Provider of such Initial Letter of Credit to the effect that such Credit Facility Provider has reinstated in full the stated amount of such Initial Letter of Credit.

*Reduction and Reinstatement of Stated Amount*

After a Credit Facility Provider of an Initial Letter of Credit honors payment of a drawing in respect of the payment of regularly scheduled interest on Series 2005 Bonds of the subseries supported by such Initial Letter of Credit, the aggregate Interest Portion of the stated amount of such Initial Letter of Credit shall be reduced by the amount of such drawing. The aggregate Interest Portion shall be reinstated by the amount of such drawing at 8:00 a.m., New York City time on the third business day following such drawing.

After a Credit Facility Provider of an Initial Letter of Credit honors payment of a drawing in respect of the payment of the principal or Redemption Price of the Series 2005 Bonds of the subseries supported by such Initial Letter of Credit, the stated amount shall be automatically and permanently reduced as follows: (1) the Principal Portion shall be reduced by the amount so drawn with respect to the payment of principal of the Series 2005 Bonds of such subseries and (2) the aggregate Interest Portion shall be reduced by the Interest Coverage Amount calculated with respect to such principal amount.

After a Credit Facility Provider of an Initial Letter of Credit honors payment of a drawing (other than a final drawing) in respect of the payment of the Purchase Price of Series 2005 Bonds of the subseries supported by such Initial Letter of Credit in connection with the tender for purchase thereof at the request of the owner or in connection with a mandatory tender for purchase of all Series 2005 Bonds of such subseries, the stated amount shall be automatically reduced as follows: (1) the Principal Portion shall be reduced by the amount so drawn with respect to the payment of principal of the Series 2005 Bonds and (2) the aggregate Interest Portion shall be reduced by the Interest Coverage Amount calculated with respect to such principal amount. The stated amount shall automatically be reinstated as follows: (a) the Principal Portion shall be reinstated by an amount equal to the principal amount of Series 2005 Bonds of such subseries that are remarketed following a purchase with the proceeds of an optional tender drawing or a mandatory tender drawing (other than the final drawing) and the receipt (or provision for receipt) by such Credit Facility provider of payment therefor and (b) the aggregate

Interest Portion shall be reinstated by an amount equal to the Interest Coverage Amount calculated with respect to such principal amount.

After a Credit Facility Provider of an Initial Letter of Credit honors payment of the Paying Agent's final drawing, the stated amount, the Principal Portion and the aggregate Interest Portion shall be automatically and permanently reduced to zero and the Initial Letter of Credit will terminate.

## **Initial Liquidity Facilities**

### *General*

The payment of the Purchase Price of the Series 2005G Bonds (other than the Series 2005G-1 Bonds and the Series 2005G-2 Bonds) (the "Insured Bonds") in the circumstances described below under the subheading "- *Extent of Purchase Obligation*" will initially be paid from proceeds drawn under Liquidity Facilities (each, a "Liquidity Facility"). This section describes certain terms of the Initial Liquidity Facilities. The identities of the issuers thereof (each, a "Liquidity Facility Provider") are set forth in the Series Descriptions following the front cover of this Official Statement. The Initial Liquidity Facilities will be standby bond purchase facilities issued under the Master Bank Agreement. See "SECURITY FOR THE BONDS – Master Bank Agreement," below and APPENDIX K – "SUMMARY OF CERTAIN PROVISIONS OF THE MASTER BANK AGREEMENT," for the definitions of certain capitalized terms used in this section and for a description of additional provisions relevant to the Master Bank Agreement and the Initial Liquidity Facilities.

EACH INITIAL LIQUIDITY FACILITY SUPPORTS ONLY THE SUBSERIES OF INSURED BONDS FOR WHICH IT IS ISSUED AND FUNDS AVAILABLE UNDER SUCH INITIAL LIQUIDITY FACILITY ARE NOT AVAILABLE FOR THE PAYMENT OF ANY OTHER SUBSERIES OF INSURED BONDS. EACH INITIAL LIQUIDITY FACILITY SECURES ONLY THE PAYMENT OF THE PURCHASE PRICE OF THE SUBSERIES OF INSURED BONDS FOR WHICH IT IS ISSUED AND DOES NOT SECURE THE PAYMENT OF THE PRINCIPAL OF, INTEREST ON OR REDEMPTION PRICE OF SUCH INSURED BONDS.

### *Cautionary Statements*

UNDER CERTAIN CIRCUMSTANCES DESCRIBED BELOW UNDER "LIQUIDITY TERMINATION EVENT" AND "LIQUIDITY SUSPENSION EVENT," THE OBLIGATION OF THE LIQUIDITY FACILITY PROVIDER OF AN INITIAL LIQUIDITY FACILITY TO PURCHASE ANY INSURED BONDS TENDERED FOR PURCHASE BY THE OWNERS THEREOF OR SUBJECT TO MANDATORY PURCHASE MAY BE TERMINATED OR SUSPENDED WITHOUT A PURCHASE OR PRIOR NOTICE. IN SUCH EVENT, SUFFICIENT FUNDS MAY NOT BE AVAILABLE TO PURCHASE INSURED BONDS TENDERED BY THE OWNERS THEREOF OR SUBJECT TO MANDATORY PURCHASE.

The ability to obtain funds under an Initial Liquidity Facility in accordance with its terms may be limited by federal or state law. Bankruptcy, conservatorship, receivership and similar laws governing financial institutions or the issuer of the Initial Liquidity Facility may prevent or restrict payment under the Initial Liquidity Facility. To the extent the short-term rating on a subseries of Insured Bonds secured by an Initial Liquidity Facility depends in any manner on the rating of the provider of the Initial Liquidity Facility, the short-term ratings on such subseries of Insured Bonds could be downgraded or withdrawn if the provider of the Initial Liquidity Facility were to be downgraded, placed on credit watch or have its ratings suspended or withdrawn or were to refuse to perform under the Initial Liquidity Facility.

The obligation of a Liquidity Facility Provider to purchase Insured Bonds of the applicable subseries under its Initial Liquidity Facility is subject to the conditions and limitations set forth therein. The Initial Liquidity Facility securing a subseries of Insured Bonds is not a guaranty to pay the purchase price of such

Insured Bonds tendered for purchase and is not a letter of credit. The Initial Liquidity Facility is a general contract, subject to certain conditions and limitations, including but not limited to disputes (whether valid or not) regarding the authority of either party to enter into or perform the Initial Liquidity Facility. More of such defenses are allowed by laws regarding contracts than by laws regarding letters of credit. A Liquidity Facility Provider may seek to have any future dispute resolved in court and appealed to final judgment before it performs under its Initial Liquidity Facility. Further, even if the Paying Agent were to prevail against a Liquidity Facility Provider, a court would not necessarily order such Liquidity Facility Provider to perform under its Initial Liquidity Facility; it could instead award damages for breach of contract. Any such award would not necessarily be in an amount sufficient to pay the purchase price of the Insured Bonds secured by such Initial Liquidity Facility. Purchasers of the Insured Bonds should consult their legal counsel for an explanation of the differences between a general contract and a letter of credit or guaranty.

#### *Available Commitment; Term*

Each Initial Liquidity Facility will have an initial available commitment equal to the aggregate principal amount of the subseries of Insured Bonds secured by such Initial Liquidity Facility (the "Principal Commitment") plus a notional amount of interest thereon (the "Interest Commitment") equal to approximately \$10,246 per \$1,000,000 of Principal Commitment. This amount is determined by assuming a rate of 11% per annum on the Principal Commitment for 34 days, calculated on the basis of a 365-day year and actual days elapsed (such method of calculating interest on any principal amount of Insured Bonds, the "Interest Coverage Amount"). The Interest Commitment of each Initial Liquidity Facility is greater than the amount of interest that will accrue on the Series 2005 Bonds secured thereby during the Initial Interest Period. The scheduled expiration date of each Initial Liquidity Facility is three, five, seven or ten years after the issuance date of the Series 2005 Bonds, as set forth on the Series Description for each subseries. Each Initial Liquidity Facility will support Insured Bonds of the applicable subseries during the Initial Interest Period and, thereafter, only during a Daily Rate Mode or a Weekly Rate Mode. The Paying Agent will be the beneficiary of each Initial Liquidity Facility. No person other than the Paying Agent shall be permitted to present drawings under any Initial Liquidity Facility. Each Initial Liquidity Facility may be transferred to a successor Paying Agent.

#### *Extent of Purchase Obligation*

So long as no termination event or suspension event (for a description thereof, see APPENDIX K – "SUMMARY OF CERTAIN PROVISIONS OF THE MASTER BANK AGREEMENT") has occurred (unless, in the case of a suspension event, the applicable Liquidity Facility Provider has provided a rescission notice to the Paying Agent), each Initial Liquidity Facility provides that the Liquidity Facility Provider thereof will purchase the Insured Bonds secured thereby by paying the Purchase Price thereof upon (1) an optional tender by the owner thereof and (2) a mandatory tender of such Insured Bonds (a) in connection with the conversion of the Interest Rate Mode with respect to the Insured Bonds, (b) in connection with the substitution of such Initial Liquidity Facility (if a mandatory tender is required under the Indenture), (c) in connection with the termination of such Initial Liquidity Facility, including a termination at the direction of the Administrative Agent following the occurrence of a Bond Insurer Approved Event of Default (for a description thereof, see APPENDIX K - "SUMMARY OF CERTAIN PROVISIONS OF THE MASTER BANK AGREEMENT") or (d) upon expiration of the Liquidity Facility or such later date or dates as such Liquidity Facility Provider shall specify from time to time in a written notice to the Paying Agent, in each case to the extent that there are no remarketing proceeds or insufficient remarketing proceeds to pay the Purchase Price thereof.

#### *Source of Payment*

Each Liquidity Facility Provider of an Initial Liquidity Facility agrees that it will pay from its own funds its pro rata share of all amounts advanced under such Initial Liquidity Facility to purchase Insured Bonds.

### *Initial Liquidity Facilities Issued by Multiple Banks*

The Initial Liquidity Facilities supporting the Series 2005G-5 Bonds, the Series 2005G-6 Bonds, the Series 2005G-11 Bonds and the Series 2005G-14 Bonds are to be issued by more than one Liquidity Facility Provider. Where an Initial Liquidity Facility is issued by more than one Liquidity Facility Provider, the obligations of each Liquidity Facility Provider thereof are several and not joint based upon the relative commitments of such Liquidity Facility Providers, which relative commitments are expressed as percentages in the Series Descriptions following the front cover of this Official Statement.

### *Liquidity Termination Event*

**An Initial Liquidity Facility will terminate automatically, without notice and without a mandatory purchase of the Insured Bonds secured thereby, upon the occurrence of a Liquidity Termination Event.** The following events each constitute a “Liquidity Termination Event” under each Initial Liquidity Facility:

(1) DWR shall fail to pay, or cause to be paid, when due, or shall have declared a moratorium on the payment of the principal of, interest on or Redemption Price of, or repudiated, any Insured Bonds secured by such Initial Liquidity Facility and such payment is not paid by the Bond Insurer whose bond insurance policy or financial guarantee secures such Insured Bonds when, as and in the amounts required to be paid pursuant to the terms of such bond insurance policy or financial guarantee that secures such Insured Bonds; or

(2) A “Bond Insurer Event of Insolvency” (described below) shall have occurred with respect to the Bond Insurer whose bond insurance policy or financial guarantee secures such Insured Bonds; or

(3) The financial strength or claims paying ability rating of the applicable Bond Insurer is lower than Baa3 (or its equivalent), in the case of Moody’s Investors Service, Inc., and BBB- (or its equivalent), in the case of Standard & Poor’s Ratings Service.

A “Bond Insurer Event of Insolvency” means, with respect to the applicable Bond Insurer, the occurrence and continuance of one or more of the following events: (a) the issuance, under the laws of the state of incorporation or formation of such Bond Insurer, of an order of relief, rehabilitation, reorganization, conservation, liquidation or dissolution of such Bond Insurer; (b) the commencement by such Bond Insurer of a voluntary case or other proceeding seeking an order for relief, rehabilitation, reorganization, conservation, liquidation or dissolution with respect to such Bond Insurer or its debts or claims under any bankruptcy, insolvency or other similar law now or hereafter in effect including, without limitation, the appointment of a trustee, receiver, liquidator, custodian, assignee, sequestrator or other similar official for such Bond Insurer or any substantial part of its property; (c) the commencement of an involuntary case or other proceeding seeking an order for relief, rehabilitation, reorganization, conservation, liquidation or dissolution with respect to such Bond Insurer or its debts or claims under any bankruptcy, insolvency or other similar law now or hereafter in effect, or seeking the appointment of a trustee, receiver, liquidator, custodian, assignee, sequestrator or other similar official for such Bond Insurer or any substantial part of its property, and such involuntary case or appointment remains undismissed and unstayed for a period of 60 days; (d) the consent of such Bond Insurer to any relief referred to in the preceding clause (c) in an involuntary case or other proceeding commenced against it; (e) the making by such Bond Insurer of a general assignment for the benefit of creditors; (f) the failure of such Bond Insurer to generally pay its debts as they become due or claims under any of its insurance policies as such claims are made; or (g) the board of directors or any senior officer of such Bond Insurer shall take any action to authorize any of the foregoing.

### *Liquidity Suspension Event*

**The obligation of a Liquidity Facility Provider of an Initial Liquidity Facility to purchase Insured Bonds of the subseries secured thereby will be suspended automatically, without notice and without a**

**mandatory purchase of such Insured Bonds, upon the occurrence of a Liquidity Suspension Event.** The following events each constitute a “Liquidity Suspension Event” under each Initial Liquidity Facility:

(1) Any provision of the bond insurance policy or financial guarantee that secures such Insured Bonds that relates to or would affect the timely payment of the principal of, interest on or Redemption Price of such Insured Bonds at any time for any reason ceases to be valid and binding on the Bond Insurer that issued such bond insurance policy or financial guarantee in accordance with the terms of such bond insurance policy or financial guarantee or is declared, announced or ruled to be null and void by a court or other governmental agency of appropriate jurisdiction; or

(2) The validity or enforceability of any provision of the bond insurance policy or financial guarantee that secures such Insured Bonds that relates to or would affect the timely payment of the principal of, interest on or Redemption Price of such Insured Bonds is contested publicly or in writing by a senior authorized officer of the Bond Insurer that issued such bond insurance policy or financial guarantee or any governmental agency or authority with appropriate jurisdiction; or a senior authorized officer of such Bond Insurer denies publicly or in writing that such Bond Insurer has any further liability or obligation to honor claims made or to be made under its bond insurance policy or financial guarantee; or

(3) The commencement of an involuntary case or other proceeding seeking an order for relief, rehabilitation, reorganization, conservation, liquidation or dissolution with respect to the Bond Insurer whose bond insurance policy or financial guarantee secures the Insured Bonds of a subseries that is also secured by such Initial Liquidity Facility or its debts or claims under any bankruptcy, insolvency or other similar law now or hereafter in effect, or seeking the appointment of a trustee, receiver, liquidator, custodian, assignee, sequestrator or other similar official for such Bond Insurer or any substantial part of its property.

Following the occurrence of a “Liquidity Suspension Event,” the obligation of a Liquidity Facility Provider to purchase Insured Bonds of the subseries secured by its Initial Liquidity Facility shall immediately be suspended and ultimately may either be reinstated or terminated. For a description of these circumstances, see APPENDIX K – “SUMMARY OF CERTAIN PROVISIONS OF THE MASTER BANK AGREEMENT.”

#### *Bond Insurer Approved Events of Default*

Each Bond Insurer whose bond insurance policy or financial guarantee secures the Insured Bonds of a subseries has agreed with the Liquidity Facility Provider whose Initial Liquidity Facility also secures such Insured Bonds that certain “Series Events of Default” or variations of certain “Series Events of Default” under the Master Bank Agreement constitute “Bond Insurer Approved Events of Default.” For a description thereof, see APPENDIX K – “SUMMARY OF CERTAIN PROVISIONS OF THE MASTER BANK AGREEMENT.”

Upon the occurrence and during the continuance of a Bond Insurer Approved Event of Default with respect to a subseries of Insured Bonds, the available commitment under the Initial Liquidity Facility securing such Insured Bonds may be terminated in accordance with the terms of the Master Bank Agreement by the Administrative Agent giving not less than 30 days prior written notice to such effect to DWR, the Trustee, the Co-Trustee, the applicable Remarketing Agent and the applicable Bond Insurer. If such a notice is given, the available commitment shall terminate at 5:00 P.M., New York City time, on the designated termination date and after such time the Liquidity Facility Provider thereof shall be under no further obligation to purchase any Insured Bonds secured by such Initial Liquidity Facility other than Insured Bonds for which the Liquidity Facility Provider has received a purchase notice satisfying the terms of such Initial Liquidity Facility prior to such termination date.

#### *Termination of Initial Liquidity Facility*

An Initial Liquidity Facility will expire and terminate upon the earliest to occur of the following (the date on which such expiration and termination occurs, the “Termination Date”): (1) 5:00 P.M., New York City time,

on the date that is three, five, seven or ten years after the issuance date of the Series 2005 Bonds, as set forth on the Series Description for each subseries, or if such day is not a business day, the next preceding business day, or such later date or dates as the Liquidity Facility Provider shall advise the Paying Agent by written notice (the "Scheduled Expiration Date"); (2) the surrender by the Paying Agent of the Initial Liquidity Facility to the Liquidity Facility Provider thereof, accompanied by a written statement from the Paying Agent certifying that all of the Insured Bonds secured by such Initial Liquidity Facility have been paid in full (or provision has been made for such payment in accordance with the Indenture) or are otherwise no longer entitled to the benefits of the Initial Liquidity Facility; (3) 5:00 P.M., New York City time, on the second business day next succeeding the date on which a Substitute Liquidity Facility or a Substitute Credit Facility is substituted for such Initial Liquidity Facility; (4) 5:00 P.M., New York City time, on the second business day next succeeding the earliest date on and as of which all of the Insured Bonds of the subseries secured by such Initial Liquidity Facility shall be converted to an Interest Rate Mode other than a Daily Rate Mode or a Weekly Rate Mode; (5) 5:00 P.M., New York City time, on the termination date set forth in a notice to the Paying Agent from the Administrative Agent to the effect that such Initial Liquidity Facility is to be terminated by reason of the occurrence and continuance of a Bond Insurer Approved Event of Default (such notice being the "Notice of Termination"), provided that such termination date shall not be less than 30 calendar days from the date the Notice of Termination is received by the Paying Agent; (6) immediately upon the occurrence of a Liquidity Termination Event; (7) (a) in the case of a Liquidity Suspension Event of the type described in paragraphs (1) and (2) above under the caption "SECURITY FOR THE BONDS – Initial Liquidity Facilities – *Liquidity Suspension Event*," if litigation is still pending and a final non-appealable judgment regarding the validity of the applicable bond insurance policy or financial guarantee has not been obtained, on the date which is three years after the effective date of suspension of the obligation of the Liquidity Facility Provider to purchase Insured Bonds secured by such Initial Liquidity Facility or (b) in the case of a Liquidity Suspension Event of the type described in paragraph (3) above under the caption "SECURITY FOR THE BONDS – Initial Liquidity Facilities – *Liquidity Suspension Event*," if the involuntary case, proceeding or appointment described in such paragraph has not been dismissed or stayed, the date which is 60 days after the commencement of such involuntary case, proceeding or appointment and (8) immediately following the payment by the Liquidity Facility of the amount requested by the Paying Agent in its final purchase certificate presented under such Initial Liquidity Facility. The Paying Agent may present a final purchase certificate prior to the occurrence of the Scheduled Expiration Date, in connection with the substitution of a Substitute Credit Facility or a Substitute Liquidity Facility for the Initial Liquidity Facility, in connection with the conversion of the Interest Rate Mode of the Insured Bonds secured by such Initial Liquidity Facility to an Auction Rate, a Term Rate or a Fixed Rate and in connection with the occurrence of a Bond Insurer Approved Event of Default.

### **Master Bank Agreement**

Each of the Initial Letters of Credit and Initial Liquidity Facilities are to be issued pursuant to the Master Credit, Liquidity and Participation Agreement, dated as of October 30, 2002, by and among DWR, JPMorgan Chase Bank, as Administrative Agent, Bayerische Landesbank, Dexia Crédit Local and The Bank of New York, as co-syndication agents, BNP Paribas, as documentation agent, and the other banks signatory thereto (the "Master Bank Agreement"). Certain provisions of the Master Bank Agreement are summarized in APPENDIX K – "SUMMARY OF CERTAIN PROVISIONS OF THE MASTER BANK AGREEMENT," but such summaries are qualified in their entirety by reference to the full text of the Master Bank Agreement. For information on obtaining a copy of the Master Bank Agreement, see "GENERAL INFORMATION." For information concerning the providers of the Initial Letters of Credit and the Initial Liquidity Facilities, see Appendix I.

Prospective investors should read Appendices I and K in their entirety for information necessary to make an informed investment decision.

### **Certain Rights of Letter of Credit and Liquidity Facility Providers**

This section summarizes certain provisions of the Indenture for the benefit of Credit Facility and Liquidity Facility providers.

So long as any Letter of Credit with respect to the Series 2005 Bonds is in full force and effect, and payment on such Letter of Credit is not in default and the issuer of such Letter of Credit is not in default thereunder, then, in all such events, the issuer of such Letter of Credit (acting through the Administrative Agent under the Master Bank Agreement described in Appendix K) shall be deemed to be the sole Owner of the Outstanding Bonds the payment of which such Letter of Credit secures or secured when the approval, consent or action of the Owners of such Bonds is required or may be exercised under the Indenture, except as provided by the provisions of the Indenture permitting modifications and amendments only with the consent of a particular Owner (see APPENDIX C – “SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE – Supplemental Indentures and Amendments”). With respect to such modifications and amendments, the consent of the issuer of the Letter of Credit shall be required in addition to the consent of such Owner.

In the event that the principal, sinking fund installments, if any, Purchase Price and Redemption Price, if applicable, or interest due on any Outstanding Series 2005 Bonds shall be paid from draws made under an Enhancement Facility (including Letters of Credit and Liquidity Facilities), all covenants, agreements and other obligations of DWR to the Owners of such Series 2005 Bonds shall continue to exist, and the issuer of such Enhancement Facility shall be subrogated to the rights of such Owners.

## CALIFORNIA DEPARTMENT OF WATER RESOURCES

### General

DWR is a department within the Resources Agency of the Executive Branch of the State. DWR was established in 1956 under California law for the purpose of planning and guiding the development of California's water resources. In addition to responsibility for the Power Supply Program, DWR is separately responsible for the planning, construction, operation and maintenance of the State Water Project, a statewide system of dams, reservoirs, pumping plants, power plants and aqueducts. DWR is the largest purchaser of power for its own use within California because of the power requirements of the State Water Project, and DWR was designated by Governor Davis to undertake the Power Supply Program because of DWR's experience in purchasing and selling power. The Power Supply Program is not part of the State Water Project, the revenues of the State Water Project are not available for the payment of the Bonds, and the Trust Estate pledged for the payment of the Bonds is not available for the payment of indebtedness incurred for the State Water Project.

The Director of Water Resources oversees DWR's activities, with the assistance of a Chief Deputy Director and four Deputy Directors. The Director and Chief Deputy Director are appointed by the Governor and report to the Governor through the Secretary of the Resources Agency. Biographical information for the DWR management officials currently responsible for the Power Supply Program is as follows.

*Lester A. Snow* has served as the Director of Water Resources since February 2004. Mr. Snow has more than 25 years of experience in public water resource management, including, but not limited to, serving as the Mid-Pacific Regional Director of the U.S. Bureau of Reclamation, the Executive Director of the CALFED Bay-Delta Program, the General Manager of the San Diego County Water Authority and the Tucson Area Director of the Arizona Department of Water Resources.

*Nancy J. Saracino* has served as Chief Counsel of DWR since August 2004. She oversees a staff of more than 20 attorneys working on DWR's varied and complex legal issues. Prior to her appointment as Chief Counsel she served as a Supervising Deputy Attorney General at the California Department of Justice from 2002 to 2004. She was a partner in a private law firm in Sacramento before joining the Attorney General's Office.

*Perla Netto-Brown* is the Chief Financial Officer of DWR. Prior to joining DWR, Ms. Netto-Brown was employed by the California Auditor General. She joined DWR in 1986, has served in various capacities in the Division of Fiscal Services and was named Chief of the Division of Fiscal Services in 2000.

*Peter Garris* is the Deputy Director of DWR responsible for the Power Supply Program. From October 1997 to January 2001, Mr. Garris served in senior management positions with the California Independent System Operator. Prior to 1997 he worked on power operations for DWR and several electric utilities. He rejoined DWR in January 2001.

*Viju Patel* is the Energy Advisor to the Deputy Director of the Power Supply Program. He develops, recommends and implements energy policy. Since joining DWR in 1982, Mr. Patel has served as a division chief and in other positions for the power operations of DWR's State Water Project. Prior to joining DWR in 1982, Mr. Patel worked for the California Energy Commission and a power company.

*James E. Olson* is the Chief, Financial Management Office, Power Supply Program. He was an audit partner with a national accounting firm prior to joining DWR as Deputy Controller in 1993 with responsibility for management of general accounting and financial reporting. He was assigned responsibility for the financial operations of the Power Supply Program in January 2001.

### **Proposed Reorganization**

Legislation has been introduced in the State Legislature that would reorganize State government, including the creation of a Department of Energy which would assume the role of DWR in the Power Supply Program. In such an event, the Department of Energy would assume all of the rights and responsibilities of DWR under the Act, the Regulations, and all contracts relating to the Power Supply Program, including the Bonds. The Act states that while any obligations of DWR incurred under the Act remain outstanding and are not fully performed or discharged, the rights, powers, duties, and existence of DWR and the CPUC shall not be diminished or impaired in any manner that will affect adversely the interests and rights of the holders of or parties to such obligations. See, however, "RISK FACTORS - Uncertainties Relating to Government Action."

### **CALIFORNIA PUBLIC UTILITIES COMMISSION**

The CPUC is the principal ratemaking authority for the IOUs' retail rates. Under the Rate Agreement, the CPUC has agreed to impose Bond Charges sufficient to provide moneys sufficient to pay all Bond Related Costs when due, and to impose Power Charges sufficient to satisfy DWR's "Retail Revenue Requirements" (defined in the Rate Agreement attached as Appendix D) as specified by DWR. Pursuant to the Act, the CPUC also issues orders approving Servicing Arrangements or otherwise directing the IOUs to provide operational, transmission, distribution, billing, collection and other services to DWR in connection with the Power Supply Program.

The CPUC consists of five members appointed by the Governor and confirmed by the Senate. Members serve for six-year, staggered terms. The Governor appoints one of the five to serve as President. The CPUC is an independent regulatory agency. It regulates the IOUs and other California entities, mostly investor-owned electric, telecommunications, natural gas, water, railroad and passenger transportation companies. Some of the entities regulated by the CPUC are not investor-owned. The CPUC's headquarters are in San Francisco.

Since January 1, 2001, the CPUC has adopted a number of decisions that relate to DWR's Power Supply Program. Additional CPUC decisions relating to the Power Supply Program and the Bonds are expected by DWR. See "CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES."

The CPUC makes no representation as to the accuracy or completeness of this Official Statement, including any forward-looking statements or projections contained in this Official Statement and any description in this Official Statement of litigation involving or affecting the CPUC. Any statements regarding such litigation do not necessarily represent the CPUC's view of such litigation or any position in such litigation. In addition, while CPUC staff may have assisted in the preparation of certain sections of this Official Statement, the CPUC can only take positions through formal action and has not taken any such action or approved this Official Statement. The CPUC is an independent five member body that must act by an affirmative vote of a majority of its members and, as a result, the CPUC can only indicate its views in formal decisions or other formal actions. In

addition, the CPUC is an independent body not subject to the control of DWR and may take positions in the future different from DWR in litigation, or other matters described in this Official Statement. As a result, statements in this Official Statement regarding electricity markets and regulation, and DWR's views of the CPUC's role or DWR's role in such markets and regulation, do not necessarily represent the views, opinions or beliefs of the CPUC and should not be construed as such by any recipient of this Official Statement.

## **THE DWR POWER SUPPLY PROGRAM**

### **Background and History**

#### *Summary of the Power Supply Program*

Under the Power Supply Program, DWR purchases power from wholesale suppliers under long-term contracts, and sells electricity to retail customers that are also served by the IOUs. DWR electricity is delivered to retail customers through the transmission and distribution systems of the IOUs. DWR's costs are recovered through Bond Charges and Power Charges imposed on retail customers. Payments from customers are collected by the IOUs pursuant to Servicing Arrangements approved or ordered by the CPUC.

#### *Electricity Service in California*

Prior to the inception of the DWR Power Supply Program, Californians generally received their electricity service from one of three types of providers: IOUs, local publicly owned electric utilities, and electric service providers.

IOUs have a defined geographic service area and are required by law to serve customers in that area. The CPUC regulates the IOUs' rates and how electricity service is provided to their customers.

Publicly owned electric utilities are public entities that provide electric service to residents and businesses in their local area. Unlike IOUs, they are not regulated by the CPUC. Major publicly owned electric utilities include the Los Angeles Department of Water and Power, the Sacramento Municipal Utility District, and the Imperial Irrigation District.

The electric service providers provide retail electricity service to customers who have chosen not to receive electricity service from the utility that serves their area. Instead, these customers have entered into "direct access" contracts with electric service providers for their electricity. This electricity is delivered to these electric service provider customers through the transmission and distribution system of their local utility. There are currently eighteen registered electric service providers operating in the State, generally serving large industrial and commercial businesses. The electric service providers also provide electricity to certain State and local government entities, such as the California State University system, several University of California campuses, some community college districts, and some local school districts.

Since the inception of the Power Supply Program, IOU customers have purchased a portion of their electricity from the IOUs and the remainder from DWR. Currently, the IOUs and DWR provide approximately 71 percent of the electricity in the State; publicly owned electric utilities provide 14 percent; and electric service providers provide 11 percent. The remaining four percent is used primarily for the State Water Project, which is operated by DWR as a separate enterprise.

#### *Deregulation and Direct Access*

California began the process of restructuring electricity service in the early 1990s by introducing competition into the generation of electricity, with the ultimate goal being lower prices for IOU customers. The deregulation legislation ultimately enacted in 1996 ("AB 1890") included a "transition" period during which the IOUs were to sell off their fossil fuel power plants to independent generators while retaining their hydroelectric

and nuclear power plants. Eventually, however, electricity purchases and customer rates were to be determined in a competitive market. In such a market, customers could choose to have the IOUs purchase the electricity on their behalf, or they could purchase electric power directly from electric service providers through direct access. During the transition period, however, the retail rates of the IOUs were to be frozen until certain conditions had been satisfied, including the recovery by the IOUs of certain “stranded” costs of uneconomic generating facilities that would not be otherwise recoverable in a competitive market. The deregulation process was suspended in response to the energy crisis that arose in 2000 and early 2001.

### *The California Energy Crisis*

By the summer of 2000, wholesale power sellers were not making sufficient power supplies available in the wholesale spot market, and spot market prices began to rise, swiftly and dramatically. At the same time, PG&E and SCE remained in the AB 1890 transition period, with frozen retail rates. The cost of procuring power in the spot market quickly surpassed the frozen retail rates. By December 2000, PG&E and SCE had incurred several billion dollars of losses, adversely affecting their creditworthiness and ultimately causing defaults in payments for power purchases in the spot markets and from other suppliers. PG&E’s and SCE’s credit deterioration had a spiraling effect, deterring power suppliers from bidding supplies into the California market, exacerbating the shortage of electric power, and causing wholesale prices to escalate further. In the SDG&E service area, retail rates had been unfrozen by the time wholesale spot market prices began escalating in 2000. SDG&E’s retail rates escalated sharply with wholesale prices, causing the State Legislature to enact a statutory cap on retail rates in the San Diego area.

### *The State’s Response to the Energy Crisis: the DWR Power Supply Program*

Recognizing an immediate need for a creditworthy party to assume the obligation of purchasing electricity for customers of the IOUs, Governor Gray Davis proclaimed a state of emergency on January 17, 2001 and authorized DWR to begin purchasing the electricity that the IOUs could not provide (such portion being referred to herein as the “net short”). Thereafter, the State Legislature passed, and Governor Davis signed, Assembly Bill 1 (“AB 1X”). AB 1X authorized DWR to undertake a program of purchasing the net short for customers of the IOUs, incurring debt to finance such purchases, implementing a mechanism to recover the costs thereof from the ratepayers of the IOUs, and related actions. Such program is referred to herein as the “Power Supply Program.”

At the height of the emergency in 2001, DWR began purchasing substantial amounts of power in daily and even hourly transactions on the spot market, and under other short-term contracts. In addition, DWR solicited proposals for, negotiated and entered into long-term power contracts, which had the effect of reducing the amount of power DWR purchased on the spot market. From January 2001 through December 2002, DWR procured the entire net short for the three IOUs from power delivered under its long-term power purchase contracts and from wholesale spot market and other short-term transactions. The Act does not authorize DWR to enter into new power contracts after December 31, 2002. As a result, DWR ceased procuring the portion of the net short not provided by the long-term power purchase contracts in effect as of such date (such portion being referred to herein as the “residual net short”), and each of the IOUs resumed procuring the residual net short for its respective bundled customers. As DWR’s existing long-term contracts expire or are otherwise terminated, the IOUs are responsible for procuring replacement power until such time as the entire load of bundled customers is provided by the IOUs. While these developments have reduced DWR’s Retail Revenue Requirements, it had no direct effect on Bond Charges. Irrespective of whether DWR continues to purchase or sell electricity under the Power Supply Program, the Rate Agreement obligates the CPUC to continue to impose Bond Charges in an amount sufficient to pay Bond Related Costs when due. See “SECURITY FOR THE BONDS – Rate Covenants.”

Also effective January 1, 2003, each of the IOUs assumed operational (but not financial) responsibility for a portion of DWR’s portfolio of long-term power contracts. Accordingly, each IOU is now responsible for scheduling the electricity produced or delivered under the contracts allocated to it by the CPUC. In addition, electric power dispatched under each contract is deemed to be utilized in the service area of the IOU to which

such contract is allocated, and the cost thereof is generally to be borne by customers in such service area. Although the IOUs have assumed operational responsibility, DWR remains financially responsible for the payment obligations under such contracts.

In response to the energy crisis, the State also halted several aspects of deregulation. Among these, the State prevented the IOUs from continuing to sell their power plants and suspended new direct access for IOU customers. Under existing law, this suspension will continue until DWR's long-term electricity contracts expire. The last of the contracts is expected to expire in 2017.

### **Statutory Authority**

AB 1X was codified as Division 27 of the California Water Code (commencing with Section 80000), and is also referred to herein as the "Act." The Act established a framework under which DWR would purchase the net short and would recover the costs of the Power Supply Program. The Act authorized DWR to contract for power under such terms and conditions as it deemed appropriate, taking into account a number of factors, including a desire to secure as much low-cost power as possible under contract. Although the Act only authorized DWR to enter into new power contracts until December 31, 2002, the Act permits DWR to continue administering its contract portfolio after that date. Under the Act, power acquired by DWR is sold directly to customers in the service areas of the IOUs, and payment for such power is a direct obligation of the customers. The Act provides that DWR is entitled to recover its costs, including power purchase costs and debt service on the Bonds (referred to herein as DWR's "revenue requirements"), in the amounts and at the times necessary to satisfy its contractual obligations, and is to advise the CPUC of its revenue requirements so that its revenue requirements can be recovered through charges imposed upon customers by the CPUC. The Act also authorized the CPUC and DWR to enter into agreements with respect to such charges. The Act authorizes DWR to contract with the IOUs for the transmission and distribution of its power, and for billing, collection and related services, all as agents of DWR. The Act also directs the CPUC, at the request of DWR, to order the IOUs to provide such services. The Act provides for the suspension of the right of customers to purchase their power from energy providers other than the IOUs and DWR, so long as DWR continues to provide power. See "THE DWR POWER SUPPLY PROGRAM – Direct Access, Departing Load and Community Choice Aggregation."

The Act also authorized DWR to issue up to \$13.423 billion principal amount of bonds to provide permanent financing for costs incurred in connection with the Power Supply Program (excluding bond anticipation notes and refunding bonds issued to achieve interest rate savings). The Series 2002 Bonds were issued pursuant to this authorization. The Series 2005 Bonds are authorized by the Act, but as refunding bonds, the Series 2005 Bonds are not subject to the principal amount limitation in the Act.

No action or approval by the Federal Energy Regulatory Commission ("FERC") or any other federal agency is required for the issuance of the Bonds or the calculation, revision, imposition or collection of Bond Charges or Power Charges.

### **Power Purchase Contracts**

#### *General*

Since December 31, 2002, DWR's power purchase activities under the Power Supply Program have been limited to purchasing power from wholesale suppliers under the 32 long-term power purchase contracts then in effect. As a result, the current operating expenses of the Power Supply Program are primarily power purchase costs under such long-term contracts, including associated fuel procurement costs. As described in "THE DWR POWER SUPPLY PROGRAM – History," responsibility for managing the remaining power purchase contracts has been largely transferred to the IOUs, although DWR continues to perform certain administrative activities with respect to the contracts, and remains financially responsible for payments under the contracts. In addition, DWR has a continuing role in the procurement and risk management of fuel requirements for the contracts. The

IOUs also advise on fuel procurement, but DWR maintains financial and ultimate operational responsibility for this function.

DWR has renegotiated 19 of the original contracts that were entered into in 2001 and that will remain in effect in 2006 or beyond. DWR has terminated five additional contracts for cause. DWR continues to monitor its contracts and determine if there are opportunities for bilateral renegotiation, which could lead to more favorable power supply terms and costs. DWR has the right to terminate one or more of its remaining contracts, but the contracts each provide that if the contract is terminated for reasons other than breach or default by the power-supplying counterparty to the contract, DWR would be obligated to pay generally the mark-to-market value of the contract, typically within 180 days of termination. Any such termination other than for an uncured default or breach by the seller would likely increase the revenue requirement due to timing of termination payments to the counterparty. In addition, energy no longer supplied by DWR would need to be replaced by the IOUs in either the short-term market or under new long-term power contracts from other suppliers. For this reason, under present market conditions and terms of the contracts, DWR does not believe that termination of any of the contracts would result in a net savings in the revenue requirement or overall ratepayer costs. A summary of the long-term power purchase contracts that will remain in effect for at least a portion of 2006 is set forth below.

For a discussion of additional credit implications of DWR's power contracts, see "SECURITY FOR THE BONDS – Priority Long-Term Power Contracts" and "RISK FACTORS – Determination of Power Charges and Bond Charges; Possible Use of Amounts in the Bond Charge Collection Account to Pay Priority Contract Costs."

#### *Priority Long-Term Power Contracts*

Priority Long Term Power Contracts are power purchase contracts that provide, in effect, that payments by DWR under the contracts are to be paid or are payable prior to bonds, notes, or other indebtedness of DWR secured by a pledge or assignment of the revenues of DWR under the Act and other amounts in the Electric Power Fund. Substantially all of DWR's power purchases, both in terms of energy and cost, will be made under the Priority Long-Term Power Contracts and for that reason substantially all of the operating expenses of the Power Supply Program will be incurred under the Priority Long-Term Power Contracts. The long-term power contracts in effect as of October 6, 2005 are summarized in the table below.

Certain of DWR's contracts for the supply of natural gas have similar payment priority provisions, and are considered "Priority Long-Term Power Contracts," as described below under the caption "THE DWR POWER SUPPLY PROGRAM – Natural Gas Supply."

#### *Description of DWR's Power Contracts*

The following table sets forth the name of the counterparty under each of DWR's power contracts, the product type, the origin of the power, whether it provides for fuel tolling, whether it is a Priority Long-Term Power Contract, the IOU to which it is allocated for operational and rate-setting purposes, and the projected annual amount of energy to be derived under such contract until it expires. The projected annual energy deliveries are estimates only and are based on production simulation analyses performed by or on behalf of DWR for purposes of planning future revenue requirements. The projected annual energy delivery estimates, particularly for dispatchable contracts, may vary significantly from actual future deliveries, depending on future events including, but not limited to, the amount and cost of IOU-contracted or -provided power available, and the bundled load requirement of each IOU, in a specific period.

Approximate Annual Energy (MWh) <sup>(1)</sup>

Counterparty, Product Type <sup>(2)</sup> , and Origin of Power <sup>(3)</sup>	Fuel Tolling <sup>(4)</sup>	Priority <sup>(5)</sup>	IOU Allocation	Approximate Annual Energy (MWh) <sup>(1)</sup>						
				2005	2006	2007	2008	2009	2010	2011
Calpeak; Dispatchable; Generator-specific; Gas-fired	Yes	Yes	PG&E/ SDG&E	368,680	67,259	84,816	143,080	218,518	247,622	350,882
Calpine 1; Must-take; Market	No	Yes	PG&E	8,761,300	8,761,303	8,760,001	8,762,654	8,761,303	-	-
Calpine 2; Must-take; Market	No	Yes	PG&E	8,761,300	8,761,303	8,760,001	8,762,654	8,761,303	-	-
Calpine 3; Dispatchable; Generator-specific; Gas-fired	Yes	Yes	PG&E	38,340	4,384	22,917	74,468	146,087	205,799	13,597
Calpine 4; Dispatchable; Generator-specific; Gas-fired	Yes	Yes	PG&E	347,520	20,299	-	-	-	-	-
Clearwood <sup>(6)</sup> ; Must-take; Generator-specific; Geothermal	No	No	PG&E	-	-	154,080	262,575	262,575	262,575	262,575
Colton; Dispatchable; Generator-specific; Gas-fired	Yes	Yes	SCE	1,060	-	-	-	1,140	5,887	-
Coral; Must-take; Market	Yes	Yes	PG&E	3,956,560	3,956,572	3,956,572	3,956,572	3,956,572	3,261,741	2,650,836
El Paso; Must-take; Market	No	Yes	PG&E/ SCE	486,420	-	-	-	-	-	-
Goldman Sachs; Must-take; Market	No	Yes	SCE	6,571,000	7,007,200	7,006,183	7,008,030	7,007,278	7,007,278	7,006,193
GWF <sup>(6)</sup> ; Dispatchable; Generator-specific; Gas-fired	Yes	Yes	PG&E	20,590	3,271	10,196	43,633	80,475	106,935	140,254
High Desert; Dispatchable; Generator-specific; Gas-fired	Yes	Yes	SCE	4,138,640	4,147,301	4,305,017	4,183,118	4,643,578	4,696,199	1,308,957
KRCD <sup>(7)</sup> ; Dispatchable; Generator-specific; Gas-fired	Yes	No	PG&E	-	-	-	-	-	-	-
Morgan Stanley; Must-take; Market	No	Yes	SDG&E	306,120	-	-	-	-	-	-
PacifiCorp; Dispatchable; Market	Yes	Yes	PG&E	1,128,930	1,423,233	1,373,692	1,097,927	1,128,236	1,134,030	286,544

Counterparty, Product Type <sup>(2)</sup> ; and Origin of Power <sup>(3)</sup>	Fuel Tolling <sup>(4)</sup>	Priority <sup>(5)</sup>	IOU Allocation	Approximate Annual Energy (MWh) <sup>(1)</sup>						
				2005	2006	2007	2008	2009	2010	2011
PG&E Energy Trading-Wind; As-Available; Generator-specific; Wind	No	Yes	SCE	144,810	144,803	144,803	144,803	144,803	144,803	108,305
Sempra; Must-take; Combination of Market and Generator-Specific	Yes	Yes	SCE	12,754,290	12,754,286	12,754,286	12,514,286	12,514,286	12,514,286	9,360,000
SF Peakers <sup>(8)</sup> ; Dispatchable; Generator-specific; Gas-fired	Yes	No	PG&E	-	-	64,267	72,310	79,232	87,433	86,882
Soledad-renewable; Must-take; Generator-specific; Biomass	No	No	PG&E	113,870	94,848	-	-	-	-	-
Sunrise; Dispatchable; Generator-specific; Gas-fired	Yes	Yes	SDG&E	3,101,230	3,217,082	3,416,554	3,223,750	3,603,693	3,705,076	3,870,130
Wellhead; Dispatchable; Generator-specific; Gas-fired	Yes	Yes	PG&E	3,140	1,644	3,609	10,974	20,097	27,552	33,822
Whitewater-wind <sup>(9)</sup> ; As-Available; Generator-specific; Wind	No	Yes	SDG&E	283,690	283,714	283,714	283,714	283,714	283,714	283,714
Williams ABC; Must-take; Market	No	Yes	SDG&E	4,254,830	4,254,857	4,254,857	1,626,857	1,626,857	1,626,857	-
Williams D; Dispatchable; Generator-specific; Gas-fired	Yes	Yes	SDG&E	<u>1,091,350</u>	<u>790,045</u>	<u>852,208</u>	<u>832,633</u>	<u>1,125,019</u>	<u>1,323,903</u>	-
<b>Total</b>				<u>56,633,670</u>	<u>55,693,401</u>	<u>56,207,770</u>	<u>53,004,035</u>	<u>54,364,764</u>	<u>36,641,688</u>	<u>25,762,690</u>

(1) Projections provided by Navigant Consulting, Inc. and have been developed in support of DWR's Revised 2006 Determination of its revenue requirements.

(2) Product types are described as "must-take," "dispatchable" and "as available." "Must-take" refers to the contract requirement that all energy generation associated with the contract is required to be purchased by DWR. "Dispatchable" refers to the contractual right to purchase only that amount of energy that DWR – or the IOUs operating on behalf of DWR – requests, up to full generation under the available capacity of the contract. "As available" means DWR is required to purchase any energy generated from a specific project, as available.

(3) Origin of power is described as "generator-specific" or "market." "Generator-specific" means the contract power is derived from a specific generator. For such contracts, the type of generation facility is also indicated. "Market" means the power is derived from market purchases.

(4) "Fuel Tolling" means a contract provision tying the contract price to natural gas prices. Under a contract with such a provision, fuel is provided by DWR or by the seller.

(5) "Priority" means the contract is a Priority Long-Term Power Contract. See "THE DWR POWER SUPPLY PROGRAM – Power Purchase Contracts – Priority Long-Term Power Contracts."

(6) Contract runs through 2012.

(7) Contract runs through 2014.

(8) Contract projected to run through 2017.

(9) Contract runs through 2013.

Source: DWR's 2006 revenue requirement.

### *Dispute with Power Supplier*

In May 2002, DWR notified Sempra Energy Resources (“Sempra”) in writing that Sempra had failed to perform its obligations under the contract, including the obligation to build new power plants to help meet the State’s long-term energy needs. In *Sempra Energy Resources v. Department of Water Resources*, filed in May 2002 in San Diego County Superior Court (Case No. 789291), Sempra sought declaratory relief as to the respective rights and duties of plaintiff and DWR under the long-term power contract between the parties. In July 2002, DWR cross-complained, alleging that Sempra failed to perform its obligations under the contract to build new power plants and to expedite permitting and construction of the Elk Hills project. DWR sought damages and either a declaration that the contract is not binding on DWR or that, if the contract is binding on DWR, a declaration that Sempra must build the projects as promised unless commercially unreasonable and an injunction prohibiting Sempra from freely substituting market energy for energy from new sources of generating capacity. Sempra’s motion for summary judgment was granted by the court on May 19, 2003. DWR appealed the entry of judgment against it. On June 21, 2005, the court of appeal reversed the judgment of the superior court and held that the contract required Sempra to utilize commercially reasonable efforts to build new power plants. The case has been remanded to superior court for resolution of remaining issues.

On a separate matter relating to the Sempra contract, DWR filed a demand for arbitration with the American Arbitration Association in February 2004, asserting that Sempra had breached the contract. DWR is currently asserting the following claims: (1) that Sempra failed to follow the annual and monthly energy delivery plans as stipulated in the contract; (2) that Sempra failed to provide adequate fuel supply plans as required by the contract; (3) that Sempra failed to provide 7 x 24 energy as required by the contract, (4) that Sempra’s delivery of power to locations that were not allowed for in the contract constituted a breach of the contract, (5) that Sempra failed to take steps to prevent or alleviate transmission curtailments or interruption, and (6) that Sempra has overcharged DWR. In March 2004, Sempra filed a complaint in the Los Angeles County Superior Court for declaratory and injunctive relief arguing that DWR is barred under the California Code of Civil Procedure from asserting the claims listed above because DWR failed to assert the matters above in a previous cross-complaint against Sempra. The Los Angeles Superior court denied Sempra’s motion for a preliminary injunction and granted DWR’s motion to compel arbitration. Sempra filed a petition in the Court of Appeal challenging the ruling, which was denied in June 2004. The arbitration hearing began on November 9, 2005, but no decision has been rendered. During this dispute, DWR has continued to perform under the contract and the contract costs are included in DWR’s revenue requirement.

## **Natural Gas Supply**

### *General*

A major component of the cost of procuring power is the cost of procuring and transporting natural gas, the fuel used to produce most of that power. During the 2006 revenue requirement period, natural gas costs are projected to account for approximately 39 percent of total contract costs. During that period, gas-fired generation is projected to account for approximately 15 percent of total contract generation and approximately 94 percent of generation from contracts that are not fixed-price, must-take contracts. “Tolling” provisions in some of DWR’s power purchase contracts give DWR the right, but not the obligation, to provide all or part of the natural gas required to generate electricity pursuant to the contract. In every instance where tolling is an option, DWR has elected to provide fuel on recommendation of the IOUs that manage the procurement of fuel for and dispatch of energy from specific contracts. See “THE DWR POWER SUPPLY PROGRAM – Power Purchase Contracts,” above, for a listing of agreements that provide for fuel tolling.

With the assistance of its consultants, DWR forecasts its natural gas costs using production simulation analyses to project contract fuel requirement volumes and natural gas prices that are fixed either through physical hedges (i.e. fixed price gas contracts) or through financial hedges or, for those volumes not covered by such hedges, using a combination of near-term natural gas price future market quotes, computer modeling and certain discretionary adjustments (as described in “CALCULATION AND IMPOSITION OF BOND CHARGES AND

POWER CHARGES – Substantive Considerations in Establishing Revenue Requirements – *Natural Gas Price and Cost Projections*”) in determining its annual Retail Revenue Requirement. If DWR’s actual natural gas costs are not within the forecast during the revenue requirement period, an adjustment to Power Charges could be required during the course of the revenue requirement period. DWR submitted Supplemental Revenue Requirement Determinations for 2003 and 2004 and a Revised Revenue Requirement Determination for 2006 based, in part, on revised natural gas cost projections. Any necessary revisions, to date, in Power Charges resulting from Supplemental or Revised Revenue Requirements have been implemented by the CPUC within the time frame required by the Rate Agreement and have not, to date, resulted in a revenue shortfall that would cause the Operating Account to fall below the Minimum Operating Expense Available Balance. See “SECURITY FOR THE BONDS – Operating Account.” The IOUs, which provide much of the operational oversight of fuel tolling, have hedged natural gas costs for a substantial portion of DWR’s natural gas needs in 2006. Such hedging is taken into consideration when formulating DWR’s Retail Revenue Requirements. See “CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES.” A portion of the gas supply, after physical or financial hedging, remains subject to future price variation. DWR estimates the reasonable potential range of that price variation and establishes its revenue requirements to maintain projected Operating Account and Operating Reserve Account balances to provide amounts sufficient to accommodate that range of potential price variance. If necessary to maintain the necessary or appropriate account balances, DWR would revise or supplement its revenue requirement and submit it to the CPUC for processing.

#### *Principal Natural Gas Contracts*

DWR’s principal natural gas contracts are described in the table below. Each is a “Priority Long-Term Power Contract” and provides, in effect, that payments by DWR under the contracts are to be paid or are payable prior to bonds, notes, or other indebtedness of DWR secured by a pledge or assignment of the revenues of DWR under the Act and other amounts in the Electric Power Fund.

Counterparty	Date Executed	End of Term	Approximate Annual Volume (MMBtu)						
			2005	2006	2007	2008	2009	2010	2011
Williams Energy Marketing & Trading	2002	2010	18.0	18.0	18.0	18.0	18.0	18.0	--
Occidental Energy Marketing Inc.	2005	2006	--	36.5	--	--	--	--	--

#### *Physical and Financial Management of Natural Gas*

CPUC-approved operating agreements (in the case of SCE and SDG&E) and a CPUC order (in the case of PG&E) define the respective responsibilities of DWR and each IOU as they relate to managing the tolling provisions of DWR’s power purchase agreements. In particular, the IOUs, as agent for DWR, (1) assume operational responsibilities for scheduling energy with the California Independent System Operator (“CAISO”) based on economic considerations including natural gas prices, spot energy prices and heat rate efficiency of generating units associated with the tolling agreements, (2) manage daily physical gas purchases for delivery to tolling agreements including: scheduling, transporting, imbalance management, storing and selling gas, as the case may be, and (3) manage natural gas price risk and volatility by physically and financially hedging natural gas needs. DWR supports and monitors the IOUs as they manage and settle the physical fuel requirements and price risk hedging for any tolling agreements while remaining legally and financially responsible for the fuel obligations under each of DWR’s power purchase contracts. To the extent the IOUs do not procure gas or fail to manage gas price risk by hedging, DWR retains the right and responsibility to assure that gas is supplied to meet the performance requirements of the contracts.

### *Current Fuel Hedging*

Based on information from and in coordination with the IOUs, DWR hedges a portion of the price risk associated with projected gas purchases that will be made to operate DWR's power purchase contracts. The primary purpose of such hedging is to reduce the gas price volatility under conditions in which the natural gas price rises (perhaps significantly) above the baseline projected market gas price identified in a specific revenue requirement determination. For the 2006 revenue requirement period, DWR estimates that the IOUs have collectively secured, or have reasonably firm plans to secure, on behalf of DWR hedges for 109 million MMBtu at or about the baseline projected gas price identified in the revised 2006 revenue requirement determination using a mix of option and fixed price instruments. In addition, 18 million MMBtu are effectively hedged at a price of \$4.00 per MMBtu through deliveries from a fuel procurement agreement with Williams Gas. The remaining unhedged exposure for such revenue requirement period is approximately 82 million MMBtu, or 39 percent of total projected fuel requirements in 2006. At baseline projected natural gas prices, this unhedged portion of fuel requirements would cost approximately \$772 million in 2006, or 14 percent of the total revenue requirement of \$5.36 billion.

### **Customer Base**

DWR supplies power to bundled customers in the same service areas served by the three IOUs, comprising approximately 11 million residential, commercial and industrial accounts representing approximately three-quarters of all Californians.

PG&E is a wholly owned subsidiary of PG&E Corporation and is headquartered in San Francisco, California. PG&E is the largest investor-owned utility in the nation, providing natural gas and electric service to approximately 5.0 million accounts. Its service area covers approximately 70,000 square miles in northern and central California.

SCE is a wholly owned subsidiary of Edison International and is headquartered in Rosemead, California. SCE provides electric service to approximately 4.6 million accounts. Its service area is approximately 50,000 square miles in central and southern California.

SDG&E is a wholly owned subsidiary of Sempra Energy and is headquartered in San Diego, California. SDG&E provides natural gas and electric service to approximately 1.3 million accounts. Its service area covers approximately 4,100 square miles in southern California, including San Diego County and southern Orange County.

In 2004, DWR supplied approximately 51 billion kWh of energy to customers in the IOU service areas and received approximately \$4.5 billion in Power Charge Revenues and approximately \$830 million in Bond Charge Revenues. The table below sets forth certain statistics relating to power supplied by DWR to and Bond Charges collected from the service areas of the IOUs. Note that in 2001 and 2002, energy delivered by DWR included both long-term contract power and short-term purchases to supply the residual net short.

<b>Service Area Statistic</b>	<b>IOU Service Area</b>			<b>DWR Total</b>
	<b>PG&amp;E</b>	<b>SCE</b>	<b>SDG&amp;E</b>	
DWR Power Supplied, March 2001 – June 2005 (% of IOU Load)	30%	25%	43%	--
DWR Power Supplied, Max. Month (% of IOU Load)	May 2001 (50%)	Feb. 2001 (40%)	May 2001 (58%)	--
DWR Power Supplied, Max. Month (GWh)	May 2001 (3,606)	May 2001 (2,368)	Aug. 2003 (786)	--
Bond Charges, December 2002 – June 2005 (In Dollars)	\$887,000,000	\$888,000,000	\$196,000,000	\$1,971,000,000
Bond Charges, December 2002 – June 2005 (as a Percentage)	45%	45%	10%	100%

## Collection of Revenues

### *General*

Because DWR does not have the personnel, equipment or customer information necessary to provide its own metering, billing and collection services, servicing arrangements obligating the IOUs to provide such services on behalf of DWR are necessary for the timely collection of Bond Charges and Power Charges. Under the Act, the CPUC is required, upon request of DWR, to order the IOUs to provide such services on terms and conditions that reasonably compensate the IOUs for such services. The CPUC has adopted orders and approved agreements with respect to each IOU providing for the terms and conditions upon which such services are to be provided (each such order, a “Servicing Arrangement”). On December 19, 2002, the CPUC adopted the currently effective servicing orders applicable to each IOU. These servicing orders amend and restate the then existing servicing agreements, as amended and supplemented, as applicable to SCE and SDG&E and the servicing order applicable to PG&E.

DWR has covenanted in the Indenture that it will maintain servicing arrangements in effect at all times while Bonds are outstanding. In addition, DWR has covenanted in the Indenture not to voluntarily consent to or permit any amendment of any servicing arrangement unless DWR determines that the amendment will not have a material adverse affect on the ability of DWR to comply with the provisions of the Indenture. See APPENDIX C – “SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE – Servicing Arrangements; Collection of Revenues” and “RISK FACTORS – Collection of Bond Charges and Power Charges.”

### *Summary of Servicing Arrangements*

Each IOU is bound by its Servicing Arrangement to transmit (or provide for the transmission of) and distribute power supplied by DWR in accordance with the Servicing Arrangement, the Act, other applicable laws, CPUC rules and regulations and agreements between the IOU and DWR. The Servicing Arrangements do not obligate the IOUs to construct high voltage transmission improvements.

Each of the IOUs is to provide metering services, meter reading services, billing services, and collection services for DWR. Each IOU is to follow its customary standards, policies and procedures in performing these services, which are regulated by the CPUC. DWR charges are included in the IOUs’ regular billing statements. The IOUs will not permit customers to direct how partial payments of balances due on consolidated bills will be applied; each IOU will allocate partial payments from customers based upon the same proportion that DWR’s charges bear to total charges on the consolidated bills. Each IOU will collect DWR’s charges and its own charges from customers using its own collection practices and disconnection policies (all of which are subject to CPUC regulation). Risk of nonpayment is borne by the IOUs and DWR proportionately. DWR does not consider nonpayment by customers to be a material risk to Bondholders because historical levels of uncollectible charges have averaged approximately 0.3% of annual IOU operating revenues over the last five years, and have been and will be accounted for in the calculation of DWR’s revenue requirements.

The IOUs remit amounts collected for Bond Charges and Power Charges to DWR on a daily basis accompanied by reports and data to support the remittances. Currently, SCE and SDG&E remit on an actual collection basis. PG&E continues to remit revenues to DWR for each day on an estimated basis, and reconciles the estimated remittances and the actual amounts approximately six months later. Reconciliations may result in refunds to the IOUs of overpaid amounts or in additional remittances to DWR in the event of under-remittances. In addition, beginning in January 2003, the IOUs have made monthly remittances of surplus energy sales-related revenues, all as further provided in the Servicing Orders.

Under the Servicing Arrangements, the IOUs are entitled to recover the reasonable costs of providing the IOU Services. DWR pays each IOU for the incremental costs of metering, meter reading, billing, collection and other IOU Services. All of the foregoing costs are included by DWR in its revenue requirement submissions to the CPUC and recovery is sought from customers through DWR charges. Delinquent payments by DWR bear

interest at a variable interest rate equal to three percent plus the prime lending rate of a commercial bank named in each Servicing Arrangement.

Each Servicing Arrangement provides that all amounts required to be remitted to DWR by the IOU shall be held by the IOU in trust for DWR and shall be remitted to DWR, subject to periodic adjustment, as described in the second preceding paragraph above.

Each Servicing Arrangement permits DWR to assign or pledge its rights to receive payments from the IOU to the Trustees under the Indenture to secure DWR's obligations thereunder. DWR has irrevocably assigned its rights to customer payments under each Servicing Arrangement under the Indenture. DWR also has the right under each Servicing Arrangement to transfer its rights and obligations to any entity created by the California Legislature to assume the rights and obligations of DWR under the Act.

Each Servicing Arrangement lists "Events of Default" by the IOU that include any failure to remit funds to DWR that continues unremedied for three business days and certain failures to observe or perform under the Servicing Arrangement. Upon any Event of Default by the IOU, DWR may, in addition to exercising its remedies under the Servicing Agreement, (in the case of SCE and SDG&E) terminate the Servicing Arrangement, and, in all cases, apply to the CPUC (and, if necessary, a court) for sequestration and payment to DWR or the Trustees of amounts due DWR under the Servicing Arrangement. DWR does not have the right to terminate PG&E's Servicing Arrangement.

Each Servicing Arrangement also states that DWR will be in default under the Servicing Arrangement if DWR fails to perform any of a number of duties listed in the Servicing Arrangement, including the failure to pay the IOU money when due. Upon any default by DWR, the IOU may not terminate the Servicing Arrangement in whole or in part or any obligation thereunder, but the IOU may exercise any other remedies available under the Servicing Arrangement, the Act, and other applicable laws, rules and regulations.

The stated termination date of each IOU's Servicing Arrangement is 180 days after the later of (i) the final date Bond Charges and Power Charges are billed to customers in the IOU's service territory and (ii) the last date that the IOU sells surplus energy on behalf of DWR.

Each Servicing Arrangement includes a *force majeure* clause that provides that neither DWR nor the IOU is liable for any delay or failure in performance of any part of the Servicing Arrangement (including the obligation to remit money at the times therein specified) from any cause beyond its reasonable control, including but not limited to: unusually severe weather; flood; fire; lightning; epidemic; quarantine restriction; war; sabotage; act of a public enemy; earthquake; insurrection; riot; civil disturbance; strike; restraint by court order or any nation or government, any state or other political subdivision of a state, and any entity exercising executive, legislative, judicial, regulatory or administrative functions of or pertaining to a government, including the CPUC; or any combination of these causes, which by the exercise of due diligence and foresight DWR or the IOU could not reasonably have been expected to avoid and which by the exercise of due diligence is unable to overcome. Notwithstanding these provisions, each party's obligation to pay money under the Servicing Arrangement continues to the extent such party is able to make such payment and any amounts required to be remitted to DWR by the IOU shall be held by the IOU in trust for DWR and remitted to DWR as soon as reasonably practicable. Amounts so paid to or by DWR pursuant to the *force majeure* clause shall not bear interest. Each Servicing Arrangement states that seeking the protection of or being forced into bankruptcy is not a *force majeure* event that excuses timely IOU performance of its Servicing Arrangement.

DWR has the right under each Servicing Arrangement to request an audit, conducted by DWR, of each IOU's records and procedures.

The IOUs have been remitting Cost Responsibility Surcharge revenues from certain direct access customers and certain departing load customers as required by CPUC decisions but no formal agreements or orders have been approved or issued by the CPUC as to the particular remittance procedures to be applied. DWR

has proposed new servicing orders to the IOUs that, among other matters, would formalize the procedures currently employed by the parties. At this time, DWR cannot predict the outcome of its discussions with the IOUs concerning Cost Responsibility Surcharge remittance procedures, or the specific procedures ultimately imposed on the IOUs by the CPUC with respect to Cost Responsibility Surcharge remittances. For a discussion of direct access, departing load and the Cost Responsibility Surcharge, see “THE DWR POWER SUPPLY PROGRAM – Direct Access, Departing Load and Community Choice Aggregation.”

#### *Additional Information*

Other important provisions are contained in the Servicing Arrangements, which are available as described under “GENERAL INFORMATION.” For a description of the IOUs, see “THE DWR POWER SUPPLY PROGRAM – Customer Base.”

#### *Collection Experience*

According to filings made by the IOUs with FERC, over the last five years each of the IOUs had uncollectible amounts that averaged approximately 0.3% of its operating revenues. No IOU had uncollectible amounts that exceeded 0.5% of operating revenues in any one year. Under the Servicing Arrangements, risk of noncollection is to be borne proportionately by DWR and the IOUs.

### **Direct Access, Departing Load and Community Choice Aggregation**

#### *General*

“Direct access” customers consist of retail electricity customers in the service areas of the IOUs who stopped purchasing electricity from the IOUs and obtain their electricity from alternative electric service providers. “Departing load” consists of retail electricity customers who commence self-generation or who leave the service areas of the IOUs and obtain their electricity from publicly owned utilities. “Community Choice Aggregation” refers to the ability of local governments within the service area of the IOUs to aggregate the power needs of their community and purchase electricity on their behalf from service providers other than the IOU. Recent regulatory developments, including the imposition of a Cost Responsibility Surcharge on certain direct access, departing load and future Community Choice Aggregation customers, have mitigated the risk that direct access, departing load and Community Choice Aggregation will create revenue shortfalls and necessitate revised revenue requirement submissions by DWR, as described below.

#### *Direct Access*

The CPUC suspended the right of IOU customers to switch to direct access after September 20, 2001. Under existing law, such suspension will continue until DWR’s long-term power contracts expire, the last of which is expected to expire in 2017. The CPUC has also imposed a Cost Responsibility Surcharge on direct access customers intended to prevent cost shifting as a result of direct access migration prior to September 20, 2001. However, retail electricity customers who elected direct access service on or before the date DWR began its Power Supply Program and have not since returned to bundled service continue to be eligible for direct access service and do not pay the Cost Responsibility Surcharge. CPUC Decision 02-03-055 prohibits the IOUs from accepting any other new direct access service requests not already approved by the CPUC, including requests from existing qualified direct access end-users that wish to add new direct access locations or accounts to their service (subject to certain flexibility described in the next paragraph). For a description of the Cost Responsibility Surcharge, including the definition thereof, see “THE DWR POWER SUPPLY PROGRAM – Direct Access, Departing Load and Community Choice Aggregation - *Cost Responsibility Surcharge*,” below.

The CPUC has granted existing direct access accounts a limited degree of flexibility with respect to the direct access suspension. On February 19, 2004, the CPUC issued Decision 04-02-024 which allows current direct access customers to increase load at one or more locations, provided that the net load of the same customer

does not increase within a utility's service territory. This provision is intended to maintain the "standstill principle" adopted in Decision 02-03-055, while accounting for "normal changes in business operations." In Decision 04-07-025, the CPUC clarified rules governing load growth for existing direct access accounts. In addition, existing direct access customers may take bundled service from the applicable IOU for up to 45 days while switching between electric service providers.

#### *Departing Load*

Departing load includes "municipal departing load" and "self-generation." Municipal departing load refers to load that either relocates to, or resides on land that is annexed by, a publicly owned utility (e.g., municipal utilities or irrigation districts). Self-generation refers to the generation of electricity by a retail customer for its own use.

In 2006, DWR expects the total load from municipal departing load and self-generation to be in an amount equal to less than 2% of total retail sales. Unlike direct access, the growth of municipal departing load and self-generation is not expressly limited by CPUC decision. However, to prevent cost shifting, the CPUC has imposed a Cost Responsibility Surcharge on certain classes of municipal departing load and self-generation customers similar to the Cost Responsibility Surcharge imposed on certain direct access customers. Pursuant to various CPUC orders, DWR shall receive a portion of its revenue requirement from that Cost Responsibility Surcharge. The CPUC is currently conducting a proceeding to establish the procedures for the IOUs to bill and collect the Cost Responsibility Surcharge from municipal departing load customers, but the municipal departing load Cost Responsibility Surcharge is not being collected at this time. While the municipal departing load Cost Responsibility Surcharge is not being collected, the amount not collected from these customers is currently being paid by bundled service customers. See "THE DWR POWER SUPPLY PROGRAM – Direct Access, Departing Load and Community Choice Aggregation - *Cost Responsibility Surcharge*," below.

#### *Community Choice Aggregation*

Community Choice Aggregation, authorized by legislation enacted in 2002 ("AB 117"), refers to the ability of a city or county to aggregate all the electrical demand of the residents, businesses and municipal users under its jurisdiction and to meet this demand from an electricity provider other than an IOU, such as an independent electrical service provider. Community Choice Aggregation has not been implemented yet, but its authorizing legislation requires Community Choice Aggregation customers to pay charges (including DWR charges) intended to prevent cost shifting to the bundled customers of the IOUs. For a description of the Cost Responsibility Surcharge, including the definition thereof, see "THE DWR POWER SUPPLY PROGRAM – Direct Access, Departing Load and Community Choice Aggregation - *Cost Responsibility Surcharge*," below.

In 2007 and beyond, the amount of Community Choice Aggregation could increase significantly. While the permitting process and the relatively high capital costs of installing micro-turbines or other on-site generation will curb the growth of self-generation, and while municipal departing load is expected to follow historical growth trends, the opportunity for whole communities to aggregate load and procure power at competitive prices under Community Choice Aggregation could lead to substantial reductions in bundled sales volumes. The CPUC is presently conducting proceedings to establish the Cost Responsibility Surcharge to be paid by Community Choice Aggregation customers and to address other issues that would need to be resolved before Community Choice Aggregation could begin. DWR is closely monitoring CPUC proceedings relating to Community Choice Aggregation. Based on the requirements of AB 117 and the progress of those CPUC proceedings, DWR does not expect Community Choice Aggregation load to rise to substantial levels before 2007.

#### *Cost Responsibility Surcharge*

In a series of decisions, the CPUC has ordered certain classes of direct access and departing load customers to pay a Cost Responsibility Surcharge related to historical stranded costs and ongoing costs. For many of these customers, the Cost Responsibility Surcharge includes a Bond Charge component and/or a Power

Charge component. The Bond Charge and the Power Charge components are CPUC-established rates imposed on total electricity usage by these direct access and departing load customers. These revenues reduce the amount of Bond Charges and Power Charges that must be imposed on bundled customers to recover Bond Related Costs and Department Costs. Community Choice Aggregation has not been implemented yet, but the authorizing legislation for Community Choice Aggregation requires Community Choice Aggregation customers to pay charges equivalent to the Bond Charges and Power Charges they would be required to pay as bundled customers.

