*This Preliminary Official Statement and the information contained herein are subject to completion and amendment. Under no circumstances shall this Preliminary Official Statement constitute an offer to sell or the solicitation of an offer to buy, nor shall there be any sale of these Certificates in any jurisdiction in which such offer, solicitation or sale would be unlawful.*

**PRELIMINARY OFFICIAL STATEMENT DATED OCTOBER 21, 2011**

**SALE DATE: NOVEMBER 1, 2011**
**NEW ISSUE, BOOK-ENTRY ONLY**

**Moody's Rating: Aa2**
**(See "RATING")**

# $33,970,000*
# STATE OF WASHINGTON
# CERTIFICATES OF PARTICIPATION, SERIES 2011D
# (STATE AND LOCAL AGENCY REAL AND PERSONAL PROPERTY)

**Evidencing and Representing Undivided Proportionate Interests of the Owners Thereof in State Payments to be Made by the State of Washington Pursuant to the Master Financing Agreements**

**Dated: Date of Initial Delivery** **Due: January 1, as shown on page i hereof**

The State of Washington Certificates of Participation, Series 2011D (State and Local Agency Real and Personal Property) (the "Certificates"), will be executed and delivered in fully registered form under a book-entry only system, initially registered in the name of Cede & Co. (the "Owner"), as owner and nominee for The Depository Trust Company ("DTC"), New York, New York. DTC will act as securities depository for the Certificates. Individual purchases of the Certificates will be made in book-entry form only, in denominations of $5,000 and any integral multiple thereof. Purchasers of the Certificates will not receive certificates representing their beneficial ownership interests in the Certificates purchased, except as described herein.

The interest evidenced and represented by the Certificates is payable semiannually on each July 1 and January 1, beginning on July 1, 2012. Principal and interest evidenced and represented by the Certificates are payable directly to DTC by The Bank of New York Mellon as Fiscal Agent for the Certificates (the "Fiscal Agent"). Upon receipt of payments of principal and interest represented by the Certificates, DTC in turn is obligated to remit such payments to the DTC participants for subsequent disbursement to the purchasers of beneficial ownership interests in the Certificates. See "THE CERTIFICATES—Book-Entry System" and Appendix E—"DTC AND ITS BOOK-ENTRY SYSTEM."

The Certificates are subject to optional and extraordinary mandatory prepayment prior to their respective Principal Payment Dates. In addition, the Certificates will be subject to mandatory sinking fund prepayment prior to their respective Principal Payment Dates if Term Certificates are specified. See "THE CERTIFICATES—Prepayment."

The Certificates are being executed and delivered to finance and/or refinance the costs of acquisition and construction of certain real and personal property for the benefit of certain State Agencies and Local Agencies (together, the "Agencies") and to fund issuance costs with respect to the Certificates. The Certificates are being executed and delivered by the Fiscal Agent pursuant to a Trust Agreement among the Fiscal Agent, the Treasurer and the Washington Finance Officers Association (the "Corporation"), a Washington nonprofit corporation. The Certificates represent undivided proportionate interests in payments to be made by the state of Washington (the "state") under Master Financing Agreements between the Corporation and the state (the "State Payments").

Except as otherwise described herein, State Payments are payable from payments to be made pursuant to the Agency Financing Agreements, each between the state and the applicable Agency ("Agency Payments"). In the event that any Local Agency fails to make any payment due under its Agency Financing Agreement, the Treasurer is obligated to withhold an amount sufficient to make such payment from the Local Agency's share, if any, of state revenues or other amounts authorized or required by law to be distributed by the state to such Local Agency, if otherwise legally permissible. Upon the failure of any Local Agency to make any Agency Payment, the Treasurer is obligated further, to the extent of legally available appropriated funds and subject to any Executive Order reduction, to make the payment on behalf of the Local Agency. Agency Payments by any State Agency due under its Agency Financing Agreement are subject to appropriation and to any Executive Order reduction by the Governor. See "SECURITY FOR THE CERTIFICATES."

THE MASTER FINANCING AGREEMENTS, INCLUDING THE STATE AGENCY FINANCING ADDENDA AND STATE AGENCY FINANCING LEASE ADDENDA, CONSTITUTE SPECIAL, LIMITED OBLIGATIONS OF THE STATE PAYABLE SOLELY FROM THE SOURCES AND SUBJECT TO THE LIMITATIONS SET FORTH THEREIN. NONE OF THE STATE PAYMENTS, THE AGENCY PAYMENTS OR THE CERTIFICATES CONSTITUTE OR REPRESENT DEBT OR GENERAL OBLIGATIONS OF THE STATE OR ANY STATE AGENCY, AND NEITHER THE FULL FAITH AND CREDIT NOR THE TAXING POWER OF THE STATE NOR ANY STATE AGENCY IS PLEDGED TO THE PAYMENT OF ANY SUCH PAYMENTS OR THE PRINCIPAL OR INTEREST EVIDENCED AND REPRESENTED BY THE CERTIFICATES. THE STATE WILL NOT BE OBLIGATED TO PAY THE SAME EXCEPT FROM AGENCY PAYMENTS AND OTHER AMOUNTS AS PROVIDED IN THE MASTER FINANCING AGREEMENTS. ANY PAYMENTS BY THE TREASURER ON BEHALF OF A LOCAL AGENCY AND PAYMENTS BY A STATE AGENCY ARE SUBJECT TO APPROPRIATION BY THE LEGISLATURE AND TO EXECUTIVE ORDER REDUCTION BY THE GOVERNOR. A DETERMINATION BY THE LEGISLATURE NOT TO APPROPRIATE, OR ANY EXECUTIVE ORDER REDUCTION BY THE GOVERNOR, WOULD NOT CONSTITUTE AN EVENT OF DEFAULT UNDER THE TRUST AGREEMENT, THE MASTER FINANCING AGREEMENTS OR ANY STATE AGENCY FINANCING ADDENDA OR STATE AGENCY FINANCING LEASE ADDENDA.

*In the opinion of Certificate Counsel, under existing federal law and assuming compliance with applicable requirements of the Internal Revenue Code of 1986, as amended, that must be satisfied subsequent to the issue date of the Certificates, interest evidenced and represented by the Certificates is excluded from gross income for federal income tax purposes and is not an item of tax preference for purposes of the alternative minimum tax applicable to individuals. While interest evidenced and represented by the Certificates also is not an item of tax preference for purposes of the alternative minimum tax applicable to corporations, interest evidenced and represented by the Certificates received by corporations is taken into account in the computation of adjusted current earnings for purposes of the alternative minimum tax applicable to corporations, interest evidenced and represented by the Certificates received by certain S corporations may be subject to tax, and interest evidenced and represented by the Certificates received by foreign corporations with United States branches may be subject to a foreign branch profits tax. Receipt of interest evidenced and represented by the Certificates may have other federal tax consequences for certain taxpayers. See "TAX MATTERS."*

This cover page contains certain information for quick reference only. It is not a summary of this issue. Investors must read the entire Official Statement to obtain information essential to the making of an informed investment decision. The Certificates are offered when, as and if executed and delivered, subject to the receipt of the approving opinion of Foster Pepper PLLC, Seattle, Washington, Certificate Counsel to the state, and certain other conditions. Certain legal matters in connection with the preparation of this Official Statement will be passed upon for the state by Foster Pepper PLLC, Seattle, Washington, as Disclosure Counsel to the state.

It is anticipated that the Certificates will be available for delivery through the facilities of DTC in New York, New York, or to the Fiscal Agent on behalf of DTC by Fast Automated Securities Transfer on or about November 16, 2011.

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* Preliminary, subject to adjustment by the state as provided in the Official Notice of Sale.

No dealer, broker, salesperson, or other person has been authorized by the state to give any information or to make any representations with respect to the Certificates other than those contained in this Official Statement and, if given or made, such information or representations must not be relied upon. 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 Certificates by any person in any jurisdiction in which it is unlawful for such person to make such offer, solicitation or sale.

The information set forth herein has been obtained from sources which are believed to be current and reliable. The state, however, makes no representation regarding the accuracy or completeness of the information in Appendix E–"DTC AND ITS BOOK-ENTRY SYSTEM" provided by DTC. Estimates and opinions should not be interpreted as statements of fact. Summaries of documents do not purport to be complete statements of their provisions and such summaries are qualified by references to the entire contents of the summarized documents. The information and expressions of opinion herein are subject to change without notice, and neither the delivery of this Official Statement nor any sale made by use of this Official Statement shall, under any circumstances, create any implication that there has been no change in the affairs of the state since the date hereof.

In connection with the offering of the Certificates, the Underwriter may overallot or effect transactions which stabilize or maintain the market price of the Certificates at levels above that which might otherwise prevail in the open market. Such stabilizing, if commenced, may be discontinued or recommenced at any time.

The presentation of certain information, including tables of receipts from taxes and other revenues, 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 the state. No representation is made that past experience, as it might be shown by such financial and other information, will necessarily continue to be repeated in the future.

This Official Statement contains forecasts, projections and estimates that are based upon expectations and assumptions that existed at the time such forecasts, projections and estimates were prepared. In light of the important factors that may materially affect economic conditions in the state, the inclusion in this Official Statement of such forecasts, projections and estimates should not be regarded as a representation by the state that such forecasts, projections and estimates will occur. Such forecasts, projections and estimates are not intended as representations of fact or as guarantees of results.

If and when included in this Official Statement, the words "plan," "expect," "forecast," "estimate," "budget," "project," "intends," "anticipates" and similar words are intended to identify forward-looking statements, and any such statements inherently are subject to a variety of risks and uncertainties that could cause actual results to differ materially from those projected. Such risks and uncertainties include, among others, general economic and business conditions, changes in political, social and economic conditions, regulatory initiatives and compliance with governmental regulations, litigation and various other events, conditions and circumstances, many of which are beyond the control of the state. These forward-looking statements speak only as of the date they were prepared.

The Certificates will not be registered under the Securities Act of 1933, as amended, in reliance upon an exception contained in such act.

This Preliminary Official Statement has been "deemed final" as of its date by the state pursuant to Rule 15c2-12 (the "Rule") of the Securities and Exchange Commission promulgated under the Securities Exchange Act of 1934, as amended, except for the omission of material permitted to be omitted by such Rule.

## CERTIFICATE PAYMENT SCHEDULE

**$33,970,000 [1]**
**STATE OF WASHINGTON**
**CERTIFICATES OF PARTICIPATION, SERIES 2011D**
**(STATE AND LOCAL AGENCY REAL AND PERSONAL PROPERTY)**

**Evidencing and Representing Undivided Proportionate Interests of the Owners Thereof in State Payments to be Made by the State of Washington Pursuant to the Master Financing Agreements**

| Principal Payment Date (January 1) | Principal Component[2] | Interest Rate | Yield | Price | CUSIP Number[3] |
|---|---|---|---|---|---|
| 2013 | $ 3,575,000 | % | % | % | |
| 2014 | 3,780,000 | | | | |
| 2015 | 3,905,000 | | | | |
| 2016 | 3,715,000 | | | | |
| 2017 | 2,375,000 | | | | |
| 2018 | 1,860,000 | | | | |
| 2019 | 1,940,000 | | | | |
| 2020 | 1,355,000 | | | | |
| 2021 | 1,410,000 | | | | |
| 2022 | 1,485,000 | | | | |
| 2023 | 1,105,000 | | | | |
| 2024 | 1,155,000 | | | | |
| 2025 | 810,000 | | | | |
| 2026 | 860,000 | | | | |
| 2027 | 890,000 | | | | |
| 2028 | 685,000 | | | | |
| 2029 | 710,000 | | | | |
| 2030 | 745,000 | | | | |
| 2031 | 790,000 | | | | |
| 2032 | 820,000 | | | | |
| Total | $33,970,000 | | | | |

(1) Preliminary, subject to adjustment by the state as provided in the Official Notice of Sale.
(2) Preliminary, subject to adjustment by the state as provided in the Official Notice of Sale. These amounts will constitute principal components of Certificates unless Term Certificates are specified by the successful bidder, in which case these amounts will constitute mandatory sinking fund prepayments of Term Certificates; provided, however, that no principal component with a principal payment date on or before January 1, 2022, may be combined with a principal component with a principal payment date on or after January 1, 2023, in a single Term Certificate.
(3) CUSIP® is a registered trademark of the American Bankers Association. The CUSIP data herein is provided by the CUSIP Global Services, managed on behalf of the American Bankers Association by Standard and Poor's. The CUSIP numbers are not intended to create a database and do not serve in any way as a substitute for CUSIP service. CUSIP numbers have been assigned by an independent company not affiliated with the state and are provided solely for convenience and reference. The CUSIP numbers for a specific maturity are subject to change after the issuance of the Certificates. Neither the state nor the Underwriter takes responsibility for the accuracy of the CUSIP numbers.

## PARTICIPATING AGENCIES

The proceeds received from the sale of the Certificates will be applied to finance and/or refinance the costs of acquisition and construction of the following items of real and personal property for the following participating State Agencies and Local Agencies:

| Term (years) | Agency Name | Property | Amount[1] |
|---|---|---|---|
| 3 | Consolidated Technology Services[2] | IT data equipment | $81,126 |
| 3 | Lower Columbia College[2] | machinery and medical equipment | 211,177 |
| 3 | Benton Fire Protection District 2 | Two ambulances | 255,000 |
| 3 | Consolidated Technology Services[2] | Computer equipment | 382,135 |
| 4 | Consolidated Technology Services[2] | Computer equipment | 47,965 |
| 4 | Consolidated Technology Services[2] | IT data equipment | 133,279 |
| 4 | Dept of Enterprise Services[2] | Computer and IT data equipment | 210,265 |
| 4 | Consolidated Technology Services[2] | IT data equipment | 232,650 |
| 4 | Dept of Enterprise Services[2] | Computer equipment | 338,470 |
| 4 | Dept of Enterprise Services[2] | Computer equipment | 348,214 |
| 4 | Dept of Enterprise Services[2] | Computer and IT data equipment | 396,668 |
| 4 | Dept of Enterprise Services[2] | Computer equipment | 401,206 |
| 4 | Dept of Enterprise Services[2] | Computer equipment | 538,071 |
| 4 | Dept of Enterprise Services[2] | Computer equipment | 1,272,713 |
| 4 | Dept of Enterprise Services[2] | Computer equipment | 1,660,333 |
| 5 | Camano Mosquito District | Truck | 25,000 |
| 5 | Department of Agriculture[2] | Truck | 27,973 |
| 5 | University of Washington[2] | Laboratory equipment | 62,812 |
| 5 | Consolidated Technology Services[2] | IT data equipment | 88,998 |
| 5 | City of Milton | Three Police Cruisers | 95,000 |
| 5 | Dept of Enterprise Services[2] | Parking meters | 130,000 |
| 5 | Consolidated Technology Services[2] | Telecom equipment | 157,590 |
| 5 | Dept of Fish and Wildlife[2] | Trucks | 286,102 |
| 5 | Klickitat Public Hospital District 1 | Hospital Equipment | 300,000 |
| 5 | City of Goldendale | Automated Meter Reading System | 450,000 |
| 5 | Metropolitan Park District of Tacoma | Fleet vehicles | 550,000 |
| 5 | Consolidated Technology Services[2] | IT data equipment | 762,852 |
| 7 | Consolidated Technology Services[2] | Telecom equipment | 25,537 |
| 7 | Consolidated Technology Services[2] | Telecom equipment | 43,269 |
| 7 | Consolidated Technology Services[2] | Telecom equipment | 82,323 |
| 7 | Consolidated Technology Services[2] | Telecom equipment | 115,901 |
| 7 | Consolidated Technology Services[2] | Telecom equipment | 1,927,731 |
| 7 | Consolidated Technology Services[2] | IT data equipment | 2,089,841 |
| 10 | Washington State University[2] | Sloan Hall energy upgrades | 68,652 |
| 10 | Washtucna School District 109 43 | HVAC system | 83,000 |
| 10 | City of Des Moines | Energy projects | 115,000 |
| 10 | Lewis Fire Protection District 3 | Ambulance | 119,491 |
| 10 | San Juan County [3] | Park renovation/development | 120,000 |
| 10 | Wishkah Valley School District 117 | Energy efficiency project | 120,000 |
| 10 | Whatcom Fire Protection District 19 | Fire suppression/wildland fire truck. | 150,000 |
| 10 | Northport School District 211 | Boiler | 162,162 |
| 10 | City of Leavenworth | Street Sweeper | 185,000 |
| 10 | Washington State University[2] | Pullman Info Tech Bldg utility upgrade | 273,663 |
| 10 | Dept of Social and Health Services[2] | Energy projects | 300,922 |
| 10 | Quincy School District 144-101 | Energy efficiency projects | 305,224 |
| 10 | Lewis Co Fire Protection District 12 | Fire Engine | 374,517 |
| 10 | Vancouver School District 37 | Energy efficiency project | 392,201 |
| 10 | City of Omak | Aerial Fire Truck | 429,500 |
| 10 | North Mason School District 403 | Energy efficiency upgrades | 505,000 |
| 12 | Metropolitan Park District of Tacoma | Energy efficiency project | 4,100,000 |
| 15 | Metropolitan Park District of Tacoma | Energy efficiency project | 1,000,000 |
| 15 | Columbia Basin College[2] | Energy project | 2,037,904 |
| 20 | City of Grandview [3] | Acquisition of joint library building | 750,000 |
| 20 | Wenatchee Valley College [2][3] | Construction of music & art building | 2,700,000 |
| 20 | Dept of Social and Health Services[2][3] | Construction of juvenile facilities | 8,500,000 |

(1) Preliminary, subject to adjustment.
(2) State Agency.
(3) Real Property Participant.