The Power Charge component of the Cost Responsibility Surcharge is limited by a maximum collections rate established by the CPUC. If the collections of the Power Charge component of the Cost Responsibility Surcharge are insufficient to cover the Department Costs allocable to the direct access and departing load customers, the amount not collected from those customers would instead be paid by bundled service customers, and tracked in utility accounts in order to be collected from direct access and departing load customers in future periods. DWR does not expect any need for such tracking in the 2006 revenue requirement period.

**Financing of the Power Supply Program**

*Prior Sources of Financing*

The original sources of funding to initiate the Power Supply Program in 2001 included advances from the State’s General Fund totaling approximately \$6.1 billion (the “State Loan”), a loan from a consortium of commercial and investment banks totaling \$4.3 billion (the “Bank Loan”), and revenues from electricity sales. In 2002, DWR issued Bonds in the aggregate principal amount of \$11.263 billion to repay the State Loan and the Bank Loan, establish certain debt service reserves and operating reserves, pay costs of obtaining credit enhancement and pay costs of issuance. The Bonds issued in 2002 are described in the following table.

<u>Series</u>	<u>Initial Principal Amount</u>	<u>Outstanding Principal Amount</u>	<u>Current Interest Rate Mode</u>
Series 2002A <sup>(1)</sup>	\$ 6,313,500,000	\$ 6,195,625,000	Fixed Rate
Series 2002B	1,000,000,000	1,000,000,000	Daily Rate
Series 2002C	2,750,000,000	2,750,000,000	Weekly Rate
Series 2002D	500,000,000	500,000,000	Auction Rate
Series 2002E (Taxable)	700,000,000	250,000,000	Fixed Rate
Total	<u>\$11,263,500,000</u>	<u>\$10,695,625,000</u>	

<sup>(1)</sup> Includes Bonds proposed to be refunded with proceeds of the Series 2005 Bonds.

*Interest Rate Hedges*

DWR has entered into floating-to-fixed interest rate swap agreements with several different counterparties in an aggregate initial notional amount of \$4,023,900,000 to reduce the risk of interest rate volatility with respect to its variable rate Bonds. These swaps include nine floating to fixed interest rate swap transactions in an aggregate initial notional amount of \$1,429,900,000 executed in connection with the issuance of the Series 2002 Bonds, and six floating to fixed interest rate swap transactions in an aggregate initial notional amount of \$2,594,000,000 executed in connection with the issuance of the Series 2005 Bonds. See “PLAN OF REFUNDING.”

Under the Indenture, required payments under Qualified Swaps are Bond Related Costs and are paid from the Bond Charge Payment Account on a parity with debt service on the Bonds. In order for an interest rate swap agreement to qualify as a Qualified Swap, the Indenture generally requires, among other things, that (i) the swap provider have ratings not lower than the third highest rating category from each rating agency then maintaining a rating for the provider, and in no event lower than the rating category designated by any such rating agency for the Bonds subject to the interest rate swap, or (ii) the interest rate swap will not result in a reduction or withdrawal

of any ratings on the Bonds subject to the swap. See “SECURITY FOR THE BONDS” and the definitions of “Qualified Swap” and “Qualified Swap Provider” in APPENDIX D – “SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE.” All of DWR’s interest rate swap agreements are Qualified Swaps. The providers of DWR’s outstanding swaps have current long-term ratings of at least Aa1 by Moody’s, A+ by S&P and A+ by Fitch. Under DWR’s credit policies currently in effect, any swap provider must maintain one rating of at least Aa3 from Moody’s or AA- from S&P.

Payments owed by DWR to each swap provider and payments owed by such swap provider to DWR are netted against each other within each interest rate swap transaction, but generally not among transactions. Any net swap receipts are deposited in the Bond Charge Collection Account. Any net swap payments by DWR are Bond Related Costs, payable from the Bond Charge Payment Account. See “SECURITY FOR THE BONDS – Accounts and Flow of Funds.”

DWR’s interest rate swap agreements generally provide that upon early termination, the mark-to-market value of the interest rate swap transaction is payable from one party to the other. For a further discussion of DWR’s interest rate swap portfolio and its contingent mark-to-market liability, see Notes 5 and 10 of the audited financial statements in Appendix A hereof.

The table below sets forth the Series of Bonds hedged, the initial notional amount of the interest rate swap, the fixed interest rate to be paid by DWR, the variable rate to be received by DWR, the expiration date and the name of the counterparty. For a further discussion of DWR’s interest rate swap portfolio, see Notes 5 and 10 of the audited financial statements in Appendix A hereof.

Hedged Bond Series	Initial Notional Amount	Fixed Rate Paid by DWR	Variable Rate Received by DWR	Expiration Date (May 1)	Counterparty
2002B/C/D	\$ 93,600,000	2.914%	67% LIBOR	2011	Bayerische Landesbank
2002B/C/D	233,700,000	3.024	67% LIBOR	2012	Bayerische Landesbank
2002B/C/D	200,000,000	3.405	100% BMA	2013	JPMorgan Chase Bank
2002B/C/D	100,000,000	3.405	100% BMA	2013	Morgan Stanley Capital Services
2002B/C/D	29,900,000	3.405	100% BMA	2013	Merrill Lynch Capital Services, Inc.
2002B/C/D	194,400,000	3.204	67% LIBOR	2014	Bank of America N.A.
2002B/C/D	174,200,000	3.280	67% LIBOR	2015	Bayerische Landesbank
2002B/C/D	202,300,000	3.342	67% LIBOR	2016	BNP Paribas
2002B/C/D	201,800,000	3.389	67% LIBOR	2017	Morgan Stanley Capital Services
2005F/G	355,100,000	3.184	66.5% LIBOR	2015	Depfa Bank
2005F/G	485,300,000	3.228	66.5% LIBOR	2016	BNP Paribas
2005F/G	480,000,000	3.282	66.5% LIBOR	2017	Wachovia Bank
2005F/G	514,200,000	3.331	66.5% LIBOR	2018	Deutsche Bank
2005F/G	306,200,000	3.256	64% LIBOR	2020	Deutsche Bank
2005F/G	<u>453,200,000</u>	3.325	64% LIBOR	2022	Royal Bank of Canada
Total	<u>\$4,023,900,000</u>				

## Investments

Funds on deposit in the Electric Power Fund are currently invested in a combination of cash and cash equivalents, unsecured investment agreements and a forward purchase agreement collateralized with U.S. Treasury securities. The following table details the Electric Power Fund investments by account, as of September 30, 2005.

<u>Investment</u>	<u>Administration, Operating and Priority Contract Accounts</u>	<u>Operating Reserve Account</u>	<u>Bond Charge Collection and Bond Charge Payment Accounts</u>	<u>Debt Service Reserve Account</u>	<u>Totals</u>
Cash and Cash Equivalents <sup>(1)</sup>	\$1,092,834,329	\$554,778,235	\$780,962,414	\$327,052,356	\$2,755,627,335
Investment Agreements <sup>(2)</sup>	--	--	--	500,000,000	500,000,000
Fwd. Purchase Agreement <sup>(3)</sup>	--	--	--	100,000,000	100,000,000
<b>Totals</b>	<b><u>\$1,092,834,329</u></b>	<b><u>\$554,778,235</u></b>	<b><u>\$780,962,414</u></b>	<b><u>\$927,052,356</u></b>	<b><u>\$3,355,627,335</u></b>

(1) Cash and Cash Equivalents includes approximately \$2.704 billion in SMIF (described below), approximately \$52 million held by a fiscal agent and a de minimis amount of cash held in the State Treasury.

(2) Investment agreement providers include AIG SunAmerica Life Insurance Company, FSA Capital Management Services LLC, Royal Bank of Canada, New York Branch and XL Asset Funding Company I LLC.

(3) The forward purchase agreement provider is Merrill Lynch Capital Services, Inc.

Of the approximately \$3.56 billion in the Electric Power Fund as of September 30, 2005, approximately \$2.70 billion or 76% was invested in the Surplus Money Investment Fund ("SMIF"). SMIF is comprised of moneys on deposit in the State's Centralized Treasury System for investment by the State Treasurer in the Pooled Money Investment Account (the "PMIA"). As of September 30, 2005, the PMIA held approximately \$35.80 billion of State moneys (which included \$26.38 billion in SMIF), and \$16.43 billion of moneys invested for about 2,675 local governmental entities through the Local Agency Investment Fund. The assets of the PMIA as of September 30, 2005 are shown in the following table:

### Analysis of the Pooled Money Investment Account Portfolio September 30, 2005

<u>Type of Security</u>	<u>Amount (in millions)</u>	<u>Percent of Total<sup>(1)</sup></u>
U.S. Treasury Bills and Notes.....	\$ 4,900	9.4%
Commercial Paper (corporate).....	8,207	15.7
Certificates of Deposit .....	10,930	20.9
Corporate Bonds .....	1,021	1.9
Federal Agency Securities .....	13,686	26.2
Bankers' Acceptances .....	-	0.0
Bank Notes.....	1,350	2.6
Loans per Government Code .....	4,753	9.1
Time Deposits .....	7,475	14.3
Repurchase Agreements.....	-	0.0
Reversed Repurchases .....	(99,600)	(0.2)
<b>Total</b>	<b><u>\$ 52,223</u></b>	<b><u>100.0%</u></b>

(1) May not add due to rounding.

The State's treasury operations are managed in compliance with the California Government Code and according to a statement of investment policy which sets forth permitted investment vehicles, liquidity parameters and maximum maturity of investments. The PMIA operates with the oversight of the Pooled Money Investment Board (consisting of the State Treasurer, the State Controller and the Director of Finance). The PMIA is not invested in leveraged products or inverse floating rate securities. The investment policy permits the use of reverse repurchase agreements subject to limits of no more than 10 percent of the PMIA. All reverses are cash matched. The average life of the investment portfolio of the PMIA as of September 30, 2005 was 169 days.

*Annual Debt Service on the Bonds*

The following table sets forth the annual debt service requirements on the Bonds.

Year Ending Dec. 31	2002A/E <sup>(1)</sup>	2002B/C/D <sup>(2)</sup>	2005F/G <sup>(3)</sup>	Totals
2005	--	\$ 1,555,556	--	\$ 1,555,556
2006	\$ 609,303,494	159,596,113	\$ 103,596,181	872,495,788
2007	591,539,644	176,306,671	104,423,468	872,269,783
2008	609,623,085	159,449,223	104,453,236	873,525,544
2009	507,664,140	261,400,108	104,657,532	873,721,780
2010	558,632,840	211,302,233	104,636,356	874,571,429
2011	405,129,148	367,463,766	104,691,300	877,284,213
2012	399,439,598	376,801,846	104,819,180	881,060,623
2013	610,160,710	167,103,758	104,918,404	882,182,872
2014	449,470,887	330,243,027	104,988,972	884,702,886
2015	367,112,510	303,682,970	216,723,964	887,519,444
2016	14,335,198	325,588,728	551,048,822	890,972,748
2017	31,490,000	333,241,491	530,040,248	894,771,738
2018	47,234,550	302,153,488	547,799,944	897,187,982
2019	--	712,539,318	188,727,291	901,266,609
2020	--	748,645,662	157,142,508	905,788,170
2021	--	741,983,832	166,506,769	908,490,601
2022	--	606,234,789	304,173,452	910,408,241
Totals	<u>\$5,201,135,802</u>	<u>\$6,285,292,581</u>	<u>\$3,603,347,623</u>	<u>\$15,089,776,006</u>

(1) Excludes debt service on the Refunded Bonds.

(2) Interest on hedged Bonds calculated at the fixed rates on the applicable interest rate swap agreements. Interest on unhedged variable rate Bonds calculated at 4.00%.

(3) Interest calculated at the fixed rates on the applicable interest rate swap agreements.

## Summary of Operating Results

The following table provides a summary of historical and projected revenues, expenditures and fund balances of the Power Supply Program for the calendar years 2003 through 2006.

	Historical		Projected	
	2003	2004	2005	2006
<b>Power Charge Accounts</b>				
Balance in Power Charge Accounts at January 1				
Operating, Priority Contract and Administrative Accounts	\$ 1,298	\$ 1,031	\$ 1,191	\$ 892
Operating Reserve Account	777	630	595	591
Total Beginning Balance in Power Charge Accounts	2,075	1,660	1,786	1,483
Power Charge Accounts Operating Revenues				
Power Charge Revenues	4,039	4,512	3,656	4,546
Surplus Power and Gas Sales Revenues	382	547	518	235
Energy Litigation Settlements	16	312	200	
Interest Earnings	39	28	40	44
Total Power Charge Accounts Operating Revenues	4,475	5,399	4,414	4,825
Power Charge Accounts Operating Expenses				
Power Costs	4,819	5,229	4,682	4,888
Administrative and General	71	45	35	36
Total Power Charge Accounts Operating Expenses	4,889	5,274	4,717	4,924
Net Revenues - Power Charge Accounts	(414)	125	(302)	(100)
Balance in Power Charge Accounts at December 31	\$ 1,660	\$ 1,786	\$ 1,483	\$ 1,384
<b>Bond Charge Accounts</b>				
Balance in Bond Charge Accounts at January 1				
Bond Charge Collection Account	\$ 77	\$ 184	\$ 199	\$ 221
Bond Charge Payment Account	211	374	572	573
Debt Service Reserve Account	927	927	927	913
Total Beginning Balance in Bond Charge Accounts	1,216	1,485	1,698	1,707
Bond Charge Accounts Revenues				
Bond Charge Revenues	722	829	838	820
Interest Earnings	22	35	54	62
Total Bond Charge Account Revenues	744	864	892	882
Bond Charge Accounts Expenses				
Debt Service on Bonds	476	651	883	898
Total Bond Charge Account Expenses	476	651	883	898
Net Revenues - Bond Charge Accounts	268	213	9	(16)
Balance in Bond Charge Accounts at December 31	\$ 1,485	\$ 1,698	\$ 1,707	\$ 1,691

Source: Results for calendar years 2003 and 2004 are derived from DWR audited financial statements. Results for calendar year 2005 are derived from DWR audited financial statements at June 30, 2005, unaudited financial reports from July 1, 2005 to September 30, 2005 and management projections for the period October 1, 2005 to December 31, 2005. Projected results for calendar year 2006 are consistent with the assumptions set forth in Section D of DWR's Revision to the Determination of Revenue Requirements for the period January 1, 2006-December 31, 2006, which is available at DWR's website at <http://www.cers.water.ca.gov> and was submitted to the CPUC on October 27, 2005 for implementation. The projections should be evaluated based on those assumptions. All figures are in millions of dollars. Numbers may not add, due to rounding. All projections are the responsibility of DWR. PricewaterhouseCoopers LLP (PwC), independent accountant for DWR, has neither examined nor compiled such projections and, accordingly, PwC does not express an opinion or any other form of assurance with respect thereto. The PwC report included in Appendix A relates to historical financial information of the Department of Water Resources Electric Power Fund. The PwC report does not extend to the projections set forth above and should not be read to do so. These projections were not prepared with a view toward compliance with the guidelines established by the American Institute of Certified Public Accountants for preparation and presentation of prospective financial information.

## **CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES**

### **General**

The primary revenues used for the payment of the Bonds and Bond Related Costs are Bond Charge Revenues, which constitute part of the Trust Estate securing the Bonds. The Rate Agreement requires the CPUC to impose Bond Charges sufficient to ensure that amounts on deposit in the Bond Charge Payment Account are adequate to pay all Bond Related Costs as they come due. Bond Related Costs include Bond debt service, Qualified Swap payments, credit enhancement and liquidity facilities charges, and costs relating to other financial instruments and servicing arrangements related to the Bonds. Bond Charges are required to be imposed on all electric power sold to each bundled customer, whether that power is provided by DWR or by the IOUs.

The Rate Agreement also requires the CPUC to impose Power Charges on customers who buy power from DWR (generally, the customers who buy power from the IOUs) for the purpose of paying “Department Costs,” including the costs that DWR incurs to procure and deliver power. The Rate Agreement requires the CPUC to impose Power Charges that are sufficient to provide moneys in the amounts and at the times necessary to satisfy the Retail Revenue Requirements as described below.

In addition, the CPUC has undertaken proceedings to establish a Cost Responsibility Surcharge on certain direct access and departing load customers. The Cost Responsibility Surcharge is intended to be imposed in amounts intended ultimately to keep the customers of the IOUs and DWR indifferent to whether customers have elected, or in the future elect, to leave bundled service. Generally, the Cost Responsibility Surcharge has a component to collect amounts for the purpose of paying Bond Related Costs and a component (currently subject to a maximum) for the purpose of paying Department Costs. Amounts collected pursuant to the Bond Related Cost component of the Cost Responsibility Surcharge offset the amounts required to be collected from Bond Charges on the customers of the IOUs and DWR, and amounts collected pursuant to the Department Cost components of the Cost Responsibility Surcharge offset amounts required to be collected from Power Charges on the customers of the IOUs and DWR.

In 2004, DWR supplied approximately 51 billion kWh of energy to its customers and received approximately \$4.5 billion in Power Charge Revenues and approximately \$830 million in Bond Charge Revenues, including Cost Responsibility Surcharge revenues in each case.

### **Rate Agreement**

The CPUC and DWR have entered into the Rate Agreement pursuant to the Act to facilitate the issuance of Bonds and for the benefit of Bondholders and all other persons to whom DWR is obligated to pay Bond Related Costs (other than the providers of servicing and administrative services to DWR after the termination of DWR’s long-term power contracts). The obligation of the CPUC to calculate, revise and impose Bond Charges is irrevocable and cannot be amended. Other provisions of the Rate Agreement may be amended only by an amendment approved by DWR and the CPUC. Under the Indenture, DWR has covenanted not to amend the Rate Agreement unless DWR has determined that the amendment will not have a material adverse effect on the ability of DWR to comply with the provisions of the Indenture.

In the Rate Agreement, the CPUC has covenanted and agreed to calculate, revise and impose from time to time, Bond Charges sufficient to provide moneys so that the amounts available for deposit in the Bond Charge Payment Account from time to time, together with amounts on deposit in the Bond Charge Payment Account, are at all times sufficient to pay or provide for the payment of all Bond Related Costs when due in accordance with the “Financing Documents” (defined in the Rate Agreement attached as Appendix D). The Rate Agreement provides that this covenant shall have the force and effect of a “financing order” under the California Public Utilities Code and shall be irrevocable and enforceable in accordance with its terms, including, without limitation, in circumstances in which DWR has breached its obligations under the Rate Agreement or in respect of the

Financing Documents. Under the California Public Utilities Code, a “financing order” is binding upon the CPUC as it may be constituted from time to time, and the CPUC has no authority to rescind, alter or amend its obligations thereunder. Under the Act, the rights, powers and duties of the CPUC may not be diminished or impaired in a manner that would adversely affect the interests or rights of Bondholders. See, however, “RISK FACTORS – Determination of Power Charges and Bond Charges; Possible Use of Amounts in the Bond Charge Collection Account to Pay Priority Contract Costs – *Application and Enforcement of CPUC’s Bond Charge Rate Covenant.*”

In the Rate Agreement, the CPUC has also covenanted and agreed to calculate, revise and impose, from time to time, Power Charges sufficient to provide moneys in the amounts and at the times necessary to satisfy DWR’s “Retail Revenue Requirements” (defined in the Rate Agreement attached as Appendix D) as specified by DWR.

In the event of a failure of the CPUC to calculate and impose Bond Charges in accordance with the Rate Agreement, the Rate Agreement is enforceable against the CPUC by the Co-Trustee under the Indenture 30 days after DWR has defaulted under its obligations contained in the Financing Documents (as defined in the Rate Agreement) and failed to enforce the Rate Agreement. The Rate Agreement imposes certain conditions to the exercise by the Co-Trustee of DWR’s rights under the Rate Agreement.

The Rate Agreement specifies the actions to be taken by DWR and the timetable that the CPUC will use to calculate, revise and impose Bond Charges and Power Charges. See “CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES – CPUC Actions to Calculate, Revise and Impose Bond Charges and Power Charges.”

To enable the CPUC to set and adjust Bond Charges and Power Charges, the Rate Agreement requires DWR to periodically determine and submit cost information and projections to the CPUC and to provide reports to the CPUC concerning fund balances under the Indenture. See “CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES – DWR Actions to Establish Revenue Requirements.” The Rate Agreement specifies information that DWR will include with its Retail Revenue Requirements.

Subject to certain conditions in the Rate Agreement, if DWR projects that within the next 120 days there will be insufficient amounts on deposit in the Bond Charge Payment Account to make timely payment of Bond Related Costs, the Rate Agreement requires DWR to submit to the CPUC a request that the CPUC increase Bond Charges, and the CPUC is required to calculate and impose revised Bond Charges to pay such Bond Related Costs no later than 120 days from the date following DWR’s request. The Rate Agreement further provides that, even if DWR does not submit such a request, the CPUC is bound by its covenant to calculate, revise and impose Bond Charges, as described above.

A decision approving the Rate Agreement was adopted by the CPUC on February 21, 2002, and the Rate Agreement was executed by the CPUC and DWR as of March 8, 2002. The decision approving the Rate Agreement is final and unappealable under California law. A copy of the Rate Agreement is attached as Appendix D to this Official Statement.

Under the Indenture, DWR may not issue Bonds unless DWR and the CPUC have entered into a rate agreement with respect to such Bonds. The Series 2005 Bonds and all other Bonds currently Outstanding are entitled to the benefits of the Rate Agreement attached as Appendix D.

Counsel to the CPUC and Bond Counsel will each deliver an opinion, in connection with the issuance of the Series 2005 Bonds, concerning the Rate Agreement, among other matters. See APPENDIX F – “PROPOSED FORM OF OPINION OF BOND COUNSEL”, for a copy of the form of proposed opinion of Bond Counsel. Such opinions represent expressions of professional judgment and not guarantees of result. See “RISK FACTORS – Determination of Power Charges and Bond Charges; Possible Use of Amounts in the Bond Charge Collection Account to Pay Priority Contract Costs.”

## **Substantive Considerations in Establishing Revenue Requirements**

DWR's revenue requirements generally consist of Bond Related Costs and Department Costs, which are to be satisfied primarily by Bond Charge Revenues and Power Charge Revenues, respectively.

### *Bond Related Costs and Bond Charge Revenues*

Bond Related Costs include (a) debt service on the Bonds, (b) payments required to be made: (i) under agreements with issuers of credit and liquidity facilities, including letters of credit, bond insurance, guarantees, debt service reserve fund surety bonds, lines of credit, reimbursement agreements, and standby bond purchase agreements, (ii) under agreements relating to other financial instruments entered into in connection with the Bonds, including but not limited to investment agreements, hedges, interest rate swaps, caps, options and forward purchase agreements, and (iii) under agreements relating to the remarketing of Bonds, including but not limited to remarketing agreements, dealer agreements and auction agent agreements, (c) deposits to the Debt Service Reserve Account, and (d) other costs as specified in the Rate Agreement, attached as Appendix D. Bond Charge Revenues include (y) revenues from Bond Charges (including the Bond Charge component of Cost Responsibility Surcharge revenues from certain direct access customers, as described in "THE DWR POWER SUPPLY PROGRAM – Direct Access, Departing Load and Community Choice Aggregation") and (z) interest earned on Bond Charge Account balances.

### *Department Costs and Power Charge Revenues*

Department Costs generally include (1) costs associated with power supply (including natural gas supply) to be delivered under DWR's power contracts, including Priority Long-Term Power Contracts; (2) gas collateral and/or hedging costs; (3) administrative and general expenses; and (4) amounts required to maintain necessary Power Charge Account balances, including any amounts required to maintain operating reserves as determined by DWR (see "SECURITY FOR THE BONDS – Operating Account" and "– Operating Reserve Account"). Revenues to be used to pay Department Costs include all Revenues other than Bond Charge Revenues and payments to DWR under Qualified Swaps relating to Bonds. Such Revenues to be used to pay Department Costs include (a) Revenues from Power Charges (including Power Charge Revenues and Cost Responsibility Surcharge revenues from certain direct access and departing load customers, as described in "THE DWR POWER SUPPLY PROGRAM – Direct Access, Departing Load and Community Choice Aggregation"); (b) revenues from other power sales; and (c) investment earnings on Power Charge Accounts.

### *DWR Projections*

In order to project Bond Related Costs for the applicable revenue requirement period, DWR determines the aggregate amount of scheduled Bond principal and interest on fixed-rate Bonds becoming due during such period (generally the calendar year), makes assumptions regarding variable interest rates (subject to certain minimum assumptions required by the Indenture) and other Bond Related Costs and determines the amounts required to be available to be transferred to the Bond Charge Payment Account at the times required by, and otherwise in accordance with, the Indenture. See APPENDIX C – "SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE."

In order to project Bond Charge Revenues, Department Costs, Power Charge Revenues and other Revenues, and in order to assist the CPUC and the IOUs in determining the appropriate charges to produce such revenues, DWR makes projections regarding IOU retail customer load, direct access, departing load, power supply, surplus energy sales, natural gas prices, administrative and general expenses and other factors affecting DWR's revenues and expenses.

The following is a description of certain of the principal considerations taken into account by DWR in determining its revenue requirements. While the considerations described below are generally representative of DWR's current practices in calculating its revenue requirements, this description does not purport to be

exhaustive. DWR currently engages consultants to assist in the development and monitoring of DWR's revenue requirements.

#### *Bond Charge Collection Account and Bond Charge Payment Account*

Under the Indenture, DWR is required to include in its revenue requirements amounts estimated to be sufficient to cause the amount on deposit in the Bond Charge Collection Account, on the first Business Day of each month, to be at least equal to the amounts projected to be required to be paid out of the Bond Charge Payment Account that month. All Bond Charge revenues are to be deposited in the Bond Charge Collection Account. Subject to the prior claim on revenues in the Bond Charge Collection Account for the payment of Priority Contract Costs, on or before the last Business Day of each month, DWR is required to transfer from the Bond Charge Collection Account to the Bond Charge Payment Account such amount as is necessary to make the amount in the Bond Charge Payment Account sufficient to pay all Bond Related Costs estimated to accrue or be due and payable during the next succeeding three calendar months. Interest accruing on unhedged Variable Rate Bonds during any future period is required by the Indenture to be, and currently is, assumed to accrue at a rate equal to the greater of (a) 130 percent of the highest average interest rate on such Variable Rate Bonds in any calendar month during the twelve (12) calendar months ending with the month preceding the date of calculation, or such shorter period that such Variable Rate Bonds shall have been outstanding, or (b) 4.0 percent.

#### *Debt Service Reserve Account*

In determining its revenue requirements, DWR includes any amounts necessary to maintain in the Debt Service Reserve Account an amount equal to the "Debt Service Reserve Requirement". The Debt Service Reserve Requirement is an amount equal to maximum aggregate annual debt service on all outstanding Bonds, determined in accordance with the Indenture. For purposes of calculating the amount of the Debt Service Reserve Requirement from time to time, interest accruing on unhedged Variable Rate Bonds during any future period is assumed to accrue at a rate equal to the greater of (a) 130 percent of the highest average interest rate on such Variable Rate Bonds in any calendar month during the twelve (12) calendar months ending with the month preceding the date of calculation, or such shorter period that such Variable Rate Bonds shall have been outstanding, or (b) 4.0 percent.

#### *Retail Load Projections*

DWR "shapes" the annual load forecasts provided by each IOU by using hourly load factor estimates that were developed by DWR in conjunction with, and reviewed by, each IOU to account for hourly variations in retail customer demand. These hourly estimates are needed in order for DWR to match hourly loads with DWR and IOU resource availability in the production simulation analyses that are performed to estimate DWR contract dispatch and cost in determining revenue requirements, as described in more detail below.

#### *Direct Access and Departing Load Projections*

DWR generally bases its estimates of direct access and departing load within each IOU's service territory on the applicable IOU's data and forecasts.

#### *Power Supply Projections*

The hourly load profile described above is utilized in DWR's electric market simulation to derive hourly energy dispatches required to serve retail customer load, including dispatches of power from DWR's power contracts. DWR projects hourly energy dispatches from its power supply contracts, IOU generation, other IOU resources and other generation resources required to serve IOU customer load. Estimates of IOU-supplied resources are generally based on IOU forecasts of utility owned generation, qualifying facility contract generation, and bilateral contract generation. DWR regularly updates its projections concerning qualifying facility contract terms and expiration dates, outage schedules, and net dependable resource capacity, among others, to reflect

current details related to each IOU's resource portfolio. To project IOU hydroelectric resources, normal hydrologic conditions are generally projected for both California and the Pacific Northwest where meaningful hydrologic forecasts are not available.

Estimates of the amount of energy from DWR's power supply contracts to be delivered to IOU retail customers and the amount available to surplus energy buyers are determined using a market simulation which produces a projection of contract-specific, hourly energy dispatches to meet the projected energy requirements of each IOU's retail customers. The terms and conditions incorporated in DWR's market simulation include, among other details, must-take energy volumes and dispatchable contract capacities, contract heat rates and unit outage rates as well as scheduling limitations. In order to be consistent with CPUC orders governing administration, operation and dispatch of DWR's contracts by the IOUs, energy dispatches from DWR's dispatchable long-term power contracts are assumed to be based on the objective of achieving the lowest possible total cost of power to IOU customers. In general, each incremental generating unit is dispatched only if the incremental cost of generating an additional MWh from that unit is less than projected market clearing prices for replacement power for that hour. Natural gas costs represent a significant component of DWR's total power supply costs under certain contracts and are discussed below. A listing of all of DWR's power supply contracts and certain of their characteristics, including whether DWR bears the risk of market changes in natural gas prices, appears under "THE DWR POWER SUPPLY PROGRAM – Power Purchase Contracts."

#### *Surplus Energy Sales Projections*

As with any retail providers of energy, due to contract obligations and daily and monthly variations in the IOUs' retail customer loads, DWR and the IOUs together, from time to time, purchase more energy than is needed to serve their retail customers. In 2002, the CPUC issued a decision allocating each of the thirty-two DWR power supply contracts to a specific IOU, and determining (with DWR's consent) that income from the sale of DWR and IOU excess energy would be shared on a pro-rata basis between DWR and the IOUs. This excess energy is sold in wholesale markets by the IOUs under the current operating arrangements governing administration, operation and dispatch of DWR's contracts. On occasion, the price obtained for surplus power sales will be less than the price paid for power. However, these losses are an expected incident of appropriate portfolio management. The income from such sales of DWR power is used to partially offset DWR's Retail Revenue Requirement.

#### *Natural Gas Price and Cost Projections*

Power costs under many of DWR's power supply contracts is dependent on the price of natural gas. DWR utilizes a combination of near-term forward gas price indices and a natural gas forecast prepared by Navigant Consulting Inc. ("NCI") using the Gas Market Data and Forecasting System owned by Energy and Environmental Analysis, Inc. ("EEA"), with certain assumptions specified by NCI. These assumptions include but are not limited to the timing of major gas pipeline capacity changes, the prices of crude oil and coal, the timing and magnitude of certain liquefied natural gas capacities, and imports and exports. The EEA model uses a structural, network simulation of the natural gas markets in the U.S. and Canada to solve for natural gas production volumes, gas demand by sector, gas flows, storage activity, and gas prices at a number of market "nodes" in North America. NCI compares the initial model results with the NYMEX forward price at Henry Hub and may adjust the forecasted prices so that they are generally in line with short-term market conditions as reflected on the NYMEX. DWR gas price modeling is performed twice annually or more often as required to reflect revised market conditions and assumptions.

In estimating natural gas costs for its revenue requirements and the potential variability in such costs during any given revenue requirement period, DWR also takes into account then existing or expected hedging of the price risk associated with projected gas purchases. The IOUs (as the entities with operational responsibility for DWR's power supply contracts) have the responsibility to arrange hedges on behalf of DWR. DWR has entered into both financial hedges and physical hedges for the 2006 revenue requirement period. Financial hedges include a mix of options and fixed-price instruments. Physical hedges consist of fixed price gas purchase

contracts. These hedges do not impact the gas price forecast provided by NCI, but they do impact the estimation of total DWR contract fuel costs since costs for the volumes associated with the hedges are estimated by applying the effective hedged price to the corresponding hedged volumes. The cost of unhedged fuel requirements is estimated by applying the NCI gas price forecast to the corresponding unhedged volumes.

#### *Administrative Cost Projections*

DWR's general and administrative cost projections include estimates for consulting services for development and monitoring of the revenue requirements, litigation support, and financial advisory services.

Certain of DWR's general and administrative costs are subject to State budget appropriations, although they are paid by DWR and are part of the Retail Revenue Requirements. These costs include labor and benefits, professional services costs and pro rata charges for services provided to the Power Supply Program by other State agencies. Costs subject to budget appropriations are subject to the State budget process, which can involve delays.

#### *Extraordinary Considerations*

DWR takes into account settlement amounts and other benefits under settlement agreements with various litigants either only when received or when placed into escrow with only ministerial conditions to be met prior to receipt by DWR. See "LITIGATION AND ADMINISTRATIVE PROCEEDINGS."

#### *Operating Account Balances*

The Indenture requires DWR to include in its revenue requirements amounts estimated to be sufficient to cause the amount on deposit in the Operating Account at all times during any calendar month to equal the Minimum Operating Expense Available Balance. The Minimum Operating Expense Available Balance is determined by DWR at the time of each revenue requirement determination and is to be an amount equal to the largest projected difference between DWR's projected operating expenses and DWR's projected Power Charge revenues during any one month period during the revenue requirement period, taking into account a range of possible future outcomes. The Indenture covenant concerns the minimum amount required to be projected to be on deposit, and leaves to DWR the determination as to what total reserves are appropriate or required in the fulfillment of its duties under the Act. DWR has taken into account not only the Indenture-required minimums, but also potential natural gas price volatility and escalation, year-over-year revenue requirement volatility, and other factors. Each year, actual and projected year-end Power Charge Account balances, including the impact of net operating results, are taken into account in the establishment of revenue requirements for the subsequent year.

### **DWR Actions to Establish Revenue Requirements**

#### *Overview of the Rate Agreement*

To enable the CPUC to set Bond Charges and Power Charges, the Rate Agreement requires DWR to periodically determine and submit to the CPUC the amount of DWR's Retail Revenue Requirements and information concerning Bond Related Costs. The Rate Agreement defines "Retail Revenue Requirements" as the amount of Department Costs that are to be recovered from Power Charges imposed by the CPUC from time to time. "Department Costs" means all amounts that DWR is entitled under the Act to recover (other than Bond Related Costs recovered from Bond Charges).

The Rate Agreement requires DWR, at least annually, and more frequently as deemed reasonably necessary or appropriate by DWR or the CPUC, to review, determine and revise its Retail Revenue Requirements and promptly to notify the CPUC following any determination or revision of DWR's Retail Revenue Requirements. The Rate Agreement also requires DWR to revise and communicate to the CPUC its Retail Revenue Requirements within 20 days of DWR projecting that within 120 days: (i) there will be insufficient funds

in the Priority Contract Account to pay Priority Contract Costs; or (ii) there will be less than the Operating Reserve Account Requirement in the Operating Reserve Account; or (iii) shortfalls in the Priority Contract Account, Operating Account and the Operating Reserve Account will require moneys in the Bond Charge Collection Account to be used to pay Priority Contract Costs; or (iv) moneys in the Debt Service Reserve Account will be used to pay Bond Related Costs. DWR is also required by the Rate Agreement to revise and communicate to the CPUC within three business days its Retail Revenue Requirements in the event of a withdrawal from the Bond Charge Collection Account to pay Department Costs or in the event of a withdrawal from the Operating Reserve Account or the Debt Service Reserve Account such that the amount in either such account is less than the amount required by the Indenture or any other financing document.

The Rate Agreement also requires DWR to provide monthly reports to the CPUC concerning DWR's receipts and costs in a form that permits comparison to Retail Revenue Requirement projections. The Rate Agreement permits the CPUC to increase Power Charges to prevent any shortfall on an interim basis if it determines that existing Power Charges are not sufficient to pay Department Costs (which for this purpose includes funding or replenishment of the Bond Charge Collection Account, Bond Charge Payment Account or Debt Service Reserve Account at the levels and at the times required by the Indenture or other financing documents) even if DWR does not provide a revised Retail Revenue Requirement to the CPUC in a timely manner. The CPUC may also require DWR to submit revised Retail Revenue Requirements. If DWR has complied with its obligations under the Rate Agreement, the CPUC is required to impose revised Bond Charges and Power Charges, as appropriate and necessary, no later than 120 days following the filing with the CPUC of DWR's request that the CPUC take such action.

DWR has covenanted in the Rate Agreement that, upon the request of the CPUC, DWR will participate in any CPUC proceedings, including providing witnesses, attending public hearings and providing any other materials necessary to facilitate the CPUC's completion of its proceedings in connection with the establishment of Power Charges or Bond Charges by the CPUC.

#### *Just and Reasonable Requirement*

DWR has agreed in the Rate Agreement that prior to including any cost in the Retail Revenue Requirements communicated to the CPUC, DWR will conduct whatever procedures are required by law to determine that such cost is "just and reasonable" within the meaning of Section 451 of the California Public Utilities Code. In a lawsuit filed by PG&E in 2001, protesting certain aspects of DWR's determination of its 2002 revenue requirements, a California Court of Appeal decided that while DWR is required by the Act to determine that its costs are just and reasonable, it is not required to treat each revenue requirement as a regulation under the California Administrative Procedures Act, or otherwise follow any specific Administrative Procedures Act process in determining its revenue requirements. Neither party appealed that decision.

In June 2002, DWR adopted regulations establishing a procedure for public participation in the determination of its revenue requirements and establishing a standard for determining that costs included in its revenue requirements are just and reasonable. See Division 23, Chapter 4, Sections 510-517 of the California Code of Regulations (the "Revenue Requirement Regulations"). The Revenue Requirement Regulations require DWR to provide to interested parties an opportunity to submit comments on each proposed determination made by DWR. Under the Revenue Requirement Regulations, the time for comment by interested parties on a proposed revenue requirement determination and the bases therefor will normally be at least 21 calendar days, but may be shorter in circumstances in which a shorter period is deemed reasonably necessary by DWR, including those circumstances in which the Rate Agreement requires revised revenue requirements to be communicated to the CPUC within a shorter period. If DWR adds significant additional material as the basis for its determination of its revenue requirements, the regulations require DWR to allow a reasonable period of time for public comment on the additional material.

The Revenue Requirement Regulations state that to protect ratepayer interests, the record of the determination must demonstrate by substantial evidence that the revenue requirement is just and reasonable,

considering the circumstances existing or projected to exist at the respective times of DWR's decisions concerning whether to incur the costs comprising such revenue requirement, and the factors which under the Act are relevant to such determination and such decisions, including but not limited to the following express provisions of the Act:

- The development and operation of the Power Supply Program as provided in the Act is in all respects for the welfare and the benefit of the people of the State, to protect the public peace, health, and safety, and constitutes an essential governmental purpose;
- DWR must do those things necessary and authorized under the Act to make power available directly or indirectly to electric consumers in California (provided that except as otherwise stated, nothing in the Act authorizes DWR to take ownership of the transmission, generation, or distribution assets of any electrical corporation in the State of California);
- Upon those terms, limitations, and conditions as it prescribes, DWR may contract with any person, local publicly owned electric utility, or other entity for the purchase of power on such terms and for such periods as DWR determines and at such prices DWR deems appropriate taking into account all of the factors listed in section 80100 of the Act;
- DWR may sell any power acquired by DWR pursuant to the Act to retail end use customers, and to local publicly owned electric utilities, at not more than DWR's acquisition costs, including transmission, scheduling, and other related costs, plus other costs as provided in section 80200 of the Act;
- DWR must, at least annually, and more frequently as required, establish and revise revenue requirements sufficient, together with any moneys on deposit in the Electric Power Fund, to provide for all of the costs listed in section 80134(a) of the Act (including but not limited to the amounts necessary to pay debt service on bonds (including the Bonds), the amounts necessary to pay for power purchased by DWR, reserves in such amount as may be determined by DWR to be necessary or desirable and DWR's administrative costs); and
- Obligations of DWR authorized by the Act shall be payable solely from the Electric Power Fund.

In a lawsuit filed by PG&E in 2002, protesting DWR's determination of its 2003 revenue requirements, the Superior Court determined that although DWR was not required by statute to adopt regulations concerning the revenue requirement process, having adopted such regulations, DWR is required to follow them. In that case, the court decided that DWR had not allowed adequate time for review and comment on significant additional material added by DWR to the record of the proceedings. Neither party appealed that decision. DWR reopened its revenue requirement proceedings in order to allow additional time for review and comment by interested parties.

Actions taken by DWR under the Revenue Requirement Regulations are subject to judicial review in State court. Any such court proceedings could delay consideration of DWR's revenue requirements or result in a judicial determination that less than all of DWR's costs are just and reasonable. See "RISK FACTORS – Determination of Power Charges and Bond Charges; Possible Use of Amounts in the Bond Charge Collection Account to Pay Priority Contract Costs."

#### *Proceedings under Revenue Requirement Regulations*

DWR has followed the procedures set forth in the Revenue Requirements Regulations with respect to each of its revenue requirement determinations since the redetermination of its 2003 revenue requirements as described above, and has determined that each such revenue requirement was just and reasonable. The 2006 revenue requirement determination is available on DWR's website or upon request to DWR.

DWR determined that its 2006 revenue requirements are just and reasonable because they comport with DWR's statutory responsibilities, accurately reflect lawfully incurred costs, do not over-collect, and contain costs that are reasonable given the circumstances under which they were incurred. DWR believes, for those and other reasons, that DWR would prevail in legal proceedings, if any, that may be brought to force a judicial review of DWR's determination. DWR also believes that with the availability of the substantial reserves described under "SECURITY FOR THE BONDS," the pendency of any such proceedings will not disrupt the cash flow for the Power Supply Program to an extent that would prevent DWR from paying scheduled debt service on the Bonds. However, if such proceedings resulted in the recovery by DWR of less than all of DWR's actual costs, the ability of DWR to pay debt service on the Bonds could be adversely affected. See "RISK FACTORS – Determination of Power Charges and Bond Charges; Possible Use of Amounts in the Bond Charge Collection Account to Pay Priority Contract Costs."

#### *Consultant to DWR*

Navigant Consulting, Inc. provides consulting services to DWR to assist it in operating the Power Supply Program. These services include, but are not limited to, evaluation of the net short electric requirements provided to DWR by the IOUs, support in the evaluation and negotiation of power supply contracts, compilation and periodic updating of power supply quantities and costs from contracted power supply sources, estimation of fuel supply costs and requirements for contracted power supplies, estimation of future power purchase costs in the short-term market, evaluation of electric transmission constraints and associated impact on power supply deliveries, review of actions by other power suppliers and state governmental agencies for effect on the availability and cost of power supplies to meet the customers' net short electric requirements, support in the development of future DWR revenue requirements, revisions to current revenue requirement determinations and support to DWR in filings with the CPUC on revenue recovery and related issues. It is anticipated that NCI will continue to provide services to DWR related to the Power Supply Program subsequent to the issuance of the Series 2005 Bonds. In addition, NCI provided the Consultant's Report for the Series 2002 Bonds. This Official Statement does not include or constitute an update to the Consultant's Report provided for the Series 2002 Bonds.

#### **CPUC Actions to Calculate, Revise and Impose Bond Charges and Power Charges**

The CPUC has authority under the Rate Agreement to set charges to recover DWR's costs. The CPUC also has the authority to establish the procedures that it will use to set electric charges, and to allocate charges among service areas and electric customers.

Applications for rehearing of any CPUC order can be sought by interested parties. Under California law, applications for rehearing of any CPUC order or decision construing, applying, or implementing the provisions of the Act that (1) relates to the determination or implementation of DWR's revenue requirements, or the establishment or implementation of Bond Charges or Power Charges, or (2) in the sole determination of DWR, the expedited review of the CPUC order or decision is necessary or desirable for the maintenance of any credit ratings on any Bonds or for DWR to meet its obligations with respect to the Bonds, must be filed within 10 days after the date of mailing of the order or decision. The CPUC is required to issue its decision and order on rehearing within 20 days after the filing of the application for rehearing.

A court challenge to a CPUC decision on rehearing subject to the expedited procedures described in the preceding paragraph is made by filing a petition for writ of review with the California Supreme Court. The petition for writ of review is time-barred unless it is filed within 30 days after the CPUC mails an order denying rehearing, or, if the CPUC grants rehearing, within 30 days after the CPUC mails its decision on rehearing. The challenge is limited to issues specifically raised in an application for rehearing. The Court may either summarily deny the petition for writ of review or it may grant the petition, in which case there is oral argument and the Court issues a written opinion. California law provides that judicial review can only result in a prospective effect on rates and charges, including Bond Charges.

The California Public Utilities Code provides that orders of the CPUC that have become final and unappealable are conclusive in all collateral actions or proceedings. The California Public Utilities Code prohibits California courts from seeking to review or change a final and unappealable CPUC order. The CPUC order authorizing the Rate Agreement and the CPUC orders adopted on December 19, 2002 comprising the currently effective servicing orders are final and unappealable.

## **Prior Revenue Requirements**

### *2001 and 2002 Revenue Requirements*

DWR submitted its revenue requirements for the calendar years 2001 and 2002 to the CPUC, made several revisions, and submitted the last such revision to the 2001 and 2002 revenue requirements in November 2001. The CPUC considered DWR's 2001 and 2002 revenue requirements, conducted proceedings to determine the allocation of DWR's costs among the IOU service areas, and in February 2002, issued an order adopting specific DWR charges for each of the IOU service areas for 2001 and 2002 (including the continuation of interim rates established during the pendency of the formal ratemaking process). Applications for rehearing of the decision were denied by the CPUC in March 2002.

### *2003 Revenue Requirements*

DWR submitted its revenue requirement for the calendar year 2003 to the CPUC in August 2002. In December 2002, the CPUC imposed Bond Charges and Power Charges sufficient, with other available moneys, to recover DWR's revenue requirements for calendar year 2003.

After submitting the 2003 revenue requirement in August 2002, new information became available to DWR. As of January 1, 2003, DWR was no longer authorized to purchase the residual net short, resulting in the ability to establish a lower Minimum Operating Expense Available Balance in the Operating Account and a lower Operating Reserve Account Requirement. In addition, the IOUs began dispatching DWR power supply contracts. This and other new information, some provided by the IOUs, some based on actual results of operations, and some resulting from changes in certain assumptions, led DWR to submit a 2003 Supplemental Determination with the CPUC in July 2003. In September 2003, the CPUC imposed revised Bond Charges and Power Charges for calendar year 2003. The allocation of the Supplemental 2003 Determination and the resulting charges became final and unappealable without challenge from the IOUs or other interested parties.

During the 2003 revenue requirement period, DWR's actual power costs exceeded projections in the Supplemental 2003 Determination by 2.5%. The primary factors contributing to the higher-than-projected costs included higher-than-projected dispatch of DWR's long-term power contracts of approximately 1.9% (954 GWh) and higher-than-projected fuel prices, particularly in March 2003 when natural gas prices rose above \$10.00/MMBtu. Actual revenues also exceeded projections during the 2003 revenue requirement period. Revenue from customers (the vast majority of total revenue) was \$102 million higher than projected. Total revenue exceeded projections by 7.0%. Total revenues less expenses were \$167 million higher than projected, an amount equal to 3.6% of projected expenses. For a discussion of the treatment of net operating results in the establishment of subsequent-year revenue requirements, see "CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES - Substantive Considerations in Establishing Revenue Requirements - Operating Account Balances."

### *2004 Revenue Requirements*

After allowing for public review and comment in accordance with its Revenue Requirement Regulations, DWR submitted its revenue requirements for the calendar year 2004 to the CPUC in September 2003. In January 2004, the CPUC adopted an order imposing Power Charges and Bond Charges to recover DWR's revenue requirements for calendar year 2004. SCE filed an application for rehearing of the decision adopting such order, which was denied by the CPUC in February 2004.

New information, some provided by the IOUs, some based on actual results of operations, and some resulting from changes in certain assumptions, led DWR to submit a Supplemental 2004 Determination with the CPUC in April 2004. In August 2004, the CPUC imposed revised Bond Charges and Power Charges. The allocation of the Supplemental 2004 Determination and the resulting charges became final and unappealable without challenge from the IOUs or other interested parties.

During the 2004 revenue requirement period, DWR experienced actual fuel prices that exceeded the projections in its Supplemental 2004 Determination. For example, the actual annual average fuel price at PG&E Citygate was nearly \$0.85/MMBtu, or 17% higher than projected. This discrepancy is the primary cause for DWR's actual costs exceeding projections by 3.5%. Actual revenues also exceeded projections during the 2004 revenue requirement period. Revenue from customers was \$280 million higher than projected. Total revenue exceeded projections by 7.9%. Total revenues less expenses were \$191 million higher than projected, an amount equal to 3.9% of projected expenses. For a discussion of the treatment of net operating results in the establishment of subsequent-year revenue requirements, see "CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES - Substantive Considerations in Establishing Revenue Requirements - *Operating Account Balances.*"

### *2005 Revenue Requirement*

In September 2004, DWR published its Proposed Determination of Revenue Requirements for 2005 to start its administrative process under its Revenue Requirement Regulations. After reviewing comments, DWR revised and made its determination in November 2004 and submitted it to the CPUC for implementation. The November 2004 Determination of \$4.824 billion was found by DWR to be just and reasonable based on the administrative record. New information became available that changed DWR's projections of its revenue requirements for 2005. The new information included updated actual Electric Power Fund operating results through December 31, 2004; settlement agreements with El Paso Energy and Williams Energy Marketing & Trading; and natural gas price forecasts and related assumptions. As a result, DWR submitted a Revised 2005 Determination with the CPUC, reflecting a reduction of \$166 million to its 2005 revenue requirements. In April 2005, the CPUC allocated the Revised 2005 Determination among the IOU service areas, consistent with the allocation methodology adopted by the CPUC in December 2004. In June, 2005 the CPUC adopted a permanent methodology to allocate the DWR revenue requirement among the IOU service areas. This methodology covers the DWR revenue requirement from 2004 onward. Any inter-IOU adjustments required to previously adopted allocations will be reflected in the CPUC decision adopting an allocation of DWR's 2006 revenue requirement.

During the 2005 revenue requirement period (ending December 31, 2005), DWR has continued to experience actual fuel prices that exceed those projected in its Revised 2005 Determination. Upward pressures in the natural gas markets, which have been exacerbated by recent natural disasters in the U.S. Gulf Coast, have led DWR to re-forecast its current fuel price projections to account for these unforeseen effects. DWR's updated forecast, developed in September 2005, is reflected in DWR's Revised 2006 Determination, submitted to the CPUC in October 2005.

Through September 30, 2005, DWR has regularly experienced actual average monthly fuel prices that have exceeded \$6.50/MMBtu, a price that is more than \$0.50/MMBtu greater than the fuel price forecast underlying DWR's Revised 2005 Determination. This discrepancy is the primary cause for DWR's power costs exceeding related projections by 3.2%, through September 30, 2005. Differences between actual and forecasted contract dispatch have not contributed to this discrepancy, as total actual contract dispatch was within 0.8% of projections through August 31, 2005. Through September 30, 2005, actual revenue from customers was \$172 million less than projected, an amount equal to 0.1% of projected revenues. Total revenues less expenses were \$109 million less than projected, an amount equal to 3.6% of projected expenses. For a discussion of the treatment of net operating results in the establishment of subsequent-year revenue requirements, see "CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES - Substantive Considerations in Establishing Revenue Requirements - *Operating Account Balances.*"

## Revenue Requirement For 2006

In June 2005, DWR published its Proposed Determination of Revenue Requirements for 2006 to start its administrative process under its Revenue Requirement Regulations. In July 2005, new information became available that changed DWR's projections of its revenue requirements for 2006. The new information included revised amounts of direct access in the SCE service area, new information regarding natural gas hedges in its fuel price projections and updated investment return projections. As a result, DWR revised and submitted to the CPUC the 2006 Determination in August 2005, reflecting a 2006 revenue requirement of \$4.991 billion consisting of \$4.128 billion in Department Costs and \$0.863 billion in Bond Related Costs

Subsequent to the August 2005 Determination, new information became available to DWR, leading it to publish the Proposed Revised 2006 Determination in October 2005. The Proposed Revised 2006 Determination reflected operating results of the Electric Power Fund through September 30, 2005, the issuance of the Series 2005 Bonds to refinance certain Series 2002 Bonds as described herein, increases in natural gas prices, and natural gas hedges in place and planned by the IOUs through September 30, 2005. The proposed revisions resulted in an increase in DWR's total revenue requirement of \$375 million relative to the August 2005 Determination. This proposed increase was comprised of two components: a \$418 million increase in DWR's Power Charge revenue requirement; and a \$43 million reduction in DWR's Bond Charge revenue requirement. During the comment period related to its Proposed Revised 2006 Determination, no comments were received from interested persons. DWR submitted its Revised 2006 Determination to the CPUC on October 27, 2005, reflecting a 2006 revenue requirement of \$5.366 billion on a cash basis, consisting of \$4.546 billion in Department Costs and \$0.820 billion in Bond Related Costs.

Based on its Revised 2006 Determination, DWR projects that it will incur the following Department Costs during 2006: (a) \$4.888 billion for long-term power contract purchases (including fuel costs) to cover the net short requirement of customers; (b) \$36 million in administrative and general expenses, and; (c) \$(100) million in other net changes to Power Charge Accounts (including operating reserves). This projection results in a total revenue need of \$4.825 billion. Funds to meet these costs (in addition to changes to Power Charge Accounts balances) are projected to be provided from (x) \$235 million from DWR's share of surplus power sales revenues; (y) \$44 million of interest earned on Power Charge Account balances; and (z) \$4.546 billion of Power Charge Revenues from customers of the IOUs and DWR and the Power Charge component of the Cost Responsibility Surcharge.

DWR projects that it will incur the following Bond Related Costs during 2006: (a) \$898 million for debt service on the Bonds and related Qualified Swap payments, payments of credit enhancement and liquidity facilities charges, and costs relating to other financial instruments and servicing arrangements in connection with the Bonds, and (b) \$(16) million for changes to Bond Charge Account balances, resulting in total Bond Charge Account expenses of \$882 million. Amounts to meet these requirements are provided from (x) \$62 million in interest earned on Bond Charge Account balances, and (y) \$820 million of Revenues from Bond Charges (including the Bond Charge component of the Cost Responsibility Surcharge). There are no projected transfers to or from Power Charge Accounts.

In aggregate, DWR's total expenses are projected to be \$5.822 billion. Revenues from interest earned and other power sales are projected to be \$341 million, and net changes in fund balances are projected to be \$(116) million, resulting in combined customer revenue requirements of \$5.366 billion. See "THE DWR POWER SUPPLY PROGRAM – Summary of Operating Results." The 2006 Revenue Requirement Determination is expected to result in an increase in the average Power Charge.

The CPUC is scheduled to consider a decision allocating the Revised 2006 Determination at its December 1, 2005, meeting, which would establish Bond Charges and Power Charges for calendar year 2006. DWR cannot predict if the CPUC's decision on the Revised 2006 Determination will be challenged by any party.

## LITIGATION AND ADMINISTRATIVE PROCEEDINGS

No litigation is pending or threatened against DWR, nor is DWR a party in any administrative proceeding pending before any administrative body, nor is any administrative proceeding pending before DWR, which (i) seeks to restrain or enjoin the sale or delivery of the Series 2005 Bonds or the performance by DWR of the purchase contract for the Series 2005 Bonds, (ii) challenges the constitutionality, validity or enforceability of the Indenture, the pledge of the Trust Estate, the Rate Agreement or any other document or approval necessary to the issuance of the Series 2005 Bonds, (iii) challenges the existence, organization or powers of DWR to adopt, execute and deliver the Indenture or the Rate Agreement or perform DWR's obligations under the Indenture or under the Rate Agreement, or (iv) challenges the constitutionality or validity of the Act or the powers of DWR thereunder.

Certain pending legal and administrative proceedings involving DWR or affecting DWR's Power Supply Program are summarized below. See also "CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES" and "RISK FACTORS – Determination of Power Charges and Bond Charges; Possible Use of Amounts in the Bond Charge Collection Account to Pay Priority Contract Costs."

### **"Block Forward Contracts" Consolidated Actions**

In February 2001, during the state of emergency described under "POWER SUPPLY PROGRAM", Governor Davis, pursuant to the California Emergency Services Act, issued executive orders "commandeering" certain power purchase arrangements, referred to as "block forward contracts", that were pledged by PG&E and SCE as collateral for their respective obligations to the California Power Exchange (the "PX") market. DWR took delivery of and paid a total of \$350 million for energy delivered under the contracts. The issue of whether, to what extent, and to whom compensation is due as a result of the commandeering of the contracts is now before the Sacramento County Superior Court in a coordinated proceeding, *Inverse Condemnation Cases*, Judicial Council Coordination Proceeding No. 4203. The PX and 31 market participants have asserted claims totaling in excess of \$1 billion against the State as a result of the Governor's actions. The State contends that the Governor's "commandeering" of the block forward contracts was a legitimate exercise of police powers and that the State is not liable for damages occurring in the exercise of such powers nor for compensation for inverse condemnation. Alternatively, the State's view is that any damages suffered by any of the defendants should not include any contract value resulting from market prices reflecting market manipulation and that damage determinations must take into account payments made by DWR for energy received under the contracts and payments subsequently made and to be made by the IOUs to the PX to satisfy the obligations for which the block forward contracts served as collateral.

No trial date has been set. Should the Electric Power Fund be determined to be the source of moneys to pay any damages as a result of this litigation, those damages would be recoverable from ratepayers through future DWR revenue requirements.

### **California Refund Proceeding**

In July 2001, FERC initiated an administrative proceeding to calculate refunds for inflated prices in the CAISO and PX markets during 2000 and 2001. However, FERC ruled that DWR would not be entitled to approximately \$3.5 billion in refunds associated with DWR's approximately \$5 billion of short term purchases because DWR made those purchases bilaterally, not in the PX or CAISO markets. FERC's decision on this issue was appealed to the Ninth Circuit Court of Appeals, argued in April 2005, and a decision is pending.

Of the above \$5 billion in purchases, \$2.9 billion was imbalance energy which DWR sold to the CAISO at DWR's cost in order to meet the CAISO's emergency needs during 2001. DWR is treated in the FERC refund proceeding as a seller of that energy to CAISO, and in May 2004, FERC issued an order requiring DWR to pay refunds on the \$2.9 billion in "sales" to the CAISO. However, FERC also later ruled that, to the extent DWR could demonstrate that payment of the refunds would result in DWR's costs exceeding its revenues remaining

after payment of refunds, DWR could request FERC to reduce the refunds that would be owed on the \$2.9 billion. In September 2005, DWR made a cost recovery filing that DWR believes demonstrates that its costs exceeded its revenues from the imbalance energy sales, a demonstration that, if approved by FERC, would eliminate any refund amount DWR would otherwise be required to pay. In addition, even in the absence of cost justification, because DWR would be the primary recipient of the refunds FERC would be requiring DWR to pay, although the refund amount would total approximately \$2.2 billion on a gross basis, DWR would actually owe less than \$150 million on a net basis. Also in September 2005, the Ninth Circuit Court of Appeals ruled that FERC could not require governmental entities such as DWR to pay refunds. Accordingly, DWR has two possible methods of eliminating its potential refund liability: (1) the cost recovery filing it has made with FERC; and (2) the claim, based on the Ninth Circuit's ruling, that FERC has no legal authority to order DWR to pay refunds.

## **RISK FACTORS**

This section of the Official Statement describes certain risk factors that may affect the payment of and security for the Bonds. Potential investors should consider, among other matters, these risk factors in connection with any purchase of the Series 2005 Bonds. The following discussion is not meant to present an exhaustive list of the risks associated with the purchase of any Series 2005 Bonds (and other considerations that may be relevant to particular investors) and does not necessarily reflect the relative importance of the various risks. Potential investors are advised to consider the following factors, along with all other information contained or incorporated by reference in this Official Statement, in evaluating whether to purchase the Series 2005 Bonds.

### **Certain Risks Associated With DWR's Power Supply Program**

DWR's purchases and sales of electricity will likely end under the Power Supply Program before the Bonds are retired. See "THE DWR POWER SUPPLY PROGRAM – Power Purchase Contracts." Bond Charges are to be the primary source of money to pay debt service on the Bonds, and must be imposed by the CPUC whether or not DWR continues to purchase or sell electricity under the Power Supply Program. See "RATE COVENANTS." Certain risks associated with the Power Supply Program are discussed in the following paragraphs.

#### *Failure of Assumptions in Calculating Revenue Requirements*

As explained above under "CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES – Substantive Considerations in Establishing Revenue Requirements" DWR makes a number of assumptions in determining its revenue requirements from time to time. A failure of any such assumptions could result in the insufficiency of Bond Charges to pay Bond Related Costs when due or the insufficiency of Power Charges to pay Department Costs, including Priority Long-Term Power Contract Costs, when due. In particular, the failure of assumptions regarding natural gas costs (and a resulting failure of assumptions regarding power purchase costs, which are in part dependent on natural gas costs), coupled with a failure to adjust Power Charges quickly enough, could lead to such a cash flow insufficiency. In the event of such an insufficiency and the depletion of the Operating Account and the Operating Reserve Account, the payment of debt service on the Bonds when due may be dependent on the ability of DWR to obtain increases in Bond Charges or Power Charges, the adequacy of minimum balances in the Bond Charge Collection Account, the Bond Charge Payment Account and the Debt Service Reserve Account, or both. For a discussion of minimum balances in funds and accounts, see "SECURITY FOR THE BONDS." For a discussion of the process to obtain revised Bond Charges and Power Charges, see "CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES."

#### *Priority Long-Term Power Contracts*

As explained below under "Determination of Power Charges and Bond Charges; Possible Use of Amounts in the Bond Charge Collection Account to Pay Priority Contract Costs," the use of amounts in the Bond Charge Collection Account (including Bond Charge Revenues) for the payment of debt service on the Bonds and other Bond Related Costs when due is subject to the possible prior use of such amounts to pay amounts due under

DWR's Priority Long-Term Power Contracts (including any termination payments which may be payable by DWR). So long as DWR continues to bear financial responsibility for the Priority Long-Term Contracts, the Power Supply Program remains subject to this risk. If amounts in the Bond Charge Collection Account are used to pay Priority Long-Term Power Contract Costs, the payment of debt service on the Bonds when due may be dependent on the ability of DWR to obtain increases in Bond Charges or Power Charges, the adequacy of minimum balances in the Bond Charge Collection Account, Bond Charge Payment Account and the Debt Service Reserve Account, or both. For a discussion of minimum balances in funds and accounts, see "SECURITY FOR THE BONDS". For a discussion of the process to obtain revised Bond Charges and Power Charges, see "CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES."

### **Determination of Power Charges and Bond Charges; Possible Use of Amounts in the Bond Charge Collection Account to Pay Priority Contract Costs**

#### *Legal Challenges to Revenue Requirement Determinations*

DWR's Bond Related Costs (including debt service on the Bonds) are payable primarily from Bond Charges, while DWR's Power Supply Program operating expenses (including Priority Contract Costs) are payable primarily from Power Charges. Bond Charges and Power Charges are established through an administrative process and, as part of that process, are subject to administrative and legal challenges by third parties. DWR believes that the possibility is remote that DWR would be prevented, as a result of any such challenges and the other circumstances described below, from paying debt service on the Bonds and other Bond Related Costs when due. There can be no guarantee, however, that such circumstances would not materially and adversely affect the ability of DWR to pay debt service on the Bonds and other Bond Related Costs when due.

In prior DWR revenue requirement proceedings, certain of the IOUs and other parties have asserted, among other things, that DWR's administrative revenue requirement process did not comply with the requirements of the DWR Revenue Requirement Regulations, that DWR did not provide adequate support and justification for its determinations that its revenue requirements are "just and reasonable", and that certain of DWR's costs included in its revenue requirements are not "just and reasonable." In the future, the IOUs or other parties could again challenge DWR's revenue requirements and its "just and reasonable" determinations.

DWR's Priority Long-Term Power Contracts require that payments by DWR under those contracts (including any termination payments that may be payable by DWR) are payable prior to payment of debt service on the Bonds. See "SECURITY FOR THE BONDS – Priority Long-Term Power Contracts." Accordingly, in the Indenture, DWR's pledge and assignment of its revenues from Bond Charges (and other funds available in the Bond Charge Collection Account) are subject to possible prior use for payment of Priority Contract Costs, as explained under "SECURITY FOR THE BONDS." The use of amounts on deposit in the Bond Charge Collection Account to pay Priority Contract Costs could occur, particularly if judicial review of DWR's determination of its revenue requirements were to result in DWR being prevented from including in its Retail Revenue Requirement all of its actual power costs or other operating expenses because any such costs or expenses were held not to be "just and reasonable." See "CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES – DWR Actions to Establish Revenue Requirements."

In the event that Power Charges imposed by the CPUC based on DWR's Retail Revenue Requirements and other amounts on deposit in the Operating Account are not sufficient to recover all of DWR's Priority Contract Costs, the Indenture requires that amounts be transferred from the Operating Reserve Account to pay Priority Contract Costs. See "SECURITY FOR THE BONDS – Operating Account" and "– Operating Reserve Account."

If a court were to determine that any of DWR's Priority Contract Costs were not "just and reasonable," DWR were prevented from including such Priority Contract Costs in its Retail Revenue Requirements and DWR were nevertheless obligated to pay such Priority Contract Costs, amounts in the Operating Account and Operating Reserve Account may be insufficient to pay such Priority Contract Costs and, as a result, the Indenture would

require amounts to be transferred from the Bond Charge Collection Account to pay such Priority Contract Costs. See “SECURITY FOR THE BONDS – Accounts and Flow of Funds under the Indenture.”

*Application and Enforcement of CPUC’s Bond Charge Rate Covenant*

Under the Rate Agreement, the CPUC has covenanted to calculate, revise and impose from time to time, Bond Charges sufficient to provide moneys so that amounts available for deposit in the Bond Charge Payment Account under the Indenture from time to time, together with amounts on deposit in the Bond Charge Payment Account, are at all times sufficient to pay or provide for the payment of debt service on the Bonds and all other Bond Related Costs when due in accordance with the Indenture and other financing documents (the “CPUC’s Bond Charge Rate Covenant”). The Rate Agreement provides that this covenant shall have the force and effect of a “financing order” under the California Public Utilities Code and shall be irrevocable and enforceable in accordance with its terms, including, without limitation, in circumstances in which DWR has breached its obligations under the Rate Agreement or in respect of the Financing Documents. The CPUC decision adopting the Rate Agreement is final and unappealable under California law. Under the California Public Utilities Code, a “financing order” is binding upon the CPUC as it may be constituted from time to time, and the CPUC shall have no authority to rescind, alter or amend its obligations thereunder. Under the Act, the rights, powers and duties of the CPUC may not be diminished or impaired in a manner that would adversely affect the interests or rights of Bondholders. See “SECURITY FOR THE BONDS – Bond Related Costs” and “Rate Covenants” and “CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES – Rate Agreement.”

Under the Indenture, DWR is obligated to “take such actions as shall be necessary and available to enforce all of the obligations required to be performed under [the] Rate Agreement by the [CPUC].” The Indenture further provides that DWR “shall commence such proceedings and take such other actions as may be necessary to assure compliance by the [CPUC] with the [CPUC’s Bond Charge Rate Covenant] in the event that Bond Charge Revenues are applied to the payment of Priority Contract Costs for any reason.” See APPENDIX C - “SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE – Protection of Security.”

However, any case involving interpretation or enforcement of the Rate Agreement would be the first case considering certain of the relevant legal questions under California law. Despite the terms of the Rate Agreement, it is possible that a court might, if asked to order the CPUC to comply with the CPUC’s Bond Charge Rate Covenant, decline to give effect to the Rate Agreement in accordance with its literal terms if the effect of so doing would be to permit the recovery by DWR of power or bond costs that had been determined previously (in a legal challenge against DWR) not to be “just and reasonable.” Any such court action could adversely affect the amount of revenues, including Bond Charge Revenues, available for the payment of the Bonds.

Transfer of amounts from the Bond Charge Collection Account to pay Priority Contract Costs could, in the absence of a sufficient increase in Bond Charges, result in a shortage of funds available in the Bond Charge Collection Account for transfer to the Bond Charge Payment Account for payment of debt service on the Bonds. Pursuant to the Indenture, if such a shortage occurred, any amounts available in the Debt Service Reserve Account would be used to pay debt service on the Bonds. There can be no assurance that the amount in the Debt Service Reserve Account would be sufficient in all such events to pay debt service on the Bonds and other Bond Related Costs. See “SECURITY FOR THE BONDS – Debt Service Reserve Account.”

*DWR’s Assessment of these Risks*

DWR believes, in light of (i) its determination that the costs included in its various revenue requirements are “just and reasonable”, (ii) the provisions of the Act to the effect that DWR is entitled to recover, as a revenue requirement, amounts and at the times necessary to enable it to pay the costs listed in the Act, including debt service on bonds, power purchase costs, reserves determined by DWR to be appropriate and DWR administrative costs, (iii) the provisions of the Revenue Requirement Regulations incorporating those provisions of the Act into the factors to be considered in determining whether DWR’s revenue requirements are just and reasonable, (iv) the operating reserves established under the Indenture, (v) the CPUC’s Bond Charge Rate Covenant, and (vi) the debt

service reserves established under the Indenture, that the possibility is remote that DWR would be prevented, as a result of the circumstances described above, from paying debt service on the Bonds and other Bond Related Costs when due. There can be no guarantee, however, that a court action as described above would not materially and adversely affect the ability of DWR to pay debt service on the Bonds and other Bond Related Costs when due.

### **Collection of Bond Charges and Power Charges**

DWR does not have the personnel, equipment or customer information necessary to bill and collect Bond Charges and Power Charges from customers or to transmit and distribute power to customers (defined above as the “IOU Services”) as described under “SERVICING ARRANGEMENTS” and is dependent upon the IOUs to provide the IOU Services. DWR believes there are no alternate servicers currently available, that alternate servicers may not be available in the future, and that it may not be feasible for any such servicers to perform effectively the IOU Services. Moreover, even if an acceptable alternate servicer were identified, the transfer of responsibilities under a Servicing Arrangement also would require regulatory approval from the CPUC, which might not be granted or which could result in additional delay. Accordingly, if one or more IOUs fails to perform or is excused by a court from performing under the Servicing Arrangements, DWR could experience a substantial delay in obtaining, or be unable to obtain, replacement services from an alternate source. A bankruptcy of an IOU could also lead to termination of its Servicing Agreement (see “Bankruptcy Risks – Potential Rejection of Servicing Agreements or Other Disruption of Servicing Arrangements” below). Any such problems could adversely affect the cash flow for the Power Supply Program and, ultimately, the ability of DWR to pay debt service on the Bonds. See “SECURITY FOR THE BONDS – Accounts and Flow of Funds under the Indenture” for information concerning reserve accounts established and required to be maintained under the Indenture to mitigate the impact of any cash flow shortfalls.