**STATE FINANCE COMMITTEE**
**OF THE**
**STATE OF WASHINGTON**

JAMES L. McINTIRE ..... Treasurer and Chairman

CHRISTINE O. GREGOIRE.....Governor and Member

BRAD OWEN .....Lieutenant Governor and Member

---

Ellen L. Evans.....Deputy State Treasurer—Debt Management

**CERTIFICATE COUNSEL AND DISCLOSURE COUNSEL TO THE STATE**

Foster Pepper PLLC
Seattle, Washington

**FINANCIAL ADVISOR TO THE STATE**

SDM Advisors, Inc.
Mount Vernon, Washington

This Official Statement will be available upon request to the Office of the State Treasurer. This Official Statement is available via the Internet at the Office of the State Treasurer's Home Page:

**http://www.tre.wa.gov/investors/investorinformation.shtml**

The availability of this Official Statement via the Internet will not under any circumstances create any implication that there has been no change in the affairs of the state since the date hereof, or that the statements and information herein are current as of any date after the date hereof.

The website of the state or any state department or agency is not part of this Official Statement, and investors should not rely on information presented in the state's website, or on any other website referenced herein, in determining whether to purchase the Certificates. Information appearing on any such website is not incorporated by reference in this Official Statement.

## CONTACT INFORMATION

| | |
|---|---|
| **Office of the State Treasurer** | Legislative Building<br>Second Floor, Room 230<br>416 Sid Snyder Avenue SW<br>Olympia, Washington 98501<br>Phone: (360) 902-9000 |
| **Fiscal Agent** | The Bank of New York Mellon<br>Global Corporate Trust-Public Finance<br>101 Barclay Street, 21st Floor<br>New York, New York 10286<br>Phone: (800) 438-5473 |
| **Certificate Counsel and Disclosure Counsel** | Foster Pepper PLLC<br>1111 Third Avenue, Suite 3400<br>Seattle, Washington 98101<br>Phone: (206) 447-4400 |
| **Financial Advisor** | SDM Advisors, Inc.<br>P.O. Box 2469<br>Mount Vernon, Washington 98273<br>Phone: (360) 445-0138<br>Email: advisors@SDMadvisors.com |

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**OFFICIAL NOTICE OF SALE**

**$33,970,000***

**STATE OF WASHINGTON**
**CERTIFICATES OF PARTICIPATION, SERIES 2011D**
**(STATE AND LOCAL AGENCY REAL AND PERSONAL PROPERTY)**

**Evidencing and Representing Undivided Proportionate Interests of the Owners Thereof in State Payments to be Made by the State of Washington Pursuant to the Master Financing Agreements**

Electronic bids will be received on behalf of the State of Washington (the "state") at the Office of the Treasurer, Legislative Building, Second Floor, Room 230, 416 Sid Snyder Avenue SW, Olympia, Washington, for the purchase of the above-referenced certificates of participation (the "Certificates") at

**8:30 A.M., PACIFIC TIME, ON NOVEMBER 1, 2011.**

The Certificates will be sold on an all-or-none basis. Bids must be submitted electronically via the Qualified Electronic Bid Provider (defined below). See "Bidding Detail."

All bids received on behalf of the state by the bid time set forth above on such date will be reviewed and verified beginning at that time, by staff acting for the Treasurer's Representative. Bids received after the bid time will not be considered. Bids will be announced and considered subsequently.

Bidders are referred to the Preliminary Official Statement for additional information regarding the state, the Certificates, the security therefor, and other matters.

***Modification; Cancellation; Postponement.*** Bidders are advised that the Treasurer's Representative may modify the terms of sale of the Certificates prior to the bidding. If such modification occurs, supplemental information with respect to the sale of the Certificates will be placed on The Bond Buyer Wire (available on TM3, the Thomson Municipal Market Monitor, at *http://www.tm3.com*, which website is not incorporated herein by reference) (the "News Service") prior to 8:30 a.m., Pacific Time, on the date bids are to be received. In addition, the Treasurer's Representative may cancel or postpone the date and time for the receipt of bids at any time prior to the opening of the bids. Notice of such cancellation or postponement will be communicated by the Treasurer's Representative through the News Service as soon as practicable following such cancellation or postponement. If a postponement occurs, bids will be received at the hour and place set forth above on any weekday as the Treasurer's Representative determines. As an accommodation to bidders, telephonic or facsimile notice of the postponement of the sale date and of the new sale date will be given to any bidder requesting such notice from the SDM Advisors, Inc., financial advisor to the state, at telephone: (360) 445-0138. Failure of any bidder to receive such notice by telephone, facsimile or the News Service will not affect the legality of the sale.

Each bidder (and not the Treasurer's Representative or the state) is responsible for the timely electronic delivery of its bid. The official time will be determined by the Treasurer's Representative and not by any bidder or Qualified Electronic Bid Provider.

* Preliminary, subject to adjustment by the state as provided in this Official Notice of Sale.

**Description of the Certificates**

***The Certificates.*** The Certificates, evidencing and representing principal in the aggregate amount of $33,970,000,* will be dated as of their date of initial delivery, which is expected to be November 16, 2011, and will be executed and delivered in fully registered form in denominations of $5,000 and any integral multiple thereof. The Certificates will evidence and represent interest at such rate or rates as are fixed at the time of sale, payable semiannually on each January 1 and July 1, beginning July 1, 2012.

The portions of the State Payments designated as principal and evidenced and represented by the Certificates will be payable on January 1 of each year as follows:

| Principal Payment Date (January 1)* | Principal Component* |
|---|---|
| 2013 | $ 3,575,000 |
| 2014 | 3,780,000 |
| 2015 | 3,905,000 |
| 2016 | 3,715,000 |
| 2017 | 2,375,000 |
| 2018 | 1,860,000 |
| 2019 | 1,940,000 |
| 2020 | 1,355,000 |
| 2021 | 1,410,000 |
| 2022 | 1,485,000 |
| 2023 | 1,105,000 |
| 2024 | 1,155,000 |
| 2025 | 810,000 |
| 2026 | 860,000 |
| 2027 | 890,000 |
| 2028 | 685,000 |
| 2029 | 710,000 |
| 2030 | 745,000 |
| 2031 | 790,000 |
| 2032 | 820,000 |
| Total | $33,970,000 |

***Adjustment of Principal.*** The Treasurer's Representative has reserved the right to adjust the foregoing principal components upward or downward. However, the principal component due on any Principal Payment Date may not be adjusted by more than 10 percent, and the aggregate of such upward and downward adjustments will not exceed 10 percent. Notice of any adjustment will be provided by the Treasurer's Representative to the successful bidder no later than 12:00 noon, Pacific Time, on the date bids are to be received. The state is not responsible in the event and to the extent that any such adjustment affects the net compensation to be realized by the successful bidder.

***Term Certificates.*** Bidders have the option to designate the total Principal Component payable on any two or more consecutive Principal Payment Dates for the Certificates as mandatory prepayments with

* Preliminary, subject to adjustment by the state as provided in this Official Notice of Sale. These amounts will constitute principal components of Certificates unless Term Certificates are specified by the successful bidder, in which case these amounts will constitute mandatory sinking fund prepayments of Term Certificates. See "Description of the Certificates-*Term Certificates*."

respect to the Term Certificates; provided, however, that no Principal Component with a Principal Payment date on or before January 1, 2022, may be combined with a Principal Component with Principal Payment Date on or after January 1, 2023, in a single Term Certificate. If no Term Certificates are designated, the Principal Components represented by Certificates payable on each Principal Payment Date will be as set forth above in this Official Notice of Sale, subject to adjustment as provided in this Official Notice of Sale.

***Optional Prepayment.*** The Certificates with Principal Payment Dates on and after January 1, 2023, are subject to prepayment prior to their respective stated Principal Payment Dates, as a whole, or in part in Authorized Denominations, on any date on or after January 1, 2022, upon the exercise by the state at the direction of any Agency of its option to prepay the Principal Components evidenced and represented by those Certificates, at the Prepayment Price (expressed as a percentage of the Principal Components prepaid) of 100 percent, plus accrued interest, if any, evidenced and represented thereby to the Prepayment Date.

***Extraordinary Mandatory Prepayment.*** The Certificates are subject to mandatory prepayment on any date prior to their respective Principal Payment Dates, as a whole, or in part in Authorized Denominations, upon certain governmental takings, loss of title and casualty loss, from amounts deposited in the Prepayment Account in the amount of the Principal Component evidenced and represented thereby being prepaid, plus accrued interest, if any, evidenced and represented thereby to the Prepayment Date, and without premium.

***Mandatory Prepayment.*** If any of the Certificates are designated as Term Certificates by the successful bidder, those Certificates are subject to mandatory prepayment prior to their respective Principal Payment Dates in the amount of the Principal Component evidenced and represented thereby being prepaid, plus accrued interest evidenced and represented thereby to the Prepayment Date, and without premium. See "Term Certificates."

***Book-Entry Only.*** The Certificates will be registered in the name of Cede & Co., as nominee of The Depository Trust Company ("DTC"), New York, New York. DTC will act as securities depository for the Certificates. Individual purchases will be made in book-entry form only, and purchasers will not receive physical certificates representing their interests in the Certificates purchased. See Appendix E–"DTC AND ITS BOOK-ENTRY SYSTEM" in the Preliminary Official Statement.

**Purpose**

The Certificates are being executed and delivered to finance and/or refinance the costs of acquisition and construction of certain real and personal property and improvements for the benefit of certain Agencies, as shown on the table entitled "Participating Agencies" on page ii, and to pay issuance costs with respect to the Certificates.

**Security**

For a description of the security for the Certificates, see "SECURITY FOR THE CERTIFICATES" in the Preliminary Official Statement.

**Bidding Detail**

***Electronic Bids.*** Electronic bids for the Certificates must be submitted via a Qualified Electronic Bid Provider only. The state has designated Parity® as the Qualified Electronic Bid Provider for purposes of

receiving electronic bids for the Certificates. By designating a bidding service as a Qualified Electronic Bid Provider, the state does not endorse the use of such bidding service.

A bidder submitting an electronic bid for the Certificates thereby agrees to the following terms and conditions:

(1) If any provision in this Official Notice of Sale with respect to the Certificates conflicts with information or terms provided or required by the Qualified Electronic Bid Provider, this Official Notice of Sale, including any amendments issued through the News Service, shall control.

(2) Each bidder will be solely responsible for making necessary arrangements to access the Qualified Electronic Bid Provider for purposes of submitting its bid in a timely manner and in compliance with the requirements of this Official Notice of Sale.

(3) The state shall not have any duty or obligation to provide or assure access to the Qualified Electronic Bid Provider to any bidder, and the state shall not be responsible for proper operation of, or have any liability for, any delays, interruptions or damages caused by use of the Qualified Electronic Bid Provider or any incomplete, inaccurate or untimely bid submitted by any bidder through the Qualified Electronic Bid Provider.

(4) The state is permitting use of the Qualified Electronic Bid Provider as a communication mechanism, and not as the state's agent, to conduct the electronic bidding for the Certificates. The Qualified Electronic Bid Provider is acting as an independent contractor, and is not acting for or on behalf of the state.

(5) The state is not responsible for ensuring or verifying bidder compliance with any Qualified Electronic Bid Provider procedures.

(6) If the bidder's bid is accepted by the state, this Official Notice of Sale and the information that is transmitted electronically through the Qualified Electronic Bid Provider shall form a contract, and the bidder shall be bound by the terms of such contract.

(7) Information provided by the Qualified Electronic Bid Provider to bidders shall form no part of any bid or of any contract between the successful bidder and the state unless that information is included in this Official Notice of Sale.

Further information about the Qualified Electronic Bid Provider, including any fees charged, may be obtained by calling Bidcomp/Parity® at (212) 849-5021.

***Form of Bids.*** Bids for the Certificates must be unconditional, and for not less than all of the Certificates. By submitting a bid, each bidder agrees to all of the terms and conditions of this Official Notice of Sale, as they may be modified in accordance herewith. Bids for the Certificates must be submitted electronically via the Qualified Electronic Bid Provider. Bids may not be withdrawn or revised after the time that bids are due.

***Interest Rates Bid.*** Bidders for the Certificates may specify any number of interest rates in multiples of one-eighth or one-twentieth of one percent (1/8 or 1/20 of 1 percent), or both. The state does not require the use of ascending coupons. Bidders may not specify more than one interest rate with respect to Certificates with a common Principal Payment Date. Each Certificate must evidence and represent interest from its date to its respective Principal Payment Date. Each Principal Component must be reoffered at a yield that will produce a price of not less than 97 percent.

***Premium and Discount.*** No bid will be considered that offers to pay an amount less than 98 percent ($33,290,600) nor more than 112 percent ($38,046,400) of the aggregate Principal Components evidenced and represented by the Certificates.

**Selection of Winning Bid**

The Certificates will be sold to the bidder submitting a bid in conformance with this Official Notice of Sale that produces the lowest true interest cost ("TIC") to the state, based on the bid price, the interest rates specified in the electronic bid and the Principal Components identified in this Official Notice of Sale. The TIC will be the rate necessary, when using 360-day year and semiannual compounding, to discount the Principal and Interest Components with respect to the Certificates from the respective Principal Payment Dates to the initial delivery date of the Certificates (currently anticipated to be November 16, 2011) and to the price bid.

The successful bidder will be bound to purchase the Certificates with the Principal Components specified in this Official Notice of Sale, with adjustments, if any, as permitted herein, at such price, and with such interest rates, as are specified in its bid. If there are adjustments to the Principal Components payable on individual Principal Payment Dates, the premium or discount bid by the successful bidder will be adjusted to take into account original issue premiums or discounts for those Principal Payment Dates.

**Right of Rejection**

The Treasurer Representative reserves the right to reject any or all bids and to waive any irregularity in any bid. In the event that two or more bidders submit bids at the same lowest TIC, the Treasurer's Representative will determine which bidder is awarded the Certificates in her sole discretion.

**Good Faith Deposit**

The successful bidder shall deliver a good faith deposit in the amount of $500,000 to the Treasurer. The good faith deposit may be paid in one of the following ways:

(1) By federal funds wire transfer delivered no later than 90 minutes following the successful bidder's receipt of the verbal award. Wiring instructions will be provided to the successful bidder at the time of the verbal award.

(2) By certified or bank cashier's check made payable to the order of the State Treasurer and delivered to the Treasurer prior to the time of receipt of the bids.

Any good faith deposit submitted by a bidder whose bid is not accepted shall be returned promptly by the state, but the state shall not be liable for interest for any delay in such return.

If the bid is accepted, the good faith deposit will be deposited by the Treasurer and be applied to the purchase price of the Certificates when the same are delivered and paid for under the terms of the bid, or shall be retained as and for liquidated damages in case the successful bidder fails to accept the Certificates when ready for delivery or fails to complete payment therefor in accordance with the terms of the bid. Pending delivery of the Certificates, the good faith deposit may be invested for the sole benefit of the state.

**Insurance; Rating**

***Insurance.*** The purchase of any insurance policy for the Certificates or the issuance of any commitment therefor will be at the sole option and expense of the successful bidder for the Certificates. Bids for the Certificates may not be conditioned upon obtaining municipal bond insurance or any other credit enhancement, and any increased costs of issuance of the Certificates resulting by reason of such insurance shall be paid by the successful bidder and shall not, in any event, be paid by the state. Payment of any insurance premium and satisfaction of any conditions to the issuance of a municipal bond insurance policy is the sole responsibility of the successful bidder. In particular, the state will neither amend nor supplement the financing documents in any way nor will it enter into any additional agreements with respect to the provision of any such policy.

*Failure of any insurance provider to issue or deliver its policy will not constitute cause for failure or refusal by the successful bidder to accept delivery of or tender payment for the Certificates.*

The successful bidder must provide the state with the municipal bond insurance commitment and information with respect to the municipal bond insurance policy and the insurance provider for inclusion in the final Official Statement within two business days following the award of the bid by the state. The state will require delivery, on or prior to the date of initial delivery of the Certificates, of:

(1) a certificate from the insurance provider regarding the accuracy and completeness of the information provided for inclusion in the Official Statement,

(2) an opinion of counsel to the insurance provider regarding the enforceability of the municipal bond insurance policy, and

(3) a certificate with respect to certain tax matters,

each in form reasonably satisfactory to the state and Certificate Counsel.

***Rating.*** The Certificates have been rated "Aa2" by Moody's Investors Service, Inc., and the state will pay the fees for this rating. Any other ratings are the responsibility of the successful bidder.

**Delivery of Certificates**

***General.*** The Certificates will be delivered to DTC in New York, New York, or to the Fiscal Agent on behalf of DTC through Fast Automated Securities Transfer, against payment of the purchase price to the state, in immediately available federal funds less the amount of the good faith deposit. On or before the date of delivery of and payment for the Certificates, the successful bidder shall provide to the state such information as Certificate Counsel to the state deems necessary to determine the yield on the Certificates for purposes of Section 148 of the Internal Revenue Code of 1986, as amended.

Upon award of the Certificates, the successful bidder shall advise the state and Certificate Counsel of the initial reoffering prices at which each Principal Component of the Certificates is reasonably expected on the sale date to be sold to the public (the "Initial Reoffering Prices") for the state's inclusion in the final Official Statement for the Certificates. Simultaneously with or before delivery of the Certificates, the successful bidder shall furnish to the state and Certificate Counsel a certificate in form and substance acceptable to Certificate Counsel:

(1) confirming the Initial Reoffering Prices;

(2) certifying that a *bona fide* offering of such Certificates has been made to the public (excluding bond houses, brokers and other intermediaries);

(3) stating the first price at which a substantial amount (at least 10 percent of each maturity) of such Certificates was sold to the public (excluding bond houses, brokers and other intermediaries);

(4) if the first price at which a substantial amount of any maturity of such Certificates does not conform to the Initial Reoffering Price of that maturity, providing an explanation of the facts and circumstances that resulted in that non-conformity; and

(5) stating which maturities, if any, are amortization installments of Term Certificates maturing in the years specified by the bidder.