### **Bankruptcy Risks**

#### *Effect of IOU Bankruptcy on Remittance to DWR of Revenues From Bond Charges and Power Charges*

DWR believes that all revenues from Bond Charges and Power Charges are the property of DWR and held in trust for DWR by the IOUs for purposes of California law and federal bankruptcy law. The Rate Agreement and the Act provide that Bond Charges and Power Charges are the property of DWR for all purposes under California law. The CPUC order authorizing the Rate Agreement is final and unappealable under California law.

It is possible that a bankrupt IOU could claim that the revenues collected by it for Bond Charges and Power Charges are property of its bankruptcy estate and are not held in trust for the benefit of DWR and could refuse to remit such revenues to DWR. PG&E, which emerged from Chapter 11 bankruptcy protection in 2003, did not make such a claim in its bankruptcy proceeding. Nonetheless, an IOU could assert an equitable and legal interest in the Power Charges and the Bond Charges and DWR can give no assurance as to whether or how long DWR or its creditors would be prevented from exercising their rights under relevant documents until the validity of such assertions are finally determined. DWR could be subject to a temporary restraining order, preliminary injunction or other interim relief affording delay pending a determination of the merits of an IOU’s assertion. DWR revenues that are in possession of the IOU at the time of commencement of a bankruptcy case that have been commingled with property of the IOU could be treated as part of the IOU’s bankruptcy estate. Finally, if revenues from Bond Charges and Power Charges were ultimately to be determined by a bankruptcy court to be property of an IOU’s bankruptcy estate and not held in trust on behalf of DWR, DWR’s efforts to collect such revenues might result in costly and time-consuming litigation.

#### *Potential Rejection of or Other Disruption of Servicing Arrangements*

As explained above under “Collection of Bond Charges and Power Charges,” DWR’s ability to collect Bond Charges and Power Charges is dependent on the IOUs acting in their capacities as servicers under the Servicing Arrangements. In the event of bankruptcy proceedings with respect to an IOU, the bankrupt IOU could

move to reject its Servicing Agreement pursuant to the Bankruptcy Code. This rejection would require the approval of the bankruptcy court, and DWR and the CPUC could raise objections to such rejection. A successful rejection of the IOU's Servicing Agreement could result in DWR and the CPUC being unable to require the IOU to continue to collect and remit Bond Charges and Power Charges to DWR (or to provide any other services) under the Servicing Agreement after the date of rejection. However, the CPUC is required under the Act to order the IOU to provide IOU Services upon request of DWR in the event the IOU's Servicing Agreement is rejected by an IOU in bankruptcy, thus replacing the Servicing Agreement with a servicing order similar to the servicing order in effect for PG&E. Although a bankrupt IOU subjected to a servicing order in this manner could challenge that order, either in its bankruptcy proceedings or under State law, DWR believes that the possibility is remote that such challenge would be successful or that the billing, collection and remittance of Bond Charges and Power Charges would be materially disrupted by such challenge.

A bankrupt IOU subject to a servicing order could seek relief from the servicing order in the bankruptcy court at any time and the bankruptcy court could grant such relief. The bankruptcy court could temporarily or permanently enjoin the CPUC from enforcing the order if the court determined that the order violated the automatic stay or other provisions of the Bankruptcy Code or could void the order altogether if it determined that the order was preempted by or otherwise violated the Bankruptcy Code or other provisions of federal law.

### **Uncertainties Relating to Electric Industry and Markets**

The electric industry and markets in the western states region, including the governing laws and regulations, continue to undergo significant changes. Some of the recent changes include restructuring of regulation of the electric industry, the abandonment or partial abandonment of restructuring changes and attempts to construct substantial amounts of new generation facilities (mostly gas-fired). In addition, effects of compliance with rapidly changing environmental, safety, licensing, regulatory and legislative requirements for the IOUs, the power production facilities and other entities involved with the Power Supply Program and shifts in the availability of different fuels (including natural gas) may also compound the uncertainties relating to electric industry and markets. There might also be significant volatility in energy prices due to a wide variety of factors that affect both the supply and demand for electric energy in the western United States. Future changes in the electric industry and markets could have an adverse effect on DWR, its Power Supply Program or its ability to pay debt service on the Bonds.

### **Departing Load and Community Choice Aggregation**

Unlike direct access, the growth of municipal departing load and Community Choice Aggregation is not expressly limited by CPUC decision or the Act. However, the CPUC has imposed a Cost Responsibility Surcharge on certain classes of self-generation and municipal departing load customers, similar to the Cost Responsibility Surcharge imposed on direct access load. Although the IOUs are collecting a Cost Responsibility Surcharge from self-generation departing load customers, the CPUC is still conducting a proceeding to establish the procedures for billing and collecting a Cost Responsibility Surcharge from municipal departing load customers. See "CALCULATION AND IMPOSITION OF BOND CHARGES AND POWER CHARGES."

In 2007 and beyond, the amount of Community Choice Aggregation could increase significantly. While the permitting process and the relatively high capital costs of installing micro-turbines or other on-site generation is expected to curb the growth of self-generation, and municipal departing load is expected to follow historical growth trends, the opportunity for whole communities to aggregate load and procure power at competitive prices under Community Choice Aggregation could lead to substantial reductions in bundled sales volumes. DWR is closely monitoring CPUC proceedings establishing processes, procedures, and a Cost Responsibility Surcharge for Community Choice Aggregation loads.

## **Uncertainties Relating to Government Action**

### *Possible State Legislation or Action*

The Act states that while any obligations of DWR incurred under the Act remain outstanding and are not fully performed or discharged, the rights, powers, duties, and existence of DWR and the CPUC shall not be diminished or impaired in any manner that will affect adversely the interests and rights of the holders of or parties to such obligations. This provision of the Act affords limited but not complete protection for the owners of Bonds against amendment of the Act and the Rate Agreement by legislation, action by the Governor under the Emergency Services Act, or voter initiative. Under California law, the electorate has the right, through its initiative powers, to propose statutes as well as amendments to the California Constitution. Generally, any matter that is a proper subject of legislation can become the subject of an initiative and be submitted to voters at the next general election.

Owners of the Bonds are entitled to the benefit of the prohibitions in Article I, section 10, of the Constitution of the United States (the “Contract Clause”) against a state’s impairment of the obligation of contracts. The prohibition, although not absolute, is particularly strong when applied to the State’s attempt to evade its own obligations. Similar protections are afforded by Article I, Section 9, of the California Constitution.

Based on the U.S. Supreme Court’s standard of review for Contract Clause challenges in *Energy Reserves Group, Inc. v. Kansas Power & Light Co.*, the State must justify the exercise of its inherent police power to safeguard the vital interests of its people before the State may alter the Act, the Indenture or the Rate Agreement in a manner that would substantially impair the rights of the Owners of the Bonds. However, to justify the enactment by the State of legislation that substantially impairs the contractual rights of the Bondholders, the State must demonstrate a significant and legitimate public purpose, such as the remedying of a broad and general social or economic problem. In the event that the State demonstrates a significant and legitimate public purpose for such legislation, the State must also show that the impairment of the Bondholders’ rights is reasonable and appropriate to the public purpose justifying the legislation’s adoption.

There have been cases in which legislative concerns with the burden of taxation or governmental charges have led to adoption of legislation reducing, eliminating or imposing a moratorium on taxes or charges that supported bonds or other contractual obligations entered into by public instrumentalities. Such concerns have not been considered by the courts to provide sufficient justification for a substantial impairment of the security for such bonds and other contractual obligations and, in several cases, have held such legislation as an unconstitutional impairment of contract.

Nonetheless, a repeal, amendment or suspension of, or moratorium on, certain provisions of the Act, the Indenture or the Rate Agreement could be sought or adopted, even if such repeal, amendment, suspension or moratorium might constitute a violation of the Indenture or the Rate Agreement. Additionally, the State might take, or refuse to take, or cause DWR or the CPUC to take, or refuse to take, action required of DWR under the Indenture or of DWR or the CPUC under the Rate Agreement, even if such action or inaction might constitute a violation of the Indenture or the Rate Agreement. Costly and time-consuming litigation might ensue which might adversely affect the price and liquidity of the Bonds and the timely payment thereof. Moreover, the outcome of such litigation might be adverse to the interests of owners of the Bonds, and accordingly, owners of the Bonds could experience a decline in value of their investment as a result of any such event.

### *Possible Federal Legislation or Action*

Congress could enact new legislation or FERC could adopt new regulations with respect to the electric industry and markets in the western states region that could adversely affect the payment of debt service on the Bonds. For example, FERC could approve new rules that increase or shift a greater portion of the costs of transmitting the power sold by DWR to retail customers. Such a change could adversely impact the cash flow for the Power Supply Program and possibly requiring the temporary use of Bond Charge Revenues to pay amounts

due under DWR's Priority Long-Term Power Contracts (as described above under "Determination of Power Charges and Bond Charges; Possible Use of Amounts in the Bond Charge Collection Account to Pay Priority Contract Costs") instead of debt service on the Bonds.

The provisions of the United States Constitution discussed under "Possible State Legislation or Action" above, affording protection against contract impairments by State action to the owners of the Bonds, do not apply to the federal government. While the Due Process Clause of the United States Constitution protects against certain contract impairments by the federal government, the Due Process Clause may not adequately protect owners of the Bonds against adverse effects of federal legislation or action.

## **Uncertainty of Projections and Assumptions**

### *General*

This Official Statement includes projections that are dependent upon projections and assumptions about, among other things, system transmission operations and capacity, weather trends, generation capacity, fuel costs, spot market prices for energy and energy consumption. In addition, the determination of DWR's revenue requirements involves the making of similar projections and assumptions. These projections and assumptions are subject to risks and uncertainties, including risks and uncertainties outside the control of DWR. The accuracy of such projections and assumptions is subject to known and unknown risks, uncertainties and other factors that may cause actual results, performance or achievements to be materially different from such projections and assumptions. Differences in actual results from projections may be difficult to recognize in a timely manner for purposes such as the adjustment of DWR's revenue requirements. Material differences could result in a variety of unpredictable consequences which could adversely affect the Power Supply Program and the ability of DWR to pay debt service on the Bonds.

This Official Statement also assumes future approvals and other actions by a number of governmental entities that regulate the energy industry, including the CPUC, FERC and the California Energy Commission. If such approvals or other actions do not occur or do not occur on a timely basis, the ability of DWR to make timely payment of debt service on the Bonds could be materially and adversely affected. In addition, DWR must act in a timely manner to revise its revenue requirements in order to conform to the assumptions made in this Official Statement.

### *CPUC Disclaimer*

The CPUC makes no representation as to the accuracy or completeness of this Official Statement, including any forward-looking statements or projections contained in this Official Statement and any description in this Official Statement of litigation involving or affecting the CPUC. Any statements regarding such litigation do not necessarily represent the CPUC's view of such litigation or any position in such litigation. In addition, while CPUC staff may have assisted in the preparation of certain sections of this Official Statement, the CPUC can only take positions through formal action and has not taken any such action or approved this Official Statement. The CPUC is an independent five member body that must act by an affirmative vote of a majority of its members and, as a result, the CPUC can only indicate its views in formal decisions or other formal actions. In addition, the CPUC is an independent body not subject to the control of DWR and may take positions in the future different from DWR in litigation, or other matters described in this Official Statement. As a result, statements in this Official Statement regarding electricity markets and regulation, and DWR's views of the CPUC's role or DWR's role in such markets and regulation, do not necessarily represent the views, opinions or beliefs of the CPUC and should not be construed as such by any recipient of this Official Statement.

## **Limited Obligations**

The Bonds shall not be or be deemed to constitute a debt or liability of the State or of any political subdivision thereof or a pledge of the faith and credit of the State or of any such political subdivision, other than

DWR to the extent provided in the Indenture. The Bonds shall be payable solely from the funds pledged therefor pursuant to the Indenture. The Bonds shall not directly or indirectly or contingently obligate the State or any political subdivision thereof to levy or to pledge any form of taxation whatever therefor or to make any appropriation for their payment.

## **FINANCIAL STATEMENTS**

The financial statements of the Department of Water Resources Electric Power Fund at June 30, 2005 and June 30, 2004 appearing in Appendix A to this Official Statement have been audited by PricewaterhouseCoopers LLP (PwC), independent accountants, as set forth in their report appearing in Appendix A.

## **RATINGS**

Moody's Investors Service ("Moody's"), Standard & Poor's Ratings Group, a division of The McGraw-Hill Companies, Inc. ("Standard & Poor's") and Fitch, Inc., doing business as Fitch Ratings, have assigned or are expected to assign to the Series 2005 Bonds the respective short- and long-term ratings set forth in the Series Description pages following the cover of this Official Statement. Such ratings are based on the delivery of the applicable letters of credit, liquidity facilities and bond insurance policies, as set forth in the Series Descriptions, and the satisfaction of certain other conditions. Moody's, Standard & Poor's and Fitch Ratings have also assigned to the Series 2005 Bonds underlying long-term ratings of "A2," "A-" and "A," respectively. An explanation of the significance of these ratings may be obtained from Moody's at 99 Church Street, New York, New York 10007, from Standard & Poor's at 55 Water Street, New York, New York 10041 and from Fitch Ratings at One State Street Plaza, New York, New York 10004. Such ratings reflect only the views of the rating agencies.

Generally, rating agencies base their ratings on such information and materials and on investigations, studies and assumptions made by the rating agencies themselves. There is no assurance that the ratings mentioned above will remain in effect for any given period of time or that the ratings might not be lowered or withdrawn entirely by the rating agencies, if in their judgment circumstances so warrant. DWR and the Underwriters have undertaken no responsibility to oppose any such proposed revision or withdrawal. DWR has agreed to notify the Municipal Securities Rulemaking Board or each Nationally Recognized Municipal Securities Information Repository and the State Repository, if any, of any change in the ratings of the Series 2005 Bonds. See "CONTINUING DISCLOSURE" herein. Any such downward change in or withdrawal of the ratings might have an adverse effect on the market price or marketability of the Series 2005 Bonds.

## **UNDERWRITING**

The Series 2005 Bonds will be purchased by an underwriting group represented by J.P. Morgan Securities Inc. (collectively called the "Underwriters") from the State Treasurer, who is authorized pursuant to the laws of the State to sell the Series 2005 Bonds on behalf of DWR. The Underwriters have agreed to purchase the Series 2005 Bonds for the principal amount thereof less an underwriting discount of \$2,495,386.56. The purchase contract pursuant to which the Series 2005 Bonds are being sold provides that the Underwriters will purchase all of the Series 2005 Bonds if any are purchased. The obligation to make such purchase will be subject to certain terms and conditions set forth in such purchase contract, the approval of certain legal matters by counsel and certain other conditions.

## **FINANCIAL ADVISOR**

Montague DeRose and Associates, LLC served as financial advisor to DWR in connection with the Series 2005 Bonds.

## **APPROVAL OF LEGAL MATTERS**

The issuance of the Series 2005 Bonds is subject to the approving opinions of the Honorable Bill Lockyer, Attorney General of the State, and Hawkins Delafield & Wood LLP, Bond Counsel to DWR. The proposed forms of such opinions are set forth in Appendix E and Appendix F to this Official Statement. Certain legal matters will be passed upon by: Nancy Saracino, Chief Counsel to DWR; Orrick, Herrington & Sutcliffe LLP, disclosure and special counsel to DWR; Randolph L. Wu, General Counsel to the CPUC; Paul, Weiss, Rifkind, Wharton & Garrison LLP, Special Counsel to the CPUC; Nixon Peabody LLP, counsel to the Underwriters; and White & Case LLP, counsel to JPMorgan Chase Bank, as Administrative Agent.

## **RELATIONSHIPS**

The Power Supply Program and related activities, including the sale of Bonds, has been made possible, in part, by hiring underwriters, financial advisors, consultants and lawyers to assist and advise DWR. Many of the firms and individuals involved in this effort have prior or ongoing relationships with the IOUs, other investor-owned utilities, public power utilities and other businesses that contract or compete with DWR or contract with the State and other State agencies or that may do so in the future. DWR has required disclosure of, and has taken into account, these relationships and has determined it to be in the best interests of DWR to continue to work with these firms and individuals.

In addition, in the ordinary course of sales, trading, brokerage and financing activities, certain of the Underwriters may at any time hold long or short positions, and may trade or otherwise effect transactions, for their own accounts or the accounts of customers, in debt or equity securities or senior loans, as applicable, of DWR, the State of California, other State agencies, the IOUs, power suppliers, municipal utilities and other participants in the electric power industry. In connection with these activities and the provision of other services, certain of the Underwriters may be or become creditors of such entities. All of the Underwriters currently serve as remarketing agents for variable rate obligations issued by DWR, the State of California and other State agencies.

## **TAX MATTERS**

In the opinion of Hawkins Delafield & Wood LLP, Bond Counsel to DWR with respect to this financing, under existing statutes and court decisions and assuming continuing compliance with certain tax covenants described herein, (i) interest on the Series 2005 Bonds is excluded from gross income for federal income tax purposes pursuant to Section 103 of the Internal Revenue Code of 1986, as amended (the "Code"), and (ii) interest on the Series 2005 Bonds is not treated as a preference item in calculating the alternative minimum tax imposed on individuals and corporations under the Code; such interest, however, is included in the adjusted current earnings of certain corporations for purposes of calculating the alternative minimum tax imposed on such corporations. In rendering its opinion, Bond Counsel has relied on certain representations, certifications of fact, and statements of reasonable expectations made by DWR in connection with the Series 2005 Bonds, and Bond Counsel has assumed compliance by DWR with certain ongoing covenants to comply with applicable requirements of the Code to assure the exclusion of interest on the Series 2005 Bonds from gross income under Section 103 of the Code.

In addition, in the opinion of Bond Counsel to DWR with respect to this financing, under existing statutes, interest on the Series 2005 Bonds is exempt from State of California personal income taxes.

Bond Counsel expresses no opinion regarding any other federal or state tax consequences with respect to the Series 2005 Bonds. Bond Counsel renders its opinion under existing statutes and court decisions as of the issue date, and assumes no obligation to update its opinion after the issue date to reflect any future action, fact or circumstance, or change in law or interpretation, or otherwise. Bond Counsel expresses no opinion on the effect of any action hereafter taken or not taken in reliance upon an opinion of other counsel on the exclusion from gross income for federal income tax purposes of interest on the Series 2005 Bonds, or under state and local tax law.

## **Certain Ongoing Federal Tax Requirements and Covenants**

The Code establishes certain ongoing requirements that must be met subsequent to the issuance of the Series 2005 Bonds in order that interest on the Series 2005 Bonds be and remain excluded from gross income under Section 103 of the Code. These requirements include, but are not limited to, requirements relating to use and expenditure of gross proceeds of the Series 2005 Bonds, yield and other restrictions on investments of gross proceeds, and the arbitrage rebate requirement that certain excess earnings on gross proceeds be rebated to the federal government. Noncompliance with such requirements may cause interest on the Series 2005 Bonds to become included in gross income for federal income tax purposes retroactive to their issue date, irrespective of the date on which such noncompliance occurs or is discovered. DWR has covenanted to comply with certain applicable requirements of the Code to assure the exclusion of interest on the Series 2005 Bonds from gross income under Section 103 of the Code.

## **Certain Collateral Federal Tax Consequences**

The following is a brief discussion of certain collateral federal income tax matters with respect to the Series 2005 Bonds. It does not purport to address all aspects of federal taxation that may be relevant to a particular owner of a Bond. Prospective investors, particularly those who may be subject to special rules, are advised to consult their own tax advisors regarding the federal tax consequences of owning and disposing of the Series 2005 Bonds.

Prospective owners of the Series 2005 Bonds should be aware that the ownership of such obligations may result in collateral federal income tax consequences to various categories of persons, such as corporations (including S corporations and foreign corporations), financial institutions, property and casualty and life insurance companies, individual recipients of Social Security and railroad retirement benefits, individuals otherwise eligible for the earned income tax credit, and taxpayers deemed to have incurred or continued indebtedness to purchase or carry obligations the interest on which is not included in gross income for federal income tax purposes. Interest on the Series 2005 Bonds may be taken into account in determining the tax liability of foreign corporations subject to the branch profits tax imposed by Section 884 of the Code.

Legislation affecting municipal bonds is regularly under consideration by the United States Congress. Legislation enacted or proposed after the date of issuance of the Series 2005 Bonds could have an adverse effect on the tax exempt status or market price of the Series 2005 Bonds.

## **VERIFICATION**

Causey Demgen & Moore Inc. has verified the accuracy of the mathematical computation of the adequacy of the amounts deposited with the Treasurer in the Escrow Fund established for the Refunded Bonds to provide for the optional redemption of such Refunded Bonds. See "PLAN OF REFUNDING."

## **CONTINUING DISCLOSURE**

DWR will covenant for the benefit of the holders and beneficial owners of the Series 2005 Bonds to provide certain financial information and operating data relating to DWR (the "Annual Report") by not later than 270 days following the end of DWR's fiscal year (which ends June 30) and to provide notices of the occurrence of certain enumerated events, if material. The Annual Report will be filed by DWR with each nationally recognized municipal securities information repository certified by the Securities and Exchange Commission (the "Repositories"). The notices of material events will be filed by DWR with the Municipal Securities Rulemaking Board or the Repositories. The specific nature of the information to be contained in the Annual Report or the notices of material events is included in the form of Continuing Disclosure Certificate attached hereto in APPENDIX H - "FORM OF CONTINUING DISCLOSURE CERTIFICATE."



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**APPENDIX A**

**AUDITED FINANCIAL STATEMENTS OF THE ELECTRIC POWER FUND FOR THE YEARS  
ENDED JUNE 30, 2005 AND 2004 AND REPORT OF INDEPENDENT AUDITORS**

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# Department of Water Resources Electric Power Fund Financial Statements

For the years ended June 30, 2005 and 2004



**Department of Water Resources Electric Power Fund  
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## Report of Independent Auditors

The Director of the State of California  
Department of Water Resources

In our opinion, the accompanying statements of net assets and the related statements of revenues, expenses and changes in net assets and of cash flows present fairly, in all material respects, the financial position of the Department of Water Resources Electric Power Fund (the Fund), a component unit of the State of California, at June 30, 2005 and 2004, and its changes in financial position and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Fund's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 2, the financial statements of the Fund, are intended to present the financial position, and the changes in financial position and cash flows, where applicable, of only that portion of the business-type activities and major funds of the State of California that is attributable to the transactions of the Fund. They do not purport to, and do not, present fairly the financial position of the State of California as of June 30, 2005 and 2004, and the changes in its financial position and its cash flows, where applicable, for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 31, 2005, on our consideration of the Fund's internal control over financial reporting and on our tests of its compliance with laws, regulations, contracts and grant agreements and other matters for the year ended June 30, 2005. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The Management's Discussion and Analysis presented on pages 3 through 11 are 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 supplementary information. However, we did not audit the information and express no opinion on it.

*Primatichuk Cooper LLP*

October 31, 2005

# Department of Water Resources Electric Power Fund Management's Discussion and Analysis

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## USING THIS REPORT

This discussion and analysis is designed to assist the reader in focusing on significant financial issues and activities and to identify any significant changes in financial position of the Department of Water Resources Electric Power Fund (the Fund), which is administered by the California Department of Water Resources (DWR). Readers are encouraged to consider the information presented in conjunction with the financial statements as a whole, which follows *Management's Discussion and Analysis*. This discussion and analysis and the financial statements do not relate to DWR's other governmental and proprietary funds.

The basic financial statements include three required statements, which provide different views of the Fund. They are: the statement of net assets, the statement of revenues, expenses and changes in net assets, and the statement of cash flows. These statements provide current and long-term information about the Fund and its activities. These financial statements report information using accounting methods similar (although not identical) to those used by private sector companies. The statement of net assets includes all assets and liabilities as of the year-end date. The statement of revenues, expenses and changes in net assets presents all of the current year's revenues, expenses, and changes in net assets. The statement of cash flows reports cash receipts, disbursements and the net change in cash resulting from three principal types of activities: operating, financing and investing. In order for the basic financial statements to be complete, they must be accompanied by a complete set of footnotes. The notes to the financial statements provide disclosures which are required to conform with generally accepted accounting principles. The Fund is required to follow accounting standards promulgated by the Governmental Accounting Standards Board.

## HISTORY AND FINANCING

The Fund was established in January 2001 through legislation to assist mitigation of the effects of a statewide energy supply emergency. DWR has the authority to secure and retain title to power for resale to end use customers of the State's investor owned utilities (IOUs) under power supply contracts entered into prior to January 1, 2003. DWR is entitled to recover revenue requirements for authorized activities, including but not limited to debt service, the costs of power purchases, administrative expenses and reserves.

In November 2002, DWR completed the issuance of \$11.3 billion in revenue bonds. The proceeds of the bond issues, along with the cash and investments in the Fund, were used to repay the outstanding balance of a \$4.3 billion term loan from a financial consortium, repay \$6.2 billion in advances from the State's General Fund with interest, and establish separate accounts in the Fund as required by the Bond Indenture.

On January 1, 2003, DWR transitioned total responsibility for the purchase of short-term power (residual net short) to the IOUs. DWR also transferred the scheduling, dispatch, and certain other administrative functions for the long-term contracts to the IOUs. However, DWR retains the legal and financial responsibility for the contracts until such time as there is complete assignment of the contracts to the IOUs and release of DWR.

While responsible for procurement of the residual net short, DWR was required under the terms of the Bond Indenture to maintain a minimum Operating Account balance of \$1 billion. After DWR transitioned responsibility for the residual net short to the IOUs, the required minimum Operating

## Department of Water Resources Electric Power Fund Management's Discussion and Analysis

Account balance for calendar 2003 was reduced to \$348 million. In July 2003, based on the impact of the 1) ability to reduce reserves, 2) collection of past due amounts from PG&E, 3) increases in costs, and 4) greater than anticipated cash balances, DWR decreased its 2003 Revenue Requirement by \$1 billion. The California Public Utilities Commission (CPUC) ordered the implementation of the revised revenue requirement through bill credits to the customers of the IOUs in fiscal 2004.

### STATEMENT OF NET ASSETS

The Fund's assets, liabilities and net assets as of June 30, are summarized as follows (in millions):

	2005	2004	2003
Long-term restricted cash and investments	\$ 1,482	\$ 1,522	\$ 1,704
Note receivable, net of current portion	-	104	-
Recoverable costs, net of current portion	7,356	7,745	7,568
Restricted cash and investments:			
Operating and priority contract accounts	1,387	1,320	1,261
Bond charge collection and bond charge payment accounts	570	539	385
Other investments	80	33	37
Recoverable costs, current portion	573	656	1,129
Other current assets	26	15	36
Total assets	<u>\$ 11,474</u>	<u>\$ 11,934</u>	<u>\$ 12,120</u>
Net assets	\$ -	\$ -	\$ -
Long-term debt, including current portion	10,982	11,414	11,636
Other current liabilities	492	520	484
Total capital and liabilities	<u>\$ 11,474</u>	<u>\$ 11,934</u>	<u>\$ 12,120</u>

### Long-Term Restricted Cash and Investments

The \$40 million and \$182 million decreases in long-term restricted cash and investments during the years ended June 30, 2005 and 2004, respectively, occur solely in the Operating Reserve Account and are a function of reduced Operating Reserve requirements. The \$555 million and \$595 million balance in the Operating Reserve Account at June 30, 2005 and 2004, respectively, are determined in accordance with the bond indenture and are equal to twelve percent of projected annual operating expenses of the Fund for calendar year 2005 and 2004, respectively. There has been no change in the \$927 million balance of the Debt Service Reserve Account; however, during the year ended June 30, 2004, \$600 million of the amount on deposit in the Debt Service Reserve Account was reinvested from the State of California Pooled Money Investment Account to investment in four guaranteed investment contracts and one forward purchase agreement with a financial institutions. The \$500 million of guaranteed investment contracts mature in May 2022, and the forward purchase agreement matures in November 2005.

# Department of Water Resources Electric Power Fund Management's Discussion and Analysis

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## Note Receivable

The \$104 million note receivable was established as a part of the energy settlement with El Paso Corporation in 2004, and represented the discounted value of a series of semi annual payments through 2024. In May 2005 El Paso Corporation exercised its option to prepay the discounted note receivable and all amounts owed were received by DWR.

## Recoverable Costs, Net of Current Portion

Long-term recoverable costs consist of costs that are recoverable through future billings. The majority of the \$389 million decrease during 2005 is attributable to the \$409 million of Bond Charge revenue in excess of interest expense. The majority of the \$177 million increase during 2004 is attributable to the \$1 billion bill credit to the customers of the IOUs, offset by the \$378 million net amount of Bond Charge revenue in excess of interest expense, and \$248 million from unanticipated energy settlements.

## Restricted Cash and Investments

The Operating and Priority Contract Accounts increased by \$67 million in 2005 as there was a net increase in cash and investments from normal operations, plus the transfer of \$40 million from the Operating Reserve Account in conjunction with the implementation of the 2005 revenue requirement. The same accounts had a net increase of \$59 million in 2004. The \$1 billion bill credit, net of the associated collection of \$539 million of past due amounts from Pacific Gas & Electric Company (PG&E) and the \$147 million transfer from the Operating Reserve, decreased the cash balance by approximately \$314 million. This net reduction was offset by the collection of \$182 million from energy settlements, an additional \$35 million in transfers from the Operating Reserve Account, and an increase from normal operations of \$156 million, attributable to marginal net revenue from the sale of more power than originally anticipated.

The Bond Charge Collection and Bond Charge Payment Accounts increased by \$31 million in 2005 reflecting lower than forecasted interest payments and in anticipation of the \$410 million principal payment due in May 2006. The same accounts increased by \$154 million in 2004 in anticipation of the \$388 million principal payment due in May 2005

From the dates of issuance of the revenue bonds through June 30, 2005, the balances in each of the restricted cash and investments accounts met or exceeded balances required by the Bond Indenture.

## Other Investments

DWR purchases natural gas as fuel for the production of power under the terms of certain long-term power purchase contracts and maintains a brokerage account with a national brokerage firm in order to hedge natural gas costs. Assets in this account are classified as other investments on the Statements of Net Assets.

During 2005, the use of the brokerage account for hedging natural gas costs increased. At June 30, 2005, the account consists of money market obligations, US Treasury bills, and government bonds valued at \$46 million and financial futures and options valued at \$34 million. At June 30, 2005, DWR has open positions with an unrealized marked-to-market value increase of \$15 million reflected in the account balance. The balance of other investments at June 30, 2004 is comparable to that at June 30, 2003.

## **Department of Water Resources Electric Power Fund Management's Discussion and Analysis**

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### **Recoverable Costs, Current Portion**

The current portion of recoverable costs reflects billings to IOU customers that have not yet been collected and amounts due for surplus sales of energy and gas. The current portion of recoverable costs decreased by \$83 million in 2005. Less power was supplied to the market in the spring months of 2005 than in 2004 with the conclusion of a major supplier contract as of December 31, 2004. Also, the remittance rate for power supplied to customers declined in fiscal year 2005 in varying amounts from each IOU. The current portion of recoverable costs decreased \$473 million in 2004, primarily due to the collection of past due amounts owed by PG&E.

### **Long-Term Debt**

The \$432 million and \$222 million decreases in long-term debt in 2005 and 2004, respectively, are attributable to \$388 million and \$180 million in revenue bond principal payments and \$44 million and \$42 million in amortization of premium in each of the two years, respectively.

### **Other Current Liabilities**

Accounts payable at each year end is comparable and reflect one month's accrual for power purchases, as payments are normally made on the 20th of the month following purchase.

Accrued interest payable at each year end is comparable as there has been limited decrease during 2005 and 2004 in the principal amount of bonds outstanding, offset by increases in the interest rate for variable rate debt.

## Department of Water Resources Electric Power Fund Management's Discussion and Analysis

### STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

The Fund's activities for the years ended June 30, are summarized as follows (in millions):

	2005	2004	2003
Revenues:			
Power charges	\$ 4,263	\$ 3,887	\$ 4,418
Surplus sales	451	421	99
Bond charges	845	800	407
Interest income	96	95	61
Total revenues	<u>5,655</u>	<u>5,203</u>	<u>4,985</u>
Expenses:			
Power purchases	4,965	5,146	4,517
Energy settlements	(191)	(248)	-
Interest expense	436	422	444
Other expenses	56	59	328
Recovery (deferral) of recoverable costs	389	(176)	(304)
Total expenses	<u>5,655</u>	<u>5,203</u>	<u>4,985</u>
Net income	-	-	-
Net assets, beginning of year	-	-	-
Net assets, end of year	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

### Power Charges

The cost of providing energy is recoverable primarily through power charges to IOU customers and certain customers of "direct access" Electric Service Providers (ESPs). Charges are determined by applying a CPUC adopted rate for each IOU service area to the megawatt hours of power delivered by DWR to each IOU's customers.

Power charges increased by \$376 million in 2005 as compared to 2004. The overall increase is attributable to recording the \$1 billion bill credit as a reduction in power charge revenue in fiscal 2004. If there had been no bill credit in fiscal 2004, power charges would have been \$4.887 billion. Excluding the bill credit, power charge revenues decreased by 13% in 2005 as compared to 2004. Even though the cost of power decreased by 4% in 2005, DWR was able to reduce its power charges by a greater amount as DWR received monies from energy settlements, thereby reducing the amount of power charges that needed to be billed to end use customers.

Power charges decreased by \$531 million in 2004 as compared to 2003. Again, the overall reduction is attributable to recording the \$1 billion bill credit as a reduction in power charge revenue in fiscal 2004. If there had been no bill credit in fiscal 2004, power charges would have been \$4.887 billion. After adjusting fiscal 2003 for the impact of the \$113 million rebate for the "20-20 Energy Rebate Program", 2004 power charges, excluding the bill credit, increased by 8% over 2003 power charges. This increase is attributable to a 13% increase in power delivered in 2004 as compared to 2003 and average lower remittance rates in 2004.

# Department of Water Resources Electric Power Fund Management's Discussion and Analysis

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## Surplus Sales

Since January 2003, DWR has received revenue from the sale of excess energy, based on DWR's pro-rata allocation of its share of energy provided to each IOU's service area to the total amount of energy provided by IOU generation in each respective IOU service area, and from the sale of surplus gas.

Surplus sales in 2005 are \$30 million greater than in 2004, as the rising price received for sales of excess energy offset lower volumes available to be sold after satisfying end-user demand in the IOU service territories. Average prices received for sales of surplus energy rose 14% over 2004 while total megawatt hours sold declined 8%. Sales of excess natural gas in 2005 also rose by 13%, reflecting overall rising natural gas prices.

Surplus sales in 2004 were \$322 million greater than in 2003. Prior to January 1, 2003, surplus energy was used to reduce the amount of residual net short energy purchased in the wholesale markets.

## Bond Charges

Bond charges were established in November 2002, provide revenue for the payment of debt service on the revenue bonds and are determined by applying a CPUC adopted rate to the total megawatt hours of power delivered to all IOU customers and certain ESP customers. Bond charges for the years ended June 30, 2005, 2004 and 2003 were \$845 million, \$800 million, and \$407 million, respectively, and were adequate to meet all debt service requirements and maintain bond indenture required account balances in the Bond Charge Collection, Bond Charge Payment, and Debt Service Reserve Accounts.

## Interest Income

Interest income for 2005 is comparable to 2004 and is attributable to increased rates received on investments in the State of California Investment Pooled Money Investment Account-Surplus Investment Fund (SMIF), a full year's interest on the Debt Service Reserve Account's \$600 million reinvestment from SMIF to guaranteed investment contracts and forward purchase agreement, less the one time interest earned in 2004 on amounts owed by PG&E. The \$34 million increase in interest income in 2004 is primarily attributable to the receipt of \$38 million for interest on past due amounts owed by PG&E, as ordered by a CPUC decision issued in January 2004.

## Power Purchases

DWR power costs are \$181 million lower in 2005 than in 2004. While there was minimal change in the amount of power purchased, DWR experienced a 4% decrease in its costs, primarily due to the completion of a high priced contract in December 2004. Total costs for purchased power decreased by approximately \$325 million in 2005; however, gas purchases used in the production of power increased by \$144 million due to increased gas prices.

DWR power costs are \$629 million higher in 2004 than in 2003. This 14% increase reflects the 13% increase in energy volumes purchases during 2004 at marginally higher costs than in 2003. The increase in power purchased is attributable to 1) power from new plants coming on line under the terms of the original power contracts, 2) increased use of DWR dispatchable contracts by the IOUs because of more downtime for an IOU nuclear facility than was originally forecast, and 3) higher market clearing prices which lead to the additional use of DWR dispatchable contracts for sale in the wholesale market.

## **Department of Water Resources Electric Power Fund Management's Discussion and Analysis**

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### **Energy Settlements**

Energy settlements received, including those related to complex regulatory proceedings before the Federal Energy Regulatory Commission arising from events in California energy markets in 2001, are recorded as a decrease in operating expenses.

Energy settlements of \$191 million were recognized in 2005 and include \$99 million from Dynegy Inc., \$76 million from Mirant Corporation, and \$14 million from Duke Energy Corporation. Future revenues under these settlements are subject to conditions outlined in the underlying settlement and allocation agreements. DWR also recognized an additional \$2 million from the 2004 settlement with El Paso Corporation.

In 2004, under the terms of a settlement between various parties and El Paso Corporation, DWR received \$225 million. The remaining \$23 million earned in 2004 is attributable to settlements with two other companies.

### **Interest Expense**

Interest expense in 2005 is \$14 million higher than in 2004 as the result of increased interest rates on variable rate debt. Interest expense in 2004 is \$22 million less than in 2003. This is expected as the bonds were outstanding for all 2004, while for a portion of 2003, interest expense includes the higher rates for the General Fund Advances and term loan.

### **Other Expenses**

Administrative expenses decreased \$3 million in 2005 due primarily to a decrease in charges for services provided to the Power Supply Program by other State agencies. Administrative expenses are \$12 million less in 2004 than in 2003 as costs incurred for contract renegotiation and litigation decreased during the year, and the IOUs have assumed more administrative responsibilities for the contracts since the transition of the residual net short in January 2003.

# Department of Water Resources Electric Power Fund Management's Discussion and Analysis

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## Recovery (Deferral) of Recoverable Costs

The individual components of the recovery (deferral) of recoverable costs are as follows (in millions):

	2005	2004	2003
Operations	\$ (116)	\$ (649)	\$ (71)
Debt service and related costs	<u>505</u>	<u>473</u>	<u>(233)</u>
	<u>\$ 389</u>	<u>\$ (176)</u>	<u>\$ (304)</u>

### Operations

In 2005 DWR was able to decrease power charges and still maintain operating funds that are in excess of the amount required by the bond indentures. The large deferral of recoverable costs in 2004 is primarily attributable to the \$1 billion bill credit. This is offset by the \$248 million of energy settlements and other revenue received in excess of the cost of purchased power and administrative expenses.

### Debt Service and Related Costs

The 2005 recovery is anticipated and is attributable to the bond charges being sufficient to pay for interest expense and retire debt. In 2004, \$473 million of recovery is attributable to 1) a full year's collection of bond charges, 2) use of \$180 million of the bond charge proceeds to retire principal on debt, 2) and collection of bond charges in the Bond Charge Payment Account in anticipation of the May 2005 principal payment of \$388 million. In 2003, the net amount deferred consists of one time costs incurred for issuance of revenue bonds that were financed through bond proceeds.

## FUTURE OPERATIONS

On August 31, 2005 the Governor introduced legislation that would establish a Department of Energy through the consolidation of the functions of several departments, commissions and offices that currently implement state energy programs. If the legislation were to be enacted, all of the powers, duties, responsibilities, rights, obligations, liabilities and jurisdiction of DWR under Division 27 of the California Water Code would be assumed by the Department of Energy.

DWR or its successor will administer the Fund until such time as the revenue bonds are completely retired. Revenue requirements for the repayment of the bonds will be determined at least annually and submitted to the CPUC for implementation. Under the terms of the rate agreement between the CPUC and DWR, the CPUC is required to set rates for the customers of the IOUs and ESPs such that the Fund will always have monies to pay the principal of and interest on the bonds and all other bond related costs when due.

DWR has the authority to administer all power supply contracts entered into before December 31, 2002, for the life of the contracts. Over 95% of the volume of power under contract expires by December 31, 2011 and the last of the contracts expires in 2017. Revenue requirements for the payment of energy purchased under the contracts will be determined at least annually and submitted to the CPUC. Under the terms of the rate agreement between the CPUC and DWR, the CPUC is required to implement power charges such that the Fund will receive necessary monies to meet its revenue requirements.

## **Department of Water Resources Electric Power Fund Management's Discussion and Analysis**

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The financial responsibility for the contracts may be transferred to the IOUs as part of a complete assignment of the contracts and release of DWR or its successor. However, there are a number of issues to be addressed, including IOU acceptance of the assignment and counterparty approval, before the contracts can be assigned.

**Department of Water Resources Electric Power Fund**  
**Statements of Net Assets**  
**June 30, 2005 and 2004**

(in millions)

	2005	2004
<b>Assets</b>		
Long-term assets:		
Restricted cash and investments:		
Operating Reserve Account	\$ 555	\$ 595
Debt Service Reserve Account	927	927
Note receivable, net of current portion	-	104
Recoverable costs, net of current portion	7,356	7,745
Total long-term assets	<u>8,838</u>	<u>9,371</u>
Current assets:		
Restricted cash and investments:		
Operating and Priority Contract Accounts	1,387	1,320
Bond Charge Collection and Bond Charge Payment Accounts	570	539
Other investments	80	33
Recoverable costs, current portion	573	656
Interest receivable	26	15
Total current assets	<u>2,636</u>	<u>2,563</u>
Total assets	<u>\$ 11,474</u>	<u>\$ 11,934</u>
<b>Capitalization and Liabilities</b>		
Capitalization:		
Net assets	\$ -	\$ -
Long-term debt:		
Revenue bonds	10,529	10,982
Total capitalization	<u>10,529</u>	<u>10,982</u>
Current liabilities:		
Current portion of long-term debt	453	432
Accounts payable	424	452
Accrued interest payable	68	68
Total current liabilities	<u>945</u>	<u>952</u>
Commitments and Contingencies (Note 7)		
Total capitalization and liabilities	<u>\$ 11,474</u>	<u>\$ 11,934</u>

The accompanying notes are an integral part of these financial statements.

**Department of Water Resources Electric Power Fund**  
**Statements of Revenues, Expenses and Changes in Net Assets**  
**For the years ended June 30, 2005 and 2004**

(in millions)

	2005	2004
Operating revenues:		
Power charges	\$ 4,263	\$ 3,887
Surplus sales	451	421
Total operating revenues	<u>4,714</u>	<u>4,308</u>
Operating expenses:		
Power purchases	4,965	5,146
Energy settlements	(191)	(248)
Administrative expenses	56	59
Deferral of recoverable operating costs	(116)	(649)
Total operating expenses	<u>4,714</u>	<u>4,308</u>
Income from operations	-	-
Bond charges	845	800
Interest income	96	95
Interest expense	(436)	(422)
Recovery of recoverable debt service and related costs	<u>(505)</u>	<u>(473)</u>
Net income	-	-
Net assets, beginning of year	<u>-</u>	<u>-</u>
Net assets, end of year	<u>\$ -</u>	<u>\$ -</u>

The accompanying notes are an integral part of these financial statements.

**Department of Water Resources Electric Power Fund**  
**Statements of Cash Flows**  
**For the years ended June 30, 2005 and 2004**

**(in millions)**

	<b>2005</b>	<b>2004</b>
Cash flows from operating income:		
Receipts:		
Power charges	\$ 4,339	\$ 4,457
Surplus sales	445	379
Energy settlements	306	133
Payments for power purchases and administrative expenses	<u>(5,046)</u>	<u>(5,144)</u>
Net cash provided by (used in) operating activities	<u>44</u>	<u>(175)</u>
Cash flows from non-capital financing activities:		
Receipt of bond charges	847	776
Bond payments	(388)	(180)
Interest payments	<u>(480)</u>	<u>(465)</u>
Net cash (used in) provided by non-capital financing activities	<u>(21)</u>	<u>131</u>
Cash flows from investing activities:		
Investments purchased	(50)	(20)
Interest received on investments	<u>85</u>	<u>95</u>
Net cash provided by investing activities	<u>35</u>	<u>75</u>
Net increase in cash and investments	58	31
Restricted cash and investments, beginning of year	<u>3,381</u>	<u>3,350</u>
Restricted cash and investments, end of year	<u>\$ 3,439</u>	<u>\$ 3,381</u>
Reconciliation of operating income to net cash provided by (used in) operating activities:		
Income from operations	\$ -	\$ -
Changes in net assets and liabilities to reconcile operating income to cash net provided by (used in) operations:		
Recoverable costs	72	(233)
Due from other funds	-	21
Accounts payable	<u>(28)</u>	<u>37</u>
Total adjustments	<u>44</u>	<u>(175)</u>
Net cash provided by (used in) operating activities	<u>\$ 44</u>	<u>\$ (175)</u>

The accompanying notes are an integral part of these financial statements.

# Department of Water Resources Electric Power Fund

## Notes to Financial Statements

For the years ended June 30, 2005 and 2004

(in millions)

### 1. Reporting Entity

In January 2001, the Governor of California issued an emergency proclamation directing the Department of Water Resources (DWR) to enter into contracts and arrangements for the purchase and sale of electric power to assist in mitigating the effect of a statewide energy supply emergency.

The Department of Water Resources Electric Power Fund (a component unit of the State of California) (the Fund), administered by DWR, was established in January 2001 through legislation adding Division 27 to the California Water Code (the Code).

DWR currently purchases power from wholesale suppliers under contracts entered into prior to January 1, 2003 for resale to ten million customers of Pacific Gas & Electric Company, Southern California Edison Company, and San Diego Gas & Electric Company (collectively referred to as the investor owned utilities or IOUs). The Code prohibits DWR from entering into new power purchase agreements, but allows DWR to enter into gas purchase contracts to provide fuel for power generation.

DWR power is delivered to the customers through the transmission and distribution systems of the IOUs and payments from the customers are collected for DWR by the IOUs pursuant to servicing arrangements approved and/or ordered by the California Public Utilities Commission (CPUC).

Under the terms of a rate agreement between DWR and the CPUC, the CPUC will implement DWR's determination of its revenue requirements by establishing customer rates that will meet DWR's revenue needs to insure the payment of debt service, power purchases, administrative expenses and changes in reserves.

### 2. Summary of Significant Accounting Policies

#### Basis of Presentation

The Fund is accounted for as an enterprise fund and is financed and operated in a manner similar to that of a private business enterprise. The Fund uses the economic resources measurement focus and the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. As allowed by governmental accounting standards, the Fund has elected not to apply statements and related interpretations issued by the Financial Accounting Standards Board after November 30, 1989. The Fund is accounted for with a set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues and expenses.

The financial statements of the Fund are intended to present the financial position, and the changes in financial position and cash flows, where applicable, of only that portion of the business-type activities and major funds of the State of California that is attributable to the transactions of the Fund. They do not purport to, and do not, present fairly the financial position of the State of California as of June 30, 2005 and 2004, and the changes in its financial position and its cash flows, where applicable, for the years then ended in conformity with accounting principles generally accepted in the United States of America.

**Department of Water Resources Electric Power Fund**  
**Notes to Financial Statements**  
**For the years ended June 30, 2005 and 2004**

**(in millions)**

**Restricted Cash and Investments**

Under the terms of the Bond Indenture separate restricted cash and investment accounts were established. The accounts and their purpose follow:

Power Charge Accounts:

- Operating Account: Power charges (see Revenues and Recoverable Costs) and miscellaneous revenue are deposited into the Operating Account. Monthly, funds are transferred to the Priority Contract Account as needed to make payments on priority contracts. Remaining monies are available for payment of all operating costs of the Fund other than priority contracts, debt service, and debt-related costs.
- Priority Contract Account: Priority contracts are those power purchase contracts that require monthly payment prior to any debt service payments. Monies in the Priority Contract Account are used to make scheduled payments on priority contracts. After the monthly transfer from the Operating Account on the fifth of the month, the Priority Contract Account is projected to have monies sufficient to make scheduled payments on priority contracts through the fifth of the following month.
- Operating Reserve Account: The Operating Reserve account must maintain a balance equal to the greater of (i) seven months of projected negative operating cash flows under a stress scenario, as defined, or (ii) twelve percent of projected annual operating expenses of the Fund, as defined.

Bond Charge Accounts:

- Bond Charge Collection Account: Bond charges (see Revenues and Recoverable Costs) are deposited into the Bond Charge Collection Account. Monthly, funds needed for debt service payments are transferred to the Bond Charge Payment Account.
- Bond Charge Payment Account: Monies in the Bond Charge Payment Account are used to pay debt service, swap payments and related fees for the revenue bonds. After receipt of the monthly transfer from the Bond Charge Collection Account, the balance in the Bond Charge Payment Account must at least equal debt service, swap payments and fees estimated to accrue or be payable for the next succeeding three months.
- Debt Service Reserve Account: The Debt Service Reserve account is to be funded at all times with the amount of maximum aggregate annual debt service on all outstanding debt, including net scheduled swap payments.

Restricted cash and investments, for purposes of the statements of cash flows, include cash on hand and short-term investments, specifically deposits in the State of California Investment Pooled Money Investment Account-Surplus Money Investment Fund (SMIF) and certain long-term investments.

SMIF has an equity interest in the State of California Pooled Money Investment Account (PMIA). Generally, the investments in PMIA are available for withdrawal on demand. The PMIA cash and investments are recorded at amortized cost, which approximates market. PMIA funds are on deposit

# Department of Water Resources Electric Power Fund

## Notes to Financial Statements

For the years ended June 30, 2005 and 2004

(in millions)

with the State's Centralized Treasury System and are managed in compliance with the California Government Code, described in Note 3 below.

Long term investments are held solely in the Debt Service Reserve Account by the bond co-trustee and consist of guaranteed investment contracts (GICs) and a U.S. government backed agency security in accordance with a forward purchase agreement (FPA). The GICs are carried at cost and the U.S. government backed agency security is carried at amortized cost.

### **Other Investments**

The Fund maintains a brokerage account with a national brokerage firm in order to take positions in futures and options for the hedging of natural gas fuel costs. Natural gas future and option agreements are reported at fair value on the statement of net assets. DWR does not enter into natural gas futures and option agreements for trading purposes, but rather to take advantage of favorable pricing and to reduce fuel price volatility. The Fund is exposed to additional fuel price risk if the counterparties default or if the future or option agreements are terminated. The Fund's position underlying open natural gas future and option agreements totaled \$34 million and \$12 million at June 30, 2005 and 2004, respectively. It is possible that the market price before or at the specified time to purchase natural gas may be lower than the price at which the Fund is committed to buy. This would reduce the value of the contract. The Fund could sell the contract at a loss, or if it were to continue to hold the contract, the Fund may make a termination payment to the counterparty to cancel its obligation under the contract and then buy natural gas on the open market.

The brokerage firm requires that the Fund maintain a security deposit, which is invested in compliance with the California Government Code. These funds are invested in money market mutual funds and government bonds and are carried at fair value. The investment in money market mutual funds amounted to \$30 million and \$20 million at June 30, 2005 and 2004, respectively, and the investments in treasury bills and government bonds amounted to \$16 million and \$1 million at June 30, 2005 and 2004, respectively.

### **Revenues and Recoverable Costs**

Customer charges are separated into two primary components, power charges and bond charges. Power charge revenues recover the cost of power purchases, administrative expenses and operating reserves and are recognized when energy provided by DWR is delivered to the IOU customers. Certain customers of "direct access" Electric Service Providers (ESPs) are assessed "cost responsibility surcharge" that is used by DWR for the same purposes as Power charge revenues. Bond charge revenues recover debt service, debt service reserves and other bond related costs and are recognized when energy provided by either DWR or the IOU, or an ESP, is delivered to IOU, or ESP, customers. Costs are recovered over the life of the bonds (2022) as determined by DWR's revenue requirement process.

During the year ended June 30, 2004, power charges were reduced by \$1 billion in the form of bill credits given to the customers of the IOUs through the CPUC's implementation of DWR's 2003 Supplemental Revenue Requirement. This reduction was based on the net impact of 1) the ability to reduce reserves as allowed under the Bond Indenture, 2) the receipt of cash for past due amounts being held in trust by PG&E, 3) increases in costs, and 4) a greater than anticipated Operating Account balance at January 1, 2003.

# Department of Water Resources Electric Power Fund

## Notes to Financial Statements

For the years ended June 30, 2005 and 2004

(in millions)

Surplus sales represent DWR's 1) allocated portion of the IOUs total surplus energy sales and 2) the sale of gas not needed for the generation of power. The revenue from the sale of excess energy by the IOUs is shared on a pro-rata basis between DWR and the IOUs, based on the amount of energy provided by DWR relative to the total amount of energy provided from IOU generation in the individual IOU's service territory.

Amounts that have been earned but not collected are recorded as the current portion of recoverable costs. Costs that are recoverable through future billings and collection of finalized energy settlements are recorded as long-term assets.

### 3. Restricted Cash and Investments

The State of California has a deposit policy for custodial credit risk. As of June 30, 2005, \$40 million of the Fund's cash deposits of \$62 million was exposed to custodial credit risk as follows:

Institution	Amount	Custodial Credit Risk
Prime Value Obligations Fund		
Institutional Shares	\$ 30	Insured
U.S. Bank	10	Uninsured and uncollateralized
	<u>\$ 40</u>	

As of June 30, 2005, the Fund had the following investments:

Investment	Maturity	Fair Value
State of California Pooled Money		
Investment Account - State Money		
Investment Fund	5.5 months average	\$ 2,807
Guaranteed investment contracts	May 1, 2022	500
Forward purchase agreement	November 1, 2005	100
Natural gas futures and options	3 months average	34
Other	5 year average	16
		<u>\$ 3,457</u>

*Interest Rate Risk:* In accordance with its investment policy, the State of California manages its exposure to declines in fair values by spreading investments over various maturities: U.S. Treasury securities, 5 years; federal agency securities, 5 years; bankers acceptances – domestic and foreign, 180 days; certificates of deposits, 5 years; collateralized time deposits, 5 years; commercial paper, 180 days; corporate bonds and notes, 5 years; repurchase agreements and reverse repurchase agreements, 1 year.

# Department of Water Resources Electric Power Fund

## Notes to Financial Statements

For the years ended June 30, 2005 and 2004

(in millions)

*Credit Risk:* PMIA funds are on deposit with the State's Centralized Treasury System and are managed in compliance with the California Government Code, according to a statement of investment policy which sets forth permitted investment vehicles, liquidity parameters and maximum maturity of investments. These investments consist of U.S. government securities, securities of federally-sponsored agencies, U.S. corporate bonds, interest bearing time deposits in California banks, prime-rated commercial paper, bankers' acceptances, negotiable certificates of deposit, repurchase and reverse repurchase agreements. The PMIA policy limits the use of reverse repurchase agreements subject to limits of no more than 10% of PMIA. The PMIA does not invest in leveraged products or inverse floating rate securities. The PMIA is not rated.

The Fund's investments in the guaranteed investment contract and forward purchase agreement are rated as follows, by Standard & Poors (S&P) and Moody's, respectively, at June 30, 2005:

	<b>Amount</b>	<b>S&amp;P</b>	<b>Moody's</b>
GIC Providers			
FSA	\$ 100	AAA	Aaa
XL Capital	150	AAA	Aaa
Royal Bank of Canada	100	AA-	Aa2
Sun America	150	AA+	Aa1
	<u>\$ 500</u>		
FPA Provider			
Merrill Lynch: FHLMC			
Discounted Notes	<u>\$ 100</u>	AAA	Aaa

*Concentration of Credit Risk:* The PMIA's concentration of credit risk is limited by spreading the investment mix over different investment types, credit ratings and issuers to minimize the impact any one industry, investment class, or institution can have on the PMIA portfolio.

Interest on deposits in PMIA varies with the rate of return of the underlying portfolio and approximated 3.0% and 1.5% at June 30, 2005 and 2004, respectively. For the years ended June 30, 2005 and 2004, interest earned on the deposit in PMIA was \$65 million and \$50 million, respectively.

Interest on the GICs is paid semi-annually at interest rates ranging from 5.2% to 5.5%. Interest earned on the GICs was \$26 million and \$3 million for the years ended June 30, 2005 and 2004, respectively. The GICs mature in 2022.

The FPA allows the revenue bond trustee to continuously reinvest funds in U.S. government or U.S. government agency securities through May 2022 to earn a minimum rate of return of 4.7%, as specified in the Reserve Fund Forward Purchase and Sale Agreement, dated May 1, 2004. The reinvested securities are to mature every six months. Interest earned on the FPA was \$5 million and \$1 million for the years ended June 30, 2005 and 2004, respectively.

**Department of Water Resources Electric Power Fund**  
**Notes to Financial Statements**  
**For the years ended June 30, 2005 and 2004**

(in millions)

**4. Long-Term Debt**

The following activity occurred in the long-term debt accounts during the years ended June 30, 2005 and 2004:

	<b>Revenue Bonds</b>	<b>Unamortized Premium</b>	<b>Total</b>
Balance, June 30, 2003	\$ 11,264	\$ 372	\$ 11,636
Payments	(180)	-	(180)
Amortization of premium	-	(42)	(42)
Balance, June 30, 2004	<u>11,084</u>	<u>330</u>	<u>11,414</u>
Payments	(388)	-	(388)
Amortization of premium	-	(44)	(44)
Balance, June 30, 2005	<u>10,696</u>	<u>286</u>	<u>10,982</u>
Less current portion	<u>410</u>	<u>43</u>	<u>453</u>
	<u>\$ 10,286</u>	<u>\$ 243</u>	<u>\$ 10,529</u>

The revenue bonds, all of which except Series E are tax-exempt, consist of the following at June 30, 2005:

<b>Series</b>	<b>Rates</b>	<b>Fiscal Year of Final maturity</b>	<b>Fiscal Year of First Call Date</b>	<b>Amount Outstanding</b>
A	3.0-6.0%	2022	2012	\$ 6,196
B	Variable	2020	Callable	1,000
C	Variable	2022	Callable	2,750
D	Variable	2022	Callable	500
E	3.6-4.3%	2006	Not callable	250
				<u>10,696</u>
				286
				<u>(453)</u>
				<u>\$ 10,529</u>

Series B and C are variable rate bonds and have daily and weekly rate reset modes, respectively, and Series D has 35-day auction periods. The variable rate bonds have a final stated maturity of 2022, but will be retired in sinking fund installments from fiscal 2007 to 2022. The interest rates for the variable debt for the year ended June 30, 2005 and 2004, ranged from 0.9% to 3.1% and from 0.4% to 1.4%, respectively.

Principal and interest payments are payable from bond charges. The Fund is subject to certain bond covenants, including establishing funding and expenditure requirements for several restricted cash

# Department of Water Resources Electric Power Fund

## Notes to Financial Statements

For the years ended June 30, 2005 and 2004

(in millions)

and investment accounts. The bonds are limited special obligations of the Fund. Neither the principal nor any interest thereon constitutes a debt of the State. The payment of principal and interest for Series B and \$1.75 billion of Series C bonds are paid from draws made under letters of credit. Draws made under the letters of credit are to be reimbursed on the same day by the Fund. There are no outstanding amounts on the letters of credit at June 30, 2005. The letters of credit expire in fiscal 2011. The Fund pays fees of 0.45% per annum on the stated amount of the letters of credit.

The remaining \$1 billion of Series C bonds is credit enhanced by bond insurance for the timely payment of principal and interest. Liquidity support for these variable rate bonds is provided by bank liquidity facilities. Any funds paid under the bond insurance facilities are immediately due and payable by the Fund. Bonds purchased under the initial liquidity facilities are required to be redeemed in equal installments over a five or seven year period. There are no outstanding amounts due under liquidity facilities at June 30, 2005. Three liquidity facilities backing \$400 million in Series C bonds expire in fiscal year 2011, and two liquidity facilities underlying \$600 million of Series C bonds expire in fiscal year 2012. The Fund pays fees of 0.22% to 0.28% per annum under the liquidity facilities.

Future payment requirements on the revenue bonds are as follows at June 30, 2005:

<b>Fiscal Year</b>	<b>Principal</b>	<b>Interest <sup>1</sup></b>	<b>Total</b>
2006	\$ 410	\$ 433	\$ 843
2007	427	416	843
2008	449	396	845
2009	471	374	845
2010	495	354	849
2011-2015	2,898	1,411	4,309
2016-2020	3,768	681	4,449
2021-2022	1,778	86	1,864
	<u>\$ 10,696</u>	<u>\$ 4,151</u>	<u>\$ 14,847</u>

<sup>1</sup> Variable portion of interest cost calculated using the June 30, 2005 Bond Market Association Municipal Swap Index (BMA).

### 5. Interest Rate Swaps

DWR, on behalf of the Fund, entered into interest rate swap agreements with various counterparties to reduce variable interest rate risk. The swaps create a synthetic fixed rate for DWR. DWR has agreed to make fixed rate payments and receive floating rate payments on notional amounts equal to a portion of the principal amount of DWR's variable rate debt.

**Department of Water Resources Electric Power Fund**  
**Notes to Financial Statements**  
**For the years ended June 30, 2005 and 2004**

**(in millions)**

The terms, fair values, and credit ratings of counterparties for the various swap agreements at June 30, 2005 are summarized in the following table:

Outstanding Notional Amount	Fixed Rate Paid by Fund	Variable Rate <sup>1</sup> Received by Fund	Fair Value	Swap Termination Date	Counterparty Credit Rating		
					S&P	Moody's	Fitch
\$ 94	2.914%	67% of LIBOR	\$ (3)	May 1, 2011	AAA	Aaa	AAA
234	3.024%	67% of LIBOR	(6)	May 1, 2012	AAA	Aaa	AAA
200	3.405%	BMA	(3)	May 1, 2013	A+	Aa3	A+
100	3.405%	BMA	(1)	May 1, 2013	A+	Aa3	AA-
30	3.405%	BMA	-	May 1, 2013	A+	Aa3	AA-
194	3.204%	67% of LIBOR	(5)	May 1, 2014	AA-	Aa1	AA-
174	3.280%	67% of LIBOR	(9)	May 1, 2015	AAA	Aaa	AAA
202	3.342%	67% of LIBOR	(8)	May 1, 2016	AA	Aa2	AA
202	3.389%	67% of LIBOR	(9)	May 1, 2017	A+	Aa3	AA-
<u>\$ 1,430</u>			<u>\$ (44)</u>				

<sup>1</sup> One month U.S. Dollar London Interbank Offered Rate or Bond Market Association Municipal Swap Index

The notional amounts of the swaps match the principal amounts of the associated debt. The swap agreements contain scheduled reductions in notional amounts that follow scheduled amortization of the associated debt.

*Fair Value:* The reported fair values from the table above were provided by the counterparties, using the par value, or marked-to-market, method.

*Credit Risk:* As of June 30, 2005, the Fund was not exposed to credit risk because the swaps had negative fair values. However, should interest rates increase and the fair values become positive, the Fund would be exposed to credit risk in the amount of the swaps' fair value. DWR has a total of nine swap agreements with six different counterparties. Three swaps, approximating 35 percent of the total notional value is with one counterparty with a credit rating of AAA/Aaa/AAA. Of the remaining swaps, two are held with a single counterparty, approximating 21 percent of the outstanding notional value. That counterparty has credit ratings of A+/Aa3/AA-. The remaining four swaps are with separate counterparties, all having A+/Aa3/A+ ratings or better.

*Basis Risk:* The Fund is exposed to basis risk on the swaps that have payments calculated on the basis of a percentage of LIBOR (a taxable rate index). The basis risk results from the fact that DWR's floating interest payments payable on the underlying debt are determined in the tax-exempt market, while DWR's floating receipts on the swaps are based on LIBOR, which is determined in the taxable market. Should the relationship between LIBOR and the tax-exempt market change and move to convergence, or should DWR's bonds trade at levels worse (higher in rate) in relation to the tax-exempt market, DWR's all-in costs would increase. As of June 30, 2005, the variable rate on DWR's hedged bonds ranged from 2.1% to 2.5%, while 67% of LIBOR received on the swap was equal to 2.2%.

# Department of Water Resources Electric Power Fund

## Notes to Financial Statements

For the years ended June 30, 2005 and 2004

(in millions)

*Termination Risk:* DWR's swap agreements do not contain any out-of-the-ordinary termination events that would expose it to significant termination risk. In keeping with market standards, DWR or the counterparty may terminate a swap agreement if the other party fails to perform under the terms of the contract. In addition, the swap documents allow either party to terminate in the event of a significant loss of creditworthiness by the other party. DWR views such events to be remote at this time. If a termination were to occur, at the time of the termination, DWR would be liable for payment equal to the swap's fair value, if it had a negative fair value at that time. The counterparty would be liable for any payment equal to the swap's fair value, if it had positive fair value at that time. In addition, a termination would mean that DWR's underlying floating rate bonds would no longer be hedged, and DWR would be exposed to floating rate risk, unless it entered into a new hedge following termination.

*Rollover Risk:* Since the swap agreements have termination dates and notional amounts that are tied to equivalent maturity dates and principal amounts of amortizing debt, there is no rollover risk associated with the swap agreements, other than in the event of a termination.

*Swap Payments and Associated Debt:* As rates vary, variable-rate bond interest payments and net swap interest payments will vary. As of June 30, 2005, 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:

Fiscal Year	Variable Rate Bonds		Interest Rate Swaps, Net	Total
	Principal	Interest		
2006	\$ -	\$ 33	\$ 14	\$ 47
2007	-	33	14	47
2008	-	33	14	47
2009	-	33	14	47
2010	-	33	14	47
2011-2015	1,026	119	55	1,200
2016-2017	404	14	7	425
	<u>\$ 1,430</u>	<u>\$ 298</u>	<u>\$ 132</u>	<u>\$ 1,860</u>

## 6. Retirement Plan

### Plan Description

The State of California is a member of the California Public Employees' Retirement System (PERS), an agent multiple-employer pension system that provides a contributory defined-benefit pension for substantially all State employees. DWR is included in the State Miscellaneous Category (Tier 1 and Tier 2) within PERS, thereby limiting the availability of certain DWR pension data. PERS functions as an investment and administrative agent for participating public agencies within the State of California. Departments and agencies within the State of California, including DWR, are in a cost-sharing arrangement in which all risks and costs are shared proportionately by participating State agencies. Copies of PERS' comprehensive annual financial report may be obtained from their

# Department of Water Resources Electric Power Fund

## Notes to Financial Statements

For the years ended June 30, 2005 and 2004

(in millions)

executive office at 400 P Street, Sacramento, California 95814. The pension plan provides retirement benefits, survivor benefits, and death and disability benefits based upon an employee's years of credited service, age and final compensation. Vesting occurs after five years of credited service except for second tier benefits, which require ten years of credited service. Employees who retire at or after age 50 with five or more years of service are entitled to a retirement benefit, payable monthly for the remainder of their lives. Several survivor benefit options which reduce a retiree's unmodified benefit are available. Benefit provisions and all other requirements are established by state statute.

### **Annual Pension Cost**

For the years ended June 30, 2005 and 2004, DWR's annual pension cost payable from the Fund and actual contribution allocated to the Fund based on the Fund's payroll costs approximated \$1 million.

## **7. Commitments and Contingencies**

### **Litigation and Regulatory Proceedings**

DWR is involved in lawsuits and regulatory proceedings that could impact power costs and future revenue requirements.

In July, 2001, the Federal Energy Regulatory Commission (FERC) initiated a proceeding to calculate refunds for inflated prices in the California Independent System Operator (CAISO) and California Power Exchange Corporation markets during 2000 and 2001. DWR purchased \$2.9 billion in energy to meet the CAISO's emergency needs during 2001. DWR is treated in the FERC refund proceeding as a seller of that energy to CAISO, and in May 2004, FERC issued an order requiring DWR to pay refunds on the \$2.9 billion in "sales" to the CAISO. The refund amount totals approximately \$2.2 billion on a gross basis, of which DWR could actually owe up to approximately \$150 million on a net basis, because DWR would be the primary recipient of the refunds FERC required DWR to pay. However, FERC also later ruled that, like all sellers, to the extent DWR could demonstrate that payment of the refunds would result in DWR's costs exceeding its revenues, DWR could request FERC to reduce the refunds that would be owed. DWR sold all energy to the CAISO at its cost of acquisition. In September 2005, DWR made a cost recovery filing to request such a reduction in its refund obligation. Also in September 2005, the Ninth Circuit Court of Appeals ruled that FERC could not require governmental entities such as DWR to pay refunds. Accordingly, DWR has two possible methods of eliminating its potential refund liability: (1) the cost recovery filing it has made with FERC; and (2) the claim, based on the Ninth Circuit's ruling, that FERC has no legal authority to order DWR to pay refunds. Should the Fund be required to pay any refunds as a result of this proceeding, the refunds would be recoverable from ratepayers through future revenue requirements.

There are a number of lawsuits and regulatory proceedings in which DWR is not a party but may be affected by the result. In one consolidated set of cases, the issue is whether and to what extent compensation is due from the State of California as a result of the State's commandeering of certain block forward contracts in early 2001. Certain market participants claim that they are entitled to damages in excess of \$1 billion, their estimation of the fair value of the block forward contracts at the time of commandeering. DWR paid approximately \$352 million for energy provided under the contracts, which expired in December 2001. Given the early state of the proceeding, it is not possible to predict or determine the outcome of this matter or to provide an estimate of any losses, if any, that may arise. However, management believes that the costs associated with this action will not have a material adverse effect on the Fund's financial position or liquidity. Should the Fund be determined

# Department of Water Resources Electric Power Fund

## Notes to Financial Statements

For the years ended June 30, 2005 and 2004

(in millions)

to be the source of moneys to pay any damages resulting from this litigation, those damages would be recoverable from ratepayers through future DWR revenue requirements.