The successful bidder for the Certificates must actually reoffer all of the Certificates to the general public (excluding bond houses, brokers or similar persons or organizations acting in the capacity of underwriters or wholesalers).

A draft form of such certificate will be available prior to the sale date from the state's financial advisor, SDM Advisors, Inc.

The Certificates will be delivered in "book-entry only" form in accordance with the Letter of Representations from the state to DTC. As of the date of award of the Certificates, the successful bidder must either participate in DTC or must clear through or maintain a custodial relationship with an entity that participates in DTC.

The state will furnish to the successful bidder one transcript of proceedings; additional transcripts will be furnished at the successful bidder's cost.

If, prior to the delivery of any of the Certificates, the interest component evidenced and represented thereby becomes includable in the gross income of the recipients thereof for federal income tax purposes, or if legislation which would have the same effect if adopted into law is passed by either house of Congress or proposed by a joint conference committee, the successful bidder, at its option, may be relieved of the obligation to purchase the Certificates, and the state, at its option, may be relieved of the obligation to deliver the Certificates.

***Cancellation of Sale.*** The successful bidder has the right, at its option, to cancel its obligation to purchase the Certificates for which it submitted the winning bid if the state fails to cause the execution and delivery of such Certificates within 45 days from the award to the successful bidder, and in such event the successful bidder will be entitled only to the return of the principal amount of the good faith deposit.

**CUSIP Numbers**

It is anticipated that CUSIP identification numbers will be printed on the Certificates; however, neither the failure to print CUSIP numbers on any Certificate nor any error with respect thereto will constitute cause for failure or refusal by the successful bidder therefor to accept delivery of and pay for the Certificates.

***The state is responsible for obtaining CUSIP numbers, and all expenses for printing CUSIP numbers on the Certificates will be paid for by the state, but the CUSIP Global Services charge for assignment of those numbers is the responsibility of and shall be paid for by the successful bidder.***

**Legal Opinion**

The state will furnish to the successful bidder and have delivered with the Certificates the legal opinion of Foster Pepper PLLC, Seattle, Washington, Certificate Counsel, in substantially the form attached to the Preliminary Official Statement in Appendix C.

**Continuing Disclosure**

The state will enter into an undertaking for the benefit of the beneficial owners of the Certificates to provide or to cause to be provided, either directly or through a designated agent, to the Municipal Securities Rulemaking Board (the "MSRB") certain historical financial information and operating data of the state and notice of certain events pursuant to the requirements of paragraph (b)(5)(1) of Securities and Exchange Commission ("SEC") Rule 15c2-12 (the "Rule"). See "CONTINUING DISCLOSURE UNDERTAKING" in the Preliminary Official Statement. The state has never failed to comply in any material respect with any previous undertakings entered into pursuant to the Rule.

**Closing Documents**

As a condition to the obligations of the successful bidder to accept delivery of and pay for the Certificates, the successful bidder will be furnished with the following, dated as of the date of the closing:

(1) a certificate of the state, signed on behalf of the state by the Treasurer's Representative, certifying that to her knowledge and belief, and after reasonable investigation, the Preliminary Official Statement relating to the Certificates did not as of its date, and the Official Statement relating to the Certificates did not as of its date or as of the date of closing, contain any untrue statement of a material fact required to be stated therein or necessary to make the statements therein, in light of the circumstances under which they were made, not misleading, and no event affecting the Certificates has occurred since the date of the Official Statement which should be disclosed in the Official Statement for the purpose for which it is to be used or which it is necessary to disclose therein in order to make the statements and information therein not misleading in any material respect (except that in no event is any representation being made with respect to information therein regarding DTC and its book-entry only system and regarding any municipal bond insurer and its municipal bond insurance policy, and information provided by the successful bidders regarding reoffering prices and yields); and

(2) a certificate of an Assistant Attorney General of the state, based on such inquiry and investigation deemed sufficient by such Assistant Attorney General, to the effect that, except as otherwise disclosed in the Preliminary Official Statement or the Official Statement, there is no action, suit or proceedings or any inquiry or investigation by or before any court, governmental agency, public board or body in which the state has been served or, to the best of his/her knowledge, is threatened that seeks to restrain or enjoin the sale, execution or delivery of the Certificates or in any other manner affects the validity of the Certificates or the proceedings or authority pursuant to which they are to be sold, executed and delivered, or the validity or enforceability of the Trust Agreement, the Master Financing Agreements, the Site Leases, the Agency Financing Agreements or the Master Assignments.

**Official Statement**

The Preliminary Official Statement is in a form deemed final by the state for the purpose of the Rule, but is subject to revision, amendment and completion in a final Official Statement, which the state will deliver to the successful bidder not later than seven business days after the state's acceptance of such bidder's proposal, in sufficient quantities to permit the successful bidder to comply with the Rule, at the state's expense.

The successful bidder shall file, or cause to be filed, the final Official Statement with the MSRB within one business day following the receipt of the Official Statement from the state.

The successful bidder also agrees:

(1) to provide to the Treasurer, in writing, within 24 hours of the acceptance of the bid, pricing and other related information, including the initial reoffering prices of the Certificates, necessary for completion of the final Official Statement as set forth under "Delivery of Certificates–General";

(2) to disseminate to all members of the underwriting syndicate, if any, copies of the final Official Statement, including any supplements or amendments prepared by the state; and

(3) to take any and all actions necessary to comply with applicable SEC and MSRB rules governing the offering, sale and delivery of the Certificates to ultimate purchasers, including without limitation, the delivery of a final Official Statement to each investor who purchases the Certificates.

**Additional Information**

Additional information may be obtained from the undersigned at the Office of the State Treasurer, Legislative Building, Second Floor, Room 230, 416 Sid Snyder Avenue SW, Olympia, Washington 98501 (telephone: (360) 902-9007). The Preliminary Official Statement may be obtained from i-Deal Prospectus, a service of i-Deal LLC, at *www.i-dealprospectus.com*; telephone (212) 849-5024.

STATE FINANCE COMMITTEE
STATE OF WASHINGTON

By: /s/ Ellen Evans
Deputy State Treasurer—Debt Management

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# OFFICIAL STATEMENT

## $33,970,000*
## STATE OF WASHINGTON
## CERTIFICATES OF PARTICIPATION, SERIES 2011D
## (STATE AND LOCAL AGENCY REAL AND PERSONAL PROPERTY)

**Evidencing and Representing Undivided Proportionate Interests of the Owners Thereof in State Payments to be Made by the State of Washington Pursuant to the Master Financing Agreements**

## INTRODUCTION

The purpose of this Official Statement, including the cover page, the inside cover page and the appendices hereto, is to provide information relating to the State of Washington (the "state" or "Washington") and the $33,970,000* aggregate principal amount of State of Washington Certificates of Participation, Series 2011D (State and Local Agency Real and Personal Property) (the "Certificates"), proposed to be issued by the state.

This Official Statement is not to be construed as a contract or agreement between the state and the purchasers of the Certificates.

### General Description

The proceeds of the Certificates are to be used to finance and/or refinance the costs of acquisition and construction of certain parcels of real property (the "Projects") and the acquisition of certain personal property for the benefit of certain State Agencies and Local Agencies (together, the "Agencies"), as shown on the table entitled "Participating Agencies" on page ii, and to pay issuance costs with respect to the Certificates.

The Certificates are being executed and delivered by The Bank of New York Mellon as Fiscal Agent for the Certificates (the "Fiscal Agent"), pursuant to a Trust Agreement with respect to the Certificates, dated as of the Dated Date (the "Trust Agreement"), among the Fiscal Agent, the Treasurer and the Washington Finance Officers Association (the "Corporation"), a Washington nonprofit corporation. The Certificates represent undivided proportionate interests in Base Rent Payments to be made by the state under a Master Financing Lease for real property (the "Master Financing Lease") and/or Installment Payments to be made by the state under a Master Financing Contract for personal property (the "Master Financing Contract" and together with the Master Financing Lease, the "Master Financing Agreements"), each dated as of the Dated Date, between the Corporation and the state. Base Rent Payments and Installment Payments are collectively referred to herein as "State Payments."

Capitalized terms used herein, if not specifically defined, are used as defined in Appendix I to the Trust Agreement. See Appendix B—"DEFINITIONS AND SUMMARY OF CERTAIN LEGAL DOCUMENTS."

### Real Property

The respective parcels of real property on which the respective Projects of the participating Agencies are located (collectively, the "Sites") are being leased to the Corporation by the respective Agencies pursuant to separate Site Leases, each dated as of the Dated Date (the "Site Leases"), between each such Agency

* Preliminary, subject to adjustment by the state as provided in the Official Notice of Sale.

and the Corporation. Pursuant to the Master Financing Lease, the state is leasing the Sites and the Projects thereon (collectively, the "Real Property") from the Corporation. The state in turn is subleasing each parcel of Real Property back to the related Agency pursuant to separate Local Agency Financing Leases or State Agency Financing Lease Addenda (collectively, the "Financing Leases"), each dated as of the Dated Date, between the state and the respective Agencies. Each Agency is required to make Agency Rent Payments to the state pursuant to its Financing Lease for the sublease of its respective Real Property.

The Agency Rent Payments payable by the participating Agencies pursuant to the Financing Leases are, in the aggregate, at least equal to the corresponding Base Rent Payments payable by the state pursuant to the Master Financing Lease. Pursuant to a Master Assignment (the "Master Assignment (Real Property)"), dated as of the Dated Date, the Corporation is assigning and transferring to the Fiscal Agent, without recourse, all of its rights to the Sites pursuant to the Site Leases, all of its rights to receive the Base Rent Payments from the state pursuant to the Master Financing Lease, its right to take all actions, exercise all remedies and give all consents under and pursuant to the Site Leases and the Master Financing Lease, and all of its remaining right, title and interest in, to and under the Site Leases, the Master Financing Lease, the Financing Leases, and the Real Property. See "SECURITY FOR THE CERTIFICATES" and Appendix B—"DEFINITIONS AND SUMMARY OF CERTAIN LEGAL DOCUMENTS."

**Personal Property**

Various Agencies have purchased personal property to be financed or refinanced with the proceeds of the Certificates (collectively, the "Personal Property" and, together with the Real Property, the "Property") on behalf of and as the agent of the Corporation. Pursuant to the Master Financing Contract, the state is purchasing the Personal Property from the Corporation. The state in turn is selling the Personal Property to the applicable Agencies pursuant to separate Local Agency Financing Contracts or State Agency Financing Addenda (collectively, the "Agency Financing Contracts"), each dated as of the Dated Date, between the state and the applicable Agencies.

Each Agency is required to make Agency Installment Payments to the state pursuant to its Agency Financing Contract for the purchase of its respective items of Personal Property. The Agency Installment Payments payable by the participating Agencies pursuant to the Agency Financing Contracts in the aggregate are at least equal to the corresponding Installment Payments payable by the state pursuant to the Master Financing Contract. Pursuant to a Master Assignment (the "Master Assignment (Equipment)"), dated as of the Dated Date, the Corporation is assigning and transferring to the Fiscal Agent, without recourse, all of its rights to receive the Installment Payments from the state pursuant to the Master Financing Contract, its right to take all actions, exercise all remedies and give all consents under and pursuant to the Master Financing Contract, and all of its remaining right, title and interest in, to and under the Master Financing Contract and the Agency Financing Contracts, and in and to the Personal Property. See "SECURITY FOR THE CERTIFICATES" and Appendix B—"DEFINITIONS AND SUMMARY OF CERTAIN LEGAL DOCUMENTS."

**State Payments and Agency Payments**

Except as otherwise described herein, payments due from the state under the Master Financing Agreements ("State Payments") are payable from Agency Rent Payments and Agency Installment Payments (together, the "Agency Payments") to be made pursuant to the Financing Leases and the Agency Financing Contracts (together, the "Agency Financing Agreements"). The obligation of each State Agency to make its Agency Payments is subject to appropriation by the Legislature and to Executive Order reduction by the Governor. The State is not obligated to pay the State Payments other than from appropriated funds of the respective State Agencies and from Agency Payments received from

Local Agencies. Payment of the Agency Payments of each Local Agency is secured by the full faith and credit of such Local Agency. In the event that any Local Agency fails to make any payment due under its Agency Financing Agreement, the Treasurer is obligated to withhold an amount sufficient to make such payment from the Local Agency's share, if any, of state revenues or other amounts authorized or required by law to be distributed by the state to such Local Agency, if otherwise legally permissible. Upon the failure of any Local Agency to make any Agency Payment as required pursuant to its Agency Financing Agreement, the Treasurer is further obligated, to the extent of legally available appropriated funds and subject to any Executive Order reduction, to make such payment on behalf of such Local Agency. See "SECURITY FOR THE CERTIFICATES."

**Document Summaries**

For summaries of the Trust Agreement, the Master Financing Lease, the Master Financing Contract, the Financing Leases, the Agency Financing Contracts, the Master Assignments, and the Site Leases, see Appendix B—"DEFINITIONS AND SUMMARY OF CERTAIN LEGAL DOCUMENTS." Such summaries and descriptions herein of the Certificates, the Master Financing Lease, the Master Financing Contract, the Financing Leases, the Agency Financing Contracts, the Master Assignments, and the Site Leases, and the Committee's authorizing resolutions and the references to and summaries of certain provisions of the Washington State Constitution (the "Constitution") and laws of the state and any other documents and agreements referred to herein do not purport to be complete and are qualified in their entirety by reference to the complete provisions thereof. Certain financial information regarding the state has been taken or derived from the audited financial statements and other financial reports of the state. General and economic information about the state is included in Appendix A—"GENERAL AND ECONOMIC INFORMATION," and audited financial statements for the state's fiscal year ended June 30, 2010, are included as Appendix D.

**State Finance Committee**

The Legislature, by statute, has delegated to the State Finance Committee (the "Committee") authority to supervise and control the issuance of all state bonds and other state obligations, including certificates of participation and other financing contracts, authorized by the Legislature. The Committee is composed of the Governor, Lieutenant Governor and Treasurer. The Treasurer is designated as Chairman of the Committee, and pursuant to Chapter 3, Laws of 1981 (Section 43.33.030 of the Revised Code of Washington ("RCW")), the Office of the State Treasurer provides administrative support to the Committee. A Deputy State Treasurer acts as recording officer for the Committee and is responsible for the administration of its official duties in accordance with prescribed policies of the Committee.

## THE CERTIFICATES

**Authorization**

The state is authorized by Chapter 39.94 RCW, as amended (the "Act"), to enter into financing contracts, for the state and its agencies or on behalf of certain local agencies specified in the Act, to acquire real and personal property to be used by the state or its agencies or such local agencies, and to issue certificates of participation in those contracts. The term "local agency" is defined in the Act to include a library or regional library, an educational service district, the superintendent of public instruction, the school directors' association, a health district, or any county, city, town, school district, or other municipal corporation or quasi-municipal corporation described as such by statute. Financing contracts may include, but are not limited to, conditional sales contracts, financing leases, lease purchase contracts, and refinancing contracts that provide for payment by the state over a term of more than one year.

All financing contracts of the state must be approved by the Committee, and financing contracts for the acquisition of real property by the state must receive the prior approval of the Legislature. The Washington Supreme Court in *State Department of Ecology v. State Finance Committee*, 116 Wn.2d 246, 804 P.2d 1241 (1991), held that a financing contract for the state's Department of Ecology did not create debt within the meaning of Article VIII, Section 1, of the Constitution.

By Resolution No. 987, adopted on October 7, 2003, the Committee authorized and approved the execution and delivery of certificates of participation (including the Certificates) in series from time to time in payments to be made by the state pursuant to master financing contracts and/or master financing leases. The Committee also approved the forms of the Trust Agreement, the Master Financing Agreements, the Agency Financing Agreements, the Site Leases and the Master Assignments and authorized and approved the execution and delivery thereof in connection with each series of certificates of participation. On September 9, 2011, the Committee approved a Finance Plan under which the aggregate principal amount of financing contracts (including certificates of participation therein) of the state to be outstanding in the 2011-2013 Biennium was set at $1,425,000,000, plus financing expenses and required reserves, including certificates expected to be issued to finance acquisition and construction of real estate and equipment for state agencies and local governments.

The Legislature authorized the state Department of Social and Health Services to enter into its State Agency Financing Lease Addendum pursuant to Chapter 48, Laws of 2011, 1st Sp. Sess., Section 7011(4). The Legislature authorized the State Board for Community and Technical Colleges to enter into its State Agency Financing Lease Addendum on behalf of Wenatchee Valley College pursuant to Chapter 48, Laws of 2011, 1st Sp. Sess., Section 7011(1)(f). The Board of County Commissioners of San Juan County, Washington, approved its Local Agency Financing Lease by Resolution No. 37-2011, adopted September 13, 2011. The City Council of the City of Grandview, Washington, approved its Local Agency Financing Lease by Ordinance No. 2011-17, passed August 23, 2011. Agency Financing Contracts for the acquisition of personal property are being entered into by the State Agencies under the general provisions of the Act and by Local Agencies under approving ordinances or resolutions passed or adopted pursuant to applicable state law.

**Payment of Principal and Interest**

The Certificates represent undivided proportionate interests in State Payments to be made by the state pursuant to the Master Financing Agreements. The Certificates are to be dated as of their date of initial delivery. The principal components of the State Payments (the "Principal Components") evidenced and represented by the Certificates will be payable on the dates (each a "Principal Payment Date") and in the amounts as shown on page i. The Certificates are to be executed and delivered as fully registered certificates without coupons in denominations of $5,000 and any integral multiple thereof.

The interest components of State Payments (the "Interest Components") evidenced and represented by the Certificates will be payable semiannually on January 1 and July 1 of each year (each an "Interest Payment Date" and together with Principal Payment Dates, the "Certificate Payment Dates"), beginning on July 1, 2012, at the rates shown on page i of this Official Statement. Such interest is to be computed using a 360-day year comprised of 12 30-day months.