Management believes that the existing lawsuits and regulatory proceedings will be resolved in the next fiscal year. Because of the early stage of the legal and regulatory proceedings, the ultimate outcome of these matters cannot be presently determined.

### Other Contingencies

The Fund is self-insured for most risks, including general liability and workers' compensation. Management believes that any costs associated with such losses are recoverable from customers as part of DWR's revenue requirement.

### Commitments

DWR has power purchase contracts that have remaining lives of up to twelve years. Payments under these contracts approximated \$3.7 billion and \$4.1 billion for fiscal 2005 and 2004, respectively.

The remaining amounts of fixed obligations under the contracts as of June 30, 2005, are as follows:

<b>Fiscal Year</b>	<b>Fixed Obligation</b>
2006	\$ 2,783
2007	2,525
2008	2,379
2009	2,238
2010	1,805
Thereafter	1,638
	<u>\$ 13,368</u>

In addition to the fixed costs there are variable costs under several of the contracts. Management projected as of June 30, 2005 that the amount of future fixed and variable obligations associated with long-term power purchase contracts would approximate \$24 billion. The difference between the fixed costs and the expected total costs of the contracts are primarily due to the variable factors associated with dispatchable contracts and the cost of natural gas.

Most of the power purchase contracts qualify as normal purchases and normal sales under the provisions of Governmental Accounting Standards Board Technical Bulletin 2003-1 (GASB TB 03-1), Disclosure Requirements for Derivatives Not Reported at Fair Value on the Statement of Net Assets. As a result, market valuation and certain risk information are not required to be disclosed.

However, five contracts do not qualify as normal purchases and normal sales under the provisions of GASB TB 03-1 primarily resulting from either pricing terms that contain variables which are not clearly and closely related to the base energy price or the seller is not a generator of electricity. As a result, certain information regarding these power purchase contracts is required to be disclosed. The fair value of these five contracts at June 30, 2005 approximated \$(104) million, using forward market

**Department of Water Resources Electric Power Fund**  
**Notes to Financial Statements**  
**For the years ended June 30, 2005 and 2004**

**(in millions)**

prices discounted at DWR's internal cost of capital. These contracts, with a total capacity of 2,385 MWh, expire at various times, from December 2005 through December 2011.

**8. Energy Settlements**

DWR and other parties have entered into settlement agreements with various energy suppliers which resolve potential and alleged causes of action against suppliers for their part in alleged manipulation of natural gas and electricity commodity and transportation markets during the 2000 - 2001 California energy crisis.

A settlement agreement with El Paso Corporation and affiliates became effective in 2004. At that time DWR received \$160 million in cash payments, \$50 million of which related to a refund of 2004 power purchase costs and is reflected as a reduction of power purchase expense. DWR received the remaining \$116 million due under the settlement agreement in 2005 of which \$114 million was the collection of amounts receivable at June 30, 2005 and \$2 million was recognized as revenue in 2005.

Also during 2004, settlement agreements with El Paso Electric Company and Portland General Electric Company were completed in which DWR received \$15 million and \$6 million, respectively.

During 2005, settlements with Dynegy Inc., Mirant Corporation, and Duke Energy Corporation became effective and DWR received \$99 million, \$76 million, and \$14 million, respectively. Future revenues from these settlements are subject to conditions outlined in the underlying settlement and allocation agreements.

**9. Related Party Transactions**

The California State Teachers' Retirement System (STRS), which is part of the California state government, participates in two letters of credit with a financial institution. The total commitment underlying the STRS' participation approximates \$177 million and expires on October 30, 2010. There are no outstanding amounts on the letters of credit at June 30, 2005.

**10. Subsequent Event**

The Fund anticipates issuing \$2.59 billion of variable rate refunding bonds in December 2005 to refund approximately \$2.35 billion of current 2002 Series A Bonds. In anticipation of the refunding bond issue, on October 11, 2005 the Fund entered into interest-rate swap agreements to pay fixed rates of interest and receive floating rate payments. Certain swap agreements contain scheduled reductions to outstanding notional amounts that are expected to approximately follow scheduled and/or anticipated reductions in the associated "bond payable" category. The swap agreements are expected to reduce interest-rate risk associated with the variable-rate refunding bonds to be issued by the Fund. The Fund is exposed to potential loss in the event that a swap counterparty is unable to perform under the terms of the agreement. However, the Fund does not anticipate nonperformance by any swap counterparty.

**Department of Water Resources Electric Power Fund**  
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**(in millions)**

The terms and credit ratings for these swap agreements as of October 11, 2005 are summarized below:

Outstanding Notional Amount	Fixed Rate Paid by Fund	Variable Rate <sup>1</sup> Received by Fund	Swap Termination Date	S&P	Counterparty Credit Rating	
					Moody's	Fitch
\$ 355	3.184%	66.5% of LIBOR	5/1/2015	AA-	Aa3	AA-
486	3.228%	66.5% of LIBOR	5/1/2016	AA	Aa2	AA
480	3.282%	66.5% of LIBOR	5/1/2017	AA-	Aa2	AA-
514	3.331%	66.5% of LIBOR	5/1/2018	AA-	Aa3	AA-
306	3.256%	64% of LIBOR	5/1/2020	AA-	Aa3	AA-
453	3.325%	64% of LIBOR	5/1/2022	AA-	Aa2	AA
<u>\$ 2,594</u>						

<sup>1</sup> One month U.S. Dollar London Interbank Offered Rate

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## APPENDIX B

### BOOK-ENTRY SYSTEM

The information in this Appendix concerning The Depository Trust Company, New York, New York (“DTC”) and DTC’s book-entry system has been obtained from sources that DWR, the Underwriters and the Trustees believe to be reliable, but DWR, the Underwriters and the Trustees take no responsibility for the accuracy thereof.

DTC will act as securities depository for the Series 2005 Bonds. The Series 2005 Bonds will be issued as fully-registered securities 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 Series 2005 Bond certificate will be issued for each maturity of Series 2005 Bonds, each in the aggregate principal amount of such maturity, and will be deposited with DTC. If, however, the aggregate principal amount of any maturity exceeds \$500 million, one certificate will be issued with respect to each \$500 million of principal amount, and an additional certificate will be issued with respect to any remaining principal amount of such maturity.

DTC, the world’s largest depository, is a limited-purpose trust company organized under the New York Banking Law, a “banking organization” within the meaning of the New York Banking Law, a member of the Federal Reserve System, a “clearing corporation” within the meaning of the New York Uniform Commercial Code, and a “clearing agency” registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 2 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments from over 85 countries that DTC’s participants (“Direct Participants”) deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants’ accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation (“DTCC”). DTCC, in turn, is owned by a number of Direct Participants of DTC and Members of the National Securities Clearing Corporation, Government Securities Clearing Corporation, MBS Clearing Corporation, and Emerging Markets Clearing Corporation, (NSCC, GSCC, MBSCC, and EMCC, also subsidiaries of DTCC), as well as by the New York Stock Exchange, Inc., the American Stock Exchange LLC, and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly (“Indirect Participants”). DTC has Standard & Poor’s highest rating: AAA. The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at [www.dtcc.com](http://www.dtcc.com).

Purchases of Series 2005 Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the Series 2005 Bonds on DTC’s records. The ownership interest of each actual purchaser of each Series 2005 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 Series 2005 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 Series 2005 Bonds, except in the event that use of the book-entry system for the Series 2005 Bonds is discontinued.

To facilitate subsequent transfers, all Series 2005 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 Series 2005 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 Series 2005 Bonds; DTC's records reflect only the identity of the Direct Participants to whose accounts such Series 2005 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. Beneficial Owners of Series 2005 Bonds may wish to take certain steps to augment the transmission to them of notices of significant events with respect to the Series 2005 Bonds, such as redemptions, tenders, defaults, and proposed amendments to the Series 2005 Bond documents. For example, Beneficial Owners of Series 2005 Bonds may wish to ascertain that the nominee holding the Series 2005 Bonds for their benefit has agreed to obtain and transmit notices to Beneficial Owners.

Redemption notices shall be sent to DTC. If less than all of the Series 2005 Bonds within an issue are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such issue to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to Series 2005 Bonds unless authorized by a Direct Participant in accordance with DTC's Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to Issuer 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 Series 2005 Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Payment of principal, interest, redemption proceeds and other distributions on the Series 2005 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 DWR or the Trustees, 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, its nominee, DWR or the Trustees, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of redemption proceeds, distributions, and dividend payments to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of DWR or the Trustees, 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.

A Beneficial Owner shall give notice to elect to have its Series 2005 Bonds purchased or tendered (in the appropriate Interest Rate Mode and subject to the terms of the Indenture), through its Participant, to the Tender Agent, and shall effect delivery of such Series 2005 Bonds by causing the Direct Participant to transfer the Participant's interest in the Series 2005 Bonds, on DTC's records, to the Tender Agent. The requirement for physical delivery of Series 2005 Bonds in connection with an optional tender or a mandatory purchase will be deemed satisfied when the ownership rights in the Series 2005 Bonds are transferred by Direct Participants on DTC's records and followed by a book-entry credit of tendered Series 2005 Bonds to the Tender Agent's DTC account.

DTC may discontinue providing its services as depository with respect to the Series 2005 Bonds at any time by giving reasonable notice to DWR or the Trustees. Under such circumstances, in the event that a successor depository is not obtained, Series 2005 Bond certificates are required to be printed and delivered.

DWR and the Trustees may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, Series 2005 Bond certificates will be printed and delivered.

THE TRUSTEES, AS LONG AS A BOOK-ENTRY ONLY SYSTEM IS USED FOR THE SERIES 2005 BONDS, WILL SEND ANY NOTICE OF REDEMPTION OR OTHER NOTICES TO OWNERS ONLY TO DTC. ANY FAILURE OF DTC TO ADVISE ANY PARTICIPANT, OR OF ANY PARTICIPANT TO NOTIFY ANY BENEFICIAL OWNER, OF ANY NOTICE AND ITS CONTENT OR EFFECT WILL NOT AFFECT THE VALIDITY OR SUFFICIENCY OF THE PROCEEDINGS RELATING TO THE REDEMPTION OF THE SERIES 2005 BONDS CALLED FOR REDEMPTION OR OF ANY OTHER ACTION PREMISED ON SUCH NOTICE.

DWR and the Trustees cannot and do not give any assurances that DTC will distribute to Participants, or that Participants or others will distribute to the Beneficial Owners, payments of principal of and interest and premium, if any, on the Bonds paid or any redemption or other notices or that they will do so on a timely basis or will serve and act in the manner described in this Official Statement. Neither DWR nor the Trustees are responsible or liable for the failure of DTC or any Direct Participant or Indirect Participant to make any payments or give any notice to a Beneficial Owner with respect to the Series 2005 Bonds or any error or delay relating thereto.

The foregoing description of the procedures and record keeping with respect to beneficial ownership interests in the Series 2005 Bonds, payment of principal of and interest and other payments with respect to the Series 200C Bonds to Direct Participants, Indirect Participants or Beneficial Owners, confirmation and transfer of beneficial ownership interest in such Bonds and other related transactions by and between DTC, the Direct Participants, the Indirect Participants and the Beneficial Owners is based solely on information provided by DTC. Accordingly, no representations can be made concerning these matters and neither the Direct Participants, the Indirect Participants nor the Beneficial Owners should rely on the foregoing information with respect to such matters but should instead confirm the same with DTC or the Participants, as the case may be.

SO LONG AS CEDE & CO. IS THE REGISTERED OWNER OF THE SERIES 2005 BONDS, AS NOMINEE OF DTC, REFERENCES HEREIN TO THE HOLDERS SHALL MEAN CEDE & CO., AS AFORESAID, AND SHALL NOT MEAN THE BENEFICIAL OWNERS OF THE SERIES 2005 BONDS.

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## APPENDIX C

### SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE

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## SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE

The following is a summary of certain provisions of the Indenture. The summary does not purport to be complete or definitive and is qualified in its entirety by reference to the Indenture, copies of which are on file with the Trustee and Co-Trustee.

### Definitions

For purposes of this Summary, capitalized terms shall have the meanings assigned to them below, or in other cases as contained elsewhere in this Official Statement as indicated in Appendix G.

**“Accreted Value”** means, with respect to any Capital Appreciation Bonds, (i) as of any Valuation Date, the amount set forth for such date in the Supplemental Indenture authorizing such Capital Appreciation Bonds and (ii) as of any date other than a Valuation Date, the sum of (a) the Accreted Value on the preceding Valuation Date and (b) the product of (1) 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 succeeding Valuation Date, and (2) the difference between the Accreted Values for such Valuation Dates. Accreted Value shall be computed on a 30/360-day basis.

**“Act”** means Division 27 (commencing with Section 80000) of the State Water Code, as amended from time to time.

**“Additional Emergency Measures”** or **“Emergency Measures”** means Executive Order No. D-56-02 dated May 23, 2002, or any Proclamation or Order of the Governor of the State hereafter issued pursuant to the California Emergency Services Act (Chapter 7, Division 1, Title 2 of the California Government Code, as amended) (including, but not limited to, any regulations issued pursuant thereto) adopted in response to or in anticipation of the need to assure the availability of power to retail end-use customers in the State due to the inability or failure of an Electrical Corporation to purchase such power following the end of the Department’s authority to enter into new Power Supply Contracts under Assembly Bill 1X.

**“Administrative Agent”** has the meaning set forth in a Credit Facility or Liquidity Facility, as the case may be.

**“Administrative Cost Account”** means the Account by that name established under the Indenture.

**“Aggregate Debt Service”** means, for any period and as of any date of calculation, the sum of the amounts of Debt Service for such period with respect to all Series of Bonds.

**“Alternate Debt Service Reserve Account Deposit”** means any irrevocable surety bond, insurance policy, letter of credit or any other similar obligation provided to the Trustee as a substitute for the deposit of cash and/or Authorized Investments, or another Alternate Debt Service Reserve Account Deposit, in the Debt Service Reserve Account.

**“Applicable Principal and Interest Coverage”** means the aggregate principal amount of Series 2005 Bonds of a Series supported by a Liquidity Facility or Credit Facility, as the case may be, plus the minimum number of days of interest, calculated at the rate, that in the judgment (evidenced by a written rating confirmation) of each Rating Agency shall be required to maintain the applicable rating on the Series 2005 Bonds of such Series.

**“Assembly Bill 1X”** means Chapter 4 of the Statutes of 2001 (AB 1 of the First Extraordinary Session) of the State, as amended from time to time, including, but not limited to, Chapter 9 of the Statutes of 2001 (SB 31 of the First Extraordinary Session).

**“Authorized Investments”** means and includes any of the following securities, if and to the extent the same are at the time legal for investment of the Department’s funds pursuant to any law, and to the extent permitted under any applicable regulation, guideline and policy of the Department, as each is in effect from time to time:

(i) bonds or interest-bearing notes or obligations of the United States, or those for which the faith and credit of the United States are pledged for the payment of principal and interest;

(ii) bonds or interest-bearing notes or obligations that are guaranteed as to principal and interest by a federal agency of the United States;

(iii) bonds of the State or bonds for which the faith and credit of the State are pledged for the payment of principal and interest;

(iv) bonds or warrants, including, but not limited to, revenue warrants, of any county, city, metropolitan water district, California water district, California water storage district, irrigation district in the State, municipal utility district or school district of the State;

(v) bonds, consolidated bonds, collateral trust debentures, consolidated debentures or other obligations issued by general land banks or federal intermediate credit banks established under the Federal Farm Loan Act, as amended, debentures and consolidated debentures issued by the Central Bank for Cooperatives and banks for cooperatives established under the Farm Credit Act of 1933, as amended, bonds or debentures of the Federal Home Loan Bank Board established under the Federal Home Loan Bank Act, stocks, bonds, debentures and other obligations of the Federal National Mortgage Association established under the National Housing Act, as amended, and the bonds of any federal home loan bank established under said act, obligations of the Federal Home Loan Mortgage Corporation, and bonds, notes and other obligations issued by the Tennessee Valley Authority under the Tennessee Valley Authority Act, as amended;

(vi) commercial paper rated within the top Rating Category by a Rating Agency and issued by corporations (1) organized and operating within the United States, (2) having total assets in excess of \$500,000,000 and (3) approved by the Pooled Money Investment Board of the State, provided, however that eligible commercial paper may not exceed one hundred eighty (180) days’ maturity, represent more than 10% of the outstanding paper of an issuing corporation nor exceed 30% of the resources of an investment program, and that at the request of the Department, such investment shall be secured by the issuer by depositing with the Trustee securities authorized by Section 53651 of the California Government Code of a market value of at least 10% in excess of the amount of the Department’s investment;

(vii) bills of exchange or time drafts drawn on and accepted by a commercial bank the general obligations of which are rated within the top two Rating Categories by a Rating Agency, otherwise known as banker’s acceptances, which are eligible for purchase by the Federal Reserve System;

(viii) negotiable certificates of deposit issued by a nationally or state-chartered bank or savings and loan association or by a state-licensed branch of a foreign bank which, to the extent they are not insured by federal deposit insurance, are issued by an institution the general obligations of which are rated in one of the top two Rating Categories by a Rating Agency;

(ix) bonds, debentures and notes issued by corporations organized and operating within the United States which securities are rated in one of the top two Rating Categories by a Rating Agency;

(x) interest-bearing accounts in state or national banks or in state or federal savings and loan associations having principal offices in the State, the deposits of which shall be secured at all times and in the same manner as state moneys are by law required to be secured;

(xi) deposits in the Surplus Money Investment Fund as referred to in the California Government Code;

(xii) repurchase agreements or reverse repurchase agreements, as such terms are defined in and pursuant to the terms of Section 16480.4 of the California Government Code;

(xiii) collateralized or uncollateralized investment agreements or other contractual arrangements with corporations, financial institutions or national associations within the United States, provided that the senior long-term debt of such corporations, institutions or associations is rated within the top two Rating Categories by a Rating Agency;

(xiv) money market funds that invest solely in obligations described in clause (i) of this definition; or

(xv) such other investments as may be authorized by a Supplemental Indenture, provided that each Rating Agency has confirmed in writing to the Trustee that the use of such additional investments will not, by itself, result in the withdrawal, suspension or downgrade of any rating issued by such Rating Agency with respect to any Outstanding Bonds.

“**Authorized Officer**” means the Director, any Deputy Director, the Chief, Division of Fiscal Services, Deputy Controller and the Chief Counsel of the Department, and any other individual authorized by the Director to perform the act or sign the document in question.

“**Bank**” means any (i) bank or trust company organized under the laws of any state of the United States of America, (ii) national banking association, (iii) savings bank or savings and loan association chartered or organized under the laws of any state of the United States of America, or (iv) federal branch or agency pursuant to the International Banking Act of 1978 or any successor provisions of law, or domestic branch or agency of a foreign bank which branch or agency is duly licensed or authorized to do business under the laws of any state or territory of the United States of America.

“**Bond Charge**” has the same meaning as that term is defined in the 2002 Rate Agreement, including, without limitation, any Bond Charges imposed on power furnished by an Electric Service Provider (as defined in the 2002 Rate Agreement).

“**Bond Charge Collection Account**” means the account by that name established under the Indenture.

“**Bond Charge Payment Account**” means the account by that name established under the Indenture.

“**Bond Charge Revenues**” means Revenues received by the Department arising from Bond Charges.

“**Bond Related Costs**” has the same meaning as that term is defined in the 2002 Rate Agreement, and shall include the items of cost specified in section D.3 under the caption “Application and Flow of Funds” below.

“**Bonds**” means any obligations, issued in any form of debt, authorized by the Indenture and secured by a pledge of and lien on the Trust Estate on a parity with each other and with Parity Obligations, including, but not limited to, bonds, notes, bond anticipation notes, and commercial paper, but such term shall not include any Subordinated Indebtedness or Subordinated Obligations. “Bonds” may also include Interim Financing Notes as described under “Special Provisions Relating to Enhancement Facilities, Qualified Swaps, Other Similar Arrangements and Interim Financing Notes” below.

**“Business Day”** (A) with respect to the Bonds, means (a) any day of the year other than (i) a Saturday or Sunday, (ii) a State legal holiday, (iii) any day which shall be in the city of Sacramento, California, or the city in which the Co-Trustee or relevant office of any Paying Agent, Registrar or Securities Depository or, if any Bond is supported by an Enhancement Facility, the provider of such Enhancement Facility is located, a legal holiday or a day on which Banks in any of such cities are required or authorized by law or other government action to close, or (b) with respect to any Series of Bonds, as may be provided by Supplemental Indenture, and (B) with respect to Series 2005 Bonds, any day of the year other than (i) a Saturday and Sunday, (ii) a State legal holiday, (iii) any day which shall be in Sacramento, California, or the city in which the Principal Office of the Trustee, the Co-Trustee or the relevant office of any Paying Agent or Registrar is located a legal holiday or a day on which Banks are authorized or required by law or other government action to close, or (iv) with respect to the Bonds of a Series, any day which shall be in the city in which the relevant office of the Tender Agent, the Auction Agent, any Broker-Dealer, the Remarketing Agent, the Administrative Agent, any Credit Facility Provider or any Liquidity Facility Provider, if any, for the Bonds of such Series is located a legal holiday or a day on which Banks are authorized or required by law or other government action to close.

**“Capital Appreciation Bonds”** means Bonds as to which interest is payable only at the maturity or prior redemption of such Bonds; provided, however, that if any such Bonds are converted to or from Bonds as to which interest is payable periodically, such Bonds shall be deemed to be Capital Appreciation Bonds only after or until such conversion, as the case may be. For the purposes of (i) receiving payment of the Redemption Price if a Capital Appreciation Bond is redeemed prior to maturity, or (ii) computing the principal amount of Bonds held by the Owner of a Capital Appreciation Bond in giving to the Department or the Trustee any notice, consent, request, or demand pursuant to the Indenture for any purpose whatsoever, the principal amount of a Capital Appreciation Bond on any date shall be deemed to be its Accreted Value as of such date.

**“Commercial Paper”** means Bonds issued as part of a program of short-term Bonds having the characteristics of commercial paper in that (i) such Bonds have a stated maturity not later than 270 days from their date of issue and (ii) maturing Bonds of such program may be paid with the proceeds of Bonds having the characteristics of Commercial Paper. Notwithstanding the foregoing, Commercial Paper may be paid with the proceeds of other Bonds.

**“Commission”** means the Public Utilities Commission of the State, or any successor to the rights, duties and obligations of the Commission under the Act.

**“Consultant”** means an accountant or firm of accountants (which may be the accountant or firm of accountants then serving as the auditor of the Department), or a management consultant or firm of management consultants, or an engineer or firm of engineers, which, in any case, shall be of recognized standing in the field of electric utility rate consulting, selected by the Department, and may be regularly retained to provide services to the Department but shall not be an officer or employee of the State.

**“Costs”** means costs, expenses and purposes for which Bonds may be issued under the Act, including, but not limited to, the following: (i) costs of Power and transmission, scheduling, and other related expenses incurred by the Department, including, but not limited to, all amounts payable by the Department, of whatever kind and nature, under and pursuant to Power Supply Contracts and costs of avoiding purchasing Power for retail end-use customers paid or incurred pursuant to an Additional Emergency Measure; (ii) reimbursement of expenditures made from the Electric Power Fund for such purposes; (iii) repayment to the General Fund of the State of appropriations made to the Electric Power Fund pursuant to Assembly Bill 1X or Senate Bill 7X, repayment to the General Fund of appropriations made to the Electric Power Fund after the effectiveness of Assembly Bill 1X for purposes of Division 27 of the State Water Code, and repayment of General Fund moneys expended by the Department pursuant to the 2001 Emergency Measures; (iv) costs of establishing or maintaining reserves required or permitted by the Indenture, including, but not limited to, debt service and operating reserves; (v) costs of issuing Bonds and Interim Financing Notes or costs incidental to their payment or security, including, but not limited to, fees, expenses, and costs payable, and reimbursements, under Enhancement Facilities and the Credit and Security Agreement; (vi) capitalized interest on Bonds; and (vii) payment of principal, interest, and

redemption, tender or purchase price of any (a) Bonds issued by the Department for the payment of any Costs, (b) Bonds issued to refund other Bonds, or (c) any other bonds, notes, or other evidences of indebtedness issued by the Department for purposes of the Act, including the Interim Financing Notes. Notwithstanding the foregoing, Costs shall not include (1) depreciation or obsolescence charges or reserves therefor, (2) amortization of intangibles or other bookkeeping entries of a similar nature; or (3) any costs of the Department relating to a Separately Financed Program.

“**Co-Trustee**” means U.S. Bank National Association, and its successor or successors and any other Person which may at any time be substituted in its place pursuant to the Indenture.

“**Counsel’s Opinion**” means an opinion signed by an attorney or firm of attorneys of nationally recognized standing in the field of law relating to municipal bonds selected by the Department.

“**Credit and Security Agreement**” means the Credit and Security Agreement, dated as of June 26, 2001, among the State acting through the Department, various lenders and Morgan Guaranty Trust Company of New York as agent for such lenders, pursuant to which the Interim Financing Notes were issued and are secured, as supplemented and amended from time to time.

“**Credit Facility**” means the Enhancement Facility which guarantees, insures or secures the payment of principal of and interest on the Series 2005 Bonds of any Series which may be obtained by the Department pursuant to the Indenture, any agreement providing for the issuance thereof and any extensions or renewals thereof, and after the Expiration or Termination of any Credit Facility shall mean a Substitute Credit Facility therefor, all as the same may be amended and supplemented.

“**Credit Facility Provider**” means, with respect to each Credit Facility, the issuer thereof.

“**Credit Facility Reimbursement Obligation**” has the meaning as defined under “Special Provisions Relating to Enhancement Facilities, Qualified Swaps, Other Similar Arrangements and Interim Financing Notes” below.

“**Debt Service**” means, for purposes of determining deposits to and balances required to be on deposit in the Bond Charge Payment Account, the Debt Service Reserve Requirement, and the additional Bonds test as provided in the Indenture, for any period and as of any date of calculation, with respect to any Outstanding Bonds, an amount equal to the sum of (i) interest accruing during such period on such Bonds, except to the extent that such interest is to be paid from deposits in the Bond Charge Payment Account made from the proceeds of Bonds or Subordinated Indebtedness, and (ii) that portion of each Principal Installment for such Bonds which would accrue during such period if such Principal Installment were deemed to accrue daily in equal amounts from the next preceding Principal Installment due date for such Bonds (or, if there shall be no such preceding Principal Installment due date or such preceding Principal Installment due date is more than one (1) year (or, in the case of the initial Principal Installment due no later than December 31, 2004 for Bonds delivered in 2002, such period as may be provided by Supplemental Indenture) prior to the due date of such Principal Installment, then from a date one (1) year preceding the due date of such Principal Installment or from the date of issuance of such Bonds, whichever date is later). For purposes of such calculations, the following assumptions are to be used:

(i) such interest and Principal Installments shall be calculated on the assumptions that (a) no Bonds (except for Option Bonds actually tendered for payment and not purchased in lieu of redemption prior to the redemption date thereof) Outstanding at the date of calculation will cease to be Outstanding except by reason of the payment of each Principal Installment on the due date thereof and (b) the principal amount of Option Bonds tendered for payment shall be deemed to be payable on the date required to be paid pursuant to such tender;

(ii) if 20% or more of the principal of such Bonds is not due until the final stated maturity of such Bonds, principal and interest on such Bonds may, at the option of the Department, written notice of

which shall be signed by an Authorized Officer and filed with the Trustee, be treated as if such principal and interest were due based upon an amortization of principal resulting in approximately level debt service (principal and interest) over the respective terms of such Bonds;

(iii) interest accruing on Variable Rate Bonds during any future period shall be assumed to accrue at a rate equal to the greater of (a) 130% of the highest average interest rate on such Variable Rate Bonds in any calendar month during the twelve (12) calendar months ending with the month preceding the date of calculation, or such shorter period that such Variable Rate Bonds shall have been Outstanding, or (b) 4.0%,

(iv) the principal of Bonds issued as Commercial Paper will be treated as if such principal were due based upon level amortization of principal from the date of calculation to the latest maturity date of any Bonds, and the interest on such Commercial Paper shall be calculated as if such Commercial Paper were Variable Rate Bonds;

(v) the principal and interest portions of the Accreted Value of Capital Appreciation Bonds becoming due at maturity or by virtue of a Sinking Fund Installment shall be included in the calculations of accrued and unpaid and accruing interest or Principal Installments in such manner and during such period of time as is specified in the Supplemental Resolution authorizing such Capital Appreciation Bonds;

(vi) notwithstanding paragraphs (iii) or (iv) above, if the Department, in connection with any Variable Rate Bonds or Commercial Paper, has entered into a Qualified Swap that provides that the Department is to pay to the counterparty an amount determined based upon a fixed rate of interest on such Outstanding principal amount of such Variable Rate Bonds or Commercial Paper, and that the counterparty is to pay to the Department an amount determined based upon a variable rate of interest on such Outstanding principal amount of such Variable Rate Bonds or Commercial Paper (a “variable rate payment”) or the amount by which the rate at which such Variable Rate Bonds or Commercial Paper bear interest exceeds a stated rate of interest or, if the Department has entered into a Qualified Swap that provides that the Department is to pay to the counterparty one variable rate payment and that the counterparty is to pay to the Department a different variable rate payment, for so long as and to the extent that such Qualified Swap remains in full force and effect it shall be assumed that such Variable Rate Bonds and Commercial Paper bear interest at a rate equal to the sum of (A) the fixed rate of interest to be paid by the Department or the rate in excess of which the counterparty is to make payment to the Department in accordance with such Qualified Swap, and (B) the greater of (if positive) (1) the average difference between the actual interest rate paid by the Department on such Variable Rate Bonds or Commercial Paper and the variable interest rate the relevant counterparty paid to the Department, taking into account all variable rate payments, during the twelve (12) calendar months ending with the calendar month preceding the date of calculation, or such shorter period that such Variable Rate Bonds or Commercial Paper shall have been Outstanding, and (2) the difference between the actual interest rate paid by the Department on such Variable Rate Bonds or Commercial Paper and the variable interest rate received from the relevant counterparty, taking into account all variable rate payments, as calculated at the end of the calendar month preceding the date of calculation;

(vii) if the Department, in connection with any fixed rate Bonds, has entered into a Qualified Swap that provides that the Department is to pay to the counterparty an amount determined based upon a variable rate of interest on the Outstanding principal amount of such Bonds, it shall be assumed that such Bonds bear interest at the variable rate of interest to be paid by the Department, with interest on such Bonds calculated as if they were Variable Rate Bonds as described in paragraph (iii) above; provided, however, if the counterparty is to pay to the Department a fixed rate of interest on the amount of such Bonds that is less than the fixed rate payable thereon by the Department, it shall be assumed that such Bonds bear additional interest at the rate which is the difference between the fixed rates payable by and to the Department; and

(viii) principal and interest payments on Bonds shall be excluded to the extent such payments are to be paid from amounts then currently on deposit with the Trustee or other Fiduciary in escrow specifically therefor and restricted to Defeasance Securities.

**“Debt Service Reserve Account”** means the account by that name established under the Indenture.

**“Debt Service Reserve Requirement”** means, as of any date of calculation, an amount equal to Maximum Aggregate Annual Debt Service. In furtherance of the covenant described below under “Covenant Relating to Retirement of Bonds”, for the purpose of calculating the Debt Service Reserve Requirement at the time of, and deposit to be made into the Debt Service Reserve Account in connection with, the issuance of the initial Series of Bonds (or more than one Series of Bonds delivered on the same date as the initial Series of Bonds) (collectively, the “initial Bonds”), Debt Service on the initial Bonds shall be calculated by assuming that the initial Bonds will mature in such amounts and at such times (with the initial Bonds assumed to bear interest as provided in the definition of Debt Service) as will result in substantially level debt service (to the extent contemplated by such covenant of the Department) on the initial Bonds, without regard to any additional Series of Bonds.

**“Defeasance Security”** means:

- (i) cash;
- (ii) an Authorized Investment specified in clause (i), (ii), (iii) or (v) of the definition thereof, which is not callable or redeemable at the option of the issuer thereof;
- (iii) an Authorized Investment specified in clause (iv) of the definition thereof (a “Municipal Bond”), which Municipal Bond is fully secured as to principal and interest by an irrevocable pledge of moneys or direct and general obligations of, or obligations guaranteed by, the United States of America, which moneys or obligations are segregated in trust and pledged for the benefit of the holder of the Municipal Bond, and which Municipal Bond is rated in the highest Rating Category by at least two Rating Agencies and provided, however, that such Municipal Bond is accompanied by a Counsel’s Opinion to the effect that such Municipal Bond is not subject to redemption prior to the date the proceeds of such Municipal Bond will be required for the purposes of the investment being made therein; or
- (iv) any other investment designated in a Supplemental Indenture as a Defeasance Security for purposes of defeasing the Bonds authorized by such Supplemental Indenture, provided that each Rating Agency has confirmed in writing to the Trustee that the use of such other investment will not, by itself, result in the withdrawal, suspension or downgrade of any rating issued by such Rating Agency with respect to any such Bonds to be defeased.

**“Department”** means the State of California Department of Water Resources, existing pursuant to Article 1 (commencing with Section 120) of Chapter 2 of Division 1 of the California Water Code, or any successor to the rights, duties and obligations of the Department under the Act and the Indenture.

**“Direct Access Power Charge”** means any charge imposed by the Commission (by an order that is final and non-appealable) on, and received by the Department from, any Person receiving power from an Electric Service Provider intended to recover the Department’s Revenue Requirements other than Bond Related Costs, and shall in no event include Bond Charges; provided, however, that Bond Charges may be separately imposed on such Persons.

**“Direct Access Power Charge Revenues”** means Revenues received by the Department arising from Direct Access Power Charges.

“**Direct-Pay Credit Facility**” means a Credit Facility issued in the form of a letter of credit and designated by the issuer thereof as a “Direct Pay Letter of Credit.”

“**Director**” means the Director of Water Resources of the State, or any successor to the rights, duties and obligations of the Director under the Act and the Indenture.

“**Electrical Corporation**” has the same meaning as that term is defined in Section 218 of the Public Utilities Code.

“**Electric Power Fund**” means the fund by that name established under the Indenture.

“**Electric Service Provider**” has the meaning given in the 2002 Rate Agreement.

“**Electronic Means**” means telecopy, facsimile transmission, e-mail transmission or other similar electronic means of communication.

“**Enabling Measures**” means, collectively, the Act and the Additional Emergency Measures, or any of them, as appropriate.

“**Enhancement Facility**” means any letter of credit, standby purchase agreement, line of credit, policy of bond insurance, surety bond, guarantee or similar instrument, or any other agreement, securing, providing liquidity for, supporting or enhancing Outstanding Bonds, or any combination of the foregoing, or any agreement relating to the reimbursement thereof whether or not such instrument or agreement has been drawn upon, obtained by the Department.

“**Events of Default**” means the events defined as such under caption “Events of Default and Remedies” below.

“**Excess Amounts**” has the meaning specified in section F under the caption “Application and Flow of Funds” below.

“**Expiration**” (and other forms of “expire”) means, when used with respect to a Credit Facility or a Liquidity Facility, the expiration of such Credit Facility or Liquidity Facility in accordance with its terms.

“**Fiduciary**” or “**Fiduciaries**” means the Trustee, the Co-Trustee, any Registrar, any Paying Agent, or any or all of them, as may be appropriate.

“**Financing Documents**” means any resolution, indenture (including the Indenture), trust agreement, loan agreement, revolving credit agreement, reimbursement agreement, standby purchase agreement or other agreement or instrument adopted or entered into by the Department authorizing, securing or enhancing any evidence of indebtedness issued pursuant to the Act, including the Bonds, Parity Obligations and Subordinated Indebtedness, as from time to time amended or supplemented in accordance therewith.

“**Fiscal Year**” means the twelve-month period commencing on July 1 of each year; provided, however, that the Department may at any time adopt a different twelve-month period as the Fiscal Year, in which case July 1, when used herein with reference to Fiscal Year, shall be construed to mean the first day of the first calendar month of such different Fiscal Year.

“**Fourth Supplemental Indenture**” means the Fourth Supplemental Trust Indenture among the Department, the Trustee, and the Co-Trustee, relating to the Series 2005 Bonds

“**Indenture**” means the Trust Indenture among the Department, the Trustee and the Co-Trustee, as from time to time amended or supplemented by Supplemental Indentures.

**“Interest Payment Date”** means (i) with respect to Series 2005 Bonds of a Series bearing interest at a Daily Rate or a Weekly Rate, the first Business Day of each calendar month, (ii) with respect to Series 2005 Bonds of a Series bearing interest at a Flexible Rate, the first Business Day following the end of each Flexible Period, (iii) with respect to Series 2005 Bonds of a Series bearing interest at a Term Rate or the Fixed Rate, the first day of May or November occurring not less than three months after the first day of the Interest Period and thereafter semiannually on the first day of each May and November, (iv) with respect to Series 2005 Bonds of a Series bearing interest at an Auction Period Rate, on such dates as set forth in the Indenture, and (v) in each such case, each mandatory Purchase Date and the Maturity Date thereof. Notwithstanding the foregoing, the Interest Payment Date with respect to Series 2005 Bonds of a Series during the Initial Interest Period shall be as prescribed in the Fourth Supplemental Indenture.

**“Interest Period”** means the period during which the Series 2005 Bonds of a Series shall bear interest at a Daily Rate, Weekly Rate, Flexible Rate, Term Rate, Auction Period Rate or Fixed Rate determined as follows:

(i) each Daily Period shall commence on a Business Day and end on the day preceding the next succeeding Business Day;

(ii) each Weekly Period shall be a period of seven calendar days and shall commence on the calendar day, determined by the Department, of a calendar week (the “Weekly Period Commencement Day”) and end on the next preceding calendar day of the next succeeding calendar week (the “Weekly Period Ending Day”), provided that the first Weekly Period following the Initial Interest Period or a change in the Interest Rate Mode to a Weekly Rate Mode shall commence on the Business Day immediately following the last day of the preceding Interest Period, may be less than seven calendar days and shall end on the day before the next Weekly Period Commencement Day;

(iii) each Flexible Period shall commence on the effective date of a change in the Interest Rate Mode to a Flexible Rate Mode for such Series 2005 Bonds or on the day immediately succeeding the last day of the immediately preceding Flexible Period for such Series 2005 Bonds, and shall end on a day preceding a Business Day, and shall be from one (1) to two hundred seventy (270) days as determined by the Remarketing Agent;

(iv) each Term Period shall commence on the effective date of a change in the Interest Rate Mode to a Term Rate Mode or on the day immediately succeeding the last day of the immediately preceding Interest Period and shall end on the date specified by the Department pursuant to the Fourth Supplemental Indenture, which date so specified shall be succeeded by a Business Day and shall be a day that is at least one year after the first day of such Term Period and that is not after the Maturity Date;

(v) each Auction Period shall be determined as set forth in the Fourth Supplemental Indenture; and

(vi) the Fixed Period shall commence on the effective date of a change in the Interest Rate Mode to a Fixed Rate Mode and end on the earlier of the day next preceding the effective date of a change in the Interest Rate Mode from such Fixed Rate Mode to another Interest Rate Mode and the Maturity Date of the Series 2005 Bonds of such Series.

Notwithstanding the foregoing, the Initial Interest Period for Series 2005 Bonds of a Series shall be as prescribed by the Fourth Supplemental Indenture.

**“Interest Rate Mode”** means, with respect to any Series 2005 Bond of a Series, the method by which the interest rate thereon shall be determined pursuant to the Fourth Supplemental Indenture and in particular shall mean the method for determining a Daily Rate, Weekly Rate, Flexible Rate or Term Rate, Auction Period Rate or the Fixed Rate, as the case may be.

“**Interim Financing Notes**” means, collectively, the Department’s “Tax-Exempt Bonds” and “Taxable Bonds” issued and outstanding under the Credit and Security Agreement.

“**Liquidity Facility**” means the Enhancement Facility which provides liquidity for the Series 2005 Bonds of any Series which may be obtained by the Department pursuant to the Fourth Supplemental Indenture, any agreement providing for the issuance thereof and any extensions or renewals thereof, and after the Expiration or Termination of any Liquidity Facility shall mean a Substitute Liquidity Facility, all as the same may be amended and supplemented.

“**Liquidity Facility Provider**” means, with respect to each Liquidity Facility, the issuer thereof.

“**Liquidity Facility Reimbursement Obligation**” has the meaning as defined under “Special Provisions Relating to Enhancement Facilities, Qualified Swaps, Other Similar Arrangements and Interim Financing Notes” below.

“**Market Rate**” means the minimum rate of interest to be borne by any Series 2005 Bonds in an Interest Rate Mode for the relevant Interest Period that, in the judgment of the Remarketing Agent, allows the Remarketing Agent to remarket such Bonds on the date such Bonds are changed to a different Interest Rate Mode or continued in successive Interest Periods within such Interest Rate Mode, at a price (without regard to accrued interest) equal to the principal amount thereof, provided, however, that in no event shall any rate so determined exceed the Maximum Rate.

“**Master Credit and Liquidity Agreement**” or “**Master Bank Agreement**” means the Master Credit, Liquidity and Participation Agreement, among the State acting through the Department, various fronting banks, various participating banks, JPMorgan Chase Bank, as administrative agent, Bayerische Landesbank, acting through its New York Branch, Dexia Crédit Local, acting through its New York Agency, and The Bank of New York, as co-syndication agents, and BNP Paribas, acting through its San Francisco Branch, as documentation agent.

“**Maximum Aggregate Annual Debt Service**” means, as of any date of calculation, an amount equal to the maximum Aggregate Debt Service coming due on Bonds then Outstanding in any calendar year thereafter, commencing with the then current calendar year, excluding interest to be paid from the proceeds of Bonds or Subordinated Indebtedness and on deposit in the Bond Charge Payment Account.

“**Maximum Rate**” means, with respect to Series 2005 Bonds of a Series other than Bank Bonds, the lesser of (a) the highest interest rate which may be borne by such Series 2005 Bonds under State law, if any, (b) while any Credit Facility (other than a bond insurance policy) agreed to by the Department is in effect with respect to such Series 2005 Bonds, the interest rate used to calculate the amount of the interest component of the Applicable Principal and Interest Coverage for such Series 2005 Bonds and (c) while any Liquidity Facility agreed to by the Department is in effect with respect to such Series 2005 Bonds, the interest rate used to calculate the amount of the interest component of the Applicable Principal and Interest Coverage for such Series 2005 Bonds. Notwithstanding the foregoing, the Maximum Rate applicable to Bonds bearing interest at an Auction Period Rate shall be the Maximum Interest Rate prescribed by the Fourth Supplemental Indenture.

“**Minimum Operating Expense Available Balance**” means, at the time Revenue Requirements are submitted to the Commission pursuant to the Indenture, (i) for so long as the Department is procuring all or a portion of the Residual Net Short, \$1 billion, and (ii) thereafter, the maximum amount projected by the Department by which Operating Expenses exceed Power Charge Revenues during any one calendar month during that Revenue Requirement Period. Such projections shall be based on such assumptions as the Department deems to be appropriate after consultation with the Commission and may take into account a range of possible future outcomes.

**“Notice Parties”** means, with respect to Series 2005 Bonds of a Series, the Department, the Trustee, the Co-Trustee, the Paying Agent, the Remarketing Agent, the Tender Agent, the Auction Agent, all Broker-Dealers, the Credit Facility Provider and the Liquidity Facility Provider, if any, relating to such Series 2005 Bonds.

**“Operating Account”** means the account by that name established under the Indenture.

**“Operating Expenses”** means the following costs and expenses of the Department in connection with its activities as permitted under the Enabling Measures: (i) payments for the purchase of Power and the delivery of such Power including, but not limited to, amounts paid under short-term Power Supply Contracts, Priority Long Term Power Contracts and other long-term Power Supply Contracts, termination and liquidation damage payments thereunder, payments thereunder relating to emission costs and emission opportunity costs, amounts payable in respect of balance of month-ahead Power, hour-ahead Power and real time balancing Power, including in-market and out-of-market purchases, costs of transmission, distribution, scheduling, dispatch and other expenses of the Department in connection with the delivery of its Power, and costs of avoiding purchasing Power for retail end-use incurred pursuant to an Additional Emergency Measure; (ii) payments for or in connection with fuel to be used in the production of Power purchased by the Department, whether paid as a charge under a Power Supply Contract or a separate agreement for the purchase, transportation or storage of fuel for use in the generation of Power, including, but not limited to, termination and liquidated damage payments under fuel purchase agreements, payments under options or other fuel or electricity instruments, and payments under financial instruments relating to fuel costs or costs related to fuel costs; (iii) payments under any security agreements executed in connection with Power Supply Contracts or in connection with agreements for the purchase, transportation and storage of fuel, or any other agreement, relating to the purchase of Power; (iv) reasonable administrative, general and overhead expenses and payments for employee benefits, including, but not limited to, payments to savings, pension, retirement, health and hospitalization funds; (v) insurance premiums including, but not limited to, bond and Qualified Swap insurance premiums; (vi) legal and engineering expenses; (vii) expenses for consulting and technical services; (viii) charges paid by the Department pursuant to any licenses, orders or mandates from any agency or regulatory body having lawful jurisdiction; (ix) any taxes, governmental charges, and any other similar costs and expenses required to be paid by the Department, and costs required by the California Independent System Operator to be paid by the Department or imposed on the Department by regulatory or other governmental requirements; (x) costs of complying with any arbitrage restrictions or rebate requirements relating to the Bonds under Section 148 of the Internal Revenue Code of 1986 as amended, or a successor statute, and applicable regulations thereunder; (xi) such other costs and expenses as may be provided for in a Rate Agreement as being recoverable as part of Revenue Requirements; and (xii) such other costs and expenses with respect to the sale of Power to local publicly owned electric utilities, as defined in Assembly Bill 1X, or in connection with the exchange of Power or the sale, transfer or other disposition of Power not required for use within the State as permitted by the Act, which would constitute current operating expenses under generally accepted accounting principles or statutory accounting principles as in effect from time to time and applicable to governmental units such as the Department. Notwithstanding the foregoing, Operating Expenses shall not include (a) any repayments to the General Fund of the State of advances made to the Department from amounts appropriated to the Electric Power Fund or interest thereon payable at the Pooled Money Investment Rate; (b) principal, Redemption Price and Purchase Price of and interest on Bonds; (c) debt service on or payments under Parity Obligations, Subordinated Indebtedness or Subordinated Obligations; (d) principal of and interest on the Interim Financing Notes and other payments required to be made by the Department under the Credit and Security Agreement; (e) depreciation or obsolescence charges or reserves therefor; (f) amortization of intangibles or other bookkeeping entries of a similar nature; (g) any amounts paid from Bond Charge Revenues pursuant to section D.1 under the caption “Application and Flow of Funds” below; or (h) any costs and expenses attributable to a Separately Financed Program.

**“Operating Reserve Account”** means the account by that name established under the Indenture.

**“Operating Reserve Account Requirement”** or **“Minimum Operating Reserve Account Requirement”** means, during each Revenue Requirement Period, the greater of (i) the largest aggregate amount projected by the Department by which Operating Expenses exceed Power Charge Revenues during any

consecutive seven (7) calendar months commencing in such Revenue Requirement Period, and (ii) either (A) 18% of the Department's projected annual Operating Expenses for any Revenue Requirement Period in which the Department is procuring all or a portion of the Residual Net Short and which commences prior to 2006, or (B) 12% of the Department's projected annual Operating Expenses for any Revenue Requirement Period in which the Department is not procuring all or a portion of the Residual Net Short or which commences after 2005; provided, however, that solely for purposes of (A) and (B) above for Revenue Requirement Periods commencing after 2003, the projected amount shall not be less than the applicable percentage of the Department's Operating Expenses for the most recent twelve (12) calendar month period for which the Department determines that reasonably full and complete Operating Expense information is available, adjusted as described in the next sentence. If the Department was financially responsible and liable under a Power Supply Contract during all or a portion of the applicable twelve (12) calendar month period, but financial responsibility has been assumed by another Person and the Department has been entirely relieved of financial liability and all other liabilities under the contract, or the contract has terminated or will terminate by its terms prior to the end of the Revenue Requirement Period for which the Operating Reserve Account Requirement is being calculated, then the relevant costs associated with that contract shall be excluded from the calculation of the historical Operating Expenses. If amended Revenue Requirements are filed with the Commission during any Revenue Requirement Period, the Operating Reserve Account Requirement shall be recalculated for the remainder of such Revenue Requirement Period as provided above. Notwithstanding the foregoing, in connection with the determination of whether additional Bonds may be issued upon compliance with the Indenture, the relevant calculation under clause (i) above shall be made in respect of a consecutive seven (7) calendar month period in the test period specified by the applicable provision of the Indenture. All projections referenced in this paragraph shall be based on such assumptions as the Department deems to be appropriate after consultation with the Commission and, in the case of clause (i) above, may take into account a range of possible future outcomes. The Operating Reserve Account Requirement shall include, but shall not be limited to, the Priority Contract Contingency Reserve Amount.

**“Option Bonds”** means Bonds which by their terms may be tendered by and at the option of the Owner thereof to the Department or to the issuer of an Enhancement Facility providing liquidity with respect to such Bonds, for purchase prior to the stated maturity thereof, or the maturities of which may be extended by and at the option of the Owner thereof.

**“Outstanding,”** when used with reference to Bonds or Bonds of a Series, means, as of any date, Bonds or Bonds of such Series theretofore or thereupon being delivered under the Indenture except:

- (i) Any Bonds canceled at or prior to such date;
- (ii) Bonds the principal and Redemption Price, if any, of and interest on which have been paid in accordance with the terms thereof;
- (iii) Bonds in lieu of or in substitution for which other Bonds shall have been delivered pursuant to the Indenture;
- (iv) Bonds deemed to have been paid as provided in the Indenture;
- (v) Option Bonds tendered or deemed tendered in accordance with the provisions of the Supplemental Indenture authorizing such Bonds on the applicable tender date, if the purchase price thereof and interest thereon shall have been paid or amounts are available and set aside for such payment as provided in such Supplemental Indenture, except to the extent such tendered Option Bonds are held by the Department or an issuer of an Enhancement Facility and/or thereafter may be resold pursuant to the terms thereof and of such Supplemental Indenture; and
- (vi) as may be provided with respect to such Bonds by the Supplemental Indenture authorizing such Bonds;

and, for purposes of certain provisions of the Indenture (see “Special Provisions Relating to Enhancement Facilities, Qualified Swaps, Other Similar Arrangements and Interim Financing Notes”), means any outstanding Interim Financing Notes.

“**Owner**” or any similar term means the registered owner of any Bond as shown on the books for the registration and transfer of Bonds maintained in accordance with the Indenture and, for the purposes of certain provisions of the Indenture (see “Special Provisions Relating to Enhancement Facilities, Qualified Swaps, Other Similar Arrangements and Interim Financing Notes”), means the holder of any Interim Financing Note.

“**Parity Obligations**” means Reimbursement Obligations and amounts payable under Qualified Swaps. For purposes of certain provisions of the Indenture, any Parity Obligations entered into or issued subsequent to the date of delivery of this Indenture shall specify, to the extent applicable, the interest and principal components of, or the scheduled payments corresponding to interest under, such Parity Obligations. Parity Obligations shall comply with the second paragraph under “Events of Default and Remedies” below.

“**Paying Agent**” means any paying agent for the Bonds of any Series and its successor or successors and any other Person which may at any time be substituted in its place pursuant to the Indenture.

“**Person**” means any individual, corporation, firm, partnership, joint venture, association, joint-stock company, trust, unincorporated association, limited liability company or partnership, or other legal entity or group of entities, including, but not limited to, a governmental entity or any agency or subdivision thereof.

“**Pooled Money Investment Rate**” means, for any amounts deposited in the Electric Power Fund from the General Fund and for any period, the rate of interest to be paid on such amounts to the State’s Pooled Money Investment Account as determined from time to time for such period.

“**Power**” means electric power and energy, including, but not limited to, capacity and output, or any of them.

“**Power Charge Revenues**” means Revenues received by the Department arising from Power Charges.

“**Power Charges**” has the same meaning as that term is defined in the 2002 Rate Agreement.

“**Power Supply Contract**” means any contract or agreement entered into by the Department pursuant to the Enabling Measures and under which the Department purchases Power, or purchases fuel for conversion to or in exchange for Power, or any option with respect thereto.

“**Principal Installment**” means, as of any date of calculation and with respect to any Series so long as any Bonds thereof are Outstanding, (i) the principal amount of Bonds (including the principal amount of any Option Bonds tendered for payment and not purchased) of such Series due (or so tendered for payment and not purchased) on any date for which no Sinking Fund Installments have been established, or (ii) the unsatisfied balance (determined as provided in section D.4 under the caption “Application and Flow of Funds” below) of any Sinking Fund Installments due on any date for Bonds of such Series, plus the amount of the sinking fund redemption premiums, if any, which would be applicable upon redemption of such Bonds on such date in a principal amount equal to said unsatisfied balance of such Sinking Fund Installments, or (iii) if both clause (i) and clause (ii) apply on the same date with respect to different Bonds of such Series, the sum of such principal amount of Bonds and of such unsatisfied balance of Sinking Fund Installments due on such date plus such applicable redemption premiums, if any.

“**Principal Payment Date**” means any date upon which the principal amount of Bonds of a Series is due hereunder at maturity or on any Redemption Date.

**“Priority Contract Contingency Reserve Amount”** means, during each Revenue Requirement Period or, for the purpose of the additional Bonds test, during the test period specified in the Indenture, the maximum amount projected by the Department to be payable by the Department under and pursuant to Priority Long Term Power Contracts in any calendar month during such Revenue Requirement Period. Each such projection shall be made at the beginning of the relevant Revenue Requirement Period. Such projections shall be based on such assumptions as the Department deems to be appropriate after consultation with the Commission and may take into account a range of possible future outcomes.

**“Priority Contract Account”** means the account by that name established under the Indenture.

**“Priority Contract Costs”** means all costs and expenses payable by the Department under or pursuant to Priority Long Term Power Contracts.

**“Priority Long Term Power Contract”** has the same meaning as that term is defined in the 2002 Rate Agreement.

**“Purchase Date”** means each date on which the Bonds of a Series shall be tendered or deemed tendered for purchase pursuant to the Fourth Supplemental Indenture.

**“Purchase Price”** means, with respect to any Series 2005 Bond, 100% of the principal amount thereof plus accrued and unpaid interest, if any, plus, in the case of a Series 2005 Bond subject to mandatory tender for purchase on a date when such Series 2005 Bond is also subject to optional redemption at a premium, an amount equal to the premium that would be payable on such Series 2005 Bond if redeemed on such date.

**“Qualified Swap”** means, to the extent from time to time permitted by law, with respect to Bonds, (a) any financial arrangement (i) which is entered into by the Department with an entity that is a Qualified Swap Provider at the time the arrangement is entered into, (ii) which is a cap, floor or collar, forward rate, future rate, swap (such swap may be based on an amount equal either to the principal amount of such Bonds of the Department as may be designated or a notional principal amount relating to all or a portion of the principal amount of such Bonds), asset, index, price or market-linked transaction or agreement, other exchange or rate protection transaction agreement, other similar transaction (however designated), or any combination thereof, or any option with respect to any of the foregoing, executed by the Department, and (iii) which has been designated as a Qualified Swap with respect to such Bonds in a written determination signed by an Authorized Officer and filed with the Trustee and Co-Trustee, and (b) any letter of credit, line of credit, policy of insurance, surety bond, guarantee or similar instrument securing the obligations of the Department under any financial arrangement described in clause (a) above.

**“Qualified Swap Provider”** means an entity whose senior long term obligations, other senior unsecured long term obligations, financial program rating, counterparty rating, or claims paying ability, or whose payment obligations under an interest rate exchange agreement are guaranteed by an entity whose senior long term debt obligations, other senior unsecured long term obligations, financial program rating, counterparty rating, or claims paying ability, are rated at the time of the execution of such Qualified Swap either (i) at least as high as the third highest Rating Category of each Rating Agency then maintaining a rating for the Qualified Swap Provider, but in no event lower than any Rating Category designated by any such Rating Agency for the Bonds subject to such Qualified Swap, or (ii) any such lower Rating Categories which each such Rating Agency indicates in writing to the Department and the Trustee will not, by itself, result in a reduction or withdrawal of its rating on the Outstanding Bonds subject to such Qualified Swap that is in effect prior to entering into such Qualified Swap.

**“Rate Agreement”** means any agreement between the Department and the Commission pursuant to the Act and other applicable provisions of law with respect to Revenue Requirements or charges in connection with Power sold by the Department and/or Electrical Corporations, as supplemented and amended from time to time.

**“Rating Agency”** means each nationally recognized securities rating agency then maintaining a rating on the Bonds at the request of the Department.

**“Rating Category”** means one of the generic rating categories of any Rating Agency without regard to any refinement or gradation of such rating by a numerical modifier or otherwise.

**“Record Date”** means (a) with respect to Series 2005 Bonds of a Series bearing interest at the Daily Rate, Weekly Rate or Flexible Rate, the close of business on the Business Day immediately preceding the Interest Payment Date therefor, (b) with respect to Series 2005 Bonds of a Series bearing interest at a Term Rate or the Fixed Rate, the fifteenth day (whether or not a Business Day) preceding the Interest Payment Date therefor, and (c) with respect to Series 2005 Bonds of a Series bearing interest at an Auction Period Rate, the Business Day immediately preceding the Interest Payment Date therefor. Notwithstanding the foregoing, the Record Date for Bonds of a Series during the Initial Interest Period shall be as prescribed by the Fourth Supplemental Indenture.

**“Redemption Date”** means the date fixed for redemption of Bonds of a Series subject to redemption in any notice of redemption given in accordance with the terms of the Indenture.

**“Redemption Price”** means, with respect to any Bond or a portion thereof, the principal amount thereof to be redeemed in whole or in part, plus the applicable premium, if any, payable upon redemption thereof pursuant to such Bond or the Indenture.

**“Registrar”** means any registrar for the Bonds of any Series and its successor or successors and any other Person which may at any time be substituted in its place pursuant to the Indenture.

**“Reimbursement Obligation”** has the meaning provided under the caption “Special Provisions Relating to Enhancement Facilities, Qualified Swaps, Other Similar Arrangements and Interim Financing Notes” below.

**“Remarketing Agent”** means the remarketing agent or agents at the time serving as such for the Series 2005 Bonds of a Series pursuant to the Fourth Supplemental Indenture.

**“Remarketing Agreement”** means, with respect to the Series 2005 Bonds of a Series, an agreement between the Department and the Remarketing Agent pursuant to which the Remarketing Agent agrees to perform the duties thereof specified in the Fourth Supplemental Indenture with respect to such Series 2005 Bonds.

**“Residual Net Short”** means the total electric requirements of the retail electric end-users served by and within the service areas of Electrical Corporations whose customers receive Power from the Department, minus electric generation available from both Utility Retained Generation and Department contract purchases. “Utility Retained Generation” means generating resources retained by Electrical Corporations, bilateral contracts held by Electrical Corporations and Qualifying Facility contracts. “Qualifying Facility” means a renewable power production or co-generation facility not primarily engaged in the generation or sale of electric power and that qualifies under Section 201 of the federal Public Utilities Regulatory Policy Act of 1978, the output from which facility is sold to an Electrical Corporation.

**“Responsible Officer”** means (i) with respect to the Trustee, any officer or employee of the State having direct responsibility for the administration of the Indenture, and in each case also, with respect to a particular matter, any other officer or employee to whom such matter is referred because of such officer’s or employee’s knowledge of and familiarity with the particular subject, and (ii) with respect to the Co-Trustee, any officer assigned to the corporate trust office of the Co-Trustee, including, but not limited to, any managing director, principal, vice president, assistant vice president, assistant treasurer, assistant secretary or any other officer of the Co-Trustee customarily performing functions similar to those performed by any of the above designated officers.

**“Revenue Requirement Period”** means any period for which the Department determines, and submits to the Commission, the Department’s Revenue Requirements. Revenue Requirement Period also includes the period commencing with the delivery of the initial Series of Bonds and ending December 31, 2002.

**“Revenue Requirements”** means the amounts needed from time to time by the Department to satisfy its obligations under the Enabling Measures.

**“Revenues”** means all revenues, receipts, charges, income, profits, proceeds or other moneys actually received by the Department, from whatever source, arising from or in connection with the conduct of the Department’s program for the purchase and sale of Power and related activities pursuant to the Enabling Measures and Senate Bill 7X, including, but not limited to, (i) all money paid directly or indirectly to or for the account of the Department with respect to any sale, exchange, transfer or disposition of Power acquired by the Department pursuant to the Enabling Measures and Senate Bill 7X, (ii) all moneys actually received by the Department which have been recovered as compensation or damages from providers of Power or other commodities or services acquired by the Department pursuant to the Enabling Measures, provided that nothing in the Indenture shall obligate the Department to recover and actually receive moneys as such compensation or damages from such providers, (iii) net payments to the Department under Qualified Swaps and (iv) Direct Access Power Charges. Revenues shall include, but shall not be limited to, Bond Charge Revenues, Power Charge Revenues, and Direct Access Power Charge Revenues, as and when received by the Department. Revenues shall not include (a) any revenues, receipts, charges, income, profits, proceeds or other money or monetary benefits attributable directly or indirectly to the ownership or operation of any Separately Financed Program, (b) any federal or state grant moneys to the extent receipt is conditioned upon their expenditure for a particular purpose or in a particular manner other than as provided in the Indenture for Revenues, (c) money actually received as compensation or damages recovered from providers of Power or other commodities or services acquired by the Department pursuant to the Enabling Measures, if and to the extent the Department’s entitlement thereto is not final and is subject to appeal, other review or refund, (d) the proceeds of any Bonds or Subordinated Indebtedness, (e) any amounts received as a result of a deposit of moneys or Defeasance Securities for the defeasance of Bonds pursuant to the Indenture, except to the extent not required for such purpose as provided in the Indenture, and (f) the proceeds of any draw on or payment under any Enhancement Facility which is intended for the payment of particular Bonds.

**“Securities Depository”** means, with respect to Bonds of a Series, the securities depository, if any, appointed for such Bonds in a Supplemental Indenture providing with respect to the issuance and payment of such Bonds.

**“Senate Bill 7X”** means Chapter 3 of the Statutes of 2001 (Senate Bill 7 of the First Extraordinary Session) of the State.

**“Separately Financed Program”** means, collectively, (i) any program, project or purpose described as such under the caption “Separately Financed Programs” below and (ii) the State Water Resources Development System.

**“Series”** means, subject to certain provisions of the Indenture (see “Special Provisions Relating to Enhancement Facilities, Qualified Swaps, Other Similar Arrangements and Interim Financing Notes”), all of the Bonds delivered on original issuance pursuant to a single Supplemental Indenture and denominated therein a single series, and any Bonds thereafter delivered in lieu of or in substitution therefor pursuant to certain provisions of the Indenture, regardless of variations in maturity, interest rate, or other provisions.

**“Series 2005F Bonds”** means the Department’s Power Supply Revenue Bonds, Series 2005F, authorized by the Indenture, including by the Fourth Supplemental Indenture.

**“Series 2005G Bonds”** means the Department’s Power Supply Revenue Bonds, Series 2005G, authorized by the Indenture, including by the Fourth Supplemental Indenture.

“**Servicing Agreement**” means any agreement, as supplemented and amended, between the Department and one or more Electrical Corporations, or, if approved by the Commission, other Persons if a Consultant advises the Trustee or Co-Trustee in writing that such other Person is reasonably expected to be capable of carrying out the provisions thereof, to provide the functions or services specified in the Indenture as agent of the Department.

“**Servicing Arrangements**” means, collectively, the Servicing Agreements and Servicing Orders, or any of them, as appropriate.

“**Servicing Order**” means each order of the Commission described below under the caption “Servicing Arrangements; Collection of Revenues”.

“**Sinking Fund Installment**” means an amount so designated for the retirement prior to maturity of Bonds of a Series of like maturity and interest rate.

“**Standby Credit Facility**” means a Credit Facility issued in the form of a letter of credit and designated by the issuer thereof as a “Standby Letter of Credit.”

“**State**” means the State of California.

“**Subordinated Indebtedness**” means any bond, note or other indebtedness authorized by a resolution or indenture of the Department and permitted under the Act and designated as constituting “Subordinated Indebtedness” in a certificate of an Authorized Officer delivered to the Trustee, which shall be payable from the Trust Estate subject and subordinate to the prior payments to be made therefrom as provided for in the Indenture. Subordinated Indebtedness may be secured by a lien on and pledge of the Trust Estate junior and inferior to the lien on and pledge of the Trust Estate created in the Indenture for the payment of the Bonds and Parity Obligations to the extent permitted by the Indenture, and may also be payable from such other sources and additionally secured as provided by the Indenture.

“**Subordinated Obligation**” means any payment obligation (other than a payment obligation constituting a Parity Obligation or Subordinated Indebtedness) of the Department incurred pursuant to the Act arising under any contract, agreement or other obligation incurred pursuant to the Act not constituting Bonds, Parity Obligations, Operating Expenses, Interim Financing Notes or the Credit and Security Agreement, provided that if such contract, agreement or other obligation is not incurred in connection with the Bonds, it shall have been approved by the Commission. Each Subordinated Obligation shall be payable from the Trust Estate subject and subordinate to the prior payments to be made therefrom as provided for in the Indenture. Subordinated Obligations may be secured by a lien on and pledge of the Trust Estate junior and inferior to the lien on and pledge of the Trust Estate created in the Indenture for the payment of the Bonds and Parity Obligations to the extent permitted by the Indenture, and may also be payable from such other sources and additionally secured as provided by the Indenture.

“**Substitute Credit Facility**” and “**Substitute Liquidity Facility**” means any substitute or replacement Credit Facility or Liquidity Facility, respectively, delivered in accordance with the Fourth Supplemental Indenture, and any extensions or renewals thereof, as the same may be amended and supplemented.

“**Supplemental Indenture**” means any indenture supplemental to or amendatory of the Indenture, adopted by, or adopted pursuant to authorization granted by, the Department in accordance with the Indenture.

“**Tender Agency Agreement**” means, with respect to the Series 2005 Bonds of a Series, an agreement between the Department and the Tender Agent pursuant to which the Tender Agent agrees to perform the duties thereof specified in the Fourth Supplemental Indenture with respect to such Bonds.

“**Tender Agent**” means the tender agent appointed for the Series 2005 Bonds of a Series pursuant to the Fourth Supplemental Indenture.

**“Termination”** (and other forms of “terminate”) means, when used with respect to any Credit Facility or Liquidity Facility, the replacement, removal, surrender or other termination of such Credit Facility or Liquidity Facility in accordance with its terms, other than an Expiration or an extension or renewal thereof.

**“Treasurer”** means the Treasurer of the State, or any successor to the rights, duties and obligations of the Treasurer under the Indenture.

**“Trustee”** means the Treasurer.

**“Trust Estate”** means, collectively:

- (i) all Revenues;
- (ii) all right, title and interest of the Department in and to Revenues, and all rights to receive the same; including but not limited to the assignment of amounts payable under the Servicing Arrangements as provided by the Indenture (see “Servicing Arrangements; Collection of Revenues”);
- (iii) the Operating Account, the Operating Reserve Account, the Bond Charge Collection Account, the Bond Charge Payment Account and the Debt Service Reserve Account, subject to the application thereof as provided in the Indenture; and
- (iv) all funds, moneys and securities and any and all other rights and interests in property, whether tangible or intangible, from time to time hereafter by delivery or by writing of any kind conveyed, mortgaged, pledged, assigned or transferred as and for additional security under the Indenture for the Bonds and Parity Obligations by the Department, or by anyone on its behalf, or with its written consent, to the Trustee, which is authorized by the Indenture to receive any and all such property at any and all times, and to hold and apply the same subject to the terms of the Indenture; provided, however, that no such additional security shall be received, held or applied by the Trustee unless accompanied by a Counsel’s Opinion to the effect that such additional security may be pledged under the Act and that it would not cause the Bonds or Parity Obligations to constitute a debt or liability of the State within the meaning of any constitutional or statutory provision or restriction, unless such constitutional or statutory provision or restriction shall have been complied with;

provided, however, that the Trust Estate shall not include, as to any Bond, any moneys or securities set aside under the Indenture specifically for the payment of other Bonds pursuant to the Indenture and, as to any Option Bond, any moneys or securities set aside for the purchase thereof as may be provided in the Indenture.

**“2001 Emergency Measures”** means all Proclamations and Orders of the Governor of the State issued in calendar year 2001 pursuant to the California Emergency Services Act (Chapter 7, Division 1, Title 2 of the California Government Code, as amended) as amended, including, but not limited to, any regulations issued pursuant thereto, issued in response to or in anticipation of the need to assure the availability of power to retail end-use customers in the State due to the inability or failure of an Electrical Corporation to purchase such power.

**“2002 Rate Agreement”** means the Rate Agreement, dated as of March 8, 2002, between the Department and the Commission, as supplemented and amended from time to time.

**“Valuation Date”** means, with respect to any Capital Appreciation Bonds, the date or dates set forth in the Supplemental Indenture authorizing such Bonds on which specific Accreted Values are assigned to the Capital Appreciation Bonds.

**“Variable Rate Bonds”** means, as of any date of determination, any Bonds on which the interest rate borne thereby may vary thereafter.

“**Weekly Period Commencement Day**” has the meaning set forth in the definition of Interest Rate Period above.

### **Security for the Bonds**

The Bonds are special obligation of the Department, payable solely from the Trust Estate. Under the Indenture, the Trust Estate is assigned and pledged to the Trustee and Co-Trustee for the benefit of the Owners of the Bonds, the holders of the Interim Financing Notes and the holders, issuers or other parties to Parity Obligations, as security for the payment of the principal and Redemption Price of and interest on the Bonds, payment of the Interim Financing Notes and payments due under Parity Obligations, in each case in accordance with their terms and the provisions of the Indenture, subject to the use of the Trust Estate for the purposes and on the terms and conditions provided in the Indenture. The Bonds, Interim Financing Notes and Parity Obligations are not payable from any income, receipts, or revenues of the Department other than those included in the Trust Estate, except as permitted by the last sentence of this paragraph, nor do the Bonds, Interim Financing Notes or Parity Obligations constitute a legal or equitable pledge, charge, lien, or encumbrance upon any of the property or upon any of the income, receipts, or revenues of the Department, except the Trust Estate. The Bonds, Interim Financing Notes, Parity Obligations, Subordinated Obligations and Subordinated Indebtedness (i) shall not be or be deemed to constitute a debt or liability of the State or of any political subdivision thereof, other than, to the extent provided in the Indenture, the Department, or a pledge of the faith and credit of the State or of any such political subdivision, other than the Department to the extent provided in the Indenture, but are payable solely from the funds pledged therefor pursuant to the Indenture, and (ii) do not directly or indirectly or contingently obligate the State or any political subdivision thereof to levy or to pledge any form of taxation whatever therefor or to make any appropriation for their payment. Subordinated Obligations and Subordinated Indebtedness may be secured by the Trust Estate, pursuant to a Supplemental Indenture, to the extent not contrary or inconsistent with the Indenture as theretofore in effect. Nothing contained in the Indenture shall prevent an Enhancement Facility from being provided with respect to any particular Bonds, Interim Financing Notes or Parity Obligations and not others, or different reserves being provided pursuant to the Indenture with respect to Bonds than are provided for Parity Obligations, or with respect to particular Parity Obligations than are provided for other Parity Obligations.

In the Indenture the Department represents that, pursuant to California Government Code Section 5451 and California Water Code Section 80132(g), the Indenture creates a valid and binding pledge of the Trust Estate for the benefit of the Owners of the Bonds, the holders of the Interim Financing Notes and the holders, issuers or other parties to Parity Obligations, as security for the payment of the Bonds, Interim Financing Notes and Parity Obligations, respectively, to the extent set forth in the Indenture, enforceable in accordance with the terms thereof. The pledge created by the Indenture shall be valid and binding from and after the date the Indenture is executed and delivered, and the Trust Estate shall immediately be subject to the lien of the pledge without any physical delivery thereof or further act, and the lien of the pledge shall be valid and binding as against all parties having claims of any kind in tort, contract or otherwise against the Department irrespective of whether such parties have notice thereof.

### **Protection of Security**

The Department shall at all times, to the extent permitted by law, defend, preserve and protect the pledge created by the Indenture and all interests of the Owners of Bonds, the holders of the Interim Financing Notes and the holders, issuers or other parties to Parity Obligations under the Indenture against all claims and demands of all Persons whomsoever.

Without limiting the generality of the foregoing, if any regulatory or judicial investigation of or challenge to any action taken by the Department in the performance of its obligations under the Act, the Indenture or the Rate Agreement is initiated, the Department shall take all legally available action which, in the judgment of the Department, may be necessary or desirable to assure that such challenge will not result in the inability of the Department to pay amounts payable under the Bonds, the Interim Financing Notes and Parity Obligations when due.

## General Provisions for the Issuance of Bonds

Bonds may be issued pursuant to the Indenture in such principal amount or amounts for each Series of the Bonds as may be specified in the applicable Supplemental Indenture. The aggregate principal amount of the Bonds that may be executed and delivered under the Indenture is not limited except as provided in the Indenture or as may be limited by law. Bonds may be issued for any purpose of the Department authorized by the Act, including, but not limited to, the payment of Costs.

Bonds may be sold in one or more Series (each of which shall contain a designation distinguishing it from other Series), and shall be delivered by the Department under the Indenture but only upon receipt by the Trustee of, among other documents, a Supplemental Indenture authorizing the Bonds, a Counsel's Opinion with respect to validity of the Bonds, a copy of the Rate Agreement applicable to such Bonds, certificates of an authorized representative of the Commission and an Authorized Officer as to the maximum aggregate principal amount of Bonds and Subordinated Indebtedness approved by or pursuant to Rate Agreements, and a certificate of an Authorized Officer stating that, upon the delivery of such Bonds, no Event of Default as defined in the Indenture, or event which, with the giving of notice or passage of time, or both, would constitute an Event of Default, shall have occurred and be continuing.

Prior to the issuance of Bonds, the Trustee shall also receive a certificate or report of a Consultant setting forth (i) the estimated Revenues for the twenty-four (24) calendar month period commencing on the first day of the calendar month next succeeding the date of delivery of such Bonds (the "**test period**"), (ii) the estimated Debt Service, and estimated amounts payable under all Parity Obligations, during the test period, (iii) the projected Debt Service on Bonds, and projected amounts payable under Parity Obligations, projected to be issued or entered into for any purpose during the test period, (iv) the sum of the estimated and projected amounts required to be paid for Operating Expenses, Subordinated Indebtedness and Subordinated Obligations during the test period, (v) the sum of the amounts estimated and projected to be available in the Operating Account, Bond Charge Collection Account and Bond Charge Payment Account for the payment of the items of cost referred to in clauses (ii) through (iv) above at the commencement of the test period, and (vi) the balances on deposit in the Debt Service Reserve Account and Operating Reserve Account at the commencement of, and projected to be on deposit therein throughout, the test period, and showing that (1) for the test period, the sum of the amounts set forth in clauses (i) and (v) above is at least equal to 100% of the sum of the amounts set forth in clauses (ii), (iii) and (iv) above, (2) the Debt Service Reserve Account is maintained throughout the test period at an amount at least equal to the Debt Service Reserve Requirement and (3) the Operating Reserve Account is maintained throughout the test period at an amount at least equal to the Operating Reserve Account Requirement. Such certificate or report shall reflect, among other things, the issuance of such Bonds and the Debt Service estimated to be payable thereon. The Consultant may base its estimates and projections upon such factors as it shall consider reasonable, including, but not limited to, future increases in Revenue Requirements, a statement to which effect shall be included in such certificate or report. For purposes of this requirement, any Debt Service, Parity Obligations, Subordinated Indebtedness and payments shall not include any amounts thereof expected by the Department to be paid from any funds, other than Revenues, reasonably expected by the Department to be available therefor (including, without limitation, the anticipated receipt of proceeds of sale of Bonds or Subordinated Indebtedness, or moneys not a part of the Trust Estate), which expectations, if included in a written determination signed by an Authorized Officer and filed with the Trustee, shall be conclusive. This paragraph shall not apply to (w) the initial Series of Bonds, (x) any Bonds assumed to be issued as part of the plan of finance of the Department's program for the purchase and sale of Power, as described in the public offering statement issued by the Department in connection with the initial Series of Bonds, (y) any Bonds issued to refund any other Bonds, and (z) any Bonds issued to refund bonds, notes or other evidences of indebtedness issued in anticipation of the issuance of such Bonds, if the requirements of this paragraph shall have been satisfied upon issuance of such bonds, notes or other evidences of indebtedness, assuming for such purpose that they are Bonds with principal due based upon level amortization of principal and interest over a period commencing on the date of issue and ending on the latest maturity date of any Bonds, and bearing interest as described for Bonds in the definition of Debt Service.

## **Separately Financed Programs**

Nothing in the Indenture shall prevent the Department from authorizing and issuing bonds, notes, or other obligations or evidences of indebtedness, other than Bonds, Parity Obligations, Subordinated Indebtedness or Subordinated Obligations, for any program, project or purpose authorized by the Enabling Measures or by other then applicable State statutory provisions, or from financing any such program, project or purpose from other available funds (a “Separately Financed Program”), if the debt service on such bonds, notes, or other obligations or evidences of indebtedness, if any, and the Department’s share of any operating expenses related to such program, are not payable from the Trust Estate.

## **Special Provisions Relating to Enhancement Facilities, Qualified Swaps, Other Similar Arrangements and Interim Financing Notes**

Any Supplemental Indenture may provide that:

(a) So long as an Enhancement Facility relating to any Series of Bonds is in full force and effect, and the issuer of the Enhancement Facility is not in default thereunder, then, in all such events, the Supplemental Indenture for such Series of Bonds may specify that either (i) the issuer of such Enhancement Facility shall be deemed to be the sole Owner of the Outstanding Bonds the payment of which such Enhancement Facility secures or secured when the approval, consent or action of the Owners of such Bonds is required or may be exercised under the Indenture, or (ii) the approval, consent or action of the issuer of such Enhancement Facility shall be required in addition to the approval, consent or action of the applicable percentage of the Owners of the Outstanding Bonds the payment of which such Enhancement Facility secures or secured when the approval, consent or action of the Owners of such Bonds is required or may be exercised under the Indenture.

(b) In the event that the principal, Sinking Fund Installments, if any, Purchase Price and Redemption Price, if applicable, or interest due on any Outstanding Bonds shall be paid under the provisions of an Enhancement Facility, all covenants, agreements and other obligations of the Department to the Owners of such Bonds shall continue to exist, and the issuer of the Enhancement Facility shall be subrogated to the rights of such Owners in accordance with the terms of such Enhancement Facility.

In addition, such Supplemental Indenture may establish such provisions as are necessary (i) to comply with the provisions of any Enhancement Facility that are not inconsistent with the Indenture, (ii) to provide relevant information and notices to the issuer of the Enhancement Facility, and (iii) to provide a mechanism for paying principal of and Sinking Fund Installments of and interest on Bonds secured by, or purchased pursuant to, the Enhancement Facility.

The Department may enter into agreements with the issuer of any Enhancement Facility providing for, among other things: (i) the payment of fees, costs, expenses and, to the extent permitted by law, indemnities to such issuer, its parent and its assignees and participants in connection with such Enhancement Facility, (ii) the terms and conditions of such Enhancement Facility and the Bonds to which the Enhancement Facility relates, and (iii) the security, if any, to be provided for the issuance of such Enhancement Facility. Any such agreement may provide for the purchase of Bonds to which the Enhancement Facility relates by the issuer of such Enhancement Facility, with such adjustments to the rate of interest, method of determining interest, maturity (which shall not be inconsistent with the requirements of the next paragraph), or redemption provisions, as shall be specified by the Supplemental Indenture authorizing the issuance of such Bonds.

The Department may, in an agreement with the issuer of any Enhancement Facility, agree to directly reimburse such issuer (or its assignees and participants, or any agent for the issuer or its assignees) for amounts paid by the issuer of the Enhancement Facility for the payment of the principal of, interest on, and Redemption Price or Purchase Price of Bonds under the terms of such Enhancement Facility (together with interest thereon, if any, and the amounts and obligations described in the next following two paragraphs, a “**Reimbursement Obligation**”), whether evidenced by an obligation to reimburse such issuer that is separate from the Department’s

obligations on Bonds (a “**Credit Facility Reimbursement Obligation**”) or by modified debt service obligations on Bonds acquired by such issuer (a “**Liquidity Facility Reimbursement Obligation**”); provided, however, that no such obligation to reimburse or modified debt service obligation shall require payments, other than from remarketing proceeds, to be made faster than on a level debt service (principal and interest) basis (calculated in three (3) month intervals) over a period ending no sooner than three (3) years following the date on which such reimbursement obligation is incurred (or, if less, extending to the final maturity date of the related Bonds) with the first installment commencing no earlier than six (6) months after the date from which the Liquidity Facility Reimbursement Obligation is incurred; and provided further, however, that the immediately preceding proviso shall not apply to any amounts payable to any issuer of any policy of bond insurance that is a subrogee of an Owner of Bonds with respect to amounts payable by the Department under such Bonds, or to any Alternate Debt Service Reserve Account Deposit. Notwithstanding anything to the contrary contained in this paragraph, no Reimbursement Obligation shall be created, for purposes of the Indenture, until amounts are paid under the related Enhancement Facility.

Any Credit Facility Reimbursement Obligation may include interest calculated at a rate higher than the interest rate on the related Bond. The following obligations also shall constitute Credit Facility Reimbursement Obligations: (i) payments of any fees, costs, expenses, indemnification, or other obligations to any such provider, its parent and its assignees and participants or any agent thereof, and (ii) payments pursuant to any advance, term-loan or other principal amortization requirements in reimbursement of any such advance or term-loan, provided that the total amount to be paid (including interest thereon) either (a) shall not be required to be paid faster than on a level debt service (principal and interest) basis (calculated in three (3) month intervals) over a period ending no sooner than three (3) years following the date on which such reimbursement obligation is incurred, with the first installment commencing no earlier than six (6) months after the date from which the Reimbursement Obligation is incurred, or (b) shall be paid from remarketing proceeds.

Any Liquidity Facility Reimbursement Obligation evidenced by Bonds of a Series may include interest calculated at a rate higher than the interest rate on other Bonds of such Series. The following obligations also shall constitute Liquidity Facility Reimbursement Obligations: (i) payments of any fees, costs, expenses, indemnification, or other obligations to any such provider, its parent and its assignees and participants, or any agent thereof, and (ii) payments of differential and/or excess interest amounts.

In connection with the issuance of any Bonds or at any time thereafter so long as Bonds remain Outstanding, the Department may, to the extent from time to time permitted pursuant to law, enter into Qualified Swaps. The total amount of the termination payment under a Qualified Swap, shall not be required to be paid by the Department faster than on a level amortization basis (calculated in three (3) month intervals) over a period ending no sooner than three (3) years following the date of termination, with the first installment commencing no earlier than six (6) months after the date of termination (in which case the termination payment also may include interest thereon); provided, however, that if the Department elects to terminate any Qualified Swap at its option, any termination payments shall be made as provided in such Qualified Swap.

For purposes of the Articles of the Indenture relating to the Trustee, Co-Trustee, Paying Agents and Registrar, Supplemental Indentures (except for provisions relating to the issuance of Bonds and certain specified amendments to the Indenture without the consent of Owners), amendments to the Indenture with the consent of Owners, Events of Defaults (except those described in (1), (2) and (6) under “Events of Default and Remedies” below) and remedies, defeasance and other miscellaneous provisions, and otherwise unless the context otherwise requires, references to “Bond” shall also include each Interim Financing Note, references to “Series” or “Series of Bonds” shall also include as a Series all outstanding Interim Financing.

Notes, and references to “Owner” shall also include the holder of any Interim Financing Note.

## **Establishment of Funds**

The Indenture establishes in the Electric Power Fund seven separate accounts, to be known as the “Operating Account”, the “Priority Contract Account”, the “Bond Charge Collection Account”, the “Bond Charge Payment Account”, the “Debt Service Reserve Account”, the “Operating Reserve Account” and the “Administrative Cost Account”. The Department may establish under the Indenture one or more additional funds, accounts or subaccounts, if not inconsistent with any Rate Agreement, by delivering to the Trustee a direction to that effect signed by an Authorized Officer, except to the extent the establishment thereof is required by other provisions of the Indenture.

The Operating Account, the Priority Contract Account, the Operating Reserve Account, the Bond Charge Collection Account and the Administrative Cost Account shall be under the control of the Department, except if an Event of Default shall happen and shall not have been remedied, in which case the Operating Account, the Priority Contract Account, the Operating Reserve Account, the Bond Charge Collection Account and the Administrative Cost Account shall be under the control of the Treasurer as Trustee. The Bond Charge Payment Account and the Debt Service Reserve Account shall be under the control of the Treasurer as Trustee at all times; provided, however, that moneys in the Bond Charge Payment Account may be held by any Paying Agent to the extent determined by the Trustee to be necessary or desirable as an administrative convenience.

All moneys and securities deposited under the Indenture in any fund, account or subaccount shall be held in trust for the benefit of the Department, the Owners of the Bonds, the holders of the Interim Financing Notes, and the parties to or holders of Parity Obligations, in each case to the extent provided in the Indenture, and applied only in accordance with the provisions of the Indenture, and each of such funds, accounts and subaccounts shall be a trust fund for purposes set forth in the Indenture.

## **Application and Flow of Funds**

In this caption any references to sections or subsections refer to sections and subsections in this “Application and Flow of Funds” caption.

A. Operating Account. 1. The Department shall pay or cause to be paid into the Operating Account, (i) upon the delivery of the initial Series of Bonds, all moneys and securities on deposit in the Electric Power Fund, except as may be provided by Supplemental Indenture, (ii) as and when received, all net proceeds of Bonds, except as may be provided by Supplemental Indenture, and (iii) all Power Charge Revenues and other Revenues, other than Bond Charge Revenues and payments to the Department under Qualified Swaps relating to Bonds. Net proceeds of Bonds shall be paid out or transferred pursuant to section A.2 below. Other amounts in the Operating Account shall be paid out, transferred, retained, accumulated or withdrawn from time to time for the following purposes and, as of any time, in the following order of priority:

(a) Amounts in the Operating Account shall be transferred to the Priority Contract Account on or before the fifth Business Day of each month in such amount as is necessary to make the amount in the Priority Contract Account sufficient to pay Priority Contract Costs estimated to be due during the balance of such month and for the first five Business Days of the next succeeding month. Additional amounts in the Operating Account also shall be transferred to the Priority Contract Account, at any time, to the extent amounts on deposit in the Priority Contract Account are insufficient to pay Priority Contract Costs then payable. Amounts on deposit in the Priority Contract Account shall be used solely to pay Priority Contract Costs then payable.

(b) Amounts in the Operating Account shall be applied to the payment of Operating Expenses then due and owing, other than Priority Contract Costs and any other costs specified in another paragraph of this section A.1, provided, however, that Operating Expenses that constitute administrative costs described in section G below shall be paid through the Administrative Cost Account pursuant to section G below subject to the priority afforded Priority Contract Costs pursuant to section A.1(a).

(c) Amounts in the Operating Account shall be applied to the payment of the Interim Financing Notes and other amounts payable by the Department under the Credit and Security Agreement, as and when due and payable.

(d) Amounts in the Operating Account shall be withdrawn and deposited in the Bond Charge Collection Account to reimburse the Bond Charge Collection Account for any amounts previously transferred therefrom (i) pursuant to section C.1 below, to the Priority Contract Account for the payment of Priority Contract Costs, and (ii) pursuant to section C.1(b) below, to the Operating Account for the payment of the Interim Financing Notes and other amounts payable by the Department under the Credit and Security Agreement.

(e) Amounts in the Operating Account shall be applied as provided by section D.7 below but only to the extent not paid from the Bond Charge Payment Account. In addition, prior to the time Bond Charge Revenues are received in the amounts sufficient to make the transfers required by section D.1 below, amounts in the Operating Account shall be transferred to the Bond Charge Payment Account in the amounts, at the times and otherwise as required by said section D.1.

(f) Amounts in the Operating Account shall be withdrawn to deposit in the Debt Service Reserve Account amounts as provided by section E below, but only to the extent such deposit is required as a result of (i) the use of Bond Charge Revenues for the payment of Priority Contract Costs, or for the payment of the Interim Financing Notes or other amounts payable by the Department under the Credit and Security Agreement, pursuant to section C.1(a) or C.1(b) below, or (ii) a change in value of Authorized Investments on deposit in the Debt Service Reserve Account.

(g) Amounts in the Operating Account shall be withdrawn to repay to the General Fund of the State advances made to the Department from amounts appropriated to the Electric Power Fund after November 15, 2001, including interest thereon payable at the Pooled Money Investment Rate, to the extent not theretofore repaid. The Department shall file with the Trustee, on or prior to the delivery of the initial Series of Bonds, a statement of the outstanding amount required to be repaid to the General Fund and promptly shall revise the same, and file such revised statement with the Trustee, upon each repayment until no amount remains to be repaid.

(h) Amounts in the Operating Account shall be withdrawn to repay to the General Fund of the State advances made to the Department from amounts appropriated to the Electric Power Fund, and General Fund moneys expended by the Department pursuant to the 2001 Emergency Measures, on or prior to November 15, 2001, including interest payable thereon at the Pooled Money Investment Rate, to the extent not theretofore repaid, in accordance with the schedule described in the immediately succeeding sentence. At such time as a schedule is established by the Commission for repayments to the General Fund described in this section A.1(h), the Department shall file such schedule with the Trustee, and shall promptly file with the Trustee each revised schedule that is similarly established until no amount remains to be repaid.

(i) Amounts in the Operating Account shall be withdrawn to deposit in the Operating Reserve Account amounts as provided by section F below.

(j) Amounts in the Operating Account shall be withdrawn for the following purposes, on a parity basis:

(i) to pay the principal of and interest on any Subordinated Indebtedness, and the redemption price or purchase price of Subordinated Indebtedness payable from mandatory sinking fund installments therefor,

(ii) to the extent not paid from the proceeds of Subordinated Indebtedness, to pay costs of issuing Subordinated Indebtedness or costs incidental to their payment and security,

(iii) to pay amounts due under any Subordinated Obligation, but only to the extent not paid from the Bond Charge Payment Account, and

(iv) to establish and maintain reserves for the payment of Subordinated Indebtedness or Subordinated Obligations to the extent required by a Financing Document; provided, however, that such a reserve may also be accumulated in the Operating Account. Any such reserve for Subordinated Indebtedness or Subordinated Obligations accumulated in the Operating Account shall be maintained in a separate subaccount which shall be established therein for such respective purpose pursuant to the Indenture.

(k) Amounts remaining in the Operating Account may be withdrawn for any purpose relating to the Department's program for the purchase and sale of Power and related activities only as permitted under the Enabling Measures, to the extent not specified in sections A.1(a) through A.1(j) above, as determined by the Department, including, without limitation, to pay or provide for the purchase or redemption of Bonds or Subordinated Indebtedness, and the payment of expenses in connection therewith to the extent not constituting Operating Expenses. Purchases of Bonds or Subordinated Indebtedness from amounts in the Operating Account pursuant to this section A.1(k) shall be made at the written direction of an Authorized Officer filed with the Trustee, with or without advertisement and with or without notice to other Owners of Bonds or Subordinated Indebtedness. Such purchases shall be made at such price or prices as determined by the Department, subject to limitations, if any, of the Supplemental Indenture authorizing the issuance of such Series of Bonds; provided, however, that such purchases shall be made at prices exceeding the next applicable Redemption Price (or, if none, the principal amount) of such Bonds, plus accrued interest, if any, only after consultation with the Commission and if the Department determines that to do so will not result in any insufficiency in the Operating Account or the Bond Charge Payment Account for any other purpose.

It shall be a condition to any withdrawal pursuant to sections A.1(j) and A.1(k) above that (1) there shall be no deficiency in either the Debt Service Reserve Account or the Operating Reserve Account without regard to the operation of the provisions of sections E.3, E.6 and F.4 permitting the replenishment thereof over time, and (2) the Department shall have determined, taking into account, among other considerations, anticipated future receipts of Revenues and other moneys constituting part of the Trust Estate, that the funds to be so withdrawn are not, and are not expected to be, needed for any of the purposes set forth in any prior lettered paragraph of this section A.1.

Notwithstanding the foregoing provisions of this section A.1, if at any time the Department determines that Power Charge Revenues are available for any of the purposes set forth in sections A.1(j) or A.1(k) above, (i) such Power Charge Revenues shall instead be used to satisfy any remaining outstanding amounts due under the Interim Financing Notes and the Credit and Security Agreements and to the General Fund of the State (without regard to any schedule for repayment referred to in section A.1(h) above), and to replenish any deficiency in the Debt Service Reserve Account and the Operating Reserve Account (without regard to the provisions of the Indenture sections E.3, E.6 and F.4 below permitting the replenishment thereof over time), in the order of priority established by the Indenture as described in section A.1 above, until the Interim Financing Notes, the Credit and Security Agreement and the General Fund, and all interest as described in sections A.1(g) and A.1(h) above shall be paid in full, and there shall be no deficiency in the Debt Service Reserve Account or the Operating Reserve Account, and (ii) after all outstanding amounts due under the Interim Financing Notes and Credit and Security Agreement, and to the General Fund of the State, and all interest payable as described by sections A.1(g) and A.1(h) above, shall be paid in full, and any deficiency in the Debt Service Reserve Account and the Operating Reserve Account shall be replenished, any use of such Power Charge Revenues for any of the purposes set forth in such sections A.1(j) and A.1(k) above shall require the consent of the Commission.

2. Amounts in the Operating Account representing proceeds of each Series of Bonds shall be paid out or transferred from time to time by the Department to pay Costs of the Department, subject to limitations, if any, of the Supplemental Indenture authorizing the issuance of such Series of Bonds.

3. That amount, if any, set aside by the Department as reserves in subaccounts in the Operating Account for the purposes specified in clause (iv) of section A.1(j) above shall be used by the Department solely for the respective purposes specified in said clauses, shall not be available for the payment of any other purpose for which amounts in the Operating Account may be applied, and shall not constitute part of the Trust Estate.

4. The Department shall separately notify the Commission in writing whenever the Minimum Operating Expense Available Balance has been reduced as a result of the Department no longer purchasing the Residual Net Short. Whenever such reduction in the Minimum Operating Expense Available Balance occurs, any resulting excess in the Operating Account shall be utilized in the same manner as Excess Amounts are required to be utilized pursuant to section F.5 below.

5. While the Department is purchasing the Residual Net Short, if on any date the Operating Account balance falls below \$750 million, unless the Operating Account balance has been restored to at least the Minimum Operating Expense Available Balance on the thirty-first (31st) day thereafter, then on or prior to the forty-fifth (45th) day following the date on which the Operating Account balance fell below \$750 million, the Department will submit a new Revenue Requirement to the Commission providing for Revenues sufficient to restore the Operating Account to the Minimum Operating Expense Available Balance within a period ending no later than two hundred forty (240) days following the date of the submission of such new Revenue Requirement to the Commission. While the Department is purchasing the Residual Net Short, if on any date the Operating Account balance falls below \$500 million and the Department has not yet submitted a Revenue Requirement pursuant to the preceding sentence, then on or prior to the earlier of (a) the tenth (10th) Business Day following the date on which the Operating Account balance falls below \$500 million or (b) the date on which a Revenue Requirement is required to be submitted to the Commission in accordance with the preceding sentence, the Department will submit a new Revenue Requirement to the Commission providing for Revenues sufficient to restore the Operating Account to the Minimum Operating Expense Available Balance within a period ending no later than two hundred forty (240) days following the date of the submission of such new Revenue Requirement to the Commission.

6. If and when the Department no longer is responsible for the payment of costs under any Power Supply Contract, all amounts in the Operating Account shall be utilized in the same manner as Excess Amounts are required to be utilized pursuant to section F.5 below, provided, however, that amounts required to satisfy a particular contingency shall be retained in the Operating Account only until the contingency has been satisfied or discharged; and provided further, however, that there may be retained in the Operating Account the amount, if any, determined by the Department to be required to pay Bond Related Costs that otherwise would have to be paid from the Bond Charge Payment Account pursuant to section D.1(d) below; and provided further, however, that any amounts not required for the purposes described in the preceding provisos shall be utilized in the same manner as Excess Amounts are required to be utilized pursuant to section F.5 below.

B. Priority Contract Account. 1. Amounts transferred to the Priority Contract Account from the Operating Account pursuant to A.1(a) above, from the Operating Reserve Account pursuant to F.3 below or from the Bond Charge Collection Account pursuant to C.1(a) below shall be applied solely to the payment of Priority Contract Costs.

2. If and when the Department no longer is responsible for the payment of costs under any Priority Long Term Power Contract, the balance if any, on deposit in the Priority Contract Account shall be utilized in the same manner as Excess Amounts are required to be utilized pursuant to section F.5 below.

C. Bond Charge Collection Account. 1. The Department shall pay or cause to be paid into the Bond Charge Collection Account, as and when received, (i) all Bond Charge Revenues, and (ii) all payments to the Department under Qualified Swaps relating to Bonds. Bond Charge Revenues shall be paid out, transferred, retained, accumulated or withdrawn from time to time for the following purposes and, as of any time, in the following order of priority:

(a) Amounts in the Bond Charge Collection Account shall be withdrawn and deposited in the Priority Contract Account, upon the written direction of an Authorized Officer filed with the Trustee, for the purpose of paying Priority Contract Costs then due and payable, but only to the extent moneys are not available for such purpose in the Operating Account, the Priority Contract Account or the Operating Reserve Account; provided, however, that no such withdrawal shall be made if and when the Department no longer responsible and liable for the payment of costs under any Priority Long Term Power Contract.

(b) Amounts in the Bond Charge Collection Account shall be withdrawn and deposited in the Operating Account, upon the written direction of an Authorized Officer filed with the Trustee, for the purpose of paying the principal of and interest on the Interim Financing Notes and other amounts payable by the Department under the Credit and Security Agreement, as and when due and payable, but only to the extent moneys are not available for such purpose in the Operating Account or in the Operating Reserve Account.

(c) Amounts in the Bond Charge Collection Account shall be transferred to the Bond Charge Payment Account and applied for the purposes of, in the amounts and at the times required by, and otherwise as provided in section D below.

(d) Amounts in the Bond Charge Collection Account shall be withdrawn for the following purposes, on a parity basis:

(i) to deposit in the Debt Service Reserve Account amounts as provided by section E below, but only to the extent amounts are not available therefor pursuant to section A.1(f) above, and

(ii) upon the written direction of an Authorized Officer filed with the Trustee, to establish and maintain reserves for the payment of Parity Obligations to the extent required by a Financing Document. Any such reserve for Parity Obligations accumulated in the Bond Charge Collection Account shall be maintained in a separate subaccount which shall be established by a supplemental indenture for such purpose pursuant to the Indenture.

2. That amount, if any, set aside as reserves in subaccounts in the Bond Charge Collection Account pursuant to clause (ii) of section C.1(d) above shall be used by the Department solely for the respective purposes specified in said clause, shall not be available for the payment of any other purpose for which amounts in the Bond Charge Payment Account may be applied, and shall not constitute part of the Trust Estate.

D. Bond Charge Payment Account. 1. There shall be transferred from the Bond Charge Collection Account to the Bond Charge Payment Account pursuant to section C.1(c) above, no later than the last Business Day of each calendar month, the amount, if any, required so that the balance in the Bond Charge Payment Account and available for Bond Related Costs as specified below shall at least equal the respective amounts as follows, on a parity basis:

(a) the Debt Service accrued and unpaid as of such Business Day and to accrue thereafter through the end of the third next succeeding calendar month;

(b) the amount accrued and unpaid as of such Business Day and estimated to be payable in the next succeeding three calendar months (i) under Reimbursement Obligations, (ii) under agreements, constituting Parity Obligations, relating to other financial instruments entered into in connection with the Bonds, including, but not limited to, investment agreements, hedges, interest rate swaps, caps, options and forward purchase agreements, (iii) under agreements, relating to the remarketing of Bonds, including, but not limited to, remarketing agreements, dealer agreements and auction agent agreements, (iv) for any Subordinated Obligations constituting Bond Related Costs, and (v) otherwise as may be permitted by a Rate Agreement to be paid from Bond Charge Revenues or the Bond Charge Payment Account;

(c) the amount accrued and unpaid as of such Business Day and estimated to be payable in the next succeeding three (3) calendar months for the cost to the Department of Fiduciaries associated with the issuance and administration of the Bonds; and

(d) if and when the Department no longer is responsible for the payment of costs under any Power Supply Contract and Bonds remain Outstanding, the amount accrued and unpaid as of such Business Day and estimated to be payable in the next succeeding three (3) calendar months for the Department's Bond Charge servicing costs, costs of preparing and providing the information and reports required under the Financing Documents, the 2002 Rate Agreement and the Act, related audit, legal and consulting costs, related administrative costs, and costs of complying with arbitrage restrictions and rebate requirements, and otherwise as may be permitted by a Rate Agreement to be paid from Bond Charge Revenues or the Bond Charge Collection Account to the extent moneys are not available therefor in the Operating Account; provided, however, that administrative costs described in section G below shall be paid through the Administrative Cost Account pursuant to section G below.

For the purpose of computing the amount to be deposited in the Bond Charge Payment Account pursuant to the foregoing provisions of this section D, there shall be excluded from the balance in the Bond Charge Payment Account (i) the amount, if any, set aside in the Bond Charge Payment Account from the proceeds of Bonds for the payment of interest on Bonds which, pursuant to section D.6 below, is to be applied on an interest payment date or dates occurring after the period specified above in this paragraph, and (ii) amounts scheduled to be paid by the Department under Qualified Swaps within the relevant period. The estimates required by the foregoing provisions of this section D shall be made by the Department, based on such assumptions and projections as the Department deems to be appropriate after consultation with the Commission, and shall be included in a written direction of an Authorized Officer filed with the Trustee.

In addition to the foregoing provisions of this section D, there shall be transferred from the Bond Charge Collection Account to the Bond Charge Payment Account, no later than the time required to make the payments required by section D.3 below, the amount, if any, required, in good funds, so that the balance in the Bond Charge Payment Account and available for the purpose shall at least equal the amount required to be paid pursuant to such section D.3 below at such time.

2. The Redemption Price of any Bonds called for redemption, other than to satisfy Sinking Fund Installment requirements, may be deposited in the Bond Charge Payment Account from the Bond Charge Collection Account or, pursuant to section A.1(k) above, from the Operating Account, in the amounts and at the times required therefor, in each case subject to any limitation set forth in any conditional notice of redemption as permitted by the Indenture. The Redemption Price of any Bonds called for redemption to satisfy Sinking Fund Installment requirements shall be deposited in the Bond Charge Payment Account pursuant to section D.1(a) above.

3. The Trustee shall pay Bond Related Costs out of the Bond Charge Payment Account as follows:

(a) The Trustee shall pay to the respective Paying Agents (i) on or before each interest payment date for any of the Bonds, whether scheduled or upon earlier redemption, the amount required for the interest payable on such date; (ii) on or before each Principal Installment due date, the amount required for the Principal Installment payable on such date; and (iii) on or before any redemption date for the Bonds, to the extent of moneys deposited in the Bond Charge Payment Account therefor, the amount required for the payment of the Redemption Price of the Bonds then to be redeemed. Such amounts shall be applied by the Paying Agents to such purposes on or before the due dates thereof.

(b) The Trustee shall pay to the holder or issuer of each Parity Obligation specified in section D.1(b) above and their participants to which an amount is due and payable thereunder, or other Person to whom an amount specified in such section D.1(b) above is due and payable, such amounts and at such times, as shall be specified in a written direction of an Authorized Officer filed with the Trustee.

(c) The Trustee shall pay to each Person to whom an amount specified in section D.1(c) above is due and payable, in such amounts and at such times as shall be specified in a written direction of an Authorized Officer filed with the Trustee.

(d) The Trustee shall pay to each Person to whom an amount specified in section D.1(d) above is due and payable, in such amounts and at such times as shall be specified in a written direction of an Authorized Officer filed with the Trustee.

4. Amounts accumulated in the Bond Charge Payment Account with respect to any Sinking Fund Installment (together with amounts accumulated therein with respect to interest on the Bonds for which such Sinking Fund Installment was established) may and, if so directed in writing by an Authorized Officer, shall be applied by the Trustee, on or prior to the forty-fifth (45th) day preceding the due date of such Sinking Fund Installment, to (i) the purchase of Bonds of the Series, maturity and interest rate within each maturity for which such Sinking Fund Installment was established, subject to section D.10 below, or (ii) the redemption at the applicable sinking fund Redemption Price of such Bonds, if then redeemable by their terms. The applicable sinking fund Redemption Price (or principal amount of maturing Bonds) of any Bonds so purchased or redeemed shall be deemed to constitute part of the Bond Charge Payment Account until such Sinking Fund Installment date, for the purpose of calculating the amount of such Account. After the forty-fifth (45th) day preceding the due date of any such Sinking Fund Installment, the Trustee shall proceed to call for redemption, by giving notice as provided in the Indenture, on such due date, Bonds of the Series, maturity and interest rate within each maturity for which such Sinking Fund Installment was established (except in the case of Bonds maturing on a Sinking Fund Installment date) in such amount as shall be necessary to complete the retirement of the unsatisfied balance of such Sinking Fund Installment after making allowances for any Bonds purchased or redeemed which the Department has directed the Trustee to apply as a credit against such Sinking Fund Installment as provided in section D.5 below.

5. If at any time Bonds of any Series or maturity for which Sinking Fund Installments shall have been established are purchased or redeemed other than pursuant to section D.4 above, or are deemed to have been paid pursuant to the Indenture, and, with respect to such Bonds which are deemed paid, irrevocable instructions have been given to the Trustee to redeem or purchase the same on or prior to the due date of the Sinking Fund Installment to be credited under this section D, an Authorized Officer may from time to time and at any time by written notice to the Trustee specify the portion, if any, of such Bonds so purchased, redeemed or deemed to have been paid and not previously applied as a credit against any Sinking Fund Installment which are to be credited against future Sinking Fund Installments for such Bonds, but in all cases subject to section D.10 below. Such notice shall specify the amounts of such Bonds to be applied as a credit against such Sinking Fund Installment or Installments and the particular Sinking Fund Installment or Installments against which such Bonds are to be applied as a credit; provided, however, that none of such Bonds may be applied as a credit against a Sinking Fund Installment to become due less than forty-five (45) days after such notice is delivered to the Trustee. All such Bonds which have been purchased or redeemed and are to be applied as a credit shall be surrendered to the Trustee for cancellation on or prior to the due date of the Sinking Fund Installment against which they are being applied as a credit. The portion of any such Sinking Fund Installment remaining after the deduction of any such amounts credited toward the same (or the original amount of any such Sinking Fund Installment if no such amounts shall have been credited toward the same) shall constitute the unsatisfied balance of such Sinking Fund Installment for the purpose of calculation of Sinking Fund Installments due on a future date.

6. The amount, if any, deposited in the Bond Charge Payment Account from the proceeds of any Series of Bonds shall be applied to the payment of interest on the Bonds, or paid to the issuers of Enhancement Facilities to satisfy Reimbursement Obligations relating to such interest, if any, paid under such Enhancement Facilities, in accordance with written directions signed by an Authorized Officer and filed with the Trustee or, in the event that the Department shall modify or amend any such direction by a subsequent direction signed by an Authorized Officer of the Department and filed with the Trustee, then in accordance with the most recent such direction or amended direction.

7. If at any time the amount in the Bond Charge Payment Account shall be less than the amount required to be on deposit pursuant to paragraphs (a), (b) and (c) of section D.1 above at the times required thereby, or to pay the items of cost specified in paragraphs (a), (b) and (c) of section D.3 above when due and payable, the Department shall apply all available amounts, if any, in the Operating Account to such deposits or payments, as the case may be, on parity basis. If at any time, after the application of moneys pursuant to the preceding sentence, the amount in the Bond Charge Payment Account shall be less than the amount required to pay the items of cost specified in paragraphs (a), (b) and (d) of said section D.3, all available amounts, if any, in the Debt Service Reserve Account shall be applied to such purposes on a parity basis. Any such application of moneys from the Operating Account or the Debt Service Reserve Account may be made directly or through the Bond Charge Payment Account.

8. In the event of the refunding of any Bonds, the Trustee shall, upon the written direction of an Authorized Officer, withdraw from the Bond Charge Payment Account all or any portion of amounts accumulated therein with respect to the principal of and redemption premium, if any, and interest on the Bonds being refunded and apply such amounts in accordance with such direction; provided, however, that such withdrawal shall not be made unless (i) immediately thereafter the Bonds being refunded shall be deemed to have been paid pursuant to the Indenture, and (ii) subject to section D.9 below, the amount remaining in the Bond Charge Payment Account with respect to Debt Service on Bonds, after such withdrawal, shall be sufficient to satisfy the requirements of section D.1 above.

9. Whenever there shall be held in the Bond Charge Payment Account, and in the Debt Service Reserve Account, without giving effect to any Alternate Debt Service Reserve Account Deposit, an aggregate amount sufficient to pay in full all Outstanding Bonds in accordance with their terms (including the maximum amount of principal or applicable sinking fund Redemption Price and interest which could become payable thereon), no transfers shall be required to be made to the Bond Charge Payment Account.

10. Any purchases of Bonds pursuant to sections D.4 and D.5 above shall be made at the direction of an Authorized Officer filed with the Trustee, with or without advertisement and with or without notice to other Owners of Bonds. Such purchases shall be made at such price or prices as is determined by an Authorized Officer; provided, however, that such purchases may be made at prices exceeding the next applicable Redemption Price (or, if none, the principal amount) of such Bonds, plus accrued interest, if any, only after consultation with the Commission and if the Department determines that to do so will not result in any insufficiency in the Bond Charge Payment Account for any other purpose.

E. Debt Service Reserve Account. 1. At the time any Series of Bonds is delivered pursuant to the Indenture, the Department shall pay into the Debt Service Reserve Account from the proceeds of such Bonds or other available funds, the amount, if any, necessary for the amount on deposit in the Debt Service Reserve Account to equal the Debt Service Reserve Requirement, after giving effect to any Alternate Debt Service Reserve Account Deposit, calculated immediately after the delivery of such Series of Bonds.

2. Amounts on deposit in the Debt Service Reserve Account shall be applied as provided in this section E and section D.7 above. Fiduciary charges and expenses (including, but not limited to, legal fees and expenses) shall not be paid from the Debt Service Reserve Account.

3. If a deficiency exists in the Debt Service Reserve Account, no later than the last Business Day of each calendar month the Department shall transfer (i) to the extent such transfer is required as a result of the use of Bond Charge Revenues for the payment of Priority Contract Costs, or the payment of the principal of and interest on the Interim Financing Notes and other amounts payable by the Department under the Credit and Security Agreement, pursuant to section C.1(a) or C.1(b) above, or a change in value of investments, first, from the Operating Account to the extent that there are sufficient moneys available therein, pursuant to section A.1(f) above, and second, to the extent necessary, from the Bond Charge Collection Account, to the extent that there are sufficient moneys available therein, pursuant to clause (i) of section C.1(d) above, and (ii) to the extent such

transfer is required otherwise than as described in clause (i), or in the event transfers pursuant to clause (i) are not sufficient, from the Bond Charge Collection Account to the extent that there are sufficient moneys available therein, and deposit in the Debt Service Reserve Account the amount, if any, required for the amount on deposit in the Debt Service Reserve Account to equal the Debt Service Reserve Requirement as of the last day of such calendar month, after giving effect to any Alternate Debt Service Reserve Account Deposit; provided, however, that any deficiency in the Debt Service Reserve Account, after giving effect to any Alternate Debt Service Reserve Account Deposit, may be cured by depositing into the Debt Service Reserve Account each month during the period commencing no later than the seventh month following such determination of the deficiency, approximately equal or greater amounts such that the deficiency shall be cured by no later than the twelfth month following such determination of the deficiency.

4. Any amount in the Debt Service Reserve Account in excess of the Debt Service Reserve Requirement, after giving effect to any Alternate Debt Service Reserve Account Deposit, may be retained therein or, upon the written direction of an Authorized Officer filed with the Trustee, may be transferred to the Bond Charge Collection Account; provided, however, that any such excess as of the last Business Day of each calendar year shall be so transferred.

5. Whenever the amount in the Debt Service Reserve Account, without giving effect to any Alternate Debt Service Reserve Account Deposit, together with the amount in the Bond Charge Payment Account with respect to Debt Service on Bonds, is sufficient to pay in full all Outstanding Bonds in accordance with their terms (including the maximum amount of principal or applicable sinking fund Redemption Price and interest which could become payable thereon), the funds on deposit in the Debt Service Reserve Account shall be transferred to the Bond Charge Payment Account, and thereupon no further deposits shall be required to be made into the Debt Service Reserve Account. Prior to said transfer, all investments held in the Debt Service Reserve Account shall be liquidated to the extent necessary in order to provide for the timely payment of principal and interest (or Redemption Price) on Bonds.

6. Alternate Debt Service Reserve Account Deposits may be made for the benefit of the Owners of the Bonds as provided in this section E.6. In lieu of any required transfers of moneys to the Debt Service Reserve Account, the Department may cause to be deposited into the Debt Service Reserve Account for the benefit of the Owners of the Bonds an Alternate Debt Service Reserve Account Deposit in an aggregate amount equal to the difference between the Debt Service Reserve Requirement and the sums of moneys or value of Authorized Investments then on deposit in the Debt Service Reserve Account, if any. In lieu of retaining all or any portion of the moneys theretofore on deposit in the Debt Service Reserve Account, the Department may cause to be deposited into the Debt Service Reserve Account an Alternate Debt Service Reserve Account Deposit in an aggregate amount equal to such moneys, subject to section E.4 above. Each Alternate Debt Service Reserve Account Deposit shall be payable (upon the giving of notice as required thereunder) on any date on which moneys may be required to be withdrawn from the Debt Service Reserve Account and applied to the payment of a Principal Installment of or interest on any Bonds, or to reimburse any issuer of an Enhancement Facility constituting a Parity Obligation for any such payment made by such issuer, and such withdrawal cannot be met by amounts on deposit in the Debt Service Reserve Account. Any insurer providing an Alternate Debt Service Reserve Account Deposit surety bond or insurance policy shall be an insurer whose municipal bond insurance policies insuring the payment, when due, of the principal of and interest on municipal bond issues results in such issues being rated in the highest Rating Category by at least one (1) Rating Agency. Any Alternate Debt Service Reserve Account Deposit letter of credit issuer shall be a bank or trust company which on the date of issuance of the letter of credit has an outstanding unsecured, uninsured and unguaranteed debt issue which is rated in the highest Rating Category by at least one (1) Rating Agency. Any provider of any other Alternate Debt Service Reserve Account Deposit obligation shall have the qualifications set forth in a Supplemental Indenture; provided, however, that prior to the deposit of such other Alternate Debt Service Reserve Account Deposit obligation in the Debt Service Reserve Account, the Trustee shall have received written confirmation from each Rating Agency to the effect that the deposit of such Alternate Debt Service Reserve Account Deposit will not, by itself, result in the withdrawal, suspension or downgrade of any rating issued by such Rating Agency with respect to any Outstanding Bonds. If a disbursement is made pursuant to an Alternate Debt Service Reserve Account Deposit,

the Department shall either (i) reinstate the maximum limits of such Alternate Debt Service Reserve Account Deposit or (ii) deposit into the Debt Service Reserve Account funds in the amount of the disbursement made under such Alternate Debt Service Reserve Account Deposit, or a combination of such alternatives, at the times and in the amounts required by section E.3 above. In the event that the rating attributable to any provider of any Alternate Debt Service Reserve Account Deposit shall fall below that required as provided above, such Alternate Debt Service Reserve Account Deposit shall no longer be deemed to be an Alternate Debt Service Reserve Account Deposit and the Department shall either (i) replace such Alternate Debt Service Reserve Account Deposit with an Alternate Debt Service Reserve Account Deposit which shall meet the requirements provided above or (ii) deposit into the Debt Service Reserve Account sufficient funds, or a combination of such alternatives, at the times and in the amounts required by section E.3 above.

7. In the event of the refunding of any Bonds, the Trustee shall, upon the written direction of an Authorized Officer, withdraw from the Debt Service Reserve Account all or any portion of amounts accumulated therein with respect to the Bonds being refunded and apply such amounts in accordance with such direction; provided, however, that such withdrawal shall not be made unless (i) immediately thereafter the Bonds being refunded shall be deemed to have been paid pursuant to the Indenture, and (ii) subject to section E.5 above, the amount remaining in the Debt Service Reserve Account, after giving effect to any Alternate Debt Service Reserve Account Deposit, after such withdrawal shall not be less than the Debt Service Reserve Requirement.

F. Operating Reserve Account. 1. At the time any Series of Bonds is delivered pursuant to the Indenture, the Department shall pay into the Operating Reserve Account from the proceeds of such Bonds or other available funds, the amount, if any, necessary for the amount on deposit in the Operating Reserve Account to equal the Operating Reserve Account Requirement.

2. Amounts on deposit in the Operating Reserve Account shall be applied as provided in this Section F.

3. If at any time the amounts in the Operating Account shall be less than the then current requirements thereof for any payment, retention, accumulation, transfer or withdrawal required by sections A.1(a) through A.1(f) above, the Department shall withdraw from the Operating Reserve Account and deposit in the Operating Account the amounts necessary (or all the moneys in the Operating Reserve Account, if less than the amounts necessary), applying available amounts in the order of priority and otherwise as specified in sections A.1(a) through A.1(f) above to make up such deficiency; provided, however, that if and for so long as the balance on deposit in the Operating Reserve Account is equal to or less than the Priority Contract Contingency Reserve Amount, amounts in the Operating Reserve Account may only be withdrawn for deposit in the Priority Contract Account for the payment of Priority Contract Costs.

4. If at any time the amount on deposit in the Operating Reserve Account is less than the Operating Reserve Account Requirement, no later than the last Business Day of each calendar month the Department shall transfer from the Operating Account to the Operating Reserve Account pursuant to section A.1(i) above the amount, if any, required for the Operating Reserve Account to equal the Operating Reserve Account Requirement as of the last day of such calendar month; provided, however, that any deficiency in the Operating Reserve Account may be cured by depositing into the Operating Reserve Account each month during the period commencing no later than the seventh month following such determination of the deficiency, approximately equal or greater amounts such that the deficiency shall be cured by no later than the twelfth month following such determination of the deficiency.

5. The Department shall separately notify the Commission in writing each time the Operating Reserve Account Requirement is reduced pursuant to the Indenture. Whenever such reduction in the Operating Reserve Account Requirement occurs, any excess amounts in the Operating Reserve Account (“Excess Amounts”) will be used at such time to satisfy any deficiencies existing at such time in the transfers, applications and withdrawals required by sections A.1(a) through A.1(h) above, including repayment in full of the General Fund of the State for all advances made to the Department from amounts appropriated to the Electric Power Fund,

whether before or after November 15, 2001, including interest payable thereon at the Pooled Money Investment Rate. Unless otherwise agreed by both the Department and the Commission, each acting in their own discretion, any Excess Amounts remaining after application to the uses described in the preceding sentence shall be used, at the direction of the Commission after consultation with the Department, to (i) adjust Department charges or (ii) with the agreement of the Department, reduce debt outstanding under the Indenture, in all instances upon consideration of, the interests of the retail customers of the Electrical Corporations and the Department, and, if applicable, Electric Service Provider retail customers.

6. If and when the Department no longer is responsible for the payment of costs under any Power Supply Contract, the entire balance, if any, on deposit in the Operating Reserve Account shall be applied as provided by section F.5 above.

G. Administrative Cost Account. Notwithstanding anything to the contrary in the Indenture, including but not limited to the provisions described in sections A, C and D above, all administrative costs of the Department incurred in administering Division 27 (commencing with Section 80000) of the Water Code, if and to the extent the payment thereof is subject to appropriation by the State Legislature pursuant to Section 80200(c) of the Water Code or other provision of law, shall be paid and accounted for through the Administrative Cost Account. Transfers shall be made from the Operating Account or, after the Department no longer is responsible for the payment of costs under any Power Supply Contract, the Operating Account or the Bond Charge Payment Account to the extent necessary to permit compliance with this section G.

### **Investment of Amounts in Accounts**

Unless otherwise provided in a Supplemental Indenture, all amounts held in any fund, account or subaccount under the Indenture shall be invested by the Trustee in Authorized Investments. Unless otherwise determined by any Supplemental Indenture, earnings on moneys and investments in (i) the Operating Reserve Account shall be credited to and deposited in the Operating Account, and (ii) any other fund, account or subaccount under the Indenture shall be credited to and deposited in such fund, account or subaccount. Authorized Investments purchased as an investment of moneys in any such fund, account or subaccount shall be deemed at all times to be a part of such fund, account or subaccount, any profit realized from the liquidation of such investment shall be credited thereto and any loss resulting from the liquidation of such investment shall be charged thereto.

### **Revenue Requirements**

The Department shall cause to be established, fixed and revised from time to time charges sufficient, together with any other available moneys and securities on deposit in the Electric Power Fund, to satisfy all of the Department's Revenue Requirements at the times and in the amounts needed. Without limiting the generality of the foregoing, such charges shall be sufficient, after taking into account any moneys and securities on deposit in the Operating Account, to produce Revenues sufficient in each calendar year: to pay all Operating Expenses in such calendar year as the same become due and payable; to pay the Interim Financing Notes and other amounts payable by the Department under the Credit and Security Agreement as the same become due and payable; to make all deposits to the Bond Charge Payment Account in the amounts and at the times required by section D under the caption "Application and Flow of Funds" above in such calendar year; to pay all Parity Obligations as and when the same become due and payable in such calendar year; to repay to the General Fund of the State advances made to the Department from amounts appropriated to the Electric Power Fund, and to repay General Fund moneys expended by the Department pursuant to the 2001 Emergency Measures, including interest thereon payable at the Pooled Money Investment Rate, at the times and in the amounts provided in the Indenture; to pay the debt service on all Subordinated Indebtedness then outstanding, and all Subordinated Obligations, as and when the same respectively become due and payable in such calendar year; to replenish the Debt Service Reserve Account as and to the extent required by section E under the caption "Application and Flow of Funds" above in the event of any deficiency therein; to replenish the Operating Reserve Account as and to the extent required by Section F under the caption "Application and Flow of Funds" above in the event of any deficiency therein; to

retain on deposit in or make any deposit to any fund, account or subaccount pursuant to and to the extent necessary under the Act or required by any Financing Document, including, but not limited to, such retentions or deposits as shall be required to maintain the Minimum Operating Expense Available Balance as may be required by section 4.5 under the caption "Application and Flow of Funds" above or to maintain reserves as may be required by clause (iv) of section A.1(j) under the caption "Application and Flow of Funds" above, and by clause (ii) of section C.1(d) under the caption "Application and Flow of Funds" above; and to pay such other obligations of the Department, payable by the Department, in such calendar year as shall be incurred in accordance with both the Enabling Measures and the Indenture.

The Department will include in its Revenue Requirements amounts estimated to be sufficient:

(a) to cause the amount on deposit in the Operating Account (except any amounts set aside as reserves in subaccounts in the Operating Account for the purposes specified in clause (iv) of section A.1(j) under the caption "Application and Flow of Funds" above, at all times during any calendar month to equal the Minimum Operating Expense Available Balance;

(b) to cause the amount on deposit in the Bond Charge Collection Account, on the first Business Day of each calendar month, to equal the amounts projected to be required to be paid out of the Bond Charge Payment Account pursuant to section D.3 under the caption "Application and Flow of Funds" above in such calendar month, which projections shall be based on such assumptions, and which may take into account a range of possible outcomes, as the Department deems to be appropriate after consultation with the Commission, and

(c) for the payment of interest on Variable Rate Bonds during the relevant Revenue Requirement Period, assuming that interest accrues on such Variable Rate Bonds at a rate equal to the greater of (i) of 130% of the highest average interest rate in any calendar month during the twelve (12) calendar months, or such shorter period that such Variable Rate Bonds shall be Outstanding, ending with the month preceding the date such Revenue Requirements are filed with the Trustee or the Commission, as the case may be, or (ii) 4.0%.

For purposes of the covenant set forth in this paragraph, the Department may take into account the issuance of Bonds or other obligations anticipated to occur prior to the applicable Revenue Requirement Period.

No later than 90 days prior to the commencement of each calendar year beginning on and after January 1, 2003, the Department shall file with the Trustee an estimate of the Department's Revenue Requirements for such calendar year. The estimate for each calendar year shall demonstrate compliance with the requirements of this caption, and shall specify, on a monthly basis and in the aggregate for such calendar year, receipts of Revenues and deposits to, retentions in and transfers and withdrawals from the funds, accounts or subaccounts under the Indenture pursuant to sections A.1 and C under the caption "Application and Flow of Funds" above, including, but not limited to, withdrawals (i) for the payment of Priority Contract Costs and other Operating Expenses, principal and Redemption Price of and interest on Bonds, principal of and interest on the Interim Financing Notes and other amounts payable by the Department under the Credit and Security Agreement, Parity Obligations, Subordinated Obligations and Subordinated Indebtedness, taking into account any proceeds of Bonds or other amounts on deposit in the Operating Account, in the Priority Contract Account, in the Bond Charge Collection Account and in the Bond Charge Payment Account, (ii) to maintain the Debt Service Reserve Account and Operating Reserve Account in the amounts required by sections E and F under the caption "Application and Flow of Funds", respectively, and (iii) to repay to the General Fund of the State advances made to the Department from amounts appropriated to the Electric Power Fund, including interest thereon payable at the Pooled Money Investment Rate in accordance with the Act at the times and in the amounts provided in the Indenture.

Such estimates may be revised from time to time for any calendar year or for the balance of any then-current calendar year to reflect actual results and revised estimates; provided, however, that such estimates (i) shall be confirmed or revised in each calendar month during which the Department is permitted by the Act to enter into new contracts for the purchase of Power, and (ii) shall be revised as soon as practicable after the amount on deposit in any fund, account or subaccount under the Indenture shall be less than the amount required by the

Indenture. Each confirmation or revision required by clause (i) of the foregoing proviso shall be filed with the Trustee as soon as practicable but no later than thirty (30) days (whether or not a Business Day) after the end of each calendar month to which it relates. Each confirmation or revision pursuant to this paragraph shall contain the same information required for the annual estimates by the foregoing paragraph.

Each such estimate and confirmation or revision thereof shall be accompanied by a written statement from a Consultant to the effect that the estimate or revision, as the case may be, reasonably can be expected to result in Revenues sufficient to satisfy the requirements of the Indenture or, if not, specifying the reasons therefor in reasonable detail.

The Department shall submit to the Commission such Revenue Requirements as shall be the subject of Rate Agreements, at such times and in such manner as the Department reasonably determines will enable the Commission to take action with respect thereto pursuant to the Rate Agreements to enable the Department to receive moneys in such amounts and at such times as shall permit the Department to fully comply with the provisions of the first two paragraphs under this caption. Without limiting the generality of the foregoing, the Department shall make projections, submit requests for changes in Revenue Requirements, Bond Charges and Power Charges, and take all other actions as are required of it under or pursuant to Section 4.1(b) and other provisions of the 2002 Rate Agreement, and by the provisions of any other Rate Agreement, to enable the Department to comply with the preceding sentence.

### **Rate Agreements**

The Department shall enter into and maintain in effect at all times one or more Rate Agreements. Nothing contained in the Indenture shall (i) require the Department to continue to purchase or sell Power or (ii) prevent the Department from assigning, terminating or suspending any Power Supply Contract if (a) a Rate Agreement is in full force and effect, and (b) the Bond Charges established under the Rate Agreement are in full force and effect. The Department shall not voluntarily consent to or permit any amendment, termination or suspension, or waive any provision, of any Rate Agreement unless the Department shall determine, in a written determination signed by an Authorized Officer and delivered to the Trustee, that the same will not have a material adverse affect on the ability of the Department to comply with the provisions of the Indenture. The Department shall perform all of the obligations and conditions required to be performed and observed by it under each Rate Agreement, and shall take such actions from time to time as shall be necessary and available to enforce all of the obligations and conditions required to be performed and observed under each Rate Agreement by the Commission, in each case to the extent material to the payment of or security for the Bonds or Parity Obligations. An Authorized Officer shall promptly notify the Trustee and Co-Trustee in writing of any dispute or default, in each case if determined by the Department to be material to the payment of or security for the Bonds or Parity Obligations, and of each event of default, arising under any Rate Agreement as soon as practicable after the Department has actual knowledge thereof. If the Department shall have defaulted under its obligations contained in any Financing Document, such default is continuing and the Department has failed to enforce such Rate Agreement to the extent it is permitted to do so thereunder, the Co-Trustee shall have the right to enforce such Rate Agreements, as permitted by and subject to such Rate Agreements. All right, title and interest of the Department in, to and under each Rate Agreement is collaterally assigned to the Co-Trustee for the benefit of the Owners of Bonds and the holders or issuers of or other parties to Parity Obligations, to the extent necessary for purposes of such enforcement, subject to the terms of such Rate Agreements. The Co-Trustee agrees to comply with all provisions of any Rate Agreement necessary to enable it to exercise the rights granted by the Indenture and described in this paragraph.

### **Cooperation with Commission**

Wherever the Indenture requires the Department to consult with the Commission with respect to assumptions made by the Department, the Department shall involve the Commission in the development of these assumptions by conferring regularly in a manner consistent with the Department's obligations under the 2002 Rate Agreement.

## **Servicing Arrangements; Collection of Revenues**

The Department shall enter into and maintain in effect at all times one or more Servicing Agreements which, in aggregate, shall provide for all of the following functions and services: transmit or provide for the transmission of, and distribute, all Power; billing, collection and remittance of all moneys constituting Bond Charges, Power Charges, Direct Access Power Charges or other charges; and all other services related to the foregoing; provided, however, that separate Servicing Agreements may be entered into and maintained for separate functions and services; and provided further, however, that no Servicing Agreement shall be required for any functions or services to the extent such functions or services are performed directly by the Department, subject to the following sentence, or pursuant to an order (“Servicing Order”) of the Commission. The Department shall not attempt to assert any authority to perform any such function or service except as permitted under an applicable Servicing Agreement or Servicing Order. The Department shall request such Servicing Orders of the Commission as the Department determines to be necessary or appropriate in connection with the performance of such functions or services and the implementation or enforcement of any Servicing Agreement.

The Department shall not voluntarily consent to or permit any amendment, termination or suspension, or waive any provision, of any Servicing Arrangement unless the Department determines, in a written determination signed by an Authorized Officer and delivered to the Trustee, that the same will not have a material adverse affect on the ability of the Department to comply with the provisions of the Indenture. The Department shall perform and observe all of the obligations and conditions required to be performed and observed by it under each Servicing Arrangement, and shall take such actions from time to time as shall be necessary and available to enforce all of the obligations and conditions required to be performed and observed under each Servicing Agreement by the other party thereto, and to enforce each Servicing Order in accordance with its terms, in each case to the extent material to the payment of and security for the Bonds or Parity Obligations.

If an Event of Default shall have occurred and be continuing, the Co-Trustee shall have the right to enforce the Servicing Arrangements to the extent the Department fails to do so, as permitted by and subject to such Servicing Arrangements. All right, title and interest of the Department in, to and under the Servicing Arrangements is hereby collaterally assigned to the Co-Trustee for the benefit of the Owners of Bonds, the holders of Interim Financing Notes and the holders or issuers of or other parties to Parity Obligations, to the extent necessary for purposes of such enforcement, subject to the terms of such Servicing Arrangements. If the Department shall have defaulted under its obligations contained in any Financing Document and such default is continuing, the Co-Trustee shall have the right to request Servicing Orders with respect to the Servicing Agreements or the functions and services described above, and to request the Commission to enforce the same, to the extent the Department fails to do so. All right, title and interest of the Department in, to and under the Servicing Arrangements, insofar as it relates to such requests and enforcement, is hereby collaterally assigned to the Co Trustee for the benefit of the Owners of Bonds, the holders of Interim Financing Notes and the holders or issuers of or other parties to Parity Obligations, to the extent necessary for purposes of such requests and enforcement, subject to the terms of such Servicing Arrangements. The Co-Trustee agrees to comply with all provisions of any Servicing Arrangements necessary to enable it to exercise the rights described above, and in doing so shall be subject to the provisions of the Indenture.

The Department shall use its best efforts to collect or cause to be collected all moneys due and payable to the Department, which, upon receipt by the Department, would constitute Revenues, as soon as practicable after the same are due and payable; provided, however, that nothing contained in the Indenture shall prohibit the effectuation of the program provided by Executive Order No. D-56-02 dated May 23, 2002, including the financing thereof, as provided thereby.

All right, title and interest of the Department in, to and under the Servicing Arrangements to amounts payable, and payments, to the Department pursuant to and under the Servicing Arrangements are hereby collaterally assigned to the Trustee and Co-Trustee for the benefit of the Owners of the Bonds, the holders of Interim Financing Notes and the holders or issuers of or other parties to Parity Obligations, subject to the terms of such Servicing Arrangements.

## **Non-Impairment Covenant of State; Extension of Sunset Date**

Under the Indenture, the State pledges and undertakes that while any obligations of the Department incurred under Division 27 of the State Water Code, including without limitation the Indenture, the Bonds and Parity Obligations, remain outstanding and not fully performed or discharged, the rights, powers, duties, and existence of the Department and the Commission shall not be diminished or impaired in any manner that will affect adversely the interests and rights of the holders of or parties to such obligations. This pledge and undertaking is included in the Indenture pursuant to the authority to do so contained in Section 80200(e) of the State Water Code.

Any extension of the January 1, 2003, termination date for the authority of the Department to contract for the purchase of Power, contained in Section 80260 of the State Water Code, shall not constitute a violation of the foregoing pledge and undertaking of the State, nor shall any such extension constitute a violation of or default under the Indenture.

## **Covenant Relating to Retirement of Bonds**

The Department shall schedule the maturity of, redeem or otherwise retire Bonds in accordance with the Indenture at such times and in such amounts as are necessary to assure that the Department complies with Paragraph II of the Summary of Material Terms referred to in Section 7.10 of the Rate Agreement, as such Summary of Material Terms was amended by Paragraph 18 of the Amended and Restated Addendum to Summary of Material Terms of Financing Documents dated as of August 8, 2002. Such provisions require that the plan of finance of the Bonds provide for substantially level debt service with principal payments commencing no later than 2004.

## **Continuing Disclosure**

The Department has covenanted in the Indenture to post on its website, so long as it maintains a website, (i) within forty-five (45) days of the end of each fiscal year quarter except the fourth quarter, unaudited financial statements of the Department relating to its Electric Power Fund for such quarter, (ii) within one hundred twenty (120) days after the end of each fiscal year, audited financial statements of the Department relating to its Electric Power Fund for such fiscal year, and (iii) promptly, each Revenue Requirement filing made by the Department with the Commission. The Department shall send notice of each such posting, by first class mail, to any Person filing with the Chief, Division of Fiscal Services, or the Chief, Financial Management Office, Power Supply Program of the Department a written request therefor, to the address specified by such Person. If the Department no longer maintains a website, the Department will send such documents by first class mail to any Person filing with the Chief, Division of Fiscal Services, or Chief, Financial Management Office, Power Supply Program, a written request therefor, to the address specified by such Person.

In the event of a failure of the Department to comply with any provision of this covenant, the Trustee may (and, at the request of the Owners of at least 50% in aggregate principal amount of Outstanding Bonds, shall), or any Owner or Beneficial Owner of the Bonds may (unless the Department has so complied within 20 days after written notice from the Trustee, such Owner or Owners, or such Beneficial Owner or Beneficial Owners, as the case may be, of the Department's failure to comply) seek specific performance by court order, to cause the Department to comply with its obligations under this covenant, as the sole remedy, and default under this covenant shall not be deemed a default or an Event of Default under the Indenture, notwithstanding anything in the Indenture to the contrary. For this purpose, "Beneficial Owner means any person which has or shares the power, directly or indirectly, to make investment decisions concerning ownership of any Bonds (including persons holding Bonds through nominees, depositories and other intermediaries).

## Supplemental Indentures and Amendments

The Department, the Trustee and the Co-Trustee may adopt (without the consent of or notice to any Owner) Supplemental Indentures to, among other purposes, prohibit, or provide limitations and restrictions in addition to the limitations and restrictions contained in the Indenture on, the delivery on original issuance of Bonds or the issuance of other evidences of indebtedness; add to the covenants and agreements of the Department in the Indenture other covenants and agreements to be observed by the Department which are not contrary to or inconsistent with the Indenture as theretofore in effect; add to the limitations and restrictions in the Indenture other limitations and restrictions to be observed by the Department which are not contrary to or inconsistent with the Indenture as theretofore in effect; surrender any right, power or privilege reserved to or conferred upon the Department by the Indenture; authorize Bonds of a Series or to amend, modify or rescind any such authorization, specification or determination at any time prior to the first delivery of such Bonds; authorize Subordinated Indebtedness and provide with respect thereto to the extent provided by, and otherwise not inconsistent with, the Indenture theretofore in effect; subject Subordinated Obligations and Subordinated Indebtedness to the lien on and pledge of the Trust Estate pursuant to the Indenture on a subordinate basis; confirm, as further assurance, any pledge under, and the subjection to any lien or pledge created or to be created by, the Indenture, of any additional security other than that previously granted or pledged under the Indenture; modify, amend or supplement the Indenture in such manner as to permit the qualification of the Indenture under the Trust Indenture Act of 1939, as amended, or any similar Federal statute hereafter in effect or to permit the qualification of the Bonds for sale under the securities laws of any of the states of the United States of America, and, if the Department so determines, to add to the Indenture such other terms, conditions and provisions as may be permitted by said Trust Indenture Act of 1939 or similar Federal statute; comply with regulations and procedures as are from time to time in effect relating to any book-entry-only system, whether within or without the United States, for the registration of beneficial ownership interests in Bonds; to evidence the assignment and transfer of rights, and the delegation of duties and obligations, of the Department by operation of law to another department, agency or instrumentality of the State that has indicated in writing its willingness to accept the rights of the Department and to assume and discharge the duties and obligations of the Department; modify any of the provisions of the Indenture in any other respect whatever with respect to any Bonds, provided that (i) (a) such modification relates only, and is to be effective prior to the issuance of, such Bonds, or (b) such modification relates only, and is to be effective only upon the remarketing of, such Bonds in connection with an optional or mandatory tender thereof for purchase by or on behalf of the Department, and (ii) such modification is disclosed in an offering or reoffering document applicable to such issuance or remarketing; or modify any of the provisions of the Indenture in any other respect whatever, provided that such modification shall be, and shall be expressed to be, effective only after all Bonds Outstanding, outstanding Interim Financing Notes and outstanding or unpaid Parity Obligations at the date of the execution and delivery of such Supplemental Indenture shall cease to be Outstanding or owing, as the case may be.

For any one or more of the following purposes and at any time or from time to time, a Supplemental Indenture may be executed by the Department, the Trustee and the Co-Trustee without the consent of or notice to any Owner, which, upon delivery to the other parties thereto and the satisfaction of the requirements of the Indenture, shall be effective in accordance with its terms: (1) to cure any ambiguity, supply any omission, or cure or correct any defect or inconsistent provision in the Indenture; or (2) to insert such provisions, or to make such other amendments to the Indenture, as are necessary or desirable which are not materially adverse to the rights under the Indenture of the Owners of Bonds, the holders of Interim Financing Notes and the holders or issuers of or other parties to Parity Obligations.