Pursuant to authority granted in chapter 43.80 RCW, the Committee appoints one or more fiscal agents with the authority to act as paying agent, transfer agent, authenticating agent and bond registrar for all obligations issued by the state and its political subdivisions. The fiscal agent appointed by the Committee from time to time is referred to herein as the "Fiscal Agent." The Committee currently has a contract with The Bank of New York Mellon to act as the Fiscal Agent for a term that began February 1, 2007, and continues to January 31, 2015. Under the terms of the current fiscal agency contract, The Bank of New

York Mellon is to authenticate the Certificates for delivery to The Depository Trust Company ("DTC") and remit to DTC payments received from the state as principal and interest represented by the Certificates.

When issued, the Certificates are to be registered in the name of Cede & Co. (or such other name as may be requested by an authorized representative of DTC), as nominee of DTC. DTC will act as securities depository for the Certificates. Individual purchases of Certificates are to be made only in book-entry form through DTC. See "Book-Entry System" below and Appendix E–"DTC AND ITS BOOK-ENTRY SYSTEM."

If at any time the Certificates are not in book-entry form, payment of the Interest Component evidenced and represented by each Certificate is to be made on each Interest Payment Date to and including the Principal Payment Date or Prepayment Date to the person whose name appears on the Certificate Register as the Owner thereof as of the close of business on the 15th day of the month immediately preceding each Interest Payment Date and Principal Payment Date (the "Record Date"), such interest to be paid by check or draft mailed by first class mail on such Interest Payment Date to such Owner at the address as it appears on such Certificate Register. Payment of the Principal Component or Prepayment Price evidenced and represented by each Certificate is to be made upon presentation and surrender thereof by the Owner at the Principal Office of the Fiscal Agent.

**Prepayment**

***Optional Prepayment.*** The Certificates with Principal Payment Dates on and after January 1, 2023, are subject to optional prepayment prior to their respective Principal Payment Dates, as a whole or in part in Authorized Denominations on any date on or after January 1, 2022, upon the exercise by the state at the direction of any Agency of its option to prepay the Principal Components evidenced and represented by such Certificates, at the Prepayment Price (expressed as a percentage of the Principal Components prepaid) of 100 percent plus accrued interest, if any, evidenced and represented thereby to the Prepayment Date.

***Extraordinary Mandatory Prepayment.*** The Certificates are subject to mandatory prepayment on any date prior to their respective Principal Payment Dates, as a whole, or in part in Authorized Denominations, upon certain governmental takings, loss of title and casualty loss to Property that result in prepayments of Financing Leases, deposited in the Prepayment Account in the amount of the Principal Component evidenced and represented thereby being prepaid, plus accrued interest, if any, evidenced and represented thereby to the Prepayment Date, without premium.

***Mandatory Prepayment.*** The Certificates with a Principal Payment Date of January 1, 20__, and the Certificates with a Principal Payment Date of January 1, 20__ (collectively, the "Term Certificates"), are subject to mandatory prepayment prior to their stated Principal Payment Dates, in part in Authorized Denominations, from State Payments in the amount of the Principal Component evidenced and represented thereby being prepaid, plus accrued interest evidenced and represented thereby to the Prepayment Date, without premium, as follows:

| 20__ Term Certificates | | 20__ Term Certificates | |
|---|---|---|---|
| **Mandatory Prepayment Date** | **Principal Component** | **Mandatory Prepayment Date** | **Principal Component** |

* Principal Payment Date.

***Selection of Certificates for Prepayment.*** If the Certificates are in book-entry form at the time of prepayment, and less than all of the State Payments are being prepaid, the Fiscal Agent is to direct DTC to instruct the DTC Participants to select such Certificates for prepayment pro rata among all beneficial owners of the Principal Payment Date being prepaid. Neither the state nor the Fiscal Agent will have responsibility to insure that DTC or its participants properly select such Certificates for prepayment. If the Certificates are not then in book-entry form at the time of prepayment, the Fiscal Agent is to select such Certificates for prepayment randomly to the greatest extent possible, subject to maintaining the Certificates in Authorized Denominations.

***Notice of Prepayment.*** Notice of prepayment is required to be given by the Fiscal Agent not less than 30 nor more than 60 days prior to the Prepayment Date, to the Treasurer, the Owner of each Certificate affected at the address shown on the Certificate Register on the date such notice is mailed, the Securities Depository and the Municipal Securities Rulemaking Board (the "MSRB"). Each notice of prepayment must state the date of such notice, the date of execution and delivery of the Certificates, the Prepayment Date, the Prepayment Prices, the place or places of prepayment (including the name and appropriate address or addresses of the Fiscal Agent), the CUSIP number of the Certificates being prepaid, the source of the funds to be used for such prepayment, the Principal Component due and evidenced and represented by the Certificates, the distinctive certificate numbers of the Certificates or portions thereof to be prepaid, the rate or rates of interest evidenced and represented by the Certificates to be prepaid, and the Principal Payment Dates of the Certificates to be prepaid. The notice also must state that the interest evidenced and represented by the Certificates designated for prepayment will cease to accrue from and after such Prepayment Date, and that on said date there will become due and payable with respect to each of the prepaid Certificates the Prepayment Price of the Certificate to be prepaid, and interest, if any, accrued thereon to the Prepayment Date. Such notice must require that such Certificates be then surrendered at the address or addresses of the Fiscal Agent specified in the prepayment notice.

With respect to any notice of optional prepayment of Certificates, unless such Certificates are to be deemed to have been paid as set forth in the defeasance provisions of the Trust Agreement or unless the Fiscal Agent has cash or Government Obligations sufficient to pay the Prepayment Price, such notice may state that such prepayment shall be conditional upon the receipt by the Fiscal Agent on or prior to the date fixed for such prepayment of money sufficient to pay the Prepayment Price due evidenced and represented by such Certificates and interest payable with respect thereto, and that if such money is not so received the notice would be of no force and effect and the Fiscal Agent would not be required to prepay such Certificates. In the event that such notice of prepayment contains such a condition and such money is not so received, the prepayment would not be required to be made and the Fiscal Agent would be required within a reasonable time thereafter to give notice, in the manner in which the notice of prepayment was given, that such money was not so received.

***Partial Prepayment.*** Upon surrender of any Certificate prepaid in part only, the Fiscal Agent is required to provide a replacement Certificate or Certificates evidencing and representing a principal amount equal to the portion of the Principal Component evidenced and represented by such Certificate not prepaid, and

deliver it to the Owner thereof. The Certificate so surrendered is required to be cancelled by the Fiscal Agent.

**Book-Entry System**

When issued, the Certificates will be registered in the name of Cede & Co. (or such other name as may be requested by an authorized representative of DTC), as nominee of DTC. DTC will act as Securities Depository for the Certificates. Individual purchases are to be made only in book-entry form through DTC, and purchasers will not receive physical certificates representing their interest in the Certificates purchased. For information about DTC and its book-entry system, see Appendix E—"DTC AND ITS BOOK-ENTRY SYSTEM."

**Termination of Book-Entry System**

If DTC resigns as the securities depository and no substitute can be obtained, or if the state determines that it is in the best interest of the beneficial owners of the Certificates that they be able to obtain certificates, the ownership of the Certificates will be transferred to any person as described in the Trust Agreement and the Certificates will no longer be held in fully immobilized form. New certificates then will be issued in Authorized Denominations and registered in the names of the beneficial owners. See Appendix E—"DTC AND ITS BOOK-ENTRY SYSTEM."

**State and Fiscal Agent Responsibilities**

Neither the state nor the Fiscal Agent will have any responsibility or any liability to beneficial owners for any error, omission, action, or failure to act on the part of DTC or any Direct Participant or Indirect Participant of DTC with respect to the following: (1) proper recording of beneficial ownership interests of the Certificates or confirmation of their ownership interest; (2) proper transfers of such beneficial ownership interests; (3) the payment, when due, to the beneficial owners of principal or Prepayment Price or interest evidenced and represented by the Certificates; (4) any notices to beneficial owners; (5) any consent given; or (6) any other DTC or Participant error, omission, action or failure to act pertaining to the Certificates.

**Defeasance**

The Trust Agreement provides that if money and/or "Government Obligations" maturing at such times and bearing interest to be earned thereon in amounts sufficient to prepay the principal and interest evidenced and represented by any or all of the Certificates in accordance with their terms and the terms of the Trust Agreement and the Master Financing Agreements are set aside irrevocably in a special trust account to effect such prepayment and are pledged for such purpose, then no further payments are required to be made to pay or secure the payment of such principal and interest evidenced and represented by such Certificates, and such Certificates are to be deemed thereafter not to be outstanding. See Appendix B–"DEFINITIONS AND SUMMARY OF CERTAIN LEGAL DOCUMENTS."