Any modification or amendment of the Indenture and of the rights and obligations of the Department and of the Owners, in any particular, may be made by a Supplemental Indenture, with the written consent given as provided in the Indenture (i) of the Owners of a majority in principal amount of the Bonds Outstanding at the time such consent is given, and (ii) in case less than all of the Bonds then Outstanding are affected by the modification or amendment, of the Owners of a majority in principal amount of the Bonds so affected and Outstanding at the time such consent is given; provided, however, that if such modification or amendment will, by its terms, not take effect so long as particular Bonds remain Outstanding, the consent of the Owners of such Bonds shall not be

required and such Bonds shall not be deemed to be Outstanding for the purpose of any calculation of Outstanding Bonds under this caption. No such modification or amendment shall (a) permit a change in the terms of redemption or maturity of the principal of any Outstanding Bond or of any installment of interest thereon or a reduction in the principal amount or the Redemption Price thereof or in the rate of interest thereon without the consent of the Owner of such Bond, (b) reduce the percentages or otherwise affect the classes of Bonds the consent of the Owners of which is required to waive an Event of Default or otherwise effect any such modification or amendment, (c) create a preference or priority of any Bond or Bonds over any other Bond or Bonds, without the consent of the Owners of all such Bonds, (d) create a lien prior to or on parity with the lien of the Indenture, without the consent of the Owners of all of the Bonds then Outstanding, except to the extent permitted by the Indenture, or (e) change or modify any of the rights or obligations of any Fiduciary without its written assent thereto. For the purposes of this paragraph, a Bond shall be deemed to be affected by a modification or amendment of the Indenture if the same materially and adversely affects the rights of the Owner of such Bond. The Trustee may in its discretion determine whether or not in accordance with the foregoing powers of amendment particular Bonds would be affected by any modification or amendment of the Indenture and any such determination shall be binding and conclusive on the Department and all Owners of Bonds.

The terms and provisions of the Indenture and the rights and obligations of the Department and of the Owners of Bonds may be modified or amended in any respect upon the execution by the Department, the Trustee and the Co-Trustee of a Supplemental Indenture, the filing of a fully executed copy with the Trustee and the Co-Trustee, and the consent of the Owners of all of the Bonds then Outstanding, such consent to be given as provided in the Indenture; provided, however, that no such modification or amendment shall change or modify any of the rights or obligations of any Fiduciary without the filing with the Trustee of the written assent thereto of such Fiduciary in addition to the consent of the Owners of Bonds.

#### **Events of Default and Remedies**

Pursuant to the Indenture, any one or more of the following events shall constitute “Events of Default”:

- (1) if default shall be made in the due and punctual payment of the principal or Redemption Price of any Bond, or in the due and punctual payment of the principal or redemption price, if any, of any Parity Obligation when and as the same shall become due and payable, whether at maturity or by call for redemption, or otherwise;
- (2) if default shall be made in the due and punctual payment of any installment of interest on any Bond or of interest, if any, on any Parity Obligation when and as such interest installment shall become due and payable, and such default shall continue for a period of 5 days;
- (3) if the Department defaults in the performance or observance on its part of any of the covenants or agreements contained in the Indenture relating to the submission by the Department of Revenue Requirements to the Commission, relating to the Rate Agreements or relating to the Servicing Arrangements, and such default shall continue for a period of 10 days after written notice thereof to the Department by the Trustee or the Co-Trustee, or to the Department, the Trustee and the Co-Trustee by the Owners of a majority in principal amount of the Bonds Outstanding; provided, however, that no such default relating to submission by the Department of Revenue Requirements to the Commission shall constitute an Event of Default if and for so long as the Commission is taking action to cure the Department’s default pursuant to Section 4.1(a) of the 2002 Rate Agreement or otherwise;
- (4) if an “event of default,” as defined in any Rate Agreement, on the part of the Commission shall have occurred and be continuing;
- (5) if any “event of default,” as defined in the Credit and Security Agreement or any Parity Obligation, on the part of the Department shall have occurred and be continuing;
- (6) if the Department defaults in the performance or observance on its part of any other of the covenants or agreements contained in the Indenture or in the Bonds to be performed, other than as specified in clauses (1) through (3) above, and such default shall continue for a period of 60 days after written notice thereof to the Department by the Trustee or Co-Trustee, or to the Department, the Trustee and the Co-Trustee by the Owners of a majority in principal amount of the Bonds Outstanding; provided, however, that if such default shall be such that it cannot be remedied by the Department within such 60 day period, it shall not constitute an Event of Default if corrective action is instituted by the Department within such period and diligently pursued by the Department until the default is remedied; or
- (7) with respect to a Series of Bonds, any additional events as may be specified in the Supplemental Indenture authorizing the issuance of such Series.

Anything in the Indenture to the contrary notwithstanding, neither the Trustee nor the Co-Trustee nor the Owners nor the issuer of any Enhancement Facility nor a party to any Swap Obligation shall have the right to accelerate the maturity of any Bond or Parity Obligation. The preceding sentence shall not be construed to prohibit any redemption of Bonds or Parity Obligations at the option of the Owner, holder or issuer thereof or other party thereto, or if required pursuant to any Enhancement Facility, or any optional or mandatory tender of Bonds or Parity Obligations pursuant to the terms thereof, or any early termination of a Qualified Swap (subject to the Indenture).

During the continuance of an Event of Default, the Trustee shall take control of the Operating Account, the Priority Contract Account, the Operating Reserve Account and the Administrative Cost Account and apply all amounts on deposit therein, Revenues and the income therefrom to payments as follows and in the following order:

(i) The reasonable and proper charges and expenses of the Trustee and the Co-Trustee (including, but not limited to, reasonable legal fees and expenses and charges and expenses of any management consultant or consulting engineer, or firm of either thereof, selected by the Trustee or Co-Trustee pursuant to paragraph (ii) below. Such charges and expenses shall only be paid from Power Charge Revenues or Bond Charge Revenues.

(ii) The amounts required for reasonable and necessary Operating Expenses, including, but not limited to, reasonable and necessary reserves and working capital. The Trustee or the Co-Trustee may retain a management consultant or consulting engineer, or firm of either thereof, of recognized standing (who may be an engineer or management consultant, or firm of either thereof, retained by the Department for other purposes) for the purpose of rendering advice with respect to such matters. For this purpose the books of record and account of the Department shall at all times be subject to the inspection of such consultant, engineer or firm of consultants or engineers during the continuance of such Event of Default.

(iii) The interest and principal or Redemption Price then due on the Bonds, and the interest and principal components of Parity Obligations (which, in the case of Swap Obligations shall consist of scheduled payments and termination payments, respectively) as follows:

**First:** To the payment to the Persons entitled thereto of all installments of interest then due on the Bonds and the interest component of Parity Obligations, in the order of the maturity of such installments, and, if the amount available shall not be sufficient to pay in full any installment or installments maturing on the same date, then to the payment thereof ratably, according to the amounts due thereon, to the Persons entitled thereto, without any discrimination or preference; and

**Second:** To the payment to the Persons entitled thereto of the unpaid principal or Redemption Price of any Bonds and the unpaid principal component of Parity Obligations, which shall have become due, whether at maturity or by call for redemption, in the order of their due dates, and, if the amount available shall not be sufficient to pay in full all the Bonds and the principal component of Parity Obligations, due on any date, then to the payment thereof ratably, according to the amounts of principal or Redemption Price due on such date, to the Persons entitled thereto, without any discrimination or preference.

If and whenever all overdue installments of interest on all Bonds and Parity Obligations, together with the reasonable and proper charges and expenses of the Trustee and the Co-Trustee, and all other sums payable by the Department under the Indenture, including, but not limited to, the principal and Redemption Price of and accrued unpaid interest on all Bonds and Parity Obligations which shall then be payable, shall either be paid by or for the account of the Department, or provision satisfactory to the Trustee and the Co-Trustee shall be made for such payment, and all defaults under the Indenture or the Bonds, the Credit and Security Agreement and all

agreements, instruments or notes evidencing Parity Obligations shall be made good or secured to the satisfaction of the Trustee and the Co-Trustee or provision deemed by the Trustee and the Co-Trustee to be adequate shall be made therefor, all Revenues shall thereafter be applied as provided under the caption "Application and Flow of Funds" above, and the Trustee shall return control of the Operating Account, the Priority Contract Account, the Operating Reserve Account, the Bond Charge Collection Account and the Administrative Cost Account to the Department. No such resumption of the application of Revenues as provided under the caption "Application and Flow of Funds" above shall extend to or affect any subsequent default under the Indenture, the Credit and Security Agreement and all agreements, instruments or notes evidencing Parity Obligations, or impair any right consequent thereon.

If (i) an Event of Default shall happen and shall not have been remedied, and (ii) whether or not an Event of Default has happened or shall have been remedied, in the event of any failure of the Department to pay into the Operating Account, as and when received, Power Charge Revenues as described under Section A under the caption "Application and Flow of Funds" above or to pay into the Bond Charge Collection Account, as and when received, Bond Charge Revenues, as described under section C under the caption "Application and Flow of Funds" above, or to collect or cause to be collected Revenues as required by the Indenture, or in the event of a violation of the pledge and agreement of the State in the Indenture, then and in every such case, the Co-Trustee, by its agents and attorneys, if the Co-Trustee shall deem it advisable, may proceed to protect and enforce its rights and the rights of the Owners of Bonds and the holders or issuers of or other parties to Parity Obligations under the Indenture forthwith by a suit or suits in equity or at law, whether for the specific performance of any covenant contained in the Indenture, or in aid of the execution of any power granted in the Indenture, or for an accounting against the Department as if the Department were the trustee of an express trust, or in the enforcement of any other legal or equitable right as the Co-Trustee, being advised by counsel, shall deem most effectual to enforce any of its rights or to perform any of its duties under the Indenture. Notwithstanding the occurrence of an Event of Default, the Co-Trustee shall have only such rights to enforce the Rate Agreements as are set forth in such Rate Agreements.

No Owner shall have any right to institute any suit, action or proceeding at law or in equity for the enforcement of any provision of the Indenture or the execution of any trust under the Indenture or for any remedy under the Indenture, unless such Owner shall have previously given to the Trustee and the Co-Trustee written notice of the happening of an Event of Default, and the Owners of at least twenty-five percent (25%) in principal amount of the Bonds then Outstanding shall have filed a written request with the Trustee and the Co-Trustee, and shall have offered the Co-Trustee reasonable opportunity, either to exercise the powers granted as described under this caption or to institute such action, suit or proceeding in its own name, and unless such Owners shall have offered to the Co-Trustee adequate security and indemnity against the costs, expenses and liabilities to be incurred therein or thereby, and the Co-Trustee shall have refused to comply with such request within a reasonable time; it being understood and intended that no one or more Owners of Bonds shall have any right in any manner whatever by his or their action to affect, disturb or prejudice the pledge created by the Indenture, or to enforce any right under the Indenture, except in the manner therein provided; and that all proceedings at law or in equity to enforce any provision of the Indenture shall be instituted, had and maintained in the manner provided in the Indenture and for the equal benefit of all Owners of the Outstanding Bonds.

### **Resignation and Removal of Co-Trustee**

The Co-Trustee may at any time resign and be discharged of the duties and obligations created by the Indenture by giving not less than 90 days' written notice to the Department and the Trustee, and the Trustee thereupon shall mail notice thereof to the Owners of the Bonds, specifying the date when such resignation shall take effect, at least 30 days prior to the effective date, provided that such resignation shall take effect upon the later of (i) the day specified in such notice and (ii) the day a successor shall have been appointed by the Department or the Owners of Bonds as provided in the Indenture.

The Co-Trustee may be removed at any time by an instrument or concurrent instruments in writing, filed with the Trustee and the Co-Trustee, and signed by the Owners of a majority in principal amount of the Bonds

then Outstanding or their attorneys-in-fact duly authorized, excluding any Bonds held by or for the account of the Department; provided, however, that the Co-Trustee may be removed only for cause unless and until an Event of Default shall have occurred and be continuing under the Indenture. In addition, so long as no Event of Default shall have occurred and be continuing under the Indenture and the Co-Trustee is not pursuing any right or remedy available to it pursuant to the Indenture, the Co-Trustee may be removed by the Department at any time for failure to provide reasonably acceptable services, failure to charge reasonably acceptable fees or any other reasonable cause, all as determined by a written determination signed by an Authorized Officer and filed with the Trustee and the Co-Trustee, which determination shall be conclusive. Any such removal shall not be effective until a successor shall have been appointed by the Department or the Owners of Bonds as provided in the Indenture.

## **Defeasance**

If the Department shall pay or cause to be paid to the Owners of all Bonds then Outstanding the principal or Redemption Price, if any, and interest to become due thereon, to the other parties to the Credit and Security Agreement all amounts payable thereunder, and to the holders or issuers of or other parties to all Parity Obligations all amounts payable thereunder and upon the termination thereof, at the times and in the manner stipulated therein and in the Indenture, then the covenants, agreements and other obligations of the Department to the Owners of Bonds, the other parties to the Credit and Security Agreement, and the holders or issuers of or other parties to all Parity Obligations shall be discharged and satisfied. In such event, the Trustee shall, upon the request of the Department, execute and deliver to the Department all such instruments as may be desirable to evidence such discharge and satisfaction and the Fiduciaries shall pay over or deliver to the Department all money, securities and funds held by them pursuant to the Indenture which are not required for the payment or redemption of Bonds not theretofore surrendered for such payment or redemption, or required to make payments under the Credit and Security Agreement and Parity Obligations.

Outstanding Bonds or any portion thereof shall, prior to the maturity or redemption date thereof, be deemed to have been paid within the meaning and with the effect expressed in the Indenture either (A) as provided in the Supplemental Indenture authorizing their issuance or (B) if (a) in case any of said Bonds are to be redeemed on any date prior to their maturity, the Department shall have given to the Trustee, in form satisfactory to it irrevocable instructions to mail, as provided in the Indenture notice of redemption on said date of such Bonds, (b) there shall have been irrevocably deposited with the Trustee or other Paying Agent either moneys in an amount which shall be sufficient, or Defeasance Securities the principal of and the interest on which when due will provide moneys which, together with the moneys, if any, deposited with the Trustee or such Paying Agent at the same time, shall be sufficient, without further investment or reinvestment of either the principal amount thereof or the interest earnings thereon, to pay when due, the principal or Redemption Price, if applicable, and interest due and to become due on such Bonds on and prior to the redemption date or maturity date thereof, as the case may be, (c) in the event such Bonds are not by their terms maturing or are not to be redeemed within the next succeeding 60 days, the Department shall have given the Trustee in form satisfactory to it irrevocable instructions to mail, as soon as practicable, a notice to the Owners of such Bonds that the deposit required by clause (b) above has been made with the Trustee and that said Bonds are deemed to have been paid as described under this caption and stating such maturity or redemption date upon which moneys are to be available for the payment of the principal or Redemption Price, if applicable, on such Bonds, and (d) in the case of Bonds subject to optional or mandatory tender for purchase prior to the maturity or earlier redemption date specified for its payment pursuant to this paragraph, the Trustee or such Paying Agent shall have received written confirmation from each Rating Agency to the effect that the deposit and provisions for defeasance made pursuant to this paragraph will not, by themselves, result in the withdrawal, suspension or downgrade of any rating issued by such Rating Agency with respect to such Bonds. Neither Defeasance Securities nor moneys deposited with the Trustee or other Paying Agent as described under this caption nor principal or interest payments on any such Defeasance Securities shall be withdrawn or used for any purpose other than, and shall be held in trust for, the payment of the principal or Redemption Price, if applicable, and interest on said Bonds; provided, however, that any moneys on deposit with the Trustee or such Paying Agent, (i) to the extent such moneys will not be required at any time for such purpose, shall be deposited in the Bond Charge Collection Account or, if the first paragraph of this caption applies, paid over to the Department as received by the Trustee or such Paying Agent, free and clear of any trust, lien or pledge

securing said Bonds or otherwise existing under the Indenture, and (ii) to the extent such moneys will be required for such purpose on another date, shall, to the extent practicable, be reinvested in Defeasance Securities maturing at times and in amounts sufficient, together with any moneys available to the Trustee or Paying Agent for such purpose, to pay when due the principal or Redemption Price, if applicable, and interest to become due on said Bonds on and prior to the redemption date or maturity date thereof, as the case may be. Notwithstanding any other provision of the Indenture, the Department may, at the time any Bonds are deemed to have been paid within the meaning and with the effect as set forth above, elect to retain the right to redeem or require the tender of any such Bonds; provided, however, that such Bonds shall at all times comply with the requirements described above for such Bonds to be deemed to have been paid as aforesaid.

Anything in the Indenture to the contrary notwithstanding, all instructions by the Department, accepted by the Trustee or any Paying Agent, given pursuant to the Indenture to mail notice of redemption of the Bonds of a Series (other than Bonds of such Series which have been purchased by the Trustee at the direction of the Department as therein provided prior to the mailing of such notice of redemption) shall be irrevocable and shall foreclose the exercise by the Department of any other optional redemption right with respect to such Bonds, except that any such instructions may be revoked prior to any deposit pursuant to the Indenture.

### **Unclaimed Moneys**

The amounts held by any Fiduciary for the payment of the interest, principal or Redemption Price due on any date with respect to particular Bonds or any amount payable under the Credit and Security Agreement or Parity Obligations shall, on and after such date and pending such payment, be set aside on its books and held in trust by it for the Owners of Bonds, the other parties to the Credit and Security Agreement or the holders or issuers of or other parties to Parity Obligations entitled thereto. Anything in the Indenture to the contrary notwithstanding, any moneys so held by the Fiduciary, which remain unclaimed for two (2) years after the date when such principal, Redemption Price, interest or amounts, respectively, became due and payable, either at their stated maturity or due dates or by call for earlier redemption, if such moneys were held by the Fiduciary at such date, or for two (2) years after the date of deposit of such moneys if deposited with the Fiduciary after the date when such principal, Redemption Price, interest or amounts, respectively, became due and payable, shall, at the written request of the Department, be repaid by the Fiduciary to the Department or such officer, board or body as then may be entitled by law to receive the same, as its absolute property and free from trust, and the Fiduciary shall thereupon be released and discharged with respect thereto and the Owners of Bonds, the other parties to the Credit and Security Agreement and the holders or issuers of or other parties to Parity Obligations, as applicable, shall look only to the Department or such officer, board or body for the payment of such principal, Redemption Price, interest or amounts, respectively. Before being required to make any such payment to the Department, the Fiduciary shall, at the expense of the Department, cause to be mailed to the Owners, holders, issuers or parties entitled to receive such moneys, at their last addresses, if any, appearing upon the registry books or other notice addresses on file with the Fiduciary or the Department, a notice that said moneys remain unclaimed and that, after a date named in said notice, which date shall be not less than 30 days after the date of the mailing, the balance of such moneys then unclaimed will be returned to the Department or such officer, board or body. The failure of any Owner of Bonds, holders, issuers or parties to receive such notice shall not affect the application of moneys as described under this caption.

### **Successors and Assigns**

Whenever in the Indenture, the Bonds, the Credit and Security Agreement, any agreement, instrument or note evidencing a Parity Obligation, Subordinated Indebtedness, Subordinated Obligation, or any other obligation of the Department under or pursuant to the Indenture, the Department is named or referred to, it shall be deemed to include its successors and assigns and all the covenants and agreements in the Indenture or in the Bonds or such other obligations contained by or on behalf of the Department shall bind and inure to the benefit of its successors and assigns whether so expressed or not; provided, however, that such successor or assign is permitted by law to assume the Department's obligations thereunder and shall agree to be bound by the terms thereof.

## **Governing Law and Venue**

The Indenture shall be governed by and interpreted in accordance with internal laws of the State without regard to conflicts of law principles. All legal actions and proceedings arising from the Indenture or the Bonds shall be brought in the courts of the State located in the County of Sacramento, except as otherwise may be expressly agreed to by the Department. The parties to the Indenture, and the Owners by their acceptance of Bonds, consent to and accept for themselves and in respect of their property, generally and unconditionally, the jurisdiction of the aforesaid courts, and to the extent permitted by law, irrevocably waive any objection, including, without limitation, any objection to the laying of venue or based on the grounds of forum non conveniens, which they may now or hereafter have to the bringing of any such action or proceeding in such respective jurisdictions, except as otherwise may be agreed to in writing by the Department, the Trustee and the Co-Trustee.

**APPENDIX D**

**RATE AGREEMENT**

**By and Between**

**STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES**

**and**

**STATE OF CALIFORNIA PUBLIC UTILITIES COMMISSION**

**Dated as of March 8, 2002**

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**RATE AGREEMENT, dated as of March 8, 2002, by and between  
STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES and  
STATE OF CALIFORNIA PUBLIC UTILITIES COMMISSION.**

The parties mutually agree as follows:

**ARTICLE I  
DEFINITIONS**

Section 1.1 Definitions. The terms set forth in this Section shall have the meanings ascribed to them herein for all purposes of this Agreement unless the context clearly requires otherwise. Words in the singular shall include the plural and words in the plural shall include the singular where the context so requires.

**“Act”** shall mean Chapter 4 of the Statutes of 2001 (AB 1 of the First 2001-02 Extraordinary Session) of the State, as amended from time to time.

**“Agreement”** shall mean this Rate Agreement, as from time to time hereafter amended or supplemented in accordance with the provisions hereof.

**“Beneficiaries”** shall mean, at any given time, the persons to whom the Department is then obligated to pay Bond Related Costs described in clauses (i) through (iv) of the definition of such term, in each case solely to the extent of such obligations.

**“Bond Charge”** shall mean a charge imposed by the Commission, by order promulgated as a result of this Agreement, upon customers in each of the Service Areas of Pacific Gas & Electric, Southern California Edison Company and San Diego Gas & Electric Company or any of their respective successors based on the aggregate amount of electric power sold to that customer by an Electrical Corporation and the Department, and to the extent determined under Section 4.3 hereof, by an Electric Service Provider, such charge to be revised from time to time by the Commission in such a manner that amounts on deposit in the Bond Charge Payment Account as a result of the charge are always sufficient to pay or provide for the payment of the Bond Related Costs; provided, that Bond Charges shall be imposed upon such customers in each Service Area at all times required by this Agreement whether or not the Department is at the time selling, or deemed to be selling, Power to such customers until such time as the Department has recovered the portion of the Department’s revenue requirements under Section 80134 of the Act constituting Bond Related Costs.

**“Bond Charge Collection Account”** shall have the meaning set forth in the Financing Documents. Revenues that the Department receives from Bond Charges shall be deposited in the Bond Charge Collection Account.

**“Bond Charge Payment Account”** shall have the meaning set forth in the Financing Documents. The primary purpose of the Bond Charge Payment Account is to hold amounts that the Financing Documents require to be periodically transferred from the Bond Charge Collection Account to provide for the payment of Bond Related Costs.

**“Bond Related Costs”** shall mean payments of, or deposits or other provision to be made by the Department under Financing Documents or the Act for the following components of the Department’s revenue requirements under Section 80134 of the Act:

(i) principal of, premium, if any, and interest on Bonds and any additional amount required under the Financing Documents to be deposited into the Bond Charge Collection Account to provide debt service coverage of the Bonds;

(ii) payments required to be made (A) under agreements with issuers of credit and liquidity facilities and their participants, including but not limited to, letters of credit, bond insurance, guarantees, debt service reserve fund surety bonds, lines of credit, reimbursement agreements, and standby bond purchase agreements, (B) under agreements relating to other financial instruments entered into in connection with the Bonds, including but not limited to investment agreements, hedges, interest rate swaps, caps, options and forward purchase agreements and (C) under agreements relating to the remarketing of Bonds, including but not limited to remarketing agreements, dealer agreements and auction agent agreements;

(iii) deposits to the Debt Service Reserve Account established under the Financing Documents to the extent necessary to provide therein an amount equal to the requirement for such account under the Financing Documents if not otherwise replenished from Power Charges;

(iv) the cost of Fiduciaries associated with the issuance and administration of the Bonds; and

(v) when and if the Department no longer sells Power under the Act and Bonds remain outstanding, the Department’s Bond Charge servicing costs, costs of preparing and providing the information and reports required under the Financing Documents, this Agreement and the Act, related audit, legal and consulting costs, related administrative costs, and costs of complying with arbitrage restrictions and rebate requirements.

**“Bonds”** shall mean State of California Department of Water Resources evidences of indebtedness issued for the purposes specified in the Act pursuant to Section 80130 of the Act and the Executive Order of the Governor of the State of California, dated June 18, 2001, in an aggregate principal amount up to \$ 13,423,000,000; provided, however, that (i) notes issued in anticipation of the issuance of Bonds and retired from the proceeds of those Bonds shall not be counted against said dollar limitation, and (ii) Bonds shall include indebtedness issued to refund prior Bonds, but such refunding indebtedness

shall not be counted against said dollar limitation; and, provided, further that, for all purposes of this definition, the Bonds shall exclude the Interim Loan.

***“Commission”*** shall mean the State of California Public Utilities Commission and any board, commission, department, corporation, authority or officer succeeding to the functions thereof, or to whom the powers conferred on the Commission by the Act shall be given by law.

***“Debt Service Reserve Account”*** shall have the meaning set forth in the Financing Documents. The purpose of the Debt Service Reserve Account is to provide for the payment of Bond Related Costs in the event that amounts in the Bond Charge Payment Account, after deposits from the Bond Charge Collection Account or other funds under the Indenture, are insufficient. The Debt Service Reserve Account is expected to be initially funded with Bond proceeds.

***“Department”*** shall mean the State of California Department of Water Resources.

***“Department Costs”*** shall mean, at any given time, all amounts which the Department is then entitled under Section 80110 of the Act to recover, as a revenue requirement, to enable it to comply with Section 80134 of the Act, (including amounts payable under the Interim Loan), except that Department Costs, unless specifically provided in this Agreement, exclude Bond Related Costs to the extent that such Bond Related Costs have been recovered from Bond Charges.

***“Electrical Corporation”*** shall have the meaning ascribed thereto in Section 218 of the Public Utilities Code, including any successor and assign thereof.

***“Electric Service Provider”*** shall mean an entity that provides electrical service to one or more retail customers located within the Service Areas of Pacific Gas & Electric, Southern California Edison Company, or San Diego Gas & Electric Company or any of their respective successors, except that Electric Service Provider excludes: the Department, any other public agency to the extent that it offers electrical service to customers within its jurisdiction or within the service territory of a local publicly owned electric utility, and Electrical Corporations. Electric Service Provider includes the unregulated affiliates and subsidiaries of an Electrical Corporation.

***“Fiduciary”*** shall mean any Trustee, any bond registrar and any paying agent in connection with Bonds pursuant to the Financing Documents, and their respective successors and assigns.

***“Financing Documents”*** shall mean any resolution, indenture, trust agreement, loan agreement, revolving credit agreement, reimbursement agreement, standby purchase agreement or other agreement or instrument adopted or entered into by the Department authorizing, securing or enhancing the Bonds, including any bond offering documents, as from time to time amended or supplemented in accordance therewith. Copies of all Financing Documents shall be provided to the Commission.

***“Fund”*** shall mean the Department of Water Resources Electric Power Fund established by the Act.

***“Interim Loan”*** shall mean obligations issued under the Credit and Security Agreement, dated as of June 26, 2001, among the Department and various lenders identified therein and Morgan Guaranty Trust Company of New York, in its capacity as agent for the lenders, and other documents and agreements described therein.

***“Minimum Operating Reserve Account Requirement”*** shall have the meaning set forth in the Financing Documents, and shall include an amount solely limited to make payments due under the Priority Long Term Power Contracts if funds are not available in the Operating Account or the Priority Contract Account.

***“Operating Account”*** shall have the meaning set forth in the Financing Documents. The purpose of the Operating Account is to provide for the payment of Department Costs, including by transfer to the Priority Contract Account. Power Charges will generally be deposited into the Operating Account.

***“Operating Reserve Account”*** shall have the meaning set forth in the Financing Documents. The purpose of the Operating Reserve Account is to provide for the payment of Department Costs in the event that amounts in the Operating Account are insufficient, or amounts in the Priority Contract Account are insufficient to make payments due under the Priority Long Term Power Contracts.

***“Power”*** shall have the meaning ascribed thereto in Section 80010 of the Water Code.

***“Power Charges”*** shall mean charges imposed by the Commission upon Retail End Use Customers for electric power deemed sold to Retail End Use Customers by the Department, except that Power Charges exclude Bond Charges.

***“Priority Contract Account”*** shall have the meaning set forth in the Financing Documents. The purpose of the Priority Contract Account is to provide solely for the payment of amounts due under Priority Long Term Power Contracts.

***“Priority Long Term Power Contracts”*** shall mean (i) those long-term electric power contracts identified in Appendix A, and shall not include any electric power contracts entered into after August 14, 2001; provided, however, that such term shall include any priority long term electric power contract entered into after August 14, 2001, as an amendment or novation of any Priority Long Term Power Contract and (ii) any contracts entered into for the purpose of securing fuel for use at generating facilities being operated pursuant to such Priority Long Term Power Contracts, if that fuel supply contract contains a provision to the general effect that payments by the Department under the contract are to be paid or payable prior to bonds, notes, or other indebtedness of the Department secured by a pledge or assignment of the revenues of the Department under the Act and other amounts in the Fund. The Department shall consult with the Commission prior to entering into any additional contract for the purpose of securing fuel

if that contract contains such a provision. Contracts shall cease to be treated as Priority Long Term Power Contracts under the circumstances described in Section 7.8.

***“Retail End Use Customer”*** shall mean each customer within the Service Area of an Electrical Corporation that is deemed to purchase electric power from the Department under the Act.

***“Retail Revenue Requirements”*** shall mean the amounts required to pay Department Costs that are to be generated from Power Charges imposed by the Commission from time to time.

***“Service Area”*** shall mean the geographic area in which an Electrical Corporation distributes electricity.

***“State”*** shall mean the State of California.

***“Trustee”*** shall mean any bank or trust company, or the State Treasurer, appointed as trustee, co-trustee or collateral agent in connection with the Bonds or bond related obligations pursuant to the Financing Documents, and its successors and assigns.

## ARTICLE II REPRESENTATIONS AND WARRANTIES

Section 2.1 Representations and Warranties of Department. The Department makes the following representations and warranties as the basis for the undertakings on its part herein contained:

(a) It is a department within the Resources Agency of the State, validly existing under the Constitution and laws of the State, and has full power and authority to execute, deliver and perform and observe all of the terms and provisions of this Agreement.

(b) The execution, delivery and performance of this Agreement have been duly authorized by all necessary action on the part of the Department.

(c) This Agreement is a legal, valid and binding agreement of the Department and is enforceable against the Department in accordance with its terms.

Section 2.2 Representations and Warranties of Commission. The Commission makes the following representations and warranties as the basis for the undertakings on its part herein contained:

(a) It is a commission of the State, validly existing under the Constitution and laws of the State, and has full power and authority to execute, deliver and perform and observe all of the terms and provisions of this Agreement.

(b) The execution, delivery and performance of this Agreement, have been duly authorized by all necessary action on the part of the Commission.

(c) This Agreement is a legal, valid and binding agreement of the Commission and is enforceable against the Commission in accordance with its terms.

### **ARTICLE III AGREEMENTS FOR BOND ISSUANCE**

Section 3.1 Agreement for Bond Issuance. The Department and the Commission agree that this Agreement is executed to facilitate the issuance of Bonds and solely for the benefit of the Beneficiaries.

Section 3.2 No Indebtedness. Nothing contained in the Agreement shall be deemed to create or constitute a debt or liability of the State or of any political subdivision thereof, or a pledge of the full faith and credit or taxing power of the State or of any such political subdivision.

Section 3.3 No Pecuniary Liability of Commission. Nothing in this Agreement shall be deemed to create any pecuniary liability of the Commission, its Commissioners, employees or agents to any person, the sole remedy for any default, breach or other nonperformance by the Commission hereunder being the exercise of remedies specifically afforded hereunder and under the Act.

### **ARTICLE IV RETAIL REVENUE REQUIREMENTS; JUST AND REASONABLE COSTS**

#### Section 4.1 Retail Revenue Requirements.

(a) Generally. The Commission agrees to cooperate with and assist the Department in its review, determination and revision of its Retail Revenue Requirement at the request of the Department. The Department shall promptly notify the Commission following any determination or revision of the Retail Revenue Requirements. If any such annual or more frequent review indicates that the Power Charges are, or will be, insufficient to meet the requirements of the Act, and the Department so notifies the Commission, the Commission shall take necessary action to cure or avoid any such deficiency, including adjustment of existing, and the calculation and imposition of additional, Power Charges. To the extent that the Department has not provided a revised Retail Revenue Requirement to the Commission within the time periods required by subsection (b) below for any reason and the Commission determines based on the record before it, that Power Charges are not sufficient to pay Department Costs (which for this purpose include replenishment of the Bond Charge Collection Account, Bond Charge Payment Account or Debt Service Reserve Account), the

Commission may modify Power Charges to cover such shortfall on an interim basis pending receipt of a revised Retail Revenue Requirement from the Department.

(b) Communication. The Department shall, at least annually, and more frequently as deemed reasonably necessary or appropriate by the Department or the Commission, review, determine and revise its Retail Revenue Requirements. The Department agrees that it shall revise and communicate to the Commission its Retail Revenue Requirement within 20 days of the occurrence of any of the following circumstances, whether or not the Commission notifies the Department of such events: (i) the Department projects that, within 120 days, there will be insufficient funds in the Priority Contract Account to pay costs incurred by the Department under the Priority Long Term Power Contracts, or (ii) the Department projects that, within 120 days, there will be less than the Minimum Operating Reserve Account Requirement in the Operating Reserve Account, or (iii) the Department projects that, within 120 days, shortfalls in the Priority Contract Account, Operating Account and the Operating Reserve Account will require the usage of moneys in the Bond Charge Collection Account to pay costs incurred by the Department under the Priority Long Term Power Contracts, or (iv) the Department projects that, moneys in the Debt Service Reserve Account will be used within 120 days to pay Bond Related Costs. The Department further agrees that if a revised Retail Revenue Requirement has not previously been submitted pursuant to the preceding sentence of this Section 4.1 the Department shall revise and communicate to the Commission within 3 business days its Retail Revenue Requirement in the event that the Department makes any withdrawal from the Bond Charge Collection Account to pay specified Department Costs, or from the Operating Reserve Account or the Debt Service Reserve Account such that, in either case, the amount in such account is less than that required under the Financing Documents.

(c) Information. In any determination of the Retail Revenue Requirements, the Department shall include the amount required to be recovered in the applicable period and shall set forth amounts projected to be required to be collected during subsequent periods in which either Bonds will remain outstanding or the Department will continue to sell Power, but not exceeding the five years succeeding the applicable revenue requirement period. The Retail Revenue Requirements for any period shall take into account any deficiency or any surplus in amounts recovered in earlier periods, as well as any anticipated surpluses in the Priority Contract Account, Operating Account and the Operating Reserve Account in the period. The Department's notification to the Commission of the Retail Revenue Requirements shall include a statement containing the Department's projections (with reasonable detail) of the following information for each month during the period covered by the Retail Revenue Requirements:

(i) the beginning balance of funds on deposit in the Fund, including the amounts on deposit in each account and subaccount of the Fund;

(ii) the amounts necessary to pay or provide for the principal of, premium, if any, and interest on all Bonds and all other Bond Related Costs under the

Financing Documents as and when the same shall become due and the amount of Bond Charges to be collected for such purpose;

(iii) the amount of its Retail Revenue Requirement for that month;

(iv) any other information requested by the Commission in its proceedings implementing a Retail Revenue Requirement.

(d) Additional Information. The Department shall provide the Commission as soon as practicable, but no later than 30 days after the end of each month, a report of Department receipts and Department Costs for the prior month, based upon the sums of known actual Department receipts and Department Costs and estimated accruals for those receipts and costs which are subject to final invoicing or accounting settlement processes. Such monthly report shall be presented in a form which enables reasonable comparison to the monthly estimates contained in the latest Retail Revenue Requirement for (i) long term Department contract electric power purchases, (ii) short term Department electric power purchases, (iii) other electric power purchases or reimbursement by the Department of purchases of electric power by others for which the Department is responsible for payment, and (iv) Department administrative costs. For items (i), (ii) and (iii) above, the Department shall report information with a level of detail that lists each counterparty, the volumes provided by the counterparty, and the cost of those volumes. In addition, for those items, the costs and volumes will be separated into day ahead, hour ahead, "out of market" purchases, and contract categories, or such comparable categories as shall be in place at the time. The Department shall also report to the Commission on a monthly basis the balance in each of the accounts or subaccounts the Department is required to keep pursuant to the Financing Documents. When actual or additional information becomes available for any of the reports identified in this Section 4.1(d), the Department will communicate such information to the Commission. In addition, the Department's monthly reports shall contain the information required by Section 4.1(c)(ii).

(e) The Commission shall receive any financial reports prepared by the Department as required by the Financing Documents at the same time as the recipients under the Financing Documents.

Section 4.2 Just and Reasonable Costs. The Department agrees that prior to including any cost in the Retail Revenue Requirements communicated to the Commission in accordance with Section 4.1(a), the Department will conduct whatever procedures are required by law to determine that such cost is just and reasonable within the meaning of Section 451 of the California Public Utilities Code.

Section 4.3 ESP Power. Bond Charges may be based on electric power provided to customers by Electric Service Providers only after an order of the Commission providing for such charges becomes final and unappealable.

**ARTICLE V  
RATE COVENANT**

Section 5.1 Rate Covenant.

(a) The Commission hereby covenants and agrees to calculate, revise and impose from time to time, Bond Charges sufficient to provide moneys so that the amounts available for deposit in the Bond Charge Payment Account from time to time, together with amounts on deposit in the Bond Charge Payment Account, are at all times sufficient to pay or provide for the payment of all Bond Related Costs when due in accordance with the Financing Documents.

(b) As provided by Section 80112 of the Act and as authorized by Section 80110 of the Act, including by reference to Article 5.5 (commencing with Section 840) of Chapter 4 of Part 1 of Division 1 of the California Public Utilities Code, the Bond Charges authorized by Commission Order and the right of the Department to receive Bond Charges as provided in this Agreement shall be property of the Department for all purposes under California law.

(c) As authorized by Section 80110 of the Act by reference to Article 5.5 (commencing with Section 840) of Chapter 4 of Part 1 of Division 1 of the California Public Utilities Code, Sections 5.1(a) and 5.1(b) of this Agreement shall have the force and effect of a "financing order" adopted thereunder and shall be irrevocable and enforceable in accordance with the terms hereof, including, without limitation, in circumstances in which the Department has breached its obligations under this Agreement or in respect of the Financing Documents.

(d) If the Department has complied with Article IV hereof to the extent applicable, but nevertheless projects that there will be insufficient monies on deposit in the Bond Charge Payment Account to make timely payment of Bond Related Costs, the Department shall submit to the Commission a request that the Commission increase Bond Charges to make timely payment of Bond Related Costs and the Commission agrees that it shall calculate and impose revised Bond Charges to pay such Bond Related Costs no later than 120 days from the date following the delivery to the Commission by the Department of its request for revised Bond Charges, provided, to the extent the insufficiency in the Bond Charge Payment Account relates to an insufficiency of Power Charges to provide for certain specified Department Costs, the Commission agrees that, no later than 120 days from the date on which the Department submits a revised Retail Revenue Requirement pursuant to Article IV covering the same projected insufficiency in the Bond Charge Payment Account, it shall respond to the revised Retail Revenue Requirement or the Bond Charge request. Whether or not the Department makes the foregoing requests, the Commission shall, in all instances, be bound by its covenants in this Article V.

**ARTICLE VI  
COVENANTS OF THE COMMISSION**

**Section 6.1    Power Charges.**

(a) The Commission hereby covenants and agrees to calculate, revise and impose, from time to time, Power Charges sufficient to provide moneys in the amounts and at the times necessary to satisfy the Retail Revenue Requirements as specified by the Department.

(b) Power Charges and Bond Charges shall be established by the Commission without regard to the levels or amounts of any particular rates or charges authorized by the Commission to be charged by any Electrical Corporation for electrical power sold by such Electrical Corporation.

(c) The Commission acknowledges that, as provided by Section 80112 of the Act, Power Charges shall be property of the Department for all purposes under California law.

(d) The Commission agrees that it shall calculate and impose Power Charges no later than 120 days following the delivery to the Commission by the Department of a statement of new or revised Retail Revenue Requirements that complies with Article IV hereof.

**Section 6.2    Compliance with Agreement.**

(a) The Commission hereby covenants with the Department that the Commission shall take all such actions or refrain from taking all such actions, as the case may be, so as to comply with the terms and provisions of the Act and this Agreement.

(b) The Commission hereby covenants that, so long as any Bonds shall be outstanding, it will not take any action, or fail to take any action, which, if taken or not taken, as the case may be, would adversely affect the tax-exempt status of the interest payable on Bonds or Interim Loan obligations then outstanding, the interest on which, at the time of issuance thereof, was exempt from Federal income taxation or not includable in gross income for purposes of Federal income taxation. In furtherance of the foregoing, the Commission agrees to act with respect to those matters within its control that could adversely affect the exclusion of interest on Bonds or Interim Loan obligations from gross income for purposes of federal income taxation.

**Section 6.3    Liens.** Until the Bonds have been paid in full or provision has been made therefor in accordance with the Financing Documents, the Commission, to the extent it has the power to do so, shall not permit to be created any purported lien upon or pledge of the Power Charges or the Bond Charges except any lien and pledge thereon created by or pursuant to the Act as security for the enforcement of the Department's obligations (including the Interim Loan) entered into pursuant thereto.

Section 6.4 Commission Acknowledgment. The Commission acknowledges that the Department intends to enter into Financing Documents that permit certain specified Department Costs to be funded out of amounts available in the Bond Charge Collection Account if insufficient moneys are available in the Priority Contract Account, Operating Account and the Operating Reserve Account to pay such specified Department Costs. In the event that such Department Costs are funded out of the Bond Charge Collection Account, the Department shall take such actions as are required under this Agreement so that the amounts applied from the Bond Charge Collection Account for such purpose shall be replenished from Power Charges, provided that any failure to do so by the Department shall not mitigate or alter the Commission's obligations under Article V.

## ARTICLE VII COVENANTS OF THE DEPARTMENT

Section 7.1 Retail Revenue Requirement. The Department hereby covenants and agrees to calculate and revise its Retail Revenue Requirement only for the purpose of recovering costs which it is permitted to collect under the Act, (including amounts payable under the Interim Loan), and not to cover any costs in connection with its responsibilities under the Act which it cannot include in such a Retail Revenue Requirement.

Section 7.2 Department Participation. Consistent with the limitations set forth in Water Code Section 80110, upon the request of the Commission, the Department will participate in any Commission proceedings, including providing witnesses, attending public hearings and providing any other materials necessary to facilitate the Commission's completion of its proceedings, taken in connection with the establishment of Power Charges or Bond Charges by the Commission.

Section 7.3 Compliance with Agreement.

(a) The Department hereby covenants with the Commission that the Department shall take all such actions or refrain from taking all such actions, as the case may be, so as to comply with the terms and provisions of the Act and this Agreement, including but not limited to, complying with the legal requirements referenced in Article IV and the requirement to review its Retail Revenue Requirement at least annually.

(b) The Department hereby covenants that, so long as any Bonds shall be outstanding, it will not take any action, or fail to take any action, which, if taken or not taken, as the case may be, would adversely affect the tax-exempt status of the interest payable on Bonds or Interim Loan obligations then outstanding, the interest on which, at the time of issuance thereof, was exempt from Federal income taxation or not includable in gross income for purposes of Federal income taxation. In furtherance of the foregoing, the Department agrees to act with respect to those matters within its control

that could adversely affect the exclusion of interest on Bonds or Interim Loan obligations from gross income for purposes of federal income taxation.

Section 7.4 Charges. The Department acknowledges the Commission's exclusive authority to spread the Department's revenue requirement among customer classes and service territories and to determine the extent or timing of rate changes that may be required in the future, consistent with the Commission's obligations in this Rate Agreement. As long as this Agreement is in effect the Department agrees that it will not attempt to fix or establish charges on retail end use customers for the purpose of paying Department Costs or Bond Related Costs. Nothing in this Agreement shall be read to establish that the Department does or does not have the authority to fix or establish such charges.

Section 7.5 Department Audits. The Department shall provide to the Commission when available a copy of any audit conducted pursuant to Section 80270 of the Act and a copy of each of the Department's audited annual financial statements for the Fund.

Section 7.6 Proceeds. The Department shall sell Bonds, as soon as practicable, in amounts sufficient to provide for the repayment to the General Fund of the State of the advances made under the Act to the Fund, together with interest on such advances as provided by the Act. The Department shall apply the proceeds of the Bonds to repayment of the General Fund with the understanding that repayment of the Interim Loan in full has priority and that the following costs may have priority: creation of adequate reserves for the payment of Bond Related Costs and payment of costs of issuance.

Section 7.7 Renegotiation of Power Contracts. The Department shall use its best efforts to renegotiate or modify its long term Power contracts.

Section 7.8 Priority Long Term Power Contracts. Any Priority Long Term Power Contract that is amended, replaced or terminated so that any resulting contract no longer contains a provision to the general effect that payments by the Department under the contract are to be paid or payable prior to bonds, notes, or other indebtedness of the Department secured by a pledge or assignment of the revenues of the Department under the Act and other amounts in the Fund shall no longer be treated as a Priority Long Term Power Contract. The Department shall immediately notify the Commission of any such amendment, replacement or termination.

Section 7.9 Appointment of Trustee. To the extent practicable, the Department shall appoint as Trustee a bank, trust company or other qualified entity or person that does not itself, or by or through any of its corporate affiliates, trade in electricity or natural gas commodity markets, and does not itself, or any of its affiliates, appear on the list of top twenty creditors for any Electrical Corporation or any entity providing electric power to the Department that has petitioned for bankruptcy.

Section 7.10 Financing Documents. The Department shall involve, to the fullest extent possible, the Commission in the development and completion of all Financing Documents and shall consult with the Commission on the sizing of operating and debt service reserves, debt service coverage, the maturity and maximum amount of Bonds to be issued and any other matters in the Financing Documents which the Commission deems material. The Department has submitted to the Commission a summary (the "Summary") of the material terms of the Financing Documents securing its Bonds. ("Material terms" means the maximum amount of the Bonds authorized, their maturity, a description of the flow of funds and a description of the sizing or methodology of sizing of reserves held or created pursuant to the Financing Documents or debt service coverage required thereby.) If the Department makes any material change to any such terms it must obtain the approval of the Commission's designee. For purposes of the last sentence, "material change" means (i) a change in the sizing or methodology of sizing of debt service reserves that would increase the projected net debt service on the Bonds by more than an amount specified in the Summary; (ii) an increase in debt service coverage required by the Financing Documents by more than an amount specified in the Summary; (iii) a change in the sizing or method of sizing of operating reserves by more than an amount specified in the Summary; (iv) any increase in the maximum amount of the Bonds authorized; (v) a change in the maturity of the Bonds beyond those changes permitted in the Summary; or (vi) a change in the flow of funds beyond those changes permitted in the Summary. At the time the Commission adopts the Rate Agreement, it will appoint a designee for purposes of this Section 7.10. Nothing in this Section 7.10 shall imply that the Commission or its designee shall have the right to approve (i) the final amortization, interest rates, or methods of determination, denominations, redemption provisions or pricing of the Bonds or (ii) final sizing of reserves and debt service coverage based on pricing considerations, or (iii) except to the extent set forth above in this Section 7.10, the terms of any revolving credit agreement, reimbursement agreement, standby purchase agreement, liquidity or credit enhancement facility, or swap agreement or other hedging agreement entered into in connection with the Bonds, or (iv) any agreements or arrangements with any Fiduciary incident to the issuance of the Bonds or (v) any offering document used in connection with the offering of the Bonds (except with respect to sections of the offering document relating to the Commission.)

## **ARTICLE VIII EVENTS OF DEFAULT AND REMEDIES**

Section 8.1 Events of Default. An "event of default" or a "default" shall mean, whenever they are used in this Agreement, a failure of the Commission to calculate and impose Bond Charges in accordance with Article V.

Section 8.2 Remedies.

(a) Whenever any event of default shall have occurred and be continuing, and written notice of the default shall have been given to the Commission by the Department and the default shall not have been cured within 30 days, the Department

may take whatever action at law or in equity may appear necessary or desirable to enforce performance and observance of any obligation, agreement or covenant of the Commission under Article V.

(b) Whenever any event shall have occurred and be continuing, such that either the Commission or the Department is not in compliance with any covenant or obligation of this Agreement, and written notice of the breach of such covenant or obligation shall have been given to either the Commission or the Department and the breach shall not have been cured within 30 days, both the Commission or the Department may take whatever action at law or in equity that may appear necessary or desirable to enforce performance and observance of any obligation, agreement or covenant under this Agreement.

### Section 8.3 Consent to Assignment.

(a) The Commission consents to the collateral assignment by the Department to the Trustee for the benefit of the Beneficiaries, as such, of the covenants of the Commission contained in Article V; provided, however, that any rights so granted to the Trustee shall not be greater than the rights of the Department under such Sections of this Agreement, and such right on the part of the Trustee to enforce such covenants shall only commence after the Department has both defaulted under its obligations contained in the Financing Documents and has failed to enforce such covenants in accordance with the terms of this Agreement. Prior to exercising any rights granted to the Trustee in accordance with this Section 8.3, the Trustee shall be required to (i) give prior written notice within the time period required in Section 8.3(b) below, (ii) certify to the Commission that an event of default, other than an event of default predicated solely on the Commission's failure to act hereunder, has occurred under the Financing Documents and (iii) comply or cause the Department to comply with the provisions of this Agreement relating to the Department's rights, duties and obligations hereunder.

(b) In addition to the requirements of Section 8.3(a) for exercising its rights hereunder, unless a default has resulted in the amount in the Debt Service Reserve Account being insufficient to pay or provide for the timely payment of all Bond Related Costs in accordance with the Financing Documents, the Trustee shall give the Commission 30 days prior written notice of the exercise by the Trustee of any of the Department's rights under Section 5.1 hereof.

## ARTICLE IX TERMINATION

Section 9.1 Termination. The Agreement shall terminate, and the covenants and other obligations contained in the Agreement shall be discharged and satisfied, when payment of the Bonds and all other Bond Related Costs required to be paid by the Department under the Financing Documents have been made or provided for in accordance with the Financing Documents.

## **ARTICLE X AMENDMENTS**

Section 10.1 Amendments to Agreement. No amendment to the Agreement shall be effective unless it is in writing and signed by each of the parties hereto, provided, however, on or after the issuance of the Bonds, Sections 5.1(a) and (b) may not be amended.

## **ARTICLE XI MISCELLANEOUS**

Section 11.1 No Waiver. No failure to exercise, and no delay in exercising by the parties hereto, any right, power or privilege hereunder shall operate as a waiver thereof; nor shall any single or partial exercise of any right, power or privilege hereunder preclude any other or further exercise thereof, or the exercise of any right, power or privilege. The rights and remedies herein provided are cumulative and not exclusive of any rights or remedies provided by law, including the Act.

Section 11.2 Notices. All notices, requests and other communications under this Agreement shall be deemed to have been duly given if in writing and delivered personally or by certified mail (a) to the Department at 1416 9<sup>th</sup> Street, 11<sup>th</sup> Floor, Sacramento, California 95814, attention: Director; (b) to the Commission at 505 Van Ness Avenue, San Francisco, California 94102, attention: Executive Director and General Counsel; or such other address as the Department, or the Commission, as the case may be, shall hereafter designate by notice in writing to the other party.

Section 11.3 Severability. In the event that any one or more of the provisions contained in the Agreement is or are invalid, irregular or unenforceable in any respect, the validity, regularity and enforceability of the remaining provisions contained in this Agreement shall be in no way affected, prejudiced or disturbed thereby.

Section 11.4 Headings. The descriptive headings of the several articles of the Agreement are inserted in the Agreement for convenience only and shall not be deemed to affect the meaning or construction of any of the provisions of the Agreement.

Section 11.5 Governing Law. The Agreement shall be governed by, and construed in accordance with, the Constitution and laws of the State of California, without regard to the provisions thereof regarding conflicts of law.

Section 11.6 Counterparts. This Agreement may be executed in several counterparts, each of which shall be an original and all of which shall constitute but one and the same instrument.

Section 11.7 Date of Agreement. The date of this Agreement shall be for identification purposes only. This Agreement shall become effective immediately upon execution and delivery by the parties hereto.

Section 11.8 Third Party Beneficiaries. Nothing in this agreement express or implied shall be construed to give any person or entity, other than the parties hereto and the Beneficiaries, any legal or equitable right, remedy, or claim under or in respect of the agreement or any covenants, agreements, representations, or provisions contained herein.

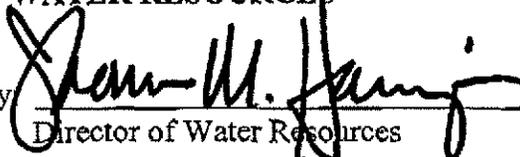
Section 11.9 Applicability. This Agreement does not apply to any Retail Revenue Requirement under consideration by the Commission as of the date of this Agreement, but does apply to any Retail Revenue Requirement submitted thereafter. Prior to the issuance of any Bonds, any provision of this Agreement referring to an account or subaccount under the Financing Documents shall be interpreted to achieve the intent of such provision as nearly as practicable.

Section 11.10 No Implied Waivers. Nothing in this Agreement shall be construed to limit the rights of the Commission or the Department to assert any rights it may have with respect to any contract entered into by the Department with respect to its obligations under the Act, or to contest in any proceeding the legality or effect of any contract entered into by the Department with respect to its obligations under the Act.

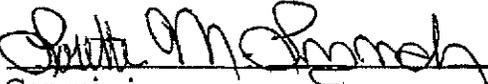
Section 11.11 No Assignment. Except as set forth in Section 8.3, neither the Department nor the Commission shall assign any of its rights or delegate any of its duties under this Agreement without the express written consent of the other party hereto, provided, however, if, with respect to either party, another governmental entity is created or designated by law to carry out the rights, powers, duties and obligations of such party, then such party may, if required by such law, transfer and assign its right, title and interest in this Agreement to such successor, provided, that such successor entity is permitted by law to assume such party's obligations under this Agreement and agrees in writing to be bound by the terms of this Agreement.

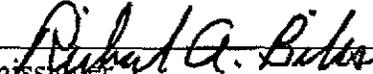
IN WITNESS WHEREOF, the Department has caused this Agreement to be executed in its name by the Director of Water Resources and the Commission by the affirmative vote of the Commission (Decision No. 02-02-051) has caused this Agreement to be executed in its name by those Commissioners who constituted a majority of the Commission when it approved this agreement, all as of the date first above written.

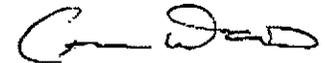
STATE OF CALIFORNIA  
DEPARTMENT OF  
WATER RESOURCES

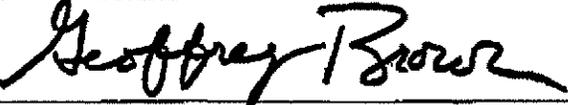
By:   
Director of Water Resources

STATE OF CALIFORNIA PUBLIC  
UTILITIES COMMISSION

By:   
Commissioner

By:   
Commissioner

By:   
Commissioner

By:   
Commissioner

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## APPENDIX E

### PROPOSED FORM OF OPINION OF ATTORNEY GENERAL

*Upon delivery of the Series 2005 Bonds, the Honorable Bill Lockyer, Attorney General of the State of California, proposes to deliver an opinion in substantially the following form:*

California Department of Water Resources  
Sacramento, California

**Department of Water Resources**  
**Power Supply Revenue Bonds**  
**\$759,400,000 Series 2005F**  
**\$1,834,600,000 Series 2005G**

Ladies and Gentlemen:

We have acted as Attorney General of the State of California in connection with the issuance by the State of California Department of Water Resources (the "Department") of \$759,400,000 aggregate principal amount of its Power Supply Revenue Bonds, Series 2005F and \$1,834,600,000 aggregate principal amount of its Power Supply Revenue Bonds, Series 2005G (collectively, the "Series 2005 Bonds"). The Series 2005 Bonds are issued under and pursuant to the Constitution and laws of the State, including, but not limited to, Division 27 (commencing with Section 80000) of the California Water Code, as amended (the "Act"), and a Trust Indenture dated as of October 1, 2002 (the "Trust Indenture"), among the Department, the Treasurer of the State of California, as Trustee (the "Trustee") and U.S. Bank, N.A., as Co-Trustee (the "Co-Trustee"), as supplemented by a Fourth Supplemental Trust Indenture dated as of December 1, 2005, among the Department, the Trustee and the Co-Trustee (collectively with the Trust Indenture, the "Indenture").

In such connection, we have examined the Indenture, the Rate Agreement dated as of March 8, 2002 (the "Rate Agreement"), by and between the Department and the California Public Utilities Commission (the "CPUC"), certifications of the Department, the Trustee, the Co-Trustee, and others, opinions of special counsel to the Department and the CPUC, and such other documents, opinions and matters to the extent we deemed necessary to render the opinions set forth herein. We have assumed, without undertaking to verify, the genuineness of all documents, certifications and opinions and signatures thereon presented to us (whether as originals or as copies); the accuracy of the factual matters represented, warranted or certified in such documents, certificates and opinions; the correctness of the legal conclusions contained in such opinions; the due and legal execution of such documents and certificates by, and validity thereof against, any parties other than the Department; and compliance with all covenants and agreements contained in the Indenture and the Rate Agreement.

This opinion is issued as of the date hereof. The opinions expressed herein are based on an analysis of existing laws, regulations, rulings and court decisions and cover certain matters not directly addressed by such authorities. Such opinions may be affected by actions taken or omitted or events occurring after the date hereof. We have not undertaken to determine, or to inform any person, whether any such actions are taken or omitted or events do occur or any other matters come to our attention after the date hereof. We assume no obligation to update, revise or supplement this opinion to reflect any action hereafter taken or not taken, or any facts or circumstances, or any changes in law or in interpretations thereof, that may hereafter arise or occur, or for any other reason.

In addition, we call attention to the fact that the rights and obligations under the Bonds (as defined in the Trust Indenture), the Indenture and their enforceability may be subject to bankruptcy, insolvency, reorganization, arrangement, fraudulent conveyance, moratorium and other laws relating to or affecting creditors' rights, to the application of equitable principles, to the exercise of judicial discretion in appropriate cases and to the limitations

on legal remedies against the State of California. We express no opinion with respect to any indemnification, contribution, penalty, choice of law, choice of forum, waiver or severability provisions contained in the documents described herein.

Finally, we express no opinion as to the accuracy, adequacy or sufficiency of any financial or other information which has been or will be supplied to purchasers of the Series 2005 Bonds and undertake no responsibility for the accuracy, completeness or fairness of the Official Statement dated November 17, 2005, pertaining to the Series 2005 Bonds or other offering material relating to the Bonds and express no opinion with respect thereto.

Based on and subject to the foregoing, and in reliance thereon, as of the date hereof, we are of the following opinions:

1. The Department is a department of the State of California, duly established and validly existing under the laws of the State of California.

2. The Indenture has been duly authorized, executed and delivered by the Department, and constitutes the valid and binding agreement of the Department, enforceable against the Department in accordance with its terms.

3. The Series 2005 Bonds constitute valid and binding limited special obligations of the Department payable solely from the Trust Estate (as defined in the Trust Indenture), including the Revenues (as defined in the Trust Indenture), as and to the extent provided in the Indenture. The Series 2005 Bonds do not constitute a debt or liability of the State or of any political subdivision thereof, and do not constitute a general obligation of the Department. Neither the faith and credit nor the taxing power of the State or of any political subdivision thereof is pledged to the payment of the principal of, premium, if any, or interest on the Series 2005 Bonds. The Department has no taxing power.

4. The Trust Indenture permits the Department to issue additional Bonds (as defined in the Trust Indenture), and incur Parity Obligations (as defined in the Trust Indenture) and other obligations thereunder from time to time on the terms and conditions and for the purposes stated therein.

5. The Indenture creates a valid pledge of the Trust Estate, including the Revenues, as set forth in the Indenture, subject only to the provisions of the Indenture permitting the payment or use of the Trust Estate for the purposes, in the manner and upon the terms and conditions set forth in the Indenture. Pursuant to the Act, the pledge of the Trust Estate, including the Revenues, made by the Department in the Indenture is valid, binding and perfected without any physical delivery, recordation, filing or further act, and the lien thereof is valid, binding and perfected against all parties having claims of any kind in tort, contract or otherwise against the Department irrespective of whether such parties have notice thereof.

6. The Rate Agreement has been duly authorized, executed and delivered by the Department and constitutes a valid and binding agreement of the Department, enforceable against the Department in accordance with its terms.

Sincerely,

Deputy Attorney General

For BILL LOCKYER  
Attorney General

## APPENDIX F

### PROPOSED FORM OF OPINION OF BOND COUNSEL

[Closing Date]

California Department of Water Resources  
Sacramento, California

Ladies and Gentlemen:

We have acted as bond counsel to the State of California (the "State") Department of Water Resources (the "Department") in connection with the issuance by the Department of \$759,400,000 aggregate principal amount of its Power Supply Revenue Bonds, Series 2005F (consisting, on the date hereof, of five subseries designated "F-1" through "F-5") and \$1,834,600,000 aggregate principal amount of its Power Supply Revenue Bonds, Series 2005G (consisting, on the date hereof, of fourteen subseries designated "G-1" through "G-14") (collectively, the "Offered Bonds"). The Offered Bonds are issued under and pursuant to the Constitution and laws of the State, including, but not limited to, Division 27 (commencing with Section 80000) of the California Water Code, as amended (the "Act"), and a Trust Indenture dated as of October 1, 2002 (the "Trust Indenture"), among the Department, the Treasurer of the State as Trustee (the "Trustee") and U.S. Bank National Association, as Co-Trustee (the "Co-Trustee"), as supplemented by a Fourth Supplemental Indenture dated as of December 1, 2005, among the Department, the Trustee and the Co-Trustee (collectively, with the Trust Indenture, the "Indenture"). Capitalized terms used but not defined herein shall have the respective meanings given to them in the Indenture.

We have examined a record of proceedings relating to the issuance of the Offered Bonds, and based thereon and on our examination of existing law, such legal proceedings and such other documents as we deem necessary to render this opinion, we are of the opinion that:

1. The Department is duly existing under the laws of the State. Under the laws of the State, including the Constitution of the State, and under the Constitution of the United States, the Act is valid with respect to all provisions thereof material to the subject matters of this opinion letter.

2. The Department is validly authorized under the laws of the State, particularly the Act, to execute and deliver the Indenture and to perform its obligations thereunder. The Indenture has been duly authorized, executed and delivered by the Department and constitutes a valid and binding agreement of the Department, enforceable against the Department in accordance with its terms. You have received an opinion from Dorsey & Whitney LLP, counsel to the Co-Trustee, to the effect that, among other things, the Indenture has been duly authorized, executed and delivered by the Co-Trustee and constitutes a valid and binding agreement of the Trustee and Co-Trustee, and with your permission we have assumed such matters for purposes of the opinions in this paragraph 2.

3. The Offered Bonds have been duly and validly authorized and issued in accordance with the laws of the State, including the Constitution of the State, the Act and the Indenture, and constitute valid and binding limited special obligations of the Department payable solely from the Trust Estate, including the Revenues, as provided in the Indenture. The Offered Bonds do not constitute a debt or liability of the State or of any political subdivision thereof, and do not constitute a general obligation of the Department. Neither the faith and credit nor the taxing power of the State or of any political subdivision thereof is pledged to the payment of the principal of, premium, if any, or interest on the Bonds. The Department has no taxing power.

The Trust Indenture permits the Department to issue additional Bonds, and incur Parity Obligations and other obligations, thereunder from time to time on the terms and conditions and for the purposes stated therein.

The Offered Bonds, such additional Bonds, if issued, and such Parity Obligations, if incurred, will be equally and ratably secured under the Trust Indenture except as otherwise provided therein.

4. The Indenture creates the valid pledge which it purports to create of the Trust Estate, including the Revenues, subject only to the provisions of the Indenture permitting the payment or use of the Trust Estate for the purposes, in the manner and upon the terms and conditions set forth in the Indenture. Pursuant to the Act, the pledge of the Trust Estate, including the Revenues, made by the Department in the Indenture is valid, binding and perfected without any physical delivery, recordation, filing or further act, and the lien thereof is valid, binding and perfected against all parties having claims of any kind in tort, contract or otherwise against the Department irrespective of whether such parties have notice thereof.

5. The Department has duly and validly covenanted in the Indenture to cause to be established, fixed and revised from time to time charges with respect to Department Power sufficient, together with any other available moneys and securities on deposit in the Electric Power Fund, to satisfy all the Department's Revenue Requirements at the times and in the amounts needed. In furtherance of such covenant, the Department has entered into a Rate Agreement dated as of March 8, 2002 (the "Rate Agreement") with the California Public Utilities Commission (the "Commission") pursuant to the Act providing for the imposition by the Commission of rates and charges to satisfy the Department's Revenue Requirements. The Rate Agreement has been duly authorized, executed and delivered by the Department.

6. The Rate Agreement is valid and binding on the parties thereto and is enforceable against the parties thereto in accordance with its terms. The Commission has full power and authority to impose Bond Charges as provided in the Rate Agreement. Under the Rate Agreement, the Department has covenanted, among other things, that prior to including any cost in the Retail Revenue Requirements communicated to the Commission in accordance with the Rate Agreement, the Department will conduct whatever procedures are required by law to determine that such cost is just and reasonable within the meaning of Section 451 of the California Public Utilities Code. However, under the rate covenant in the Rate Agreement, the Commission has the obligation to impose Bond Charges to provide moneys sufficient to pay all Bond Related Costs when due, including debt service on the Bonds (including the Offered Bonds), and this obligation as set forth in the rate covenant is not conditioned upon any determination that the Department's costs are just and reasonable under Section 451 of the California Public Utilities Code.

7. No registration with, consent of, or approval by any governmental officer, agency or commission is necessary for the execution and delivery by the Department of the Indenture, the Offered Bonds or the Rate Agreement, other than those that have been obtained.

8. The Department has validly included in the Indenture and the Offered Bonds the pledge and undertaking of the State that so long as any obligations of the Department incurred under the Act, including without limitation the Indenture, the Bonds and Parity Obligations, remain outstanding and not fully performed or discharged, the rights, powers, duties and existence of the Department and the Commission shall not be diminished or impaired in any manner that will adversely affect the interests and rights of the holders of or parties to such obligations.

9. Under existing statutes, interest on the Offered Bonds is exempt from State of California personal income taxes.

10. Under existing statutes and court decisions, interest on the Offered Bonds is excluded from gross income for Federal income tax purposes pursuant to Section 103 of the Internal Revenue Tax Code of 1986, as amended (the "Tax Code"). Under the Tax Code, interest on the Offered Bonds is not treated as a preference item in calculating alternative minimum taxable income for purposes of the alternative minimum tax applicable to individuals and corporations; such interest, however, is includable in the adjusted current earnings of certain corporations for purposes of computing the alternative minimum tax imposed on such corporations by the Tax Code. In rendering the opinions in this paragraph 10, we have relied upon and assumed (i) the material accuracy

of the representations, statements of intention and reasonable expectations, and certifications of fact, contained in the Tax Certificate delivered on the date hereof by the Department with respect to the use of proceeds of the Offered Bonds and the investment of certain funds, and other matters affecting the exclusion of interest on the Offered Bonds from gross income for Federal income tax purposes under Section 103 of the Tax Code, and (ii) compliance by the Department with procedures and covenants set forth in the Tax Certificate and with the tax covenants set forth in the Indenture as to such matters. Under the Tax Code, failure to comply with such procedures and covenants may cause the interest on the Offered Bonds to be included in gross income for Federal income tax purposes, retroactive to the date of issuance of the Offered Bonds, irrespective of the date on which such noncompliance occurs or is ascertained.

Except as stated in paragraphs 9 and 10 above, we express no opinion as to any Federal, State or local tax consequences arising with respect to the Offered Bonds or the ownership or disposition thereof. Furthermore, we express no opinion as to the effect of any action hereafter taken or not taken in reliance upon an opinion of counsel other than ourselves on the exclusion from gross income for Federal income tax purposes of interest on the Offered Bonds, or under State and local tax law.

You have received an opinion of Randolph L. Wu, Esq., General Counsel to the Commission, to the effect that, among other things, (i) the Commission's Decision No. 02-02-051 dated February 21, 2002, approving the Rate Agreement is final and unappealable under the laws of the State, (ii) the Rate Agreement has been duly executed and delivered by the Commission, and (iii) the Commission has lawfully consented to, in accordance with the Rate Agreement and such Decision, the issuance by the Department of the outstanding principal amount of the Bonds, and with your permission we have assumed such matters for purposes of the opinions expressed in this letter.

We call attention to the fact that the enforceability of rights and remedies with respect to the Offered Bonds, the Indenture and the Rate Agreement may be limited by, and may be subject to: bankruptcy, insolvency, reorganization, arrangement, fraudulent conveyance, moratorium and other laws relating to or affecting creditors' rights; the application of equitable principles; the exercise of judicial discretion in appropriate cases; and generally applicable limitations on legal remedies against the State. We express no opinion with respect to any indemnification, contribution, choice of law, choice of forum or waiver provisions contained in the foregoing documents.

We express no opinion as to the accuracy, adequacy or sufficiency of any financial or other information which has been or will be supplied to purchasers of the Offered Bonds.

This letter is issued as of the date hereof, and we assume no obligation to update, revise or supplement this opinion to reflect any action hereafter taken or not taken, or any facts or circumstances, or any changes in law or in interpretations thereof, that may hereafter arise or occur, or for any other reason.

Very truly yours,

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## APPENDIX G

### INDEX OF PRINCIPAL DEFINITIONS

The following is an index of certain terms used in the forepart of this Official Statement, with references to the pages on which the definitions or descriptions of such terms may be found. Other terms used but not defined or described in the forepart of this Official Statement have the meanings given in APPENDIX C – “SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE – Definitions” and in APPENDIX K – “SUMMARY OF CERTAIN PROVISIONS OF THE MASTER BANK AGREEMENT – Defined Terms.”

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## APPENDIX H

### FORM OF CONTINUING DISCLOSURE CERTIFICATE

This Continuing Disclosure Certificate (the “Disclosure Certificate”) is executed and delivered by the State of California Department of Water Resources (the “Department”) in connection with the issuance of its Power Supply Revenue Bonds, Series 2005F and Series 2005G (collectively, the “Bonds”). The Bonds are being issued pursuant to the Trust Indenture among the Department, the Treasurer of the State of California, as Trustee, and U.S. Bank National Association, as Co-Trustee, dated as of October 1, 2002, as amended and supplemented (the “Indenture”). The Department covenants and agrees as follows:

SECTION 1. *Purpose of the Disclosure Certificate.* This Disclosure Certificate is being executed and delivered by the Department for the benefit of the Owners and Beneficial Owners of the Bonds and in order to assist the Participating Underwriters in complying with the Rule.

SECTION 2. *Definitions.* In addition to the definitions set forth in the Indenture, which apply to any capitalized term used in this Disclosure Certificate unless otherwise defined in this Section, the following capitalized terms shall have the following meanings:

“Annual Report” shall mean any Annual Report provided by the Department pursuant to, and as described in, Sections 3 and 4 of this Disclosure Certificate.

“Beneficial Owner” shall mean any person which has or shares the power, directly or indirectly, to make investment decisions concerning ownership of any Bonds (including persons holding Bonds through nominees, depositories and other intermediaries).

“Consultant’s Report” shall mean the report of Navigant Consulting, Inc., appended as Appendix A to the Official Statements for the Power Supply Revenue Bonds, Series 2002.

“Dissemination Agent,” if any, shall mean the person or firm, or any successor Dissemination Agent, designated in writing by the Department pursuant to Section 7 of this Disclosure Certificate and which has filed with the Department and the Trustee a written acceptance of such designation.

“Listed Event” shall mean any of the events listed in Section 5(a) of this Disclosure Certificate.

“National Repository” shall mean any Nationally Recognized Municipal Securities Information Repository for purposes of the Rule. The National Repositories currently approved by the Securities and Exchange Commission can be obtained at <http://www.sec.gov/info/municipal/nrmsir.htm>.

“Official Statement” shall mean the Department’s final Official Statement relating to the Bonds.

“Participating Underwriter” shall mean any of the original underwriters of the Bonds.

“Repository” shall mean each National Repository and the State Repository.

“Rule” shall mean Rule 15c2-12(b)(5) adopted by the Securities and Exchange Commission under the Securities Exchange Act of 1934, as the same may be amended from time to time.

“State” shall mean the State of California.

“State Repository,” if any, shall mean any public or private repository or entity designated by the State as the state repository for the purpose of the Rule and recognized as such by the Securities and Exchange Commission. As of the date of this Certificate, there is no State Repository.

SECTION 3. *Provision of Annual Reports.* For so long as any Bonds are Outstanding:

(a) The Department shall, or shall cause the Dissemination Agent to, not later than nine (9) months after the end of the Department's Fiscal Year (presently June 30), commencing with the report due on or before March 31, 2006, provide to each Repository an Annual Report which is consistent with the requirements of Section 4 of this Disclosure Certificate, with a copy to the Trustee. The Annual Report may be submitted as a single document or as separate documents comprising a package, and may cross-reference other information as provided in Section 4 of this Disclosure Certificate; provided that the audited financial statements of the Department may be submitted separately from the balance of the Annual Report and later than the date required above for the filing of the Annual Report if they are not available by that date. If the Department's Fiscal Year changes, it shall give notice of such change in the same manner as for a Listed Event under Section 5(b).

(b) Not later than fifteen (15) Business Days prior to the due date of each Annual Report as specified in subsection (a), the Department shall provide the Annual Report to the Dissemination Agent, if any. If the Department is unable to provide the Repositories an Annual Report by its due date, the Department shall send a notice to each Repository or the Municipal Securities Rulemaking Board and the State Repository, if any, in substantially the form attached as Exhibit A.

(c) If a Dissemination Agent is appointed by the Department, the Dissemination Agent shall:

(i) determine, prior to the due date of each Annual Report, the name and address of each National Repository and the State Repository, if any; and

(ii) file a report with the Department certifying that the Annual Report has been provided pursuant to this Disclosure Certificate, stating the date it was provided and listing all the Repositories to which it was provided.

SECTION 4. *Content of Annual Reports.* The Department's Annual Report shall contain or include by reference the following:

(a) The audited financial statements of the Department relating to its Electric Power Fund for the prior Fiscal Year, prepared in accordance with generally accepted accounting principles applicable to governmental entities, as specified from time to time by the Government Accounting Standards Board. If such audited financial statements are not available by the time the Annual Report is required to be filed pursuant to Section 3(a), the Annual Report shall contain unaudited financial statements and such audited financial statements shall be filed in the same manner as the Annual Report when they become available.

(b) Operating results and other financial data for the prior calendar year (to the extent not otherwise included in the Annual Report pursuant to this Section 4), in the categories set forth in the table under the caption "Summary of Operating Results" in the Official Statement, but only to the extent such information is or becomes historical and does not constitute projections.

(c) Financial and operating data for the prior calendar year (to the extent not otherwise included in the Annual Report pursuant to this Section 4), in the categories set forth in the table entitled "Estimated Average Power Charges and Bond Charges to the Customers" in the Consultant's Report, but only to the extent such information is or becomes historical information and does not constitute projections.

(d) The Department's residual net short costs and direct access surcharge revenues, if any, for the prior calendar year (to the extent not otherwise included in the Annual Report pursuant to this Section 4).

(e) The Department's staffing of its power supply program, specifying the number of permanent staff, number of contract employees and consulting advisors and number of employees on loan from other departments within State government, as of December 31 of the prior calendar year.

Any or all of the items listed above may be included by specific reference to other documents, including official statements relating to debt issues of the Department, which have been submitted to each of the Repositories or the Securities and Exchange Commission. If the document included by reference is a final official statement, it must be available from the Municipal Securities Rulemaking Board. The Department shall clearly identify each document so included by reference.

SECTION 5. *Reporting of Material Events.* For so long as any Bonds are Outstanding:

(a) Pursuant to the provisions of this Section 5, the Department shall give, or cause to be given, notice of the occurrence of any of the following events with respect to the Bonds, if material:

1. principal and interest payment delinquencies;
2. non-payment related defaults;
3. modifications to rights of Bondholders;
4. optional, contingent, or unscheduled bond calls;
5. defeasances;
6. rating changes;
7. adverse tax opinions or events affecting the tax-exempt status of the Bonds;
8. unscheduled draws on the debt service reserves reflecting financial difficulties;
9. unscheduled draws on the credit enhancements reflecting financial difficulties.;
10. substitution of the credit or liquidity providers or their failure to perform; and
11. release, substitution or sale of property securing repayment of the Bonds.

(b) The Department shall promptly file a notice of each occurrence of a Listed Event, if material, with the Repositories or the Municipal Securities Rulemaking Board and the State Repository, with a copy to the Trustee.

SECTION 6. *Termination of Reporting Obligation.* The Department's obligations under this Disclosure Certificate shall terminate upon the legal defeasance, prior redemption or payment in full of all of the Bonds. If such termination occurs prior to the final maturity of the Bonds, the Department shall give notice of such termination in the same manner as for a Listed Event under Section 5(b).

SECTION 7. *Dissemination Agent.* The Department may, from time to time, appoint or engage a Dissemination Agent to assist it in carrying out its obligations under this Disclosure Certificate, and may discharge any such Dissemination Agent, with or without appointing a successor Dissemination Agent. The Dissemination Agent shall not be responsible in any manner for the content of any notice or report prepared by the Department pursuant to this Disclosure Certificate. Initially, the Department will serve as its own dissemination agent.

SECTION 8. *Amendment; Waiver.* The Department may amend this Disclosure Certificate, and any provision of this Disclosure Certificate may be waived, provided that all of the following conditions are satisfied:

(a) If the amendment or waiver relates to the provisions of Sections 3(a), 4, 5(a) or (b), or 8, it may only be made in connection with a change in circumstances that arises from a change in legal requirements, change in law, or change in the identity, nature or status of an obligated person with respect to the Bonds, or the type of business conducted;

(b) The undertakings contained in this Disclosure Certificate, as amended or taking into account such waiver, would, in the opinion of nationally recognized bond counsel, have complied with the requirements of the Rule at the time of the original issuance of the Bonds, after taking into account any amendments or interpretations of the Rule, as well as any change in circumstances; and

(c) The amendment or waiver either (i) is approved by the Owners of the Bonds in the same manner as provided in the Indenture for amendments to the Indenture with the consent of Owners, or (ii) does not, in the opinion of the Trustee or nationally recognized bond counsel, materially impair the interests of the Owners or Beneficial Owners of the Bonds. The Department also may amend this Disclosure Certificate without approval by the Owners of the Bonds to the extent permitted by rule, order or other official pronouncement of the Securities and Exchange Commission.

In the event of any amendment or waiver of a provision of this Disclosure Certificate, the Department shall describe such amendment in the next Annual Report, and shall include, as applicable, a narrative explanation of the reason for the amendment or waiver and its impact on the type (or in the case of a change of accounting principles, on the presentation) of financial information or operating data being presented by the Department. In addition, if the amendment relates to the accounting principles to be followed in preparing financial statements, (i) notice of such change shall be given in the same manner as for a Listed Event under Section 5(b), and (ii) the Annual Report for the year in which the change is made should present a comparison (in narrative form and also, if feasible, in quantitative form) between the financial statements as prepared on the basis of the new accounting principles and those prepared on the basis of the former accounting principles.

SECTION 9. *Additional Information.* Nothing in this Disclosure Certificate shall be deemed to prevent the Department from disseminating any other information, using the means of dissemination set forth in this Disclosure Certificate or any other means of communication, or including any other information in any Annual Report or notice of occurrence of a Listed Event, in addition to that which is required by this Disclosure Certificate. If the Department chooses to include any information in any Annual Report or notice of occurrence of a Listed Event in addition to that which is specifically required by this Disclosure Certificate, the Department shall have no obligation under this Certificate to update such information or include it any future Annual Report or notice of occurrence of a Listed Event.

SECTION 10. *Default.* In the event of a failure of the Department to comply with any provision of this Disclosure Certificate, the Trustee may (and, at the request of the Owners of at least 50% in aggregate principal amount of Outstanding Bonds, shall), or any Owner or Beneficial Owner of the Bonds may (unless the Department has so complied within 20 days after written notice from the Trustee, such Owner or Owners, or such Beneficial Owner or Beneficial Owners, as the case may be, of the Department's failure to comply) seek specific performance by court order, to cause the Department to comply with its obligations under this Disclosure Certificate, as the sole remedy. A default under this Disclosure Certificate shall not be deemed a default or an Event of Default under the Indenture.

SECTION 11. *Duties, Immunities and Liabilities of Dissemination Agent.* The Dissemination Agent shall have only such duties as are specifically set forth in this Disclosure Certificate, and the Department agrees to indemnify and save the Dissemination Agent, its officers, directors, employees and agents, harmless against any loss, reasonable expense and liabilities which it may incur arising out of or in the exercise or performance of its powers and duties hereunder, including the reasonable costs and expenses (including reasonable attorneys fees) of

defending against any claim of liability, but excluding liabilities due to the Dissemination Agent's default or negligence or willful misconduct. The obligations of the Department under this Section shall survive resignation or removal of the Dissemination Agent and termination of this Disclosure Certificate.

SECTION 12. *Beneficiaries.* This Disclosure Certificate shall inure solely to the benefit of the Owners and Beneficial Owners from time to time of the Bonds, and shall create no rights in any other person or entity.

Date:

DEPARTMENT OF WATER RESOURCES

By: \_\_\_\_\_  
Name:  
Title:

**EXHIBIT A**

**Notice to Repositories of Failure to File Annual Report**

Name of Issuer: State of California Department of Water Resources  
Name of Bond Issue: Department of Water Resources Power Supply Revenue Bonds,  
Series 2005F and Series 2005G  
Date of Issuance: December 1, 2005

NOTICE IS HEREBY GIVEN that the Department has not provided an Annual Report with respect to the above-named Bonds as required by Section 3 of the Continuing Disclosure Certificate dated December 1, 2005 of the Department. The Department anticipates that the Annual Report will be filed by \_\_\_\_\_.

Dated: \_\_\_\_\_

STATE OF CALIFORNIA  
DEPARTMENT OF WATER RESOURCES

By: \_\_\_\_\_

cc: Trustee  
Co-Trustee

## APPENDIX I

### INFORMATION CONCERNING INITIAL LETTER OF CREDIT PROVIDERS AND INITIAL LIQUIDITY FACILITY PROVIDERS

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## **BANK OF AMERICA**

Bank of America, N.A. (the “Bank”) is a national banking association organized under the laws of the United States, with its principal executive offices located in Charlotte, North Carolina. The Bank is a wholly-owned indirect subsidiary of Bank of America Corporation (the “Corporation”) and is engaged in a general consumer banking, commercial banking and trust business, offering a wide range of commercial, corporate, international, financial market, retail and fiduciary banking services. As of June 30, 2005, the Bank had consolidated assets of \$1,048 billion, consolidated deposits of \$685 billion and stockholder’s equity of \$102 billion based on regulatory accounting principles.

The Corporation is a bank holding company and a financial holding company, with its principal executive offices located in Charlotte, North Carolina. Additional information regarding the Corporation is set forth in its Annual Report on Form 10-K for the fiscal year ended December 31, 2004, together with any subsequent documents it filed with the Securities and Exchange Commission (the “Commission”) pursuant to the Securities Exchange Act of 1934, as amended (the “Exchange Act”).

Recent Developments: On April 1, 2004, the Corporation completed its merger with FleetBoston Financial Corporation, and, on June 13, 2005, the Bank completed its merger with Fleet National Bank. On June 30, 2005, the Corporation announced its intention to acquire MBNA Corporation.

Additional information regarding the foregoing is available from the filings made by the Corporation with the SEC, which filings can be inspected and copied at the public reference facilities maintained by the SEC at 100 F Street, N.E., Washington, D.C. 20549, United States, at prescribed rates. In addition, the SEC maintains a website at <http://www.sec.gov>, which contains reports, proxy statements and other information regarding registrants that file such information electronically with the SEC.

The information concerning the Corporation, the Bank and the foregoing mergers contained herein is furnished solely to provide limited introductory information and does not purport to be comprehensive. Such information is qualified in its entirety by the detailed information appearing in the documents and financial statements referenced herein.

The Letter of Credit has been issued by the Bank. Moody’s Investors Service, Inc. (“Moody’s”) currently rates the Bank’s long-term debt as “Aa1” and short-term debt as “P-1.” Standard & Poor’s rates the Bank’s long-term debt as “AA” and its short-term debt as “A-1+.” Fitch Ratings, Inc. (“Fitch”) rates long-term debt of the Bank as “AA-” and short-term debt as “F1+.” Further information with respect to such ratings may be obtained from Moody’s, Standard & Poor’s and Fitch, respectively. No assurances can be given that the current ratings of the Bank’s instruments will be maintained.

The Bank will provide copies of the most recent Bank of America Corporation Annual Report on Form

10-K, any subsequent reports on Form 10-Q, and any required reports on Form 8-K (in each case as filed with the Commission pursuant to the Exchange Act), and the publicly available portions of the most recent quarterly Call Report of the Bank delivered to the Comptroller of the Currency, without charge, to each person to whom this document is delivered, on the written request of such person. Written requests should be directed to:

Bank of America Corporate Communications  
100 North Tryon Street, 18th Floor  
Charlotte, North Carolina 28255  
Attention: Corporate Communications

PAYMENTS OF PRINCIPAL AND INTEREST ON THE BONDS WILL BE MADE FROM DRAWINGS UNDER THE LETTER OF CREDIT. PAYMENTS OF THE PURCHASE PRICE OF THE BONDS WILL BE MADE FROM DRAWINGS UNDER THE LETTER OF CREDIT IF REMARKETING PROCEEDS ARE NOT AVAILABLE. ALTHOUGH THE LETTER OF CREDIT IS A BINDING OBLIGATION OF THE BANK, THE BONDS ARE NOT DEPOSITS OR OBLIGATIONS OF THE CORPORATION OR ANY OF ITS AFFILIATED BANKS AND ARE NOT GUARANTEED BY ANY OF THESE ENTITIES. THE BONDS ARE NOT INSURED BY THE FEDERAL DEPOSIT INSURANCE CORPORATION OR ANY OTHER

GOVERNMENTAL AGENCY AND ARE SUBJECT TO CERTAIN INVESTMENT RISKS, INCLUDING POSSIBLE LOSS OF THE PRINCIPAL AMOUNT INVESTED.

The delivery hereof shall not create any implication that there has been no change in the affairs of the Corporation or the Bank since the date hereof, or that the information contained or referred to in this Appendix C is correct as of any time subsequent to its date.

## **THE BANK OF NEW YORK**

The Bank of New York (the “Bank”) is the principal subsidiary of The Bank of New York Company, Inc. (NYSE: BK), a financial holding company (the “Company”). The Company provides a complete range of banking and other financial services to corporations and individuals worldwide through its basic businesses, namely, Securities Servicing and Global Payment Services, Private Client Services and Asset Management, Corporate Banking, Global Market Services, and Retail Banking.

The Bank of New York was founded in 1784 by Alexander Hamilton and is the nation’s oldest bank. The Bank is a state chartered New York banking corporation and a member of the Federal Reserve System. Its business is subject to examination and regulation by federal and state banking authorities.

The Bank has long-term senior debt ratings of “AA-”/”Aa2” and short-term ratings of “A-1+/P1” from Standard & Poor’s Ratings Services and Moody’s Investors Service, Inc., respectively.

The Bank of New York’s principal office is located at One Wall Street, New York, New York 10286. A copy of the most recent annual report and 10-K of the Company may be obtained from the Bank’s Public Relations Department, One Wall Street, 31st Floor, (212) 635-1569.

## BAYERISCHE LANDESBANK

The Bank has nominal capital of € 1,800 million, of which € 1,692.5 million is paid up. The Bank is wholly owned by a holding company, BayernLB Holding AG, a stock corporation (Aktiengesellschaft), of which each of the Free State of Bavaria (“Bavaria”) and the Association of Bavarian Savings Banks (Sparkassenverband Bayern), the central organisation of the Bavarian Savings Banks (the “Association”), owns 50% of the outstanding shares. In anticipation of the loss of State Guarantee Mechanisms, BayernLB Holding AG has been entrusted under public law with the holding of the Bank as a public law institution (beliehener Anstaltsträger). Bavaria and the Association have announced that they will each retain at least 25.01% of the shares of BayernLB Holding AG, if additional shareholders are added later. This structure enables third parties to acquire indirect minority interests in the Bank without changing the legal character of the Bank as a public law institution.

The Bank was established by statute in 1972 as the state bank of Bavaria and as the central institution for Bavarian municipalities and local public authorities and the Savings Banks. It also supports the Bavarian savings banks organized under public law (Bayerische Sparkassen, the “Savings Banks”) in the fulfillment of their public mandates.

The Bank provides its commercial and investment banking services to domestic and international customers, including other banks, governments, corporations, other organizations and individuals. As part of its public duties, the Bank also finances public and private development projects, administers public funds for federal and state subsidized credit programs and performs certain treasury functions for Bavaria.

To fund its business activities, the Bank raises money in the capital and money markets, borrows from banks and other lenders and uses its retained earnings and reserves. In 2004, the Bank raised € 53.5 billion through the issuance of bonds and notes and through debt certificate borrowings.

The Bank is one of the larger banks in Germany in terms of total consolidated assets. The following table shows the Bank’s unconsolidated and the Group’s consolidated total assets and equity capital at December 31 of each of the years indicated and net income for each of the years indicated:

	<u>Bank</u>			<u>Group</u>		
	Year ended Dec. 31 <u>2004</u>	Year ended Dec. 31 <u>2003</u>	Change <u>In %</u>	Year ended Dec. 31 <u>2004</u>	Year ended Dec. 31 <u>2003</u>	Change <u>In %</u>
	(€ in millions)			(€ in millions)		
Total asset	285,583	272,772	4.70	333,102	313,431	(6.28)
Equity Capital <sup>(1)</sup>	15,631	16,088	(2.85)	16,671	17,177	(2.95)
Net Income	63	63	0.00	98	79	24.05

<sup>(1)</sup> Including subordinated debt and non-subordinated accrued interest expense thereon.

### **The New York Branch**

Since October 1, 1981, the Bank’s New York branch (the “Branch”) has been licensed by the Comptroller of the currency (the “Comptroller”) pursuant to the International Banking Act of 1978, as amended. The Branch conducts an extensive banking business providing services to subsidiaries of large German corporations in North America and to United States and international companies. As of December 31, 2004, the assets of the Branch, together with the Bank’s Grand Cayman branch and the New York International Banking Facility, amounted to approximately U. S. \$ 29.4 billion.

## CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM (CALPERS)

The following information concerning CalPERS has been provided by representatives of CalPERS and has not been independently confirmed or verified by any other party. No representation is made herein as to the accuracy or adequacy of such information or as to the absence of material adverse changes in such information subsequent to the date hereof, or that the information given below or incorporated herein by reference is correct as of any time subsequent to its date.

California Public Employees' Retirement System ("CalPERS" or the "System"), a unit of the California State and Consumer Services Agency, provides retirement and health benefits to more than 1.4 million public employees, retirees, and their families, based on employment services provided to more than 2,500 cities, counties, districts, and other local authorities or public bodies of or within the State of California. CalPERS is created pursuant to, and governed by the provisions of, Title 2, Division 5, Parts 3 through 8, of the Government Code, section 20000 et seq. (the "Public Employees' Retirement Law").

California Constitution Article XVI, Section 17 (the "Constitutional Provision") grants to the CalPERS Board plenary authority and financial responsibility for the investment of System assets. These assets are held in trust under the Constitutional Provision, to be used for the exclusive purposes of providing benefits to System members and their beneficiaries and defraying reasonable expenses of administering the System. Under paragraph (c) of the Constitutional Provision, the Board may make investments consistent with the trust imposed upon it, with the further obligation to diversify the investments so as to minimize the risk of loss and maximize the rate of return and to act with the care, skill, prudence and diligence "under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with these matters would use in the conduct of an enterprise of a like character and with like aims." The sole additional limit on the Board's investment authority is that it will not invest in instruments prohibited by the legislature as being violative of the public interest. California Government Code (the "Government Code") section 7514.3 provides express statutory authority for CalPERS to establish a credit enhancement program to assist entities of state and local government and other issuers of municipal and public finance debt to secure more favorable financing terms through a variety of types of credit enhancement including, but not limited to, enhancement of the credit of bonds, notes, and other indebtedness.

The standards set forth in the Constitutional Provision are further defined in several provisions of the Government Code. For example, the same "prudent person" standard is restated in Section 20151(c) of the Government Code. In Section 20190, the Government Code recognizes the Board as possessing the "exclusive control" for investment of the retirement fund, again authorizing the Board, in its discretion, to "invest the assets of the fund through the purchase, holding or sale . . . [of] any investment, financial instrument, or financial transaction [that] is prudent in the informed opinion of the board."

Under Section 20191 of the Government Code, the Board may further specify guidelines "by which to designate those securities and real property that are acceptable for purchase" through the adoption of investment resolutions. The Board may delegate its investment authority to its executive officer, who may further delegate to his or her subordinates, unless the Board has reserved authority to the executive officer to act personally (Section 20099 of the Government Code).

Financial data for June 30, 2004 are taken from the audited financial statements presented in CalPERS' Comprehensive Annual Financial Report ("Annual Report") for the fiscal year ended June 30, 2004. As of June 30, 2004, the Fund had net assets held in trust for pension benefits with a market value of approximately \$167.6 billion, compared to approximately \$144.8 billion as of June 30, 2003. As of April 30th, 2005, net assets had a total market value of approximately \$182.8 billion (unaudited).

CalPERS is independently rated "Aaa/P-1" by Moody's Investors Service and "AAA/F1+" by Fitch Ratings.

CalPERS will provide without charge, upon request, a copy of the 2004 Annual Report containing its financial statements for the years ended June 30, 2004 and 2003. Requests to CalPERS for the Annual Report should be directed by mail or phone to 400 P Street Suite 3492, Sacramento, CA 95814, Attention: Investment

Operations / Credit Enhancement Program, telephone (916) 795-4029. The most recent Annual Report and other information regarding CalPERS can be viewed at <http://www.calpers.ca.gov>

*The foregoing information has been provided by CalPERS and is not intended to serve as a representation, warranty, or contract modification of any kind.*

## CALYON

The following information relates to and has been obtained from Calyon. The delivery of this information shall not create any implication that there has been no change in the affairs of Calyon since the date hereof, or that the information contained or referred to below is correct as of any time subsequent to its date.

Calyon is 95.2% owned by Crédit Agricole S.A. The Crédit Agricole Group is one of the largest banking organizations in Europe, with total assets of €875 billion as of December 31, 2003. Crédit Agricole Group's shareholders' equity group share totaled €38.6 billion at December 31, 2003. With 20 million individual customers, the Crédit Agricole Group is the leading retail bank in France, drawing on the depth of the network of its Crédit Agricole Regional Banks and the Crédit Lyonnais retail network.

Calyon is the new name, as of April 30, 2004, of Crédit Agricole Indosuez, the international wholesale banking and capital markets arm of the Crédit Agricole Group, following the consolidation and transfer described below. Calyon is a limited liability company incorporated in France as a "société anonyme" and established under the laws of France. Calyon's registered office is located at 9, quai du Président Paul Doumer, 92920 Paris La Défense Cedex, France. Crédit Agricole Indosuez was formed by the merger on 30th September, 1975 of two French banks, Banque de l'Indochine and Banque de Suez et de l'Union des Mines, to form Banque Indosuez and, after its acquisition in 1996 by Caisse Nationale de Crédit Agricole ("CNCA", renamed Crédit Agricole S.A. in November 2001), by the merger in 1997 of Banque Indosuez with Unicredit, the French corporate banking specialized subsidiary of CNCA and by the contribution of CNCA's international markets, corporate and trade finance activities to Banque Indosuez, then renamed Crédit Agricole Indosuez. In 1999, the Bank's private banking activity was reinforced by the contribution of CNCA's specialized subsidiaries (Banque de Gestion Privée in France and Banque du Crédit Agricole Suisse SA). Finally, in 2000, and then 2001, Crédit Agricole Indosuez took full control of CPR, a French specialized bank (notably in asset management, structured products and on-line brokerage activities, as well as trading in hybrid products).

The transfer of Crédit Lyonnais' corporate and investment banking business to Crédit Agricole Indosuez occurred by way of a partial contribution of assets (Apport Partiel d'Actif) in accordance with Articles L 236-1 et seq. of the French Commercial Code (Code de Commerce). The transfer and the change of name were approved by extraordinary general meetings of shareholders of both Crédit Lyonnais and Crédit Agricole Indosuez held on April 30, 2004 (the "Effective Date"). The transfer operated by way of universal succession whereby, with effect from the Effective Date, all rights and obligations of Crédit Lyonnais related to its corporate and investment banking business became rights and obligations of Crédit Agricole Indosuez and was back valued to January 1, 2004 for accounting and tax purposes. It should be noted that Calyon is not a new legal entity but a continuation of Crédit Agricole Indosuez under a new name, effective from the moment Crédit Agricole Indosuez received the partial contribution of assets from Crédit Lyonnais.

As a French limited liability corporation, Calyon is subject to Articles L.225 1 et seq. and Book 2 of the Code de Commerce and as a financial institution, Calyon is subject to Articles L.511 1 et seq. and L.531 1 et seq. of the French Monetary and Financial Code (Code monétaire et financier). Calyon is included in the list of credit institutions under the category of commercial banks and it is, therefore, subject to the control of bank supervisory authorities and of the Banking Commission in particular. As a nearly wholly owned subsidiary of Crédit Agricole, its shares are not admitted to trading on a regulated market for dealing in financial instruments. Calyon carries short-term debt ratings of A-1+/P-1/F1+ and long-term senior unsecured debt ratings of AA-/Aa2/AA (by Standard & Poor's Ratings Group, Moody's and Fitch Ratings, respectively). All these ratings are stable.

The first unaudited consolidated financial statements of Calyon based on its new consolidated business scope are as of June 30, 2004. They show a total balance sheet of € 320 billion, total equity of € 9,883 million (€ 8,997 million excluding minority interests) and total net income of € 371million (€ 349 million excluding minority interests). The international solvency ratio was 9.2 % as of June 30, 2004, with a Tier 1 ratio of 9.0%. The Calyon Financial Report for the first six months of 2004 includes the aforementioned unaudited consolidated financial statements and details the accounting rules and policies in accordance with which they were prepared, as well as the underlying consolidation scope. This report may be obtained from Calyon, Finance Department, attn. V. Souchier, 9 quai du Président Paul Doumer, 92920 Paris La Défense Cedex.

## CITIBANK, N.A.

Citibank, N.A. (“Citibank”) was originally organized on June 16, 1812, and now is a national banking association organized under the National Bank Act of 1864. Citibank is an indirect wholly-owned subsidiary of Citigroup Inc. (“Citigroup”), a Delaware holding company. As of June 30, 2005, the total assets of Citibank and its consolidated subsidiaries represented approximately 46% of the total assets of Citigroup and its consolidated subsidiaries.

The long-term ratings of Citibank and its consolidated subsidiaries are Aa1, AA and AA+ by Moody’s, S&P and Fitch, respectively. The short-term ratings of Citibank and its consolidated subsidiaries are P-1, A-1+ and F1+ by Moody’s, S&P and Fitch, respectively.

Citibank is a commercial bank that, along with its subsidiaries and affiliates, offers a wide range of banking and trust services to its customers throughout the United States and the world. As a national bank, Citibank is a regulated entity permitted to engage only in banking and activities incidental to banking. Citibank is primarily regulated by the Office of the Comptroller of the Currency (the “Comptroller”), which also examines its loan portfolios and reviews the sufficiency of its allowance for credit losses.

Citibank’s deposits at its U.S. branches are insured by the Federal Deposit Insurance Corporation (the “FDIC”) and are subject to FDIC insurance assessments. The Letter of Credit is not insured by the FDIC or any other regulatory agency of the United States or any other jurisdiction. Citibank may, under certain circumstances, be obligated for the liabilities of its affiliates that are FDIC-insured depository institutions.

Legislation enacted as part of the Omnibus Budget Reconciliation Act of 1993 provides that deposits in U.S. offices and certain claims for administrative expenses and employee compensation against a U.S. insured depository institution which has failed will be afforded a priority over other general unsecured claims, including deposits in non-U.S. offices and claims under non-depository contracts in all offices, against such an institution in the “liquidation or other resolution” of such an institution by any receiver. Such priority creditors (including the FDIC, as the subrogee of insured depositors) of such FDIC-insured depository institution will be entitled to priority over unsecured creditors in the event of a “liquidation or other resolution” of such institution.

For further information regarding Citibank, reference is made to the Annual Report on Form 10-K of Citicorp and its subsidiaries for the year ended December 31, 2004 and to and to Form 10-Q for the quarter ended June 30, 2005 filed by Citicorp with the Securities and Exchange Commission (“SEC”). Further information regarding Citibank subsequent to June 30, 2005 will be included in the Form 10-Q’s (quarterly) and Form 10-K’s (annually) subsequently filed by Citigroup with the SEC. Copies of such material may be obtained, upon payment of a duplicating fee, by writing to the SEC at 450 Fifth Street, N.W., Washington, D.C. 20549. In addition, such reports are available at the SEC’s web site (<http://www.sec.gov>).

In addition, Citibank submits quarterly to the Comptroller certain reports called “Consolidated Reports of Condition and Income for a Bank With Domestic and Foreign Offices” (“Call Reports”). The Call Reports, which include income statement and balance sheet information, are on file with and publicly available at the Comptroller’s offices at 250 E Street, S.W., Washington, D.C. 20219 and are also available on the web site of the FDIC (<http://www.fdic.gov>).

Any of the reports referenced above are available upon request, without charge, by writing or calling Citigroup Document Services, 140 58th Street, Brooklyn, New York 11220, (718) 765-6514.

The information contained in this disclosure relates to and has been obtained from Citibank. The information concerning Citibank contained herein is furnished solely to provide limited introductory information regarding Citibank and does not purport to be comprehensive. Such information is qualified in its entirety by the detailed information appearing in the documents and financial statements referenced above.

## DEPFA BANK PLC

The following information has been provided by the Bank (at times referred to hereinafter as “DEPFA”) for use in this Official Statement. Such information is not guaranteed as to accuracy or completeness by, and is not to be construed as a representation by, DWR, its consultants, the underwriters or any remarketing agent. This information has not been independently verified by DWR, its consultants, the underwriters or any remarketing agent. No representation is made by DWR, its consultants, the underwriters or any remarketing agent as to the accuracy or adequacy of such information or as to the absence of material adverse changes in such information subsequent to the date hereof.

DEPFA BANK plc (“DEPFA”) is the parent company of the DEPFA BANK plc group of companies comprising DEPFA and its consolidated subsidiaries (the “Group”). DEPFA will act through its New York Branch, which is licensed by the Banking Department of the State of New York as an unincorporated branch of DEPFA BANK plc, Dublin. DEPFA is based in Dublin and has a banking license issued under the Irish Central Bank Act, 1971 (as amended) and is supervised by the Financial Regulator. It is registered in the Irish Companies Registration Office with company number 348819 and its shares are listed on the Frankfurt Stock Exchange. DEPFA has a network of subsidiaries, branches and offices across many European countries, as well as in North America and Asia.

The Group provides a broad range of products and services to public sector entities, from governmental budget financing and financing of infrastructure projects to placing of public sector assets and investment banking and other advisory services. The Group has direct client contacts with many state entities and focuses on those public sector entities involved in large volume business. The Group advises individual public sector borrowers on their international capital market transactions and preparations for the ratings process.

As of December 31, 2004, DEPFA had total consolidated assets of Euro 190.4 billion, shareholders’ equity of Euro 1.9 billion and consolidated net income of Euro 540 million, determined in accordance with the United States generally accepted accounting principles (US GAAP). DEPFA maintains its records and prepares its financial statements in Euro. At December 31, 2004, the exchange rate was 1.0000 Euro equals 1.3621 United States dollars. Such exchange rate fluctuates from time to time.

DEPFA is rated “Aa3” long-term and “P-1” short-term by Moody’s, “AA-” long-term and “A-1+” short-term by S&P, and “AA-” long-term and “F1+” short-term by Fitch. Currently, the long-term ratings of DEPFA BANK plc and related entities are on negative outlook at Moody’s, although DEPFA’s short-term ratings have not been affected.

DEPFA will provide without charge a copy of its most recent publicly available annual report. Written requests should be directed to: DEPFA BANK plc, New York Branch, 623 Fifth Avenue, 22nd Floor, New York, New York 10022, Attention: General Manager. The delivery of this information shall not create any implication that the information contained or referred to herein is correct as of any time subsequent to its date. In addition, updated financial information may be found from the DEPFA website at: [www.depfa.com](http://www.depfa.com).

## **FORTIS BANK**

Fortis Bank S.A./N.V. (“Fortis Bank”) conducts the banking activities of Fortis, an international financial services provider active in the fields of banking, insurance and investment.

Fortis Bank is a wholly-owned indirect subsidiary of Fortis SA/NV and Fortis N.V., whose principal offices are located in Brussels (Belgium) and Utrecht (the Netherlands) respectively.

Fortis Bank is a commercial bank offering a full range of banking and insurance products and services to a wide range of customers. In its home market, the Benelux countries, Fortis Bank occupies a leading position. Fortis is the largest bank in Belgium, the second-largest in Luxembourg, and the fourth-largest in the Netherlands. The bank had full-time staff of over 36,000 in 2004. Outside its home market, Fortis Bank concentrates on selected market segments. Its business is subject to examination and regulation by the Belgian Banking and Finance Commission.

As of December 31, 2004 Fortis Bank had total assets of EUR 484.2 billion.

Fortis Bank’s Connecticut branch (the “Connecticut Branch”) has been licensed by the Connecticut Department of Banking (the “Banking Department”) to conduct a wholesale banking business since October 9, 2002. The Connecticut Branch is subject to examination by the Banking Department and the Federal Reserve Bank of New York. In addition, the Connecticut Branch is required to file periodic and other reports containing financial information with the Banking Department and the Federal Reserve Bank of New York.

Additional information, including the Fortis Annual Report for 2004, may be obtained without charge by each person to whom this Official Statement is delivered upon the written request of any such person to Fortis Bank, 301 Tresser Boulevard, Stamford, Connecticut, 06301. This information is also available at [www.Fortis.com](http://www.Fortis.com).

The financial statements appearing in the Fortis Annual Report for 2004 were prepared in accordance with Belgian accounting standards, which differ from generally accepted accounting principles in use in the United States.

The information in this Appendix has been obtained from Fortis Bank, which is solely responsible for its content. The delivery of the Official Statement shall not create any implication that there has been no change in the affairs of Fortis Bank since the date hereof, or that the information contained or referred to in this Appendix is correct as of any time subsequent to its date.

## **JPMORGAN CHASE BANK, NATIONAL ASSOCIATION**

JPMorgan Chase Bank, National Association (“JPMCB”) is a wholly owned bank subsidiary of JPMorgan Chase & Co. (“JPMorgan Chase”), a Delaware corporation whose principal office is located in New York, New York. JPMCB is a commercial bank offering a wide range of banking services to its customers, both domestically and internationally. It is chartered and its business is subject to examination and regulation by the Office of the Comptroller of the Currency.

As of September 30, 2005, JPMorgan Chase Bank, National Association, had total assets of \$1,008.4 billion, total net loans of \$386.9 billion, total deposits of \$529.4 billion, and total stockholder’s equity of \$85.1 billion. These figures are extracted from JPMCB’s unaudited Consolidated Reports of Condition and Income as at September 30, 2005, which are filed with the Federal Deposit Insurance Corporation.

Additional information, including the most recent Form 10-K for the year ended December 31, 2004, of JPMorgan Chase & Co., the 2004 Annual Report of JPMorgan Chase & Co. and additional annual, quarterly and current reports filed or furnished with the Securities and Exchange Commission by JPMorgan Chase & Co., as they become available, may be obtained without charge by each person to whom this Official Statement is delivered upon the written request of any such person to the Office of the Secretary, JPMorgan Chase & Co., 270 Park Avenue, New York, New York 10017.

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The information contained in this Appendix relates to and has been obtained from JPMCB. The delivery of the Official Statement shall not create any implication that there has been no change in the affairs of JPMCB since the date hereof, or that the information contained or referred to in this Appendix is correct as of any time subsequent to its date.

## KBC BANK N.V.

KBC Bank N.V., New York Branch (“KBC NYB”) is an unincorporated branch of KBC Bank N.V., a naamloze vennootschap (public company of limited liability) organized under the laws of Belgium, whose principal office is located in Brussels, Belgium. KBC Bank N.V. conducts operations through additional offices and agencies in the United States and around the world. Created on June 4, 1998 through the combination of two predecessor Belgian banks, Kredietbank N.V. and CERA Bank C.V., KBC Bank N.V. is subject to regulation by the Belgium Banking Commission and to Belgian banking and accounting law. KBC Bank N.V. maintains its records and prepares its financial statements in accordance with accounting principles generally accepted in Belgium. Such records and financial statements are maintained and prepared in Euro currency (EUR).

One of the largest commercial banks in Belgium, KBC Bank N.V. operates as a universal bank, engaged in commercial and investment banking, and offers comprehensive financial services. In contrast with the two other major Belgian banks, KBC Bank N.V.’s branches in Belgium are located exclusively in Flanders and Brussels. KBC Bank N.V. is indirectly represented through CBC Banque S.A., a majority-owned subsidiary with branches in the Walloon region and Brussels.

KBC NYB was originally established in 1977 as a New York Branch of Kredietbank N.V., and has been relicensed by the Banking Department of the State of New York as a New York Branch of KBC Bank N.V. to provide a full range of services in New York. In addition to handling foreign exchange transactions, KBC NYB is active in international payment transactions and the clearing of commercial payments and professional transactions in U.S. Dollars. KBC NYB is also involved in providing financial services, particularly credit, for European (including Belgian) companies operating in the United States, as well as for United States corporations.

### Selected Consolidated Financial Data of KBC Bank N.V.

Year Ended  
December 31, 2004  
(EUR Millions)

Total Assets	EUR	249,234
Amounts Owed to Customers		148,735
Loans and Advances to Customers		106,499
Capital and Reserves		10,519
Net Income		1,758

Conversion Rate: As of December 31, 2004, EUR 0.734 = US\$1.00

KBC NYB will provide, upon written request and without charge, a copy of KBC Bank N.V.’s Annual Report for the year ended December 31, 2004. Written requests should be directed to: KBC Bank N.V., New York Branch, 125 West 55th Street, 10th Floor, New York, New York 10019, Attention: Controller.

The delivery of this Official Statement shall not create any implication that there has been no change in the affairs of KBC Bank N.V. since December 31, 2004 or that information contained or referred to in this Exhibit K is current as of any time subsequent to such date.

## **LANDESBANK BADEN-WÜRTTEMBERG**

LBBW is a public law institution (rechtsfähige Anstalt des öffentlichen Rechts) owned and controlled jointly by the State of Baden-Württemberg, the Savings Bank Association of Baden-Württemberg (the Association of Baden-Württemberg), the City of Stuttgart, the Savings Bank and Giro Association of Rhineland-Palatinate (SGV-RP), and Landeskreditbank Baden-Württemberg (L-Bank). Baden-Württemberg holds 35.611% of LBBW's nominal capital, the Association of Baden-Württemberg holds 35.611%, Stuttgart holds 18.932%, the SGV RP holds 4.923% and L-Bank holds 4.923%. With a balance sheet total of approximately € 340 billion at December 31, 2004, the LBBW Group is among the ten largest German banks and among the 50 largest credit institutions in the world.

The LBBW Act (Gesetz über die Landesbank Baden-Württemberg; the "LBBW Act") authorizes LBBW to engage in all types of banking and financial service activities as well as in all other activities that are useful to LBBW, including issuing mortgage Pfandbriefe (Hypothekendarlehen), public sector Pfandbriefe (Öffentliche Pfandbriefe or Kommunalobligationen), and other debt obligations. In addition, LBBW is the central bank for the savings banks (Sparkassen) in the State of Baden-Württemberg. Furthermore, LBBW and its 100 per cent subsidiary Landesbank Rheinland-Pfalz act together as the central bank for the savings banks in Rheinland-Pfalz. In this regard, LBBW conducts its activities with due consideration of the interests of these savings banks. Furthermore, LBBW also performs the activities of a savings bank through its brand "BW-Bank" in the territory of Stuttgart.

As a German "universal bank," LBBW provides a comprehensive range of commercial banking and investment banking services to businesses, other banking institutions, governmental entities, counties, municipalities, other organizations and individuals. LBBW makes loans, extends guaranties, underwrites securities, deals and trades in debt and equity securities and makes equity investments. LBBW underwrites, trades in, and acts as paying agent and fiscal agent with respect to debt securities issued by the State of Baden-Württemberg.

### **Landesbank Baden-Württemberg, New York Branch**

The New York Branch of LBBW was licensed by the Banking Department of New York State in December 1998, and amended its license in April 1999 to reflect the merger that created LBBW. The Branch is not required to be and is not a member of the Federal Deposit Insurance Corporation (the "FDIC"). The Branch is engaged in numerous business activities such as extending credit and providing banking services to the middle market clientele of Baden-Württemberg and their North American subsidiaries, as well as to international corporations. The Branch is also involved in the financing of commercial real estate in select U.S. cities and in public finance with U.S. municipal entities. The Branch also engages in capital markets and asset management activities, which include the management of an investment portfolio consisting entirely of investment-grade notes, including floating- and fixed-rate asset-backed securities, collateralized obligations, and senior debt medium-term notes issued by higher quality banks, finance companies, and other corporate issuers. The Branch funds itself with corporate, bank and government entity deposits, and the issuance of certificates of deposit, medium-term notes and other obligations. The Branch is active in both the inter-bank and corporate markets.

### **Phase-out of Guaranty Obligation and Maintenance Obligation**

In 2001 and 2002, the European Commission, the Federal Republic of Germany and the German federal states (including Baden-Württemberg) reached agreements to make the Guaranty Obligation (Gewährträgerhaftung) and Maintenance Obligation (Anstaltslast) of the owners of German Landesbanken compatible with the state aid provisions of the Treaty Establishing the European Community, as amended by the Treaty on European Union. Under these agreements, Germany and its federal states began to phase out the Guaranty and Maintenance Obligations. On July 18, 2005, this phase-out was completed. Obligations of LBBW incurred after that date are no longer backed by the Guaranty Obligation or Maintenance Obligation of its owners. Furthermore, LBBW became capable of being subject to insolvency proceedings after 18 July 2005.

## LANDESBANK HESSEN-THÜRINGEN GIROZENTRALE, NEW YORK BRANCH

The co-provider of the Initial Liquidity Facility for the Series 2005G-14 Bonds is the New York Branch of Landesbank Hessen-Thüringen Girozentrale (“Helaba”). Helaba took its present name on July 1, 1992 upon the effectiveness of the Treaty on the Formation of a Joint Savings Banks Organization (the “State Treaty”) between the federal states of Hesse and Thuringia. The former Hessische Landesbank was formed in 1953 by the merger of Hessische Landesbank Darmstadt (founded 1940), Nassauische Landesbank Wiesbaden (founded 1840) and Landeskreditkasse zu Kassel (founded 1832).

Helaba is a legal entity under public law. The owners and guarantors of Helaba are the states of Hesse and Thuringia and the Savings Banks and Giro Association Hesse-Thuringia (Sparkassen- und Giroverband Hessen-Thüringen- SGVHT) (the “Association”), a joint institution of the municipal savings banks and their guarantors in Hesse and Thuringia. Helaba, like other banking institutions in Germany, is subject to governmental supervision and regulation by the Federal Financial Services Supervisory Authority, an independent authority with regulatory powers, with the assistance of the Deutsche Bundesbank under the German Banking Act of July 10, 1961, as amended. State supervision of Helaba and the Association is exercised by the Thuringian Ministry of Finance and the Hessian Ministry for Economics. Executive bodies of Helaba are the Board of Guarantors, the Supervisory Board and the Board of Managing Directors.

In accordance with its Charter, Helaba acts as a central bank for the savings banks and the Association, and acts as a state bank for the states of Hesse and Thuringia. Helaba pays an annual dividend to its owners and, in the case of the savings banks, cooperates with them to develop their businesses. The savings banks are at the same time customers, owners and partners of Helaba, and therefore are of particular importance. At the end of 2003 Helaba and the Association, Helaba’s 85 per cent owner, created the S-Verbund. The S-Verbund provides a framework for a single economic group that combines the retail strength of its member savings banks with Helaba’s wholesale expertise.

Headquartered in Frankfurt/Main and Erfurt, Helaba concentrates on wholesale financial services offering comprehensive banking facilities for multinational corporations, central banks, public sector entities, and other financial institutions. Outside of Germany, Helaba maintains branch offices and subsidiaries in the financial centers of London, New York and Dublin. In addition, it is represented in Luxembourg and Zurich through participations in Banque LBLux S.A. and LB(Swiss) Privatbank AG held jointly with Bayerische Landesbank Girozentrale. Helaba also maintains representative offices in Madrid and Paris.

The New York Branch of Helaba, licensed under New York law, provides a full range of wholesale commercial banking services in the New York City metropolitan area and throughout the United States.

In the year ending December 31, 2004, total assets of Helaba and its consolidated subsidiaries rose by 3% to € 143.6 billion from € 139.4 billion. Business volume rose 7.8% to € 198.4 billion from the previous year’s level of € 184 billion. Helaba increased its risk provision to € 167 million from € 148.8 million. Helaba’s operating profit after risk provisioning rose 55.3% to € 146 million from € 93.9 million.

Helaba will provide without charge, upon written request, a copy of its most recent Annual Report. Requests should be directed to Landesbank Hessen-Thüringen Girozentrale, New York Branch, 420 Fifth Avenue, 24th Floor, New York, NY 10018, Tel: (212) 703-5200, Fax: (212) 703-5256. The most current published financial information may also be obtained via Helaba’s website: [www.helaba.de](http://www.helaba.de).

In December 2004, Helaba implemented the decision of the European Commission, released on October 20, 2004, concerning the transfer to Helaba of the state of Hesse’s special housing fund of € 1.264 billion as a silent participation. The Commission essentially calculated a repayment obligation of € 7.3 million, affirming the view asserted by Helaba and the state of Hesse that the state was in principle compensated for its silent participation in accordance with market conventions. In December 2004 the Association of German Banks brought an action against the decision of the European Commission at the European Court in Luxembourg.

The Brussels I agreement between the European Commission, the German federal government and the German states on July 17, 2001 provides for the abolition or replacement, following a transitional phase, of maintenance obligation (Anstaltslast) and statutory guarantee (Gewährträgerhaftung). On July 19, 2005, maintenance obligation was replaced by a 'normal market ownership structure' between the owners and Helaba. Statutory guarantee is scheduled to expire as follows: Obligations that already existed on July 18, 2001 will also in the future and without limitation in time be subject to statutory guarantee. This applies irrespective of their maturity. Obligations incurred after July 18, 2001 but prior to July 19, 2005 are covered in full by statutory guarantee, if their maturity ends by December 31, 2015. Liabilities created after July 18, 2005 do not benefit from statutory guarantee.

As of July 19, 2005 Helaba's long-term credit ratings on an unguaranteed basis are 'Aa2' from Moody's Investors Service, 'A+' from Fitch Ratings and 'A' from Standard & Poor's Rating Services. Helaba's short-term credit ratings are 'P-1' from Moody's, 'F1+' from Fitch and 'A-1' from Standard & Poor's. For Helaba's liabilities subject to statutory guarantee long-term credit ratings of 'Aaa' from Moody's, 'AAA' from Fitch, 'AA+' from Standard & Poor's and short-term credit ratings of 'P-1' from Moody's, 'F1+' from Fitch, 'A-1+' from Standard & Poor's still apply.

Helaba has supplied information relating to it in the previous paragraphs. Helaba does not accept any responsibility for any information contained in this Official Statement other than the information relating to Helaba.

NOTE: The official (FOREX fixing) exchange rate on December 30, 2004, the last trading day in 2004, was € 0.73497 = US \$1.00

## **THE LLOYDS TSB BANK GROUP**

Lloyds TSB Bank plc (the “Bank”) is a wholly-owned subsidiary of Lloyds TSB Group plc (“LTSB Group”). The Bank and its subsidiaries (the “Bank’s Group”) comprise one of the leading United Kingdom-based financial services groups, whose businesses provide a wide range of banking and financial services in the United Kingdom and overseas.

At the end of 2004, total consolidated assets of LTSB Group were approximately £280 billion. The total number of persons employed by LTSB Group and its subsidiaries was approximately 70,000.

The main business activities of the Bank’s Group during 2004 are described below:

### **UK Retail Banking and Mortgages**

UK Retail Banking and Mortgages provides banking and other financial services, private banking, stockbroking and mortgages to 15 million personal customers in England, Scotland and Wales.

### **Insurance and Investments**

Insurance and Investments offers life assurance, pensions, and investment products, general insurance and fund management services in the United Kingdom.

### **Wholesale and International Banking**

The Bank’s Group’s relationships with major United Kingdom and multinational companies, banks and institutions and small and medium-sized United Kingdom businesses, together with its activities in financial markets, are managed through dedicated offices in the United Kingdom and a number of locations overseas, including New York and Tokyo.

The Bank’s Group provides banking, investment and other financial services overseas in two main areas: (i) The Americas (including the international bank agency of the Bank in Miami, Florida) and (ii) Europe and Offshore Banking. During 2004, the LTSB Group completed the disposal of substantially all of its local businesses in Argentina, Panama, Guatemala, Honduras and Colombia.

### **Availability of Public Information**

The Bank will provide, upon request, to each person to whom this Official Statement is delivered a copy of the most recently available (i) annual Report and Accounts of LTSB Group for the fiscal year ended December 31, 2004 (ii) Annual Report on Form 20F of LTSB Group. Written requests should be directed to the Bank at 1251 Avenue of the Americas, 39th Floor, New York, New York 10020; Attention: Structured Finance. Additional information (including a full copy of such Report and Accounts) is available from the LTSB Group web site at <http://www.investorrelations.lloydstsb.com>

## **MORGAN STANLEY BANK**

Morgan Stanley Bank (the “Bank”) is a Utah industrial bank with its principal offices in West Valley City, Utah, and an indirect, wholly owned subsidiary of Morgan Stanley, a Delaware corporation (“Morgan Stanley”). The Bank’s obligations are not guaranteed by Morgan Stanley. As a state chartered nonmember of the Federal Reserve System, the Bank is subject to regulation and supervision by the Federal Deposit Insurance Corporation (the “FDIC”) and the Utah Department of Financial Institutions.

The Bank’s long term ratings are Aa3, A+ and AA- by Moody’s, S&P and Fitch, respectively. The Bank’s short term ratings are P-1, A-1 and F1+ by Moody’s, S&P and Fitch, respectively. In April 2005, the Bank’s outlook was changed from stable to negative by Moody’s and S&P and from stable to ratings watch negative by Fitch. In October 2005, S&P returned the Bank’s outlook from negative to stable.

The Bank files call reports each quarter with the FDIC, which include income statement and balance sheet information. The call reports are publicly available on the FDIC’s website at [http://www2.fdic.gov/Call\\_TFR\\_Rpts/search.asp](http://www2.fdic.gov/Call_TFR_Rpts/search.asp). The availability of the Bank’s past financial information at this website shall not create any implication that the information contained or referred to herein or therein is correct as of any time subsequent to its date.

## SCOTIABANK

The Bank of Nova Scotia (“Scotiabank” or the “Bank”), founded in 1832, is a Canadian chartered bank with its principal office located in Toronto, Ontario. Scotiabank is one of North America’s premier financial institutions and Canada’s most international bank. With 48,000 employees, Scotiabank and its affiliates serve over 10 million customers throughout the world.

Scotiabank provides a full range of personal, commercial, corporate and investment banking services through its network of branches located in all Canadian provinces and territories. Outside Canada, Scotiabank has branches and offices in over 50 countries and provides a wide range of banking and related financial services, both directly and through subsidiary and associated banks, trust companies and other financial firms.

For the fiscal year ended October 31, 2004, Scotiabank recorded total assets of CDN\$279.2 billion (US\$229.2 billion) and total deposits of CDN\$195.2 billion (US\$160.3 billion). Net income for the fiscal year ended October 31, 2004 equaled CDN\$2.931 billion (US\$2.406 billion), compared to CDN\$2.477 billion (US\$2.034 billion) for the prior fiscal year. Amounts above are shown in Canadian dollars and also reflect the United States dollar equivalent as of October 29, 2004 (1.0000 United States dollar equals 1.218 Canadian dollars).

For the quarter ended July 31, 2005, Scotiabank recorded total assets of CDN\$317.5 billion (US\$259.4 billion) and total deposits of CDN\$220 billion (US\$179.7 billion). Net income for the quarter ended July 31, 2005 equaled CDN\$784 million (US\$640.5 million), compared to CDN\$731 million (US\$597.2 million) for the same period the prior year. Amounts above are shown in Canadian dollars and also reflect the United States dollar equivalent as of Friday, July 29, 2005 (1.0000 United States dollar equals 1.2241 Canadian dollars).

Scotiabank will provide to anyone, upon written request, a copy of its most recent annual report, as well as a copy of its most recent quarterly financial report. Requests should be directed to: The Bank of Nova Scotia, New York Agency, One Liberty Plaza, 26th Floor, New York, NY, 10006. Attention: Public Finance Department.

The information concerning the Bank contained herein is furnished solely to provide limited introductory information regarding the Bank and does not purport to be comprehensive. Such information is qualified in its entirety by the detailed information appearing in the documents and financial statements referenced above.

The delivery hereof shall not create any implication that there has been no change in the affairs of the Bank since the date hereof, or that the information contained or referred to in this disclosure information is correct as of any time subsequent to its date.

## SOCIÉTÉ GÉNÉRALE

Société Générale, New York Branch is a licensed New York branch of Société Générale, a French banking corporation. The executive offices of Société Générale, New York Branch are located at 1221 Avenue of the Americas, New York, New York 10020. Its telephone number is (212) 278-6000.

Société Générale (the “Bank”) is a French banking corporation and the most important constituent entity of the Société Générale Group (the “Group”). The Group is an international banking and financial services group based in France that includes approximately 300 French and foreign banking and non-banking companies. The Group also holds (for investment) minority interests in industrial and commercial companies. In this Official Statement, the term “Bank” refers to Société Générale (the parent company) only and the term “Group” refers to Société Générale and its domestic and foreign subsidiaries and affiliates which are consolidated in full or under the equity method.

The Bank was originally incorporated in 1864 and was nationalized along with other major French commercial banks in 1945. In July 1987, the Bank was returned to the private sector through offerings of shares in France and abroad. The Bank and other French financial institutions of the Group are subject to laws and regulations which are applicable generally to financial institutions doing business in the relevant jurisdictions and which cover such matters as liquidity and asset coverage, reserve requirements, risk diversification and limitations on equity investments in non-financial companies, all of which require compliance with numerous reporting and accounting requirements.

The Group is engaged in a broad range of banking and financial services activities, including retail banking, deposit-taking, lending and leasing, asset management, securities brokerage services, investment banking, capital markets activities and foreign exchange transactions. The Group’s customers are served by its extensive network of domestic and international branches, agencies and other offices. The Group is one of the leading financial service groups in the eurozone and is among the largest French companies in terms of market capitalization (EUR 33.1 billion at December 31, 2004). The Group has approximately 92,000 employees and its business portfolio is based on three core activities:

- Retail Banking and Financial Services
- Asset Management, Private Banking and Securities Services
- Corporate and Investment Banking

The head office of the Bank is 29, boulevard Haussmann, 75009 Paris, France. Its administrative offices are at Tour Société Générale, 17, cours Valmy, 92972 Paris-La-Défense Cedex, France. Its telephone number is 42 14 20 00.

The Group has had operations in the United States since 1940. The Bank maintains offices in New York, Chicago, Dallas, Greenwich (Connecticut), Houston and San Francisco. The Group also conducts business in the United States through a number of subsidiaries.

At December 31, 2004, the Group had total consolidated assets of approximately 601.1<sup>(1)</sup> billion Euros and total consolidated shareholders’ equity of approximately 18.6 billion Euros, and the Bank had total assets of approximately 513.6 billion Euros and total shareholders’ equity of approximately 16.8 billion Euros.

The foregoing financial figures have been derived from, and are qualified by reference to, the Group’s audited consolidated financial statements and notes (including note 1 which contains a discussion of the significant accounting principles applied) and the Bank’s audited financial statements that are contained in the Group’s 2004 Annual Report (the “Annual Report”). Such financial statements are prepared in accordance with French accounting principles, which differ in certain significant respects from generally accepted accounting principles in the United States.

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(1) At December 31, 2004, the buying rate expressed in U.S. dollars per Euro was 1.3538 U.S. dollars.

Copies of the English version of the Annual Report (translated in full from the underlying French document) will be mailed to each person to whom this Official Statement is delivered, upon written request mailed to Société Générale, New York Branch, 1221 Avenue of the Americas, New York, New York 10020, Attention: Corporate Communications Department.

**APPENDIX J**

**INFORMATION CONCERNING THE BOND INSURERS AND THE  
FORMS OF FINANCIAL GUARANTY INSURANCE POLICIES**

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## FINANCIAL GUARANTY INSURANCE COMPANY

### **Bond Insurance**

Financial Guaranty has supplied the following information for inclusion in this Official Statement. No representation is made by the issuer or the underwriter as to the accuracy or completeness of this information.

### **Payments Under the Policy**

Concurrently with the issuance of the Series 2005 Bonds, Financial Guaranty Insurance Company, doing business in California as FGIC Insurance Company (“Financial Guaranty”) will issue its Municipal Bond New Issue Insurance Policy (the “FGIC Policy”) for the Series 2005G-10 Bonds, the Series 2005G-12 Bonds, the Series 2005G-13 Bonds and the Series 2005G-14 Bonds (collectively, the “FGIC-Insured Bonds.” The FGIC Policy unconditionally guarantees the payment of that portion of the principal or accreted value (if applicable) of and interest on the FGIC-Insured Bonds which has become due for payment, but shall be unpaid by reason of nonpayment by the issuer of the FGIC-Insured Bonds (the “Issuer”). Financial Guaranty will make such payments to U.S. Bank Trust National Association, or its successor as its agent (the “Fiscal Agent”), on the later of the date on which such principal, accreted value or interest (as applicable) is due or on the business day next following the day on which Financial Guaranty shall have received notice (in accordance with the terms of the FGIC Policy) from an owner of FGIC-Insured Bonds or the trustee or paying agent (if any) of the nonpayment of such amount by the Issuer. The Fiscal Agent will disburse such amount due on any FGIC-Insured Bond to its owner upon receipt by the Fiscal Agent of evidence satisfactory to the Fiscal Agent of the owner’s right to receive payment of the principal, accreted value or interest (as applicable) due for payment and evidence, including any appropriate instruments of assignment, that all of such owner’s rights to payment of such principal, accreted value or interest (as applicable) shall be vested in Financial Guaranty. The term “nonpayment” in respect of a FGIC-Insured Bond includes any payment of principal, accreted value or interest (as applicable) made to an owner of a FGIC-Insured Bond which has been recovered from such owner pursuant to the United States Bankruptcy Code by a trustee in bankruptcy in accordance with a final, nonappealable order of a court having competent jurisdiction.

Once issued, the FGIC Policy is non-cancellable by Financial Guaranty. The FGIC Policy covers failure to pay principal (or accreted value, if applicable) of the FGIC-Insured Bonds on their stated maturity dates and their mandatory sinking fund redemption dates, and not on any other date on which the FGIC-Insured Bonds may have been otherwise called for redemption, accelerated or advanced in maturity. The FGIC Policy also covers the failure to pay interest on the stated date for its payment. In the event that payment of the FGIC-Insured Bonds is accelerated, Financial Guaranty will only be obligated to pay principal (or accreted value, if applicable) and interest in the originally scheduled amounts on the originally scheduled payment dates. Upon such payment, Financial Guaranty will become the owner of the FGIC-Insured Bond, appurtenant coupon or right to payment of principal or interest on such Bond and will be fully subrogated to all of the Bondholder’s rights thereunder.

The FGIC Policy does not insure any risk other than Nonpayment by the Issuer, as defined in the FGIC Policy. Specifically, the FGIC Policy does not cover: (i) payment on acceleration, as a result of a call for redemption (other than mandatory sinking fund redemption) or as a result of any other advancement of maturity; (ii) payment of any redemption, prepayment or acceleration premium; or (iii) nonpayment of principal (or accreted value, if applicable) or interest caused by the insolvency or negligence or any other act or omission of the trustee or paying agent, if any.

As a condition of its commitment to insure Bonds, Financial Guaranty may be granted certain rights under the Bond documentation. The specific rights, if any, granted to Financial Guaranty in connection with its insurance of the FGIC-Insured Bonds may be set forth in the description of the principal legal documents appearing elsewhere in this Official Statement, and reference should be made thereto.

The FGIC Policy is not covered by the Property/Casualty Insurance Security Fund specified in Article 76 of the New York Insurance Law.

The FGIC Policy is not covered by the California Insurance Guaranty Association (California Insurance Code, Article 14.2).California.

### **Financial Guaranty Insurance Company**

Financial Guaranty, a New York stock insurance corporation, is a direct, wholly-owned subsidiary of FGIC Corporation, a Delaware corporation, and provides financial guaranty insurance for public finance and structured finance obligations. Financial Guaranty is licensed to engage in financial guaranty insurance in all 50 states, the District of Columbia, the U.S. Virgin Islands, the Commonwealth of Puerto Rico and, through a branch, in the United Kingdom.

On December 18, 2003, an investor group consisting of The PMI Group, Inc. (“PMI”), affiliates of The Blackstone Group L.P. (“Blackstone”), affiliates of The Cypress Group L.L.C. (“Cypress”) and affiliates of CIVC Partners L.P. (“CIVC”) acquired FGIC Corporation (the “FGIC Acquisition”) from a subsidiary of General Electric Capital Corporation (“GE Capital”). PMI, Blackstone, Cypress and CIVC acquired approximately 42%, 23%, 23% and 7%, respectively, of FGIC Corporation’s common stock. FGIC Corporation paid GE Capital approximately \$284.3 million in pre-closing dividends from the proceeds of dividends it, in turn, had received from Financial Guaranty, and GE Capital retained approximately \$234.6 million in liquidation preference of FGIC Corporation’s convertible participating preferred stock and approximately 5% of FGIC Corporation’s common stock. Neither FGIC Corporation nor any of its shareholders is obligated to pay any debts of Financial Guaranty or any claims under any insurance policy, including the Policy, issued by Financial Guaranty.

Financial Guaranty is subject to the insurance laws and regulations of the State of New York, where it is domiciled, including Article 69 of the New York Insurance Law (“Article 69”), a comprehensive financial guaranty insurance statute. Financial Guaranty is also subject to the insurance laws and regulations of all other jurisdictions in which it is licensed to transact insurance business. The insurance laws and regulations, as well as the level of supervisory authority that may be exercised by the various insurance regulators, vary by jurisdiction, but generally require insurance companies to maintain minimum standards of business conduct and solvency, to meet certain financial tests, to comply with requirements concerning permitted investments and the use of policy forms and premium rates and to file quarterly and annual financial statements on the basis of statutory accounting principles (“SAP”) and other reports. In addition, Article 69, among other things, limits the business of each financial guaranty insurer, including Financial Guaranty, to financial guaranty insurance and certain related lines.

For the nine months ended September 30, 2005, and the years ended December 31, 2004, and December 31, 2003, Financial Guaranty had written directly or assumed through reinsurance, guaranties of approximately \$58.5 billion, \$59.5 billion and \$42.4 billion par value of securities, respectively (of which approximately 55%, 56% and 79%, respectively, constituted guaranties of municipal bonds), for which it had collected gross premiums of approximately \$312.5 million, \$323.6 million and \$260.3 million, respectively. For the nine months ended September 30, 2005, Financial Guaranty had reinsured, through facultative and excess of loss arrangements, approximately 7.8% of the risks it had written.

As of September 30, 2005, Financial Guaranty had net admitted assets of approximately \$3.401 billion, total liabilities of approximately \$2.246 billion, and total capital and policyholders’ surplus of approximately \$1.155 billion, determined in accordance with statutory accounting practices prescribed or permitted by insurance regulatory authorities.

The unaudited financial statements of Financial Guaranty as of September 30, 2005, the audited financial statements of Financial Guaranty as of December 31, 2004, and the audited financial statements of Financial Guaranty as of December 31, 2003, which have been filed with the Nationally Recognized Municipal Securities Information Repositories (“NRMSIRs”), are hereby included by specific reference in this Official Statement. Any statement contained herein under the heading “APPENDIX J – INFORMATION CONCERNING THE BOND INSURERS AND THE FORMS OF FINANCIAL GUARANTY INSURANCE POLICIES – FINANCIAL GUARANTY INSURANCE COMPANY,” or in any documents included by specific reference herein, shall be modified or superseded to the extent required by any statement in any document subsequently filed by Financial Guaranty with such NRMSIRs, and shall not be deemed, except as so modified or superseded, to constitute a part of this Official Statement. All financial statements of Financial Guaranty (if any) included in documents filed by

Financial Guaranty with the NRMSIRs subsequent to the date of this Official Statement and prior to the termination of the offering of the Bonds shall be deemed to be included by specific reference into this Official Statement and to be a part hereof from the respective dates of filing of such documents.

Financial Guaranty also prepares quarterly and annual financial statements on the basis of generally accepted accounting principles. Copies of Financial Guaranty's most recent GAAP and SAP financial statements are available upon request to: Financial Guaranty Insurance Company, 125 Park Avenue, New York, NY 10017, Attention: Corporate Communications Department. Financial Guaranty's telephone number is (212) 312-3000.

### **Financial Guaranty's Credit Ratings**

The financial strength of Financial Guaranty is rated "AAA" by Standard & Poor's, a Division of The McGraw-Hill Companies, Inc., "Aaa" by Moody's Investors Service, and "AAA" by Fitch Ratings. Each rating of Financial Guaranty should be evaluated independently. The ratings reflect the respective ratings agencies' current assessments of the insurance financial strength of Financial Guaranty. Any further explanation of any rating may be obtained only from the applicable rating agency. These ratings are not recommendations to buy, sell or hold the Bonds, and are subject to revision or withdrawal at any time by the rating agencies. Any downward revision or withdrawal of any of the above ratings may have an adverse effect on the market price of the Bonds. Financial Guaranty does not guarantee the market price or investment value of the Bonds nor does it guarantee that the ratings on the Bonds will not be revised or withdrawn.

Neither Financial Guaranty nor any of its affiliates accepts any responsibility for the accuracy or completeness of the Official Statement or any information or disclosure that is provided to potential purchasers of the Bonds, or omitted from such disclosure, other than with respect to the accuracy of information with respect to Financial Guaranty or the FGIC Policy under the heading "APPENDIX J – INFORMATION CONCERNING THE BOND INSURERS AND THE FORMS OF FINANCIAL GUARANTY INSURANCE POLICIES – FINANCIAL GUARANTY INSURANCE COMPANY." In addition, Financial Guaranty makes no representation regarding the Bonds or the advisability of investing in the Bonds.



**Financial Guaranty Insurance Company**  
 Doing business in California as *FGIC Insurance Company*  
 125 Park Avenue  
 New York, NY 10017  
 T 212-312-3000  
 T 800-352-0001

## Municipal Bond New Issue Insurance Policy

<b>Issuer:</b>	<b>Policy Number:</b>
	<b>Control Number:</b> 0010001
<b>Bonds:</b>	<b>Premium:</b>

Financial Guaranty Insurance Company ("Financial Guaranty"), a New York stock insurance company, in consideration of the payment of the premium and subject to the terms of this Policy, hereby unconditionally and irrevocably agrees to pay to U.S. Bank Trust National Association or its successor, as its agent (the "Fiscal Agent"), for the benefit of Bondholders, that portion of the principal and interest on the above-described debt obligations (the "Bonds") which shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Issuer.

Financial Guaranty will make such payments to the Fiscal Agent on the date such principal or interest becomes Due for Payment or on the Business Day next following the day on which Financial Guaranty shall have received Notice of Nonpayment, whichever is later. The Fiscal Agent will disburse to the Bondholder the face amount of principal and interest which is then Due for Payment but is unpaid by reason of Nonpayment by the Issuer but only upon receipt by the Fiscal Agent, in form reasonably satisfactory to it, of (i) evidence of the Bondholder's right to receive payment of the principal or interest Due for Payment and (ii) evidence, including any appropriate instruments of assignment, that all of the Bondholder's rights to payment of such principal or interest Due for Payment shall thereupon vest in Financial Guaranty. Upon such disbursement, Financial Guaranty shall become the owner of the Bond, appurtenant coupon or right to payment of principal or interest on such Bond and shall be fully subrogated to all of the Bondholder's rights thereunder, including the Bondholder's right to payment thereof.