## SOURCES AND USES OF CERTIFICATE PROCEEDS

The following table shows the sources and uses of Certificate proceeds:

### SOURCES AND USES

| | |
|---|---|
| **Sources** | |
| Principal Component of Certificates | |
| [Net] Original Issue [Premium/Discount] | |
| **Total Sources** | |
| **Uses** | |
| Deposit to Project Fund (Real Property) | |
| Deposit to Acquisition Fund (Personal Property) | |
| Costs of Issuance (1) | |
| Underwriting Spread | |
| **Total Uses** | |

(1) Includes fees for services of the rating agency, financial advisor, certificate counsel and disclosure counsel, and other costs.

## PRINCIPAL PARTICIPATING AGENCIES

A complete listing of the Agencies and their respective real and personal property being financed is shown at page ii under the heading "PARTICIPATING AGENCIES." The Agencies for which the acquisition or construction of real property is being financed and their respective projects are further described below.

### State Agency – Department of Social and Health Services

***The Project.*** The Department of Social and Health Services ("DSHS") is funding renovations and improvements to facilities to be used to house juveniles with mental disabilities and behavioral issues. Construction commenced in September 2011 and completion is scheduled for November 2012. The total cost of the project is estimated at $15,850,000, of which $2,000,000 is funded by state appropriations and $5,350,000 from agency operating funds. Proceeds of the Certificates will provide $8,500,000 to complete the funding for the projects. The financing contract will have a 20-year term.

***The State Agency.*** DSHS is the State's largest agency, serving nearly a third of the state's population, and providing a range of medical and behavioral health care, juvenile rehabilitation, child protective, food assistance, and other services. DSHS is administered by a Secretary, who is appointed by the Governor. The current Secretary is Susan N. Dreyfus, who was appointed in May 2009. DSHS's 2011-13 biennial budget is $21.3 billion, including $8.8 billion in General Fund-State dollars. DSHS has approximately 17,000 full-time equivalent ("FTE") employees.

### State Agency – State Board for Community and Technical Colleges

***The Project.*** The State Board for Community and Technical Colleges, on behalf of Wenatchee Valley College, is constructing a music hall and art center to be used for art instruction, an art gallery and a recital hall. Construction commenced in July 2011 and completion is scheduled for July 2012. The total cost of the project is estimated at $9,200,000, of which $2,000,000 is funded by state appropriations and $4,500,000 from college reserves and donations. Proceeds of the Certificates will provide $2,700,000 to complete funding for the project. The financing contract will have a 20-year term.

***The State Agency.*** In 1967, the Legislature created a system of state-funded community colleges in Washington and established a State Board of Community College Education, with members appointed by the Governor. In 1991, the Legislature made significant changes to the community college system and the title of the board was changed to the State Board for Community and Technical Colleges (the "State Board").

The State Board's primary responsibilities are to submit single system operating and capital budget requests to the Governor and the Legislature, to represent the community and technical colleges on state-level policy issues, to allocate funds to the colleges, to provide research and information about the community and technical college system, and to provide policy guidance to the colleges.

The State Board's activities are administered by an executive director, who is appointed by the State Board. The State Board received state funding appropriations of $216,346,000 for the 2011-2013 biennium, and has approximately 38 FTE employees.

***Wenatchee Valley College.*** Wenatchee Valley College is a two-year public college that offers degrees and certificates in academic and professional-technical programs, as well as courses in continuing education and developmental education. The college began operation in 1941 and serves Chelan, Douglas and Okanogan counties. The college has approximately 73 full-time faculty and 162 part-time faculty. The student population is approximately 8,000 full- and part-time students annually.

**Local Agency – City of Grandview**

***The Project.*** The City of Grandview (the "City") is acquiring a joint interest in a library to be jointly owned and occupied by Yakima Valley Community College and the City. Construction of the project has been completed. The total cost of the library project is estimated at $4,000,000, of which $2,000,000 was from state appropriation and $1,250,000 was from donations, grants, college funds and federal funds obtained cooperatively between the college and the City. Proceeds of the Certificates will provide $750,000 to complete the City's share of funding for the project. The financing contract will have a 20-year term.

***The Local Agency.*** The City is in Yakima County, in central Washington, and was incorporated in 1909. The City has approximately 10,920 residents and operates under a mayor-council form of government, with a seven-member council and an elected mayor.

**Local Agency – San Juan County**

***The Project.*** San Juan County (the "County") renovated and developed park improvements, including water system improvements and restroom facility rehabilitation. Construction was completed in August 2011. Proceeds of the Certificates will provide $120,000 to reimburse the County for a portion of the project costs. The financing contract will have a 10-year term.

***The Local Agency.*** The County is located in the northwest corner of the State and was established in 1873. It encompasses approximately 175 square miles of islands, and has 15,769 residents. The County has operated under a Home Rule Charter since January 2006 and is governed by a six-member County Council and is administered by a County Administrator.

## SECURITY FOR THE CERTIFICATES

### State Payments

The Certificates represent undivided proportionate interests in State Payments. Pursuant to the Master Financing Agreements, the Corporation will lease or sell the Property to the state. In consideration thereof, the state is required to make State Payments to the Fiscal Agent, as assignee of the Corporation, during the terms of the Master Financing Agreements. State Payments are composed of Principal Components and/or Interest Components. State Payments are due on each Certificate Payment Date.

Except as otherwise described below, State Payments due from the state under the Master Financing Agreements are payable solely from Agency Payments to be made by the respective Agencies pursuant to the related Agency Financing Agreements. The total of the Agency Payments payable by the participating Agencies on each Agency Payment Date pursuant to the Agency Financing Agreements is at least equal to the State Payment payable by the state pursuant to the Master Financing Agreements on the next succeeding Base Rent Payment Date and Installment Payment Date. Agency Payments are due one month prior to the corresponding Base Rent Payment Date and Installment Payment Date.

Pursuant to the Master Assignments, the Corporation is assigning and transferring to the Fiscal Agent, without recourse, all of its rights to receive the State Payments; its right to take all actions, exercise all remedies and give all consents under and pursuant to the Master Financing Agreements; and all of its remaining right, title and interest in, to and under the Master Financing Agreements, the Site Leases and the Agency Financing Agreements, and in and to the Property.

### State Intercept

If any Local Agency fails to make any Agency Payment due under its Agency Financing Agreement, the Treasurer is obligated pursuant to the related Master Financing Agreement to withhold an amount sufficient to make that payment from the Local Agency's share, if any, of state revenues or other amounts that are authorized or required by law to be distributed by the state to that Local Agency, including but not limited to leasehold excise taxes, sales and use taxes, excise taxes, property taxes and liquor control board receipts; *provided*, that the use of any such revenues or amounts to make the payments is otherwise authorized or permitted by state law. This withholding will continue until all payments due under the related Agency Financing Agreement have been made. Amounts withheld by the Treasurer are to be applied to make any payment due under the related Agency Financing Agreement on behalf of the Local Agency, or to reimburse the Treasurer for any payment made by the Treasurer.

THERE CAN BE NO ASSURANCE AS TO THE AVAILABILITY OF FUNDS FOR INTERCEPT BY THE TREASURER WITH RESPECT TO ANY LOCAL AGENCY UPON THE LOCAL AGENCY'S FAILURE TO MAKE ANY AGENCY PAYMENT PURSUANT TO ITS AGENCY FINANCING AGREEMENT.

### Payment History

The principal and interest represented by certificates of participation in lease or other payment obligations that are payable by the state have always been paid when due. The state never has failed to appropriate funds to meet its lease, installment sale or other payment obligations with respect to outstanding certificates of participation. No local agency has failed to make its lease, installment sale or other payment obligations with respect to agency financing contracts or agency financing leases with the state in respect of outstanding certificates of participation.

**Conditional State Payment Obligations**

If any Local Agency fails to make any Agency Payment due under its Agency Financing Agreement, the Treasurer is obligated, to the extent of legally available appropriated funds and subject to any Executive Order reduction, to make such payment on behalf of such Local Agency within 10 Business Days after the Agency Payment was due.

The Treasurer currently has appropriation authority sufficient to make any such payments that may come due within the current biennium. The Treasurer has covenanted in the Master Financing Agreements to include in its biennial budget all scheduled Agency Payments due during such biennium pursuant to any Agency Financing Agreement with a Local Agency, and to use its best efforts to obtain appropriations by the Legislature in amounts sufficient to make any such payments.

**Limited Obligation of State**

THE MASTER FINANCING AGREEMENTS, INCLUDING THE RELATED STATE AGENCY FINANCING ADDENDA AND STATE AGENCY FINANCING LEASE ADDENDA, CONSTITUTE SPECIAL, LIMITED OBLIGATIONS OF THE STATE PAYABLE SOLELY FROM THE SOURCES AND SUBJECT TO THE LIMITATIONS SET FORTH THEREIN. NONE OF THE STATE PAYMENTS, THE AGENCY PAYMENTS OR THE CERTIFICATES CONSTITUTE OR REPRESENT DEBT OR GENERAL OBLIGATIONS OF THE STATE OR ANY STATE AGENCY, AND NEITHER THE FULL FAITH AND CREDIT NOR THE TAXING POWER OF