This Policy is non-cancellable for any reason. The premium on this Policy is not refundable for any reason, including the payment of the Bonds prior to their maturity. This Policy does not insure against loss of any prepayment premium which may at any time be payable with respect to any Bond.

As used herein, the term "Bondholder" means, as to a particular Bond, the person other than the Issuer who, at the time of Nonpayment, is entitled under the terms of such Bond to payment thereof. "Due for Payment" means, when referring to the principal of a Bond, the stated maturity date thereof or the date on which the same shall have been duly called for mandatory sinking fund redemption and does not refer to any earlier date on which payment is due by reason of call for redemption (other than by mandatory sinking fund redemption), acceleration or other advancement of maturity and means, when referring to interest on a Bond, the stated date for payment of interest. "Nonpayment" in respect of a Bond means the failure of the Issuer to have provided sufficient funds to the paying agent for payment in full of all



**Financial Guaranty Insurance Company**  
*Doing business in California as FGIC Insurance Company*  
 125 Park Avenue  
 New York, NY 10017  
 T 212-312-3000  
 T 800-352-0001

**Municipal Bond  
 New Issue Insurance Policy**

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principal and interest Due for Payment on such Bond. "Notice" means telephonic or telegraphic notice, subsequently confirmed in writing, or written notice by registered or certified mail, from a Bondholder or a paying agent for the Bonds to Financial Guaranty. "Business Day" means any day other than a Saturday, Sunday or a day on which the Fiscal Agent is authorized by law to remain closed.

In Witness Whereof, Financial Guaranty has caused this Policy to be affixed with its corporate seal and to be signed by its duly authorized officer in facsimile to become effective and binding upon Financial Guaranty by virtue of the countersignature of its duly authorized representative.

SPECIMEN

**President**

**Effective Date:**

**Authorized Representative**

U.S. Bank Trust National Association, acknowledges that it has agreed to perform the duties of Fiscal Agent under this Policy.

**Authorized Officer**



**Financial Guaranty Insurance Company**  
 Doing business in California as *FGIC Insurance Company*  
 125 Park Avenue  
 New York, NY 10017  
 T 212-312-3000  
 T 800-352-0001

**Endorsement**  
**To Financial Guaranty Insurance Company**  
**Insurance Policy**

**Policy Number:**

**Control Number:** 0010001

It is further understood that the term "Nonpayment" in respect of a Bond includes any payment of principal or interest made to a Bondholder by or on behalf of the issuer of such Bond which has been recovered from such Bondholder pursuant to the United States Bankruptcy Code by a trustee in bankruptcy in accordance with a final, nonappealable order of a court having competent jurisdiction.

NOTHING HEREIN SHALL BE CONSTRUED TO WAIVE, ALTER, REDUCE OR AMEND COVERAGE IN ANY OTHER SECTION OF THE POLICY. IF FOUND CONTRARY TO THE POLICY LANGUAGE, THE TERMS OF THIS ENDORSEMENT SUPERSEDE THE POLICY LANGUAGE.

In Witness Whereof, Financial Guaranty has caused this Endorsement to be affixed with its corporate seal and to be signed by its duly authorized officer in facsimile to become effective and binding upon Financial Guaranty by virtue of the countersignature of its duly authorized representative.

**President**

**Effective Date:**

**Authorized Representative**

**Acknowledged as of the Effective Date written above:**

**Authorized Officer**  
**U.S. Bank Trust National Association, as Fiscal Agent**



**Financial Guaranty Insurance Company**  
*Doing business in California as FGIC Insurance Company*  
 125 Park Avenue  
 New York, NY 10017  
 T 212-312-3000  
 T 800-352-0001

**Mandatory California State  
 Amendatory Endorsement  
 To Financial Guaranty Insurance Company  
 Insurance Policy**

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**Policy Number:** \_\_\_\_\_ **Control Number:** 0010001

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SPECIMEN

The insurance provided by this Policy is not covered by the California Insurance Guaranty Association (California Insurance Code, Article 14.2).

NOTHING HEREIN SHALL BE CONSTRUED TO WAIVE, ALTER, REDUCE OR AMEND COVERAGE IN ANY OTHER SECTION OF THE POLICY. IF FOUND CONTRARY TO THE POLICY LANGUAGE, THE TERMS OF THIS ENDORSEMENT SUPERSEDE THE POLICY LANGUAGE.

In Witness Whereof, Financial Guaranty has caused this Endorsement to be affixed with its corporate seal and to be signed by its duly authorized officer in facsimile to become effective and binding upon Financial Guaranty by virtue of the countersignature of its duly authorized representative.

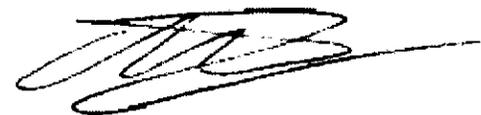


**President**

**Effective Date:**

**Authorized Representative**

**Acknowledged as of the Effective Date written above:**



**Authorized Officer**  
**U.S. Bank Trust National Association, as Fiscal Agent**



**Financial Guaranty Insurance Company**  
*Doing business in California as FGIC Insurance Company*  
 125 Park Avenue  
 New York, NY 10017  
 T 212-312-3000  
 T 800-352-0001

**Mandatory California State  
 Amendatory Endorsement  
 To Financial Guaranty Insurance Company  
 Insurance Policy**

**Policy Number:**

**Control Number:** 0010001

**SPECIMEN**

Notwithstanding the terms and conditions in this Policy, it is further understood that there shall be no acceleration of payment due under such Policy unless such acceleration is at the sole option of Financial Guaranty.

NOTHING HEREIN SHALL BE CONSTRUED TO WAIVE, ALTER, REDUCE OR AMEND COVERAGE IN ANY OTHER SECTION OF THE POLICY. IF FOUND CONTRARY TO THE POLICY LANGUAGE, THE TERMS OF THIS ENDORSEMENT SUPERSEDE THE POLICY LANGUAGE.

In Witness Whereof, Financial Guaranty has caused this Endorsement to be affixed with its corporate seal and to be signed by its duly authorized officer in facsimile to become effective and binding upon Financial Guaranty by virtue of the countersignature of its duly authorized representative.

**President**

**Effective Date:**

**Authorized Representative**

**Acknowledged as of the Effective Date written above:**

**Authorized Officer  
 U.S. Bank Trust National Association, as Fiscal Agent**

## **FINANCIAL SECURITY ASSURANCE INC.**

### **Bond Insurance Policy**

Concurrently with the issuance of the Series 2005 Bonds, Financial Security Assurance Inc. (“Financial Security”) will issue its Municipal Bond Insurance Policy (the “FSA Policy”) for the Series 2005G-3 Bonds, the Series 2005G-4 Bonds, the Series 2005G-5 Bonds, the Series 2005G-6 Bonds, the Series 2005G-7 Bonds and the Series 2005G-11 Bonds (collectively, the “FSA-Insured Bonds”). The FSA Policy guarantees the scheduled payment of principal of and interest on the FSA-Insured Bonds when due as set forth in the form of the FSA Policy included as an exhibit to this Official Statement.

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

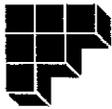
### **Financial Security Assurance Inc.**

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

At June 30, 2005, Financial Security’s total policyholders’ surplus and contingency reserves were approximately \$2,365,896,000 and its total unearned premium reserve was approximately \$1,719,641,000 in accordance with statutory accounting principles. At June 30, 2005, Financial Security’s total shareholder’s equity was approximately \$2,819,103,000 and its total net unearned premium reserve was approximately \$1,404,195,000 in accordance with generally accepted accounting principles.

The financial statements included as exhibits to the annual and quarterly reports filed by Holdings with the Securities and Exchange Commission are hereby incorporated herein by reference. Also incorporated herein by reference are any such financial statements so filed from the date of this Official Statement until the termination of the offering of the FSA-Insured Bonds. Copies of materials incorporated by reference will be provided upon request to Financial Security Assurance Inc.: 31 West 52nd Street, New York, New York 10019, Attention: Communications Department (telephone (212) 826-0100).

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



**FINANCIAL  
SECURITY  
ASSURANCE®**

## **MUNICIPAL BOND INSURANCE POLICY**

ISSUER:

Policy No.:

BONDS:

Effective Date:

Premium:

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

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

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

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

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

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

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

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

[Countersignature]

FINANCIAL SECURITY ASSURANCE INC.

By \_\_\_\_\_

By \_\_\_\_\_  
Authorized Officer

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

(212) 826-0100

Form 500NY (5/90)

**ENDORSEMENT NO. 1 TO  
MUNICIPAL BOND  
INSURANCE POLICY  
(California Insurance  
Guaranty Association)**

ISSUER:

Policy No.: -M

BONDS: \$ in aggregate principal amount of

Effective Date:

Notwithstanding the terms and provisions contained in this Policy, it is further understood that the Insurance provided by this Policy is not covered by the California Insurance Guaranty Association established pursuant to Article 14.2 (commencing with Section 1063) of Chapter 1 of Part 2 of Division 1 of the California Insurance Code.

Nothing herein shall be construed to waive, alter, reduce or amend coverage in any other section of the Policy. If found contrary to the Policy language, the terms of this Endorsement supersede the Policy language.

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

FINANCIAL SECURITY ASSURANCE INC.

By \_\_\_\_\_  
Authorized Officer

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

(212) 826-0100

Form 560NY (CA 1/91)

## **MBIA INSURANCE CORPORATION**

### **The MBIA Insurance Corporation Insurance Policy**

The following information has been furnished by MBIA Insurance Corporation (“MBIA”) for use in this Official Statement. Reference is made to the following pages of this Appendix for a specimen of MBIA’s policy (the “MBIA Policy”).

MBIA does not accept any responsibility for the accuracy or completeness of this Official Statement or any information or disclosure contained herein, or omitted herefrom, other than with respect to the accuracy of the information regarding the Policy and MBIA set forth under the heading “APPENDIX J – INFORMATION CONCERNING BOND INSURERS AND FORMS OF FINANCIAL GUARANTY INSURANCE POLICIES – MBIA INSURANCE CORPORATION “. Additionally, MBIA makes no representation regarding the Bonds or the advisability of investing in the Bonds.

The MBIA Policy unconditionally and irrevocably guarantees the full and complete payment required to be made by or on behalf of the Issuer to the Paying Agent or its successor of an amount equal to (i) the principal of (either at the stated maturity or by an advancement of maturity pursuant to a mandatory sinking fund payment) and interest on, the Series 2005G-8 Bonds and the Series 2005G-9 Bonds (collectively, the “MBIA-Insured Bonds”) as such payments shall become due but shall not be so paid (except that in the event of any acceleration of the due date of such principal by reason of mandatory or optional redemption or acceleration resulting from default or otherwise, other than any advancement of maturity pursuant to a mandatory sinking fund payment, the payments guaranteed by the MBIA Policy shall be made in such amounts and at such times as such payments of principal would have been due had there not been any such acceleration, unless MBIA elects in its sole discretion, to pay in whole or in part any principal due by reason of such acceleration); and (ii) the reimbursement of any such payment which is subsequently recovered from any Owner of the MBIA-Insured Bonds pursuant to a final judgment by a court of competent jurisdiction that such payment constitutes an avoidable preference to such Owner within the meaning of any applicable bankruptcy law (a “Preference”).

MBIA’s Policy does not insure against loss of any prepayment premium which may at any time be payable with respect to the MBIA-Insured Bonds. MBIA’s Policy does not, under any circumstance, insure against loss relating to: (i) optional or mandatory redemptions (other than mandatory sinking fund redemptions); (ii) any payments to be made on an accelerated basis; (iii) payments of the purchase price of MBIA-Insured Bonds upon tender by an owner thereof; or (iv) any Preference relating to (i) through (iii) above. MBIA’s Policy also does not insure against nonpayment of principal of or interest on the MBIA-Insured Bonds resulting from the insolvency, negligence or any other act or omission of the Paying Agent or any other paying agent for the MBIA-Insured Bonds.

Upon receipt of telephonic or telegraphic notice, such notice subsequently confirmed in writing by registered or certified mail, or upon receipt of written notice by registered or certified mail, by MBIA from the Paying Agent or any owner of a MBIA-Insured Bond the payment of an insured amount for which is then due, that such required payment has not been made, MBIA on the due date of such payment or within one business day after receipt of notice of such nonpayment, whichever is later, will make a deposit of funds, in an account with U.S. Bank Trust National Association, in New York, New York, or its successor, sufficient for the payment of any such insured amounts which are then due. Upon presentment and surrender of such MBIA-Insured Bonds or presentment of such other proof of ownership of the MBIA-Insured Bonds, together with any appropriate instruments of assignment to evidence the assignment of the insured amounts due on the MBIA-Insured Bonds as are paid by MBIA, and appropriate instruments to effect the appointment of MBIA as agent for such owners of the MBIA-Insured Bonds in any legal proceeding related to payment of insured amounts on the MBIA-Insured Bonds, such instruments being in a form satisfactory to U.S. Bank Trust National Association, U.S. Bank Trust National Association shall disburse to such owners or the Paying Agent payment of the insured amounts due on such MBIA-Insured Bonds, less any amount held by the Paying Agent for the payment of such insured amounts and legally available therefor.

## **MBIA Insurance Corporation**

MBIA Insurance Corporation (“MBIA”) is the principal operating subsidiary of MBIA Inc., a New York Stock Exchange listed company (the “Company”). The Company is not obligated to pay the debts of or claims against MBIA. MBIA is domiciled in the State of New York and licensed to do business in and subject to regulation under the laws of all 50 states, the District of Columbia, the Commonwealth of Puerto Rico, the Commonwealth of the Northern Mariana Islands, the Virgin Islands of the United States and the Territory of Guam. MBIA, either directly or through subsidiaries, is licensed to do business in the Republic of France, the United Kingdom and the Kingdom of Spain and is subject to regulation under the laws of those jurisdictions.

The principal executive offices of MBIA are located at 113 King Street, Armonk, New York 10504 and the main telephone number at that address is (914) 273-4545.

## **Regulation**

As a financial guaranty insurance company licensed to do business in the State of New York, MBIA is subject to the New York Insurance Law which, among other things, prescribes minimum capital requirements and contingency reserves against liabilities for MBIA, limits the classes and concentrations of investments that are made by MBIA and requires the approval of policy rates and forms that are employed by MBIA. State law also regulates the amount of both the aggregate and individual risks that may be insured by MBIA, the payment of dividends by MBIA, changes in control with respect to MBIA and transactions among MBIA and its affiliates.

The Policy is not covered by the Property/Casualty Insurance Security Fund specified in Article 76 of the New York Insurance Law.

## **Financial Strength Ratings of MBIA**

Moody’s Investors Service, Inc. rates the financial strength of MBIA “Aaa.”

Standard & Poor’s, a division of The McGraw-Hill Companies, Inc. rates the financial strength of MBIA “AAA.”

Fitch Ratings rates the financial strength of MBIA “AAA.”

Each rating of MBIA should be evaluated independently. The ratings reflect the respective rating agency’s current assessment of the creditworthiness of MBIA and its ability to pay claims on its policies of insurance. Any further explanation as to the significance of the above ratings may be obtained only from the applicable rating agency.

The above ratings are not recommendations to buy, sell or hold the Bonds, and such ratings may be subject to revision or withdrawal at any time by the rating agencies. Any downward revision or withdrawal of any of the above ratings may have an adverse effect on the market price of the Bonds. MBIA does not guaranty the market price of the Bonds nor does it guaranty that the ratings on the Bonds will not be revised or withdrawn.

## **MBIA Financial Information**

As of December 31, 2004, MBIA had admitted assets of \$10.3 billion (unaudited and restated), total liabilities of \$7.0 billion (unaudited and restated), and total capital and surplus of \$3.2 billion (unaudited and restated) determined in accordance with statutory accounting practices prescribed or permitted by insurance regulatory authorities. As of September 30, 2005 MBIA had admitted assets of \$10.8 billion (unaudited), total liabilities of \$7.1 billion (unaudited), and total capital and surplus of \$3.7 billion (unaudited) determined in accordance with statutory accounting practices prescribed or permitted by insurance regulatory authorities.

For further information concerning MBIA, see the consolidated financial statements of MBIA and its subsidiaries as of December 31, 2004 and December 31, 2003 and for each of the three years in the period ended

December 31, 2004, prepared in accordance with generally accepted accounting principles, included in the Annual Report on Form 10-K of the Company for the year ended December 31, 2004 and the consolidated financial statements of MBIA and its subsidiaries as of September 30, 2005 and for the nine month periods ended September 30, 2005 and September 30, 2004 included in the Quarterly Report on Form 10-Q of the Company for the period ended September 30, 2005, which are hereby incorporated by reference into this Official Statement and shall be deemed to be a part hereof.

Copies of the statutory financial statements filed by MBIA with the State of New York Insurance Department are available over the Internet at the Company's web site at <http://www.mbia.com> and at no cost, upon request to MBIA at its principal executive offices.

#### **Incorporation of Certain Documents by Reference**

The following documents filed by the Company with the Securities and Exchange Commission (the "SEC") are incorporated by reference into this Official Statement:

- (1) The Company's Annual Report on Form 10-K for the year ended December 31, 2004; and
- (2) The Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2005.

Any documents, including any financial statements of MBIA and its subsidiaries that are included therein or attached as exhibits thereto, filed by the Company pursuant to Sections 13(a), 13(c), 14 or 15(d) of the Exchange Act after the date of the Company's most recent Quarterly Report on Form 10-Q or Annual Report on Form 10-K, and prior to the termination of the offering of the Bonds offered hereby shall be deemed to be incorporated by reference in this Official Statement and to be a part hereof from the respective dates of filing such documents. Any statement contained in a document incorporated or deemed to be incorporated by reference herein, or contained in this Official Statement, shall be deemed to be modified or superseded for purposes of this Official Statement to the extent that a statement contained herein or in any other subsequently filed document which also is or is deemed to be incorporated by reference herein modifies or supersedes such statement. Any such statement so modified or superseded shall not be deemed, except as so modified or superseded, to constitute a part of this Official Statement.

The Company files annual, quarterly and special reports, information statements and other information with the SEC under File No. 1-9583. Copies of the Company's SEC filings (including (1) the Company's Annual Report on Form 10-K for the year ended December 31, 2004, and (2) the Company's Quarterly Reports on Form 10-Q for the quarters ended March 31, 2005, June 30, 2005 and September 30, 2005) are available (i) over the Internet at the SEC's web site at <http://www.sec.gov>; (ii) at the SEC's public reference room in Washington D.C.; (iii) over the Internet at the Company's web site at <http://www.mbia.com>; and (iv) at no cost, upon request to MBIA at its principal executive offices.

In the event the Insurer were to become insolvent, any claims arising under a policy of financial guaranty insurance are excluded from coverage by the California Insurance Guaranty Association, established pursuant to Article 14.2 (commencing with Section 1063) of Chapter 1 of Part 2 of Division 1 of the California Insurance Code.

# FINANCIAL GUARANTY INSURANCE POLICY

## MBIA Insurance Corporation Armonk, New York 10504

Policy No. [NUMBER]

MBIA Insurance Corporation (the "Insurer"), in consideration of the payment of the premium and subject to the terms of this policy, hereby unconditionally and irrevocably guarantees to any owner, as hereinafter defined, of the following described obligations, the full and complete payment required to be made by or on behalf of the Issuer to [PAYING AGENT/TRUSTEE] or its successor (the "Paying Agent") of an amount equal to (i) the principal of (either at the stated maturity or by any advancement of maturity pursuant to a mandatory sinking fund payment) and interest on, the Obligations (as that term is defined below) as such payments shall become due but shall not be so paid (except that in the event of any acceleration of the due date of such principal by reason of mandatory or optional redemption or acceleration resulting from default or otherwise, other than any advancement of maturity pursuant to a mandatory sinking fund payment, the payments guaranteed hereby shall be made in such amounts and at such times as such payments of principal would have been due had there not been any such acceleration); and (ii) the reimbursement of a such payment which is subsequently recovered from any owner pursuant to a final judgment by a court of competent jurisdiction that such payment constitutes an avoidable preference to such owner within the meaning of any applicable bankruptcy law. The amounts referred to in clauses (i) and (ii) of the preceding sentence shall be referred to herein collectively as the "Insured Amounts." "Obligations" shall mean:

[PAR]  
[LEGAL NAME OF ISSUE]

Upon receipt of telephonic or telegraphic notice, such notice subsequently confirmed in writing by registered or certified mail, or upon receipt of written notice by registered or certified mail, by the Insurer from the Paying Agent or any owner of an Obligation the payment of an Insured Amount for which is then due, that such required payment has not been made, the Insurer on the due date of such payment or within one business day after receipt of notice of such nonpayment, whichever is later, will make a deposit of funds, in an account with State Street Bank and Trust Company, N.A., in New York, New York, or its successor, sufficient for the payment of any such Insured Amounts which are then due. Upon presentment and surrender of such Obligations or presentment of such other proof of ownership of the Obligations, together with any appropriate instruments of assignment to evidence the assignment of the Insured Amounts due on the Obligations as are paid by the Insurer, and appropriate instruments to effect the appointment of the Insurer as agent for such owners of the Obligations in any legal proceeding related to payment of Insured Amounts on the Obligations, such instruments being in a form satisfactory to State Street Bank and Trust Company, N.A., State Street Bank and Trust Company, N.A. shall disburse to such owners, or the Paying Agent payment of the Insured Amounts due on such Obligations, less any amount held by the Paying Agent for the payment of such Insured Amounts and legally available therefor. This policy does not insure against loss of any prepayment premium which may at any time be payable with respect to any Obligation.

As used herein, the term "owner" shall mean the registered owner of any Obligation as indicated in the books maintained by the Paying Agent, the Issuer, or any designee of the Issuer for such purpose. The term owner shall not include the Issuer or any party whose agreement with the Issuer constitutes the underlying security for the Obligations.

Any service of process on the Insurer may be made to the Insurer at its offices located at 113 King Street, Armonk, New York 10504 and such service of process shall be valid and binding.

This policy is non-cancellable for any reason. The premium on this policy is not refundable for any reason including the payment prior to maturity of the Obligations.

In the event the Insurer were to become insolvent, any claims arising under a policy of financial guaranty insurance are excluded from coverage by the California Insurance Guaranty Association, established pursuant to Article 14.2 (commencing with Section 1063) of Chapter 1 of Part 2 of Division 1 of the California Insurance Code.

IN WITNESS WHEREOF, the Insurer has caused this policy to be executed in facsimile on its behalf by its duly authorized officers, this [DAY] day of [MONTH, YEAR].

MBIA Insurance Corporation

\_\_\_\_\_  
President

Attest:

\_\_\_\_\_  
Assistant Secretary

## APPENDIX K

### SUMMARY OF CERTAIN PROVISIONS OF THE MASTER BANK AGREEMENT

DWR has entered into a Master Credit, Liquidity and Participation Agreement with various lenders, JPMorgan Chase Bank in its capacity as administrative agent for such lenders, Bayerische Landesbank, Dexia Crédit Local and The Bank of New York, as co-syndication agents, and BNP Paribas as documentation agent (as supplemented, the “Master Bank Agreement”). Pursuant to the terms of the Master Bank Agreement, certain of the lenders have agreed to issue Letters of Credit in order to secure the payment of the principal of, interest on, Redemption Price of and Purchase Price of certain subseries of the Series 2005 Bonds and certain of the lenders have agreed to execute and deliver Liquidity Facilities in order to purchase certain subseries of the Series 2005 Bonds upon the tender thereof by the owner thereof in the event remarketing proceeds are not sufficient to pay the Purchase Price thereof and upon certain mandatory tenders. See the Series Descriptions following the cover of this Official Statement.

The Master Bank Agreement contemplates two types of lenders, Fronting Banks and Participating Banks. “Fronting Banks” are the entities that will issue Letters of Credit and Liquidity Facilities. Letters of Credit and Liquidity Facilities delivered to the Paying Agent in accordance with the terms of the Master Bank Agreement are referred to in this Appendix as “Enhancement Facilities”. “Participating Banks” are the entities that have agreed to purchase undivided participation interests in (1) unpaid drawings under Letters of Credit, (2) advances made to DWR, (3) Bank Bonds purchased with proceeds advanced pursuant to Enhancement Facilities and (4) rights accruing to the Applicable Fronting Bank under the Financing Documents (as defined below) as a result of the Applicable Fronting Bank honoring drawings under its Enhancement Facility and making advances.

Participating Banks in an Enhancement Facility are not required to make any payments to the owners of Series 2005 Bonds secured thereby. Accordingly, owners of Series 2005 Bonds secured by an Enhancement Facility should look solely to the Fronting Bank or Banks that issue such Enhancement Facility for payments thereunder.

Set forth below is a summary of certain provisions of the Master Bank Agreement as well as certain defined terms therein. Capitalized terms used in this Appendix and not otherwise defined in this Appendix shall be given the same meanings as those contained in body of this Official Statement. See APPENDIX G – “INDEX OF PRINCIPAL DEFINITIONS.”

#### Defined Terms

“Act” means, collectively, (a) Division 27 (commencing with Section 80000) of the California Water Code, as amended from time to time, and (b) the Chapter 7, Division 1, Title 2 of the California Government Code, the proclamation of the Governor of the State made on January 17, 2001, and Executive Order D-42-01 dated June 18, 2001, of the Governor of the State issued pursuant to the Chapter 7, Division 1, Title 2 of the California Government Code, as supplemented and amended from time to time, including but not limited to any regulations issued pursuant thereto, or any of them, as appropriate.

“Advance” means the amount of each Purchase Drawing that is deemed converted to an “advance” in accordance with the Master Bank Agreement.

“Applicable Bond Insurer” means, in the case of a Bond Insurance Policy, the entity that issues such Bond Insurance Policy.

“Applicable Financing Document” means, with respect to a subseries of Series 2005 Bonds, the Fourth Supplemental Trust Indenture among DWR, the Treasurer of the State, as trustee, and U.S. Bank National Association (also known as U.S. Bank, N.A.), as co-trustee, the Series 2005 Bonds of such subseries, any bond purchase agreement, any tender and paying agency agreement, any remarketing agreement, any Bond Insurance

Policy, in each case applicable to the Series 2005 Bonds of such subseries, and any notice of issuance in respect of any Enhancement Facility that secures Series 2005 Bonds of such subseries.

“Applicable Fronting Bank” means, for any subseries of Series 2005 Bonds secured by an Enhancement Facility, the Fronting Bank of such Enhancement Facility.

“Applicable Participating Banks” means, for any subseries of Series 2005 Bonds secured by an Enhancement Facility, the Participating Banks of such Enhancement Facility.

“Available Commitment” means, for a Liquidity Facility at any time, the maximum amount available to be advanced under such Liquidity Facility to purchase the applicable Series 2005 Bonds at such time determined in accordance with the terms of such Liquidity Facility.

“Bank” shall mean, as the context may require, a Fronting Bank, a Participating Bank or both.

“Bank Bonds” means Series 2005 Bonds purchased with the proceeds of a Purchase Drawing under an Enhancement Facility.

“Bank Rate” means, on any day, the (a) rate determined by the Administrative Agent to be the higher of (i) the prime lending rate on that date and (ii) the aggregate of the federal funds rate on that date plus 0.50% plus (b) a margin which varies over time. Except with respect to FSA Insured Liquidity Provider Bonds, interest that accrues at the Bank Rate under the Master Credit Agreement is not limited. Interest on FSA Insured Liquidity Provider Bonds is subject to a maximum accrual limitation of 30% per annum.

“Bond Insurance Policy” means, with respect to a subseries of Series 2005 Bonds, a bond insurance policy or financial guarantee that insures the timely payment of the principal of, and interest on, such subseries, including any Bank Bonds of such subseries, together with all endorsements thereto.

“Bond Insurer Event of Insolvency” means, with respect to an Applicable Bond Insurer, the occurrence and continuance of one or more of the following events: (a) the issuance, under the laws of the state of incorporation or formation of such Applicable Bond Insurer, of an order of relief, rehabilitation, reorganization, conservation, liquidation or dissolution of such Applicable Bond Insurer; (b) the commencement by such Applicable Bond Insurer of a voluntary case or other proceeding seeking an order for relief, rehabilitation, reorganization, conservation, liquidation or dissolution with respect to such Applicable Bond Insurer or its debts or claims under any bankruptcy, insolvency or other similar law in effect on or after the date of the Master Bank Agreement including, without limitation, the appointment of a trustee, receiver, liquidator, custodian, assignee, sequestrator or other similar official for such Applicable Bond Insurer or any substantial part of its property; (c) the commencement of an involuntary case or other proceeding seeking an order for relief, rehabilitation, reorganization, conservation, liquidation or dissolution with respect to such Applicable Bond Insurer or its debts or claims under any bankruptcy, insolvency or other similar law in effect on or after the effective date of the Master Bank Agreement, or seeking the appointment of a trustee, receiver, liquidator, custodian, assignee, sequestrator or other similar official for such Applicable Bond Insurer or any substantial part of its property, and such involuntary case or appointment remains undismissed and unstayed for a period of 60 days; (d) the consent of such Applicable Bond Insurer to any relief referred to in the preceding clause (c) in an involuntary case or other proceeding commenced against it; (e) the making by such Applicable Bond Insurer of a general assignment for the benefit of creditors; (f) the failure of such Applicable Bond Insurer to generally pay its debts as they become due or claims under any of its insurance policies as such claims are made; or (g) the board of directors or any senior officer of such Applicable Bond Insurer shall take any action to authorize any of the foregoing.

“Business Day” means any day of the year other than (a) a Saturday, (b) a Sunday, (c) a State legal holiday, (d) any day which shall be in Sacramento, California or the city in which the relevant office of the Administrative Agent, the Trustee or the Co-Trustee is located a legal holiday or a day on which banking institutions are authorized or required by law or other government action to close, and (e) with respect to Series

2005 Bonds of a subseries secured by an Enhancement Facility, any day which shall be in the city in which the relevant office of any Applicable Fronting Bank, applicable remarketing agent, applicable tender agent or the Paying Agent is located a legal holiday or a day on which banking institutions are authorized or required by law or other government action to close.

“Differential Interest Amount” means, with respect to the remarketing of any Bank Bond purchased from the proceeds of a Liquidity Facility, (a) the interest which has accrued on such Bank Bond at the Bank Rate up to but excluding the Business Day on which such Bank Bond is remarketed, less (b) the interest component of the remarketing proceeds received by the Administrative Agent upon the remarketing of such Bank Bond.

“Electric Power Fund” means the Department of Water Resources Electric Power Fund established in the State treasury.

“Electrical Corporation” has the meaning provided in the California Public Utilities Code and includes Pacific Gas and Electric Company, San Diego Gas & Electric Company and Southern California Edison.

“Excess Interest Amount” means the amount of interest that accrues on Bank Bonds purchased from the proceeds of a Liquidity Facility in excess of the payment cap set forth in the Master Credit Agreement.

“Financing Documents” means the Master Bank Agreement, each supplement thereto, each Letter of Credit, each Liquidity Facility, the custodian agreement among the administrative agent and the Tender Agent, certain fee letters, each notice of issuance of an Enhancement Facility, each assignment and acceptance agreement between Participating Banks, Bank Bonds, the Indenture, each supplemental indenture thereto, each Bond Insurance Policy relating to a subseries of Series 2005 Bonds secured by an Enhancement Facility, each tender and paying agency agreement relating to a subseries of Series 2005 Bonds secured by an Enhancement Facility, each remarketing agreement relating to a subseries of Series 2005 Bonds secured by an Enhancement Facility, the bond purchase agreement relating to a subseries of Series 2005 Bonds secured by an Enhancement Facility and the Rate Agreement.

“FSA/Dexia Liquidity Facility” means a Liquidity Facility executed and delivered by Dexia Crédit Local that secures Bonds that are also secured by a Bond Insurance Policy issued by Financial Security Assurance Inc.

“FSA Insured Liquidity Provider Bonds” means Bonds that are purchased with funds advanced pursuant to a FSA/Dexia Liquidity Facility.

“Governmental Authority” means any nation or government, any state (including the Governor of the State) or other political subdivision thereof, any central bank (or similar monetary or regulatory authority) thereof, any entity or officer exercising executive, legislative, judicial, regulatory or administrative functions of or pertaining to government, and any corporation or other entity owned or controlled, through stock or capital ownership or otherwise, by any of the foregoing.

“Key Documents” means the Master Bank Agreement, the Indenture and the Rate Agreement.

“Majority Banks” means, (a) in the case of all Participating Banks, Participating Banks whose Participation Commitments at any time when added together exceed 50% of the Participation Commitments of all Participating Banks at such time, or (b) in the case of the Participating Banks relating to a specific Enhancement Facility, Participating Banks whose Participation Commitments at any time in such Enhancement Facility when added together exceed 50% of the Participation Commitments of all Participating Banks in such Enhancement Facility at such time.

“Material Adverse Effect” means an event or occurrence, including, without limitation, (1) the adoption after the date of the Master Bank Agreement of a law, regulation, rule or order, decision or directive of a Governmental Authority and/or (2) the amendment, modification or repeal of a law, regulation, rule or order,

decision or directive of a Governmental Authority after the date of the Master Credit Agreement, (a) the effect of which could reasonably be expected to have a material adverse effect on the ability of DWR to prescribe, revise or collect its Revenue Requirement, (b) which adversely affects in a significant manner the ability of DWR to timely perform its material obligations under the Financing Documents to which it is a party, (c) which adversely affects the ability of the CPUC to timely establish Bond Charges and Power Charges in accordance with the Rate Agreement, (d) which materially adversely affects the enforceability of any Key Document or any Supplemental Indenture for a subseries of Series 2005 Bonds, (e) which materially adversely affects the privileges, rights and remedies of the Administrative Agent or any Bank under the Financing Documents to which any of them is a party or (f) which materially adversely affects the Trust Estate or the lien of the Trustee with respect thereto.

“Obligations” means all drawings made under Letters of Credit, Advances, Bank Bonds, principal, interest, fees, expenses, costs and other amounts owed to the Administrative Agent or any Bank pursuant to the terms of the Master Bank Agreement, any other Financing Document or any other document, instrument or agreement entered into by DWR with or in favor of the Administrative Agent or any Bank in connection therewith, together with all guaranties, covenants and duties owing by DWR to any of the foregoing of any kind or description, whether direct or indirect, absolute or contingent, due or to become due, existing on or arising after the effective date of the Master Bank Agreement.

“Participating Bank” means (a) with respect to a Letter of Credit, each of the Participating Banks that is obligated by the terms of the Master Bank Agreement to purchase participation interests in drawings honored thereunder and Advances made in accordance therewith and, to the extent the Fronting Bank of such Letter of Credit, retains any economic interest in reimbursement obligations arising from drawings made under such Letter of Credit, Advances made or deemed made in connection therewith and/or Bank Bonds purchased with the proceeds of Purchase Drawings made under such Letter of Credit, the Fronting Bank and (b) with respect to a Liquidity Facility, each of the participating Banks that is obligated by the terms of the Master Bank Agreement to purchase participation interests in Bank Bonds purchased in accordance therewith and, to the extent the Fronting Bank of such Liquidity Facility, retains any economic interest in Bank Bonds purchased with the proceeds of such Liquidity Facility and Excess Interest Amounts and Differential Interest Amounts arising therefrom, the Fronting Bank.

“Participation Commitment” means, for any Participating Bank and for any subseries of Series 2005 Bonds, the maximum dollar amount such Participating Bank is obligated to expend in order to purchase participating interests in unpaid drawings, Advances, Bank Bonds, Excess Interest Amounts and Differential Interest Amounts.

“Purchase Drawing” means, with respect to a Letter of Credit, a drawing made by the Paying Agent to purchase Series 2005 Bonds of the applicable subseries in accordance with the terms of such Letter of Credit, whether pursuant to an optional tender drawing or a mandatory tender drawing.

“Quarter End Date” means the last Business Day of each March, June, September and/or December.

“Rate Agreement” means the Rate Agreement dated as of March 8, 2002, between DWR and the CPUC.

“Revenue Requirement” means, (a) for the period from January 17, 2001 through and including December 31, 2002, \$9,045,462,000, and (b) for each calendar year thereafter, the amount determined by DWR as being necessary to enable DWR to comply with Section 80134 of the Water Code during such period.

“Service Area” means the geographic area in which an Electrical Corporation is required to distribute electricity.

“Specified Event” means a Key Event of Default, a Series Event of Default, a Liquidity Termination Event or a Liquidity Suspension Event.

“State” means the State of California.

“Stated Amount” means, for a Letter of Credit at any time, the maximum amount available to be drawn under such Letter of Credit at such time determined in accordance with the terms of such Letter of Credit.

### **Reimbursement of Drawings under Letters of Credit**

If the Fronting Bank of a Letter of Credit shall honor a drawing made under such Letter of Credit other than a Purchase Drawing, DWR shall, or shall cause the Paying Agent, the Co-Trustee or Trustee to, reimburse the aggregate amount of such drawing to the Administrative Agent on the business day on which such drawing is honored. If the Fronting Bank of a Letter of Credit honors payment of any Purchase Drawing, DWR shall be deemed to have requested, and such Fronting Bank shall be deemed to have made, an Advance to DWR on the date and in the amount of such Purchase Drawing. Each Advance made by the Fronting Bank of a Letter of Credit shall be payable in eleven equal installments following the termination date of such Letter of Credit, with the first such installment due on the first Quarter End Date that is at least six months after such termination date and with each subsequent installment due on each Quarter End Date occurring thereafter. Interest shall accrue on each Advance until it is repaid or prepaid in full, at a rate per annum equal to the Bank Rate. Interest on each Advance shall be payable in arrears (i) on each Quarter End Date of each year, (ii) on the date on which the Bank Bonds purchased with the proceeds of the Purchase Drawing which gave rise to such Advance mature, are redeemed or are remarketed and (iii) on each date on which such Advance is prepaid. Remarketing proceeds, Redemption Price and other payments, if any, received by the Administrative Agent in respect of Bank Bonds purchased pursuant to a Purchase Drawing made under a Letter of Credit shall be applied against the Advance derived from such Purchase Drawing.

### **Terms of Bank Bonds**

Any Bank Bond purchased by the Fronting Bank of a Liquidity Facility will bear interest at the Bank Rate for the period commencing from the date of purchase and continuing until such Bank Bond is paid in full or remarketed. Interest on any such Bank Bond shall be payable (i) on each Quarter End Date of each year; (ii) at maturity; (iii) upon redemption and (iv) on the date such Bank Bond is remarketed. Bank Bonds purchased pursuant to a Liquidity Facility shall be redeemed by DWR in nineteen equal installments (or, in the case of FSA/Dexia Liquidity Facilities, twenty-seven equal installments) following the termination date of such Liquidity Facility, with the first such installment due on the first Quarter End Date that is at least six months after such termination date and with each subsequent installment due on each Quarter End Date occurring thereafter; provided, however, if the redemption or sinking fund schedule for such Bank Bonds under the Indenture (absent their purchase by the Fronting Bank) would result in the payment or redemption in full of such Bank Bonds prior to the installment schedule described immediately above, then the Participating Banks in such Liquidity Facility may elect to have such Bank Bonds paid or redeemed in accordance with the redemption or sinking fund schedule for such Bank Bonds established in the Indenture. The redemption or payment price of such Bank Bonds shall be equal to the principal amount of the Bank Bonds being redeemed or paid plus accrued interest at the Bank Rate to the redemption or payment date.

### **Payment of Other Amounts**

Pursuant to the Master Bank Agreement, DWR has agreed to pay certain fees to the Administrative Agent, the Fronting Banks, the Participating Banks, to pay increased costs and compensate the Fronting Banks, the Participating Banks for loss of return in the event of certain changes in law and to indemnify to the maximum extent permitted by law the Administrative Agent, the Fronting Banks, the Participating Banks and certain other persons in certain circumstances. DWR has also agreed to pay, in the manner set forth in the Master Bank Agreement, (1) the interest component of the Purchase Price advanced by a Fronting Bank of a Liquidity Facility to purchase Bank Bonds, (2) Differential Interest Amounts and (3) Excess Interest Amount.

## Obligations Secured on a Parity with Bonds

The Obligations of DWR under the Master Bank Agreement are secured under the Indenture on a parity with debt service on the Bonds. See “SECURITY FOR THE BONDS – Accounts and Flow of Funds Under the Indenture” and “- Bond Related Costs.”

## Series Events of Default

The occurrence or existence of any of the following specified events shall each constitute a “Series Event of Default” with respect to a subseries of Series 2005 Bonds:

- (1) A Key Event of Default (as defined below under the caption “Key Events of Default”); or
- (2) DWR shall default, and such default shall continue unremedied for three or more Business Days, in the payment when due of (a) any interest on any unpaid drawing or Advance made (or deemed made) in respect of the Series 2005 Bonds of such subseries; (b) any interest on any Bank Bond of such subseries; or (iii) any Excess Interest Amount or any Differential Interest Amount owing in respect of the Series 2005 Bonds of such subseries; or
- (3) DWR shall default, and such default shall continue unremedied for ten or more calendar days after written notice thereof from the Administrative Agent or any Fronting Bank of any Enhancement Facility securing or formerly securing the Series 2005 Bonds of such subseries or any Participating Bank therein, in the payment when due of any fees or any other amounts (other than those amounts described in paragraph (1) under the caption “Key Events of Default” and paragraph (2) under the caption “Series Events of Default”) owing to any such Bank, any person that controls such Bank or any sub-participant of any such Bank under the Master Bank Agreement or under any Applicable Financing Document; or
- (4) Any representation, warranty or statement made by DWR in the Applicable Financing Documents to which it is a party for such subseries or in any certificate delivered pursuant thereto shall prove to be untrue in any material respect on the date as of which made or deemed made; or
- (5) (a) DWR shall default in the due performance or observance by it of any of the following terms, covenants or agreements: (i) the limitation on the use of the proceeds of the Bonds and amounts drawn or advanced under an Enhancement Facility; (ii) the failure to consult with the Administrative Agent and the Applicable Fronting Bank in connection with the removal and appointment of the Co-Trustee, the applicable Tender Agent or the applicable Remarketing Agent; (iii) the agreement of DWR to redeem Bank Bonds of a subseries prior to redeeming any other Series 2005 Bonds of such subseries; (iv) to return a Letter of Credit to the Fronting Bank thereof following payment by such Fronting Bank of a final drawing thereunder; (v) the agreement of DWR regarding the substitution of an existing Enhancement Facility for a new facility; or (vi) the agreement of DWR not to change a reference to a Fronting Bank in any disclosure document related to the Bonds without the prior written consent of such Fronting Bank, in each case as such terms, covenants and agreements apply to such subseries, any Enhancement Facility for Series 2005 Bonds of such subseries, the Obligations owing to any Fronting Bank of any Enhancement Facility that secures or formerly secured Series 2005 Bonds of such subseries and any Participating Bank therein, the Applicable Financing Documents for such subseries or the Applicable Fiduciaries for such subseries; or (b) DWR shall default in the due performance or observance by it of any term, covenant or agreement contained in the Applicable Financing Documents to which it is a party for such subseries and such default shall continue unremedied for a period of thirty days after receipt of written notice thereof from the Administrative Agent or any Fronting Bank of any Enhancement Facility securing or formerly securing the Series 2005 Bonds of such subseries or any Participating Bank therein; or

(6) The Supplemental Indenture for such subseries of Series 2005 Bonds or any material provision thereof shall (a) cease to be in full force and effect and, as a result thereof, a Material Adverse Effect occurs or could reasonably be expected to occur; or (b) be declared to be unconstitutional or null and void by any court of competent jurisdiction in a final non-appealable judgment and, as a result thereof, a Material Adverse Effect occurs or could reasonably be expected to occur; or

(7) For a subseries of Series 2005 Bonds secured by a Bond Insurance Policy and a Liquidity Facility, for an uninterrupted period of ninety days there is not in effect at least two of the following in respect of the Applicable Bond Insurer: (i) in the case of Fitch, Inc., a financial strength or claims paying ability rating of AA- (or its equivalent) or higher; (ii) in the case of Moody's Investors Service, Inc., a financial strength or claims paying ability rating of Aa3 (or its equivalent) or higher; and (iii) in the case of Standard & Poor's Ratings Service, a financial strength or claims paying ability rating of AA- (or its equivalent) or higher; or

(8) An "event of default" shall have occurred under the Supplemental Indenture for such subseries of Series 2005 Bonds.

### **Key Events of Defaults**

The occurrence or existence of any of the following specified events shall each constitute a "Key Event of Default":

(1) DWR shall default in the payment when due of any principal of any unpaid drawing, Advance or Bank Bond; or

(2) Any representation, warranty or statement made by DWR in the Master Bank Agreement, in the Indenture or the Rate Agreement or in any certificate delivered pursuant thereto shall prove to be untrue in any material respect on the date when made or deemed to be made; or

(3) (a) DWR shall default in the due performance or observance by it of any of the following terms, covenants or agreements: (i) the agreement of DWR to notify the Administrative Agent following the occurrence of a Specified Event; (ii) the agreement of DWR, subject to certain exceptions, not to amend, modify or terminate any provision of the applicable Bond Insurance Policy, certain provisions of the Rate Agreement and the Financing Documents or substitute a Bond Insurance Policy without certain consents; (iii) the agreement of DWR not to encumber the Trust Estate and to defend the lien of the Indenture over the Trust Estate; (iv) the agreement of DWR to redeem the Series 2005 Bonds of all subseries secured or formerly secured by an Enhancement Facility on a pro rata basis in the event it decides to redeem any of such Series 2005 Bonds; (v) the agreement of DWR to include in each Supplemental Indenture pursuant to which Series 2005 Bonds secured by an Enhancement Facility are issued (or to be issued), provisions granting to the Administrative Agent and/or the Applicable Fronting Bank certain consent rights, approval rights and rights to take action as the "owner" of the Series 2005 Bonds under the Indenture and the applicable Supplemental Indenture; or (vi) the agreement of DWR not to issue Bonds secured by the Trust Estate in an amount in excess of \$11,950,000,000; or

(b) DWR shall default in the due performance or observance by it of its agreement to provide: (i) notices with respect to: certain litigation, governmental proceedings, legislative developments, voter initiatives, official action of the Governor of the State, changes or withdrawals of DWR's unenhanced long term debt ratings; (ii) copies of all DWR filings with, and actions of, the CPUC in respect of certain matters; or (iii) a copy of any agreement between DWR and any other person to advance funds, loan money or extend credit or liquidity to DWR in connection with DWR's power supply program, and in each such case such default shall continue unremedied for a period of five Business Days from the occurrence of such default; or

- (c) DWR shall default in the due performance or observance by it of any term, covenant or agreement contained the Master Bank Agreement or any other Key Document (other than those referred to in paragraph 5(a) above under the caption “Series Event of Default” and in paragraphs (1), (2), 3(a) and (3)(b) immediately above) and such default shall continue unremedied for a period of thirty days after receipt by DWR of written notice thereof from the Administrative Agent or any Bank; or
- (4) The State shall default in the due performance or observance by it of its “no-impairment” covenant; or
- (5) (a) DWR shall (i) default in any payment of any debt secured by the Trust Estate (other than the Obligations) beyond the period of grace (not to exceed five days), if any, provided in the instrument or agreement under which such debt was created or (ii) default in the observance or performance of any agreement or condition relating to any debt secured by the Trust Estate (other than the Obligations) or contained in any instrument or agreement evidencing, guaranteeing, securing or relating to any such debt, or any other event shall occur or condition exist, the effect of which default or other event or condition is to cause, or to permit the holder or holders of any such debt (or a trustee or agent on behalf of such holder or holders) to cause (determined without regard to whether any notice is required), such debt to become due (whether by acceleration, purchase, repurchase, redemption or otherwise) prior to its stated maturity or cash collateral in respect thereof to be demanded; or (b) any debt of the type described in clause (a) above shall be declared to be due and payable, or required to be prepaid or purchased other than by a regularly scheduled required prepayment, prior to the stated maturity thereof; or
- (6) A moratorium, debt restructuring, debt adjustment or comparable restriction on repayment when due of monetary obligations secured by the Trust Estate or any part thereof is imposed by the State or any agency or department of the State; or
- (7) DWR shall deny or disaffirm its material obligations under any Key Document, or shall contest the validity or enforceability of any Key Document or any material provision thereof; or
- (8) The CPUC shall (a) default in the due performance or observance by it of its rate covenant contained in the Rate Agreement; (b) default in the due performance or observance by it of any other term, covenant or agreement contained in the Rate Agreement and, as a result thereof, a Material Adverse Effect occurs or could reasonably be expected to occur; (c) deny or disaffirm its material obligations under the Rate Agreement or any material provision thereof; or (d) contest the validity or enforceability of the Rate Agreement or any material provision thereof; or
- (9) Any Key Document or any material provision thereof shall (a) cease to be in full force and effect and, as a result thereof, a Material Adverse Effect occurs or could reasonably be expected to occur; (b) be suspended or stayed by any court, the CPUC or any other Governmental Authority and, as a result thereof, a Material Adverse Effect occurs or could reasonably be expected to occur; or (c) be declared to be unconstitutional or null and void by any court of competent jurisdiction in a final non-appealable judgment and, as a result thereof, a Material Adverse Effect occurs or could reasonably be expected to occur; or
- (10) The Act or any material provision thereof shall (i) cease to be in full force and effect and, as a result thereof, a Material Adverse Effect occurs or could reasonably be expected to occur; (ii) be suspended or stayed by any court, the CPUC or any other Governmental Authority and, as a result thereof, a Material Adverse Effect occurs or could reasonably be expected to occur; (iii) be declared to be unconstitutional or null and void by any court of competent jurisdiction in a final non-appealable judgment and, as a result thereof, a Material Adverse Effect occurs or could reasonably be expected to occur; or (iv) be repealed, modified or amended and, as a result thereof, a Material Adverse Effect occurs or could reasonably be expected to occur; or

(11) The failure, if such failure results in a Material Adverse Effect or could reasonably be expected to result in a Material Adverse Effect, (a) to transmit and distribute Power to the each customer within the Service Area of an Electrical Corporation that is deemed to purchase Power from DWR under the Act; (b) to bill such customers for Power distributed to such customers; (c) to attempt collection from such customers for Power distributed to such customers; (d) in the case of any person other than DWR, to hold in trust funds received from such customers in respect of Bond Charges and Power Charges; or (e) in the case of any person other than DWR, to remit to DWR or the Trustee on a timely basis funds received from such customers in respect of Bond Charges and Power Charges; or

(12) The adoption after the date of the Master Bank Agreement of a law, regulation, rule or order, decision or directive of a Governmental Authority (other than Assembly Bill 117 of the 2001-02 Regular Session of the California legislature, as enrolled on September 13, 2002) and/or the amendment, modification or repeal of a law, regulation, rule or order, decision or directive of a Governmental Authority after the date of the Master Bank Agreement (a “Change in Law”), other than a Change in Law that includes a provision for the imposition of surcharges on customers who acquire power from a supplier other than an Electrical Corporation or DWR that is, in the reasonable judgment of the Majority Banks, sufficient to compensate DWR for any foregone Bond Charges or Power Charges attributable to such customers, in either case that (a) enables a customer or customers within a Service Area to acquire electric power and energy from a supplier other than an Electrical Corporation or DWR and (b) results in a Material Adverse Effect or could reasonably be expected to result in a Material Adverse Effect; or

(13) The Trustee ceases to have a first priority lien over the Trust Estate; or

(14) An “event of default” shall have occurred under the Indenture or the Rate Agreement; or

(15) DWR, the Trustee or the Co-Trustee shall (a) apply for or consent to the appointment of, or the taking of possession by, a receiver, custodian, trustee (other than the Trustee or the Co-Trustee) or liquidator of the Electric Power Fund or of any part of the assets of the Electric Power Fund, (b) admit in writing the inability of the Electric Power Fund to pay its debts as such debts become due, (c) make a general assignment for the benefit of creditors of DWR that are secured by the Trust Estate, (d) commence a voluntary case or file a petition seeking to take advantage of any law relating to bankruptcy, insolvency, reorganization, winding-up, or composition or readjustment of debts or (e) fail to controvert in a timely and appropriate manner, or acquiesce in writing to, any petition filed against the Electric Power Fund in an involuntary case under any law described in the preceding clause; or

(16) A case or other proceeding shall be commenced without the application or consent of DWR, the Trustee or the Co-Trustee in any court of competent jurisdiction, seeking (a) the liquidation, reorganization, dissolution or winding-up of the Electric Power Fund, or the composition or readjustment of any debts of DWR secured by the Trust Estate, (b) the appointment of a trustee, receiver, custodian, liquidator or the like of the Electric Power Fund or any part of the assets of the Electric Power Fund or (c) similar relief in respect of the Electric Power Fund or any part of the assets of the Electric Power Fund under any law relating to bankruptcy, insolvency, reorganization, winding-up, or composition or readjustment of debts, or a warrant of attachment, execution, or similar process shall be issued against the Electric Power Fund or any assets therein, and such case, proceeding, warrant or process shall continue undismissed and unstayed and in effect for a period of 60 days, or an order, judgment or decree approving or ordering any of the foregoing shall be entered and continue unstayed and in effect, for a period of 60 days; or an order for relief against DWR, the Trustee or the Co-Trustee in respect of the Electric Power Fund shall be entered in an involuntary case under law relating to bankruptcy, insolvency, reorganization, winding-up, or composition or readjustment of debts.

## **Rights and Remedies: Letters of Credit**

Upon the occurrence and during the continuance of a Series Event of Default with respect to a subseries of Series 2005 Bonds that is secured by a Letter of Credit, the Majority Banks of such Letter of Credit may, in their sole discretion, instruct the Fronting Bank of such Letter of Credit to do any or all of the following:

(1) Deliver a written notice to the Paying Agent requiring the Paying Agent to (a) cause a mandatory purchase of all outstanding Series 2005 Bonds of such subseries and (b) submit a final drawing under such Letter of Credit to pay the Purchase Price of such Series 2005 Bonds upon their mandatory purchase; or

(2) Deliver (a) a written notice to the Paying Agent requiring the Paying Agent to (i) cause a mandatory purchase of all outstanding Series 2005 Bonds of such subseries and (ii) submit a mandatory purchase drawing under such Letter of Credit to pay the Purchase Price of such Series 2005 Bonds upon their mandatory purchase; and (b) a written notice to the remarketing agent(s) for the Series 2005 Bonds of such subseries instructing such remarketing agent(s) to cease remarketing such Series 2005 Bonds following their purchase from the proceeds of a mandatory purchase drawing under such Letter of Credit until such time, if any, as such remarketing agent(s) shall have received written notice from the Fronting Bank of such Letter of Credit to the effect that such Fronting Bank has reinstated in full the Stated Amount of such Letter of Credit; or

(3) Exercise any and all of the rights and remedies available to the Administrative Agent, the Applicable Fronting Bank and the Applicable Participating Banks under the Financing Documents to which it is a party, at law or equity (including, without limitation, the right to seek specific performance and/or a writ of mandamus).

## **Liquidity Termination Events; Automatic Termination of Liquidity Facility**

The following events each constitute a “Liquidity Termination Event” under each Liquidity Facility:

(1) DWR shall fail to pay, or cause to be paid, when due, or shall have declared a moratorium on the payment of the principal of, interest on or Redemption Price of, or repudiated, any subseries of Series 2005 Bonds secured by such Liquidity Facility and such payment is not paid by the Bond Insurer whose Bond Insurance Policy secures such subseries when, as and in the amounts required to be paid pursuant to the terms of such Bond Insurance Policy that secures such subseries; or

(2) A Bond Insurer Event of Insolvency shall have occurred with respect to the Bond Insurer whose Bond Insurance Policy secures such Series 2005 Bonds; or

(3) The financial strength or claims paying ability rating of the Applicable Bond Insurer is lower than Baa3 (or its equivalent), in the case of Moody’s Investors Service, Inc., and BBB- (or its equivalent), in the case of Standard & Poor’s Ratings Service.

Upon the occurrence of a Liquidity Termination Event for a Liquidity Facility, the Available Commitment under such Liquidity Facility and the obligation of the Applicable Fronting Bank to purchase Series 2005 Bonds secured by such Liquidity Facility shall immediately terminate without notice or demand or purchase and thereafter the Applicable Fronting Bank shall no longer be obligated to purchase such Series 2005 Bonds.

## **Liquidity Suspension Event; Suspension, Termination and Reinstatement of Liquidity Facility**

The following events each constitute a “Liquidity Suspension Event” under each Liquidity Facility:

(1) Any provision of the Bond Insurance Policy that secures the applicable subseries of Series 2005 Bonds that relates to or would affect the timely payment of the principal of, interest on or Redemption Price of such subseries of Series 2005 Bonds (a “material provision”) at any time for any reason ceases to be valid and binding on Bond Insurer that issued such Bond Insurance Policy in accordance with the terms of such Bond Insurance Policy or is declared, announced or ruled to be null and void by a court or other governmental agency of appropriate jurisdiction; or

(2) The validity or enforceability of any material provision of the Bond Insurance Policy that secures such subseries of Series 2005 Bonds is contested publicly or in writing by a senior authorized officer of the Bond Insurer that issued such Bond Insurance Policy or any governmental agency or authority with appropriate jurisdiction; or a senior authorized officer of such Bond Insurer denies publicly or in writing that such Bond Insurer has any further liability or obligation to honor claims made or to be made under its Bond Insurance Policy; or

(3) The commencement of an involuntary case or other proceeding seeking an order for relief, rehabilitation, reorganization, conservation, liquidation or dissolution with respect to the Bond Insurer whose Bond Insurance Policy secures the Series 2005 Bonds of a subseries that is also secured by such Initial Liquidity Facility or its debts or claims under any bankruptcy, insolvency or other similar law in effect on or after the effective date of the Master Bank Agreement, or seeking the appointment of a trustee, receiver, liquidator, custodian, assignee, sequestrator or other similar official for such Bond Insurer or any substantial part of its property.

Upon the occurrence of any Liquidity Suspension Event for a Liquidity Facility, the obligation of the Applicable Fronting Bank to purchase Series 2005 Bonds secured by such Liquidity Facility shall immediately be suspended without further action on the part of any Person until either the Applicable Fronting Bank delivers a rescission notice to the Paying Agent or, (a) in the case of a Liquidity Suspension Event of the type described in paragraphs (1) and (2) above, a final non-appealable order of a court having jurisdiction in the premises shall be entered declaring that all material contested provisions of the Bond Insurance Policy issued by such Applicable Bond Insurer are upheld in their entirety or (b) in the case of a Liquidity Suspension Event of the type described in paragraph (3) above, a court having jurisdiction in the premises shall dismiss or stay such involuntary case, proceeding or appointment within 60 days.

In the event a final non-appealable order is entered declaring any material provision of such Bond Insurance Policy to be null and void, or declaring that the Applicable Bond Insurer does not have any further liability or obligation under such Bond Insurance Policy or in the event an involuntary case, proceeding or appointment of the type described in paragraph (3) above is not dismissed or stayed within 60 days by a court having jurisdiction in the premises, then the obligation of the Applicable Fronting Bank to purchase Series 2005 Bonds secured by such Liquidity Facility shall immediately terminate without any further action by the Administrative Agent, any Applicable Fronting Agent or any Applicable Participating Bank.

In the event a final non-appealable order is entered declaring that all material contested provisions of such Bond Insurance Policy are upheld in their entirety or in the event a court having jurisdiction in the premises shall dismiss or stay any such involuntary case, proceeding or appointment of the type described in paragraph (3) above within 60 days, the obligation of the Applicable Fronting Bank to purchase Series 2005 Bonds secured by such Liquidity Facility shall be automatically reinstated and the terms of such Liquidity Facility will continue in full force and effect (unless such Liquidity Facility shall otherwise have terminated by its terms or there shall have occurred a Liquidity Termination Event or a different Liquidity Suspension Event) as if there had been no such suspension. Notwithstanding the foregoing, if the Applicable Fronting Bank has not delivered a rescission notice to the Co-Trustee and if, upon the earlier of (a) the termination date of such Liquidity Facility or (b) (i) in the case of a Liquidity Suspension Event of the type described in paragraphs (1) and (2) above, the date which is three years after the effective date of suspension of the obligation of the Applicable Fronting Bank to purchase Series 2005 Bonds secured by such Liquidity Facility, litigation is still pending and a judgment regarding the validity of such Bond Insurance Policy has not been obtained or (ii) in the case of a Liquidity Suspension Event of

the type described in paragraph (3) above, the date which is 60 days after the commencement of the involuntary case, proceeding or appointment, such involuntary case, proceeding or appointment has not been dismissed or stayed, then the Available Commitment of such Liquidity Facility and the obligation of the Applicable Fronting Bank to purchase Series 2005 Bonds secured by such Liquidity Facility shall at such time terminate without notice or demand and thereafter, the Applicable Fronting Bank shall be under no further obligation to purchase Series 2005 secured by such Liquidity Facility.

### **Bond Insurer Approved Events of Default; Remedy**

Each of the Series 2005G-10 Bonds, the Series 2005G-12 Bonds, the Series 2005G-13 Bonds and the Series 2005G-14 Bonds is to be insured by a Bond Insurance Policy to be issued by Financial Guaranty Insurance Company (“FGIC”). Each of the Series 2005G-3 Bonds, the Series 2005G-4 Bonds, the Series 2005G-5 Bonds, the Series 2005G-6 Bonds, the Series 2005G-7 Bonds and the Series 2005G-11 Bonds is to be insured by a Bond Insurance Policy to be issued by Financial Security Assurance Inc. (“FSA”). Each of the Series 2005G-8 Bonds and the Series 2005G-9 Bonds is to be insured by a Bond Insurance Policy to be issued by MBIA Insurance Corporation (“MBIA”).

Upon the occurrence and during the continuance of a Bond Insurer Approved Event of Default with respect to a subseries of Series 2005 Bonds, the Majority Banks of the Liquidity Facility securing such Series 2005 Bonds may terminate the Available Commitment thereunder by instructing the Administrative Agent to give written notice to DWR, the Trustee, the Co-Trustee, the Paying Agent, the applicable Remarketing Agent and the applicable Bond Insurer, specifying the date on which at 5:00 P.M., New York City time, the Available Commitment shall terminate, which termination date shall be not less than thirty days from the date of receipt of such written notice by the Paying Agent, and after such termination date the Applicable Fronting Bank shall be under no further obligation to purchase Series 2005 Bonds secured by such Liquidity Facility other than Series 2005 Bonds which are the subject of a notice of presentation delivered by the Paying Agent in accordance with such Liquidity Facility and received by the Administrative Agent on or prior to such termination date. Upon receipt of such a notice, the Co-Trustee is required to cause a mandatory tender of the Series 2005 Bonds. See “THE SERIES 2005 BONDS – Optional and Mandatory Tender for Purchase –*Mandatory Tender for Purchase.*”

The occurrence or existence of any of the following specified events shall each constitute a “Bond Insurer Approved Event of Default” with respect to all insured Series 2005 Bonds (the Series 2005G-3 Bonds through the Series 2005G-14 Bonds, inclusive):

(a) DWR shall default in the due performance or observance by it of any of the following agreements: (i) the agreement of DWR, subject to certain exceptions, not to amend, modify or terminate any provision of the applicable Bond Insurance Policy, certain provisions of the Rate Agreement and the Financing Documents or substitute a Bond Insurance Policy without certain consents or (ii) the agreement of DWR not to issue Bonds secured by the Trust Estate in an amount in excess of \$11,950,000,000; or

(b) The State shall default in the due performance or observance by it of its “no-impairment” covenant; or

(c) The State or any department or agency of the State imposes a moratorium, debt restructuring, debt adjustment or comparable restriction on repayment when due of monetary obligations secured by the Trust Estate or any part thereof; or

(d) DWR shall deny or disaffirm its material obligations under any Key Document, or shall contest the validity or enforceability of any Key Document or any material provision thereof; or

(e) The CPUC shall (a) default in the due performance or observance by it of its rate covenant contained in the Rate Agreement; (b) default in the due performance or observance by it of any other term, covenant or agreement contained in the Rate Agreement and, as a result thereof, a Material Adverse Effect occurs

or could reasonably be expected to occur; (c) deny or disaffirm its material obligations under the Rate Agreement or any material provision thereof; or (d) contest the validity or enforceability of the Rate Agreement or any material provision thereof; or

(f) Any Key Document or any material provision thereof shall (a) cease to be in full force and effect and, as a result thereof, a Material Adverse Effect occurs or could reasonably be expected to occur; (b) be suspended or stayed by any court, the CPUC or any other Governmental Authority and, as a result thereof, a Material Adverse Effect occurs or could reasonably be expected to occur; or (c) be declared to be unconstitutional or null and void by any court of competent jurisdiction in a final non-appealable judgment and, as a result thereof, a Material Adverse Effect occurs or could reasonably be expected to occur; or

(g) The Act or any material provision thereof shall (i) cease to be in full force and effect and, as a result thereof, a Material Adverse Effect occurs or could reasonably be expected to occur; (ii) be suspended or stayed by any court, the CPUC or any other Governmental Authority and, as a result thereof, a Material Adverse Effect occurs or could reasonably be expected to occur; (iii) be declared to be unconstitutional or null and void by any court of competent jurisdiction in a final non-appealable judgment and, as a result thereof, a Material Adverse Effect occurs or could reasonably be expected to occur; or (iv) be repealed, modified or amended and, as a result thereof, a Material Adverse Effect occurs or could reasonably be expected to occur; or

(h) The Trustee ceases to have a first priority Lien over the Trust Estate; or

(i) DWR or the Trustee shall (i) apply for or consent to the appointment of, or the taking of possession by, a receiver, custodian, trustee (other than the Trustee) or liquidator of the Electric Power Fund or of any part of the assets of the Electric Power Fund, (ii) admit in writing the inability of the Electric Power Fund to pay its debts as such debts become due, (iii) make a general assignment for the benefit of creditors of DWR that are secured by the Trust Estate, (iv) commence a voluntary case or file a petition seeking to take advantage of any law relating to bankruptcy, insolvency, reorganization, winding-up, or composition or readjustment of debts or (vi) fail to controvert in a timely and appropriate manner, or acquiesce in writing to, any petition filed against the Electric Power Fund in an involuntary case under any law described in the preceding clause; or

(j) A case or other proceeding shall be commenced without the application or consent of DWR or the Trustee in any court of competent jurisdiction, seeking (i) the liquidation, reorganization, dissolution or winding-up of the Electric Power Fund, or the composition or readjustment of any debts of DWR secured by the Trust Estate, (ii) the appointment of a trustee, receiver, custodian, liquidator or the like of the Electric Power Fund or any part of the assets of the Electric Power Fund or (iii) similar relief in respect of the Electric Power Fund or any part of the assets of the Electric Power Fund under any law relating to bankruptcy, insolvency, reorganization, winding-up, or composition or readjustment of debts, or a warrant of attachment, execution, or similar process shall be issued against the Electric Power Fund or any assets therein, and such case, proceeding, warrant or process shall continue undismissed and unstayed and in effect for a period of 60 days, or an order, judgment or decree approving or ordering any of the foregoing shall be entered and continue unstayed and in effect, for a period of 60 days; or an order for relief against DWR or the Trustee in respect of the Electric Power Fund shall be entered in an involuntary case under law relating to bankruptcy, insolvency, reorganization, winding-up, or composition or readjustment of debts; or

(k) DWR shall default, and such default shall continue unremedied for 90 or more calendar days after written notice thereof from the Administrative Agent or any Fronting Bank of any Liquidity Facility securing or formerly securing the Bonds of the Series described immediately above or any Participating Bank therein, in the payment when due of any commitment fees owing to any such Bank under the Master Bank Agreement; provided, however, that no Bond Insurer Approved Event of Default shall occur if the State or the applicable bond insurer causes such commitment fees to be timely paid; or

(l) DWR shall default, and such default shall continue unremedied for 180 or more calendar days after written notice thereof from the Administrative Agent or any Fronting Bank of any Liquidity Facility

securing or formerly securing the Bonds of the Series described immediately above or any Participating Bank therein, in the payment when due of any fees (other than those described in clause (m) above) or any other amounts (other than those amounts described in paragraph (1) under the caption “Liquidity Termination Events; Automatic Termination of Liquidity Facility”) owing to any such Bank, any parent of any such Bank or any sub-participant of any such Bank under the Master Bank Agreement or under any Applicable Financing Document; provided, however, that no Bond Insurer Approved Event of Default shall occur if the State or the applicable bond insurer causes such fees or other amounts to be timely paid; or

(m) The Supplemental Indenture for such Series of Bonds or any material provision thereof shall (i) cease to be in full force and effect and, as a result thereof, a Material Adverse Effect occurs or could reasonably be expected to occur; or (ii) be declared to be unconstitutional or null and void by any court of competent jurisdiction in a final non-appealable judgment and, as a result thereof, a Material Adverse Effect occurs or could reasonably be expected to occur; or

(n) For a Series of Bond secured by a Bond Insurance Policy and a Liquidity Facility, for an uninterrupted period of ninety days there is not in effect at least two of the following in respect of the Applicable Bond Insurer: (i) in the case of Fitch, Inc., a financial strength or claims paying ability rating of AA- (or its equivalent) or higher; (ii) in the case of Moody’s Investors Service, Inc., a financial strength or claims paying ability rating of Aa3 (or its equivalent) or higher; and (iii) in the case of Standard and Poor’s Ratings Service, a financial strength or claims paying ability rating of AA- (or its equivalent) or higher.

#### **Rights and Remedies: Liquidity Facilities**

Upon the occurrence of a Series Event of Default, a Liquidity Termination Event or a Liquidity Suspension Event with respect to a subseries of Series 2005 Bonds secured by a Liquidity Facility, the Administrative Agent, the Applicable Fronting Bank and the Applicable Participating Banks of the Liquidity Facility securing such Series 2005 Bonds may exercise any and all of the rights and remedies available to them under the Financing Documents, at law or in equity (including, without limitation, the right to seek specific performance and/or a writ of mandamus).

#### **Reduction of Available Commitment Under Liquidity Facility**

By causing notice to be delivered to the Fronting Bank of a Liquidity Facility, DWR may elect to reduce the Available Commitment of a Liquidity Facility at any time; provided that DWR may not elect to reduce the Available Commitment to an amount less than the sum of the Outstanding principal amount of Series 2005 Bonds supported thereby, together with the applicable interest coverage with respect to such Series 2005 Bonds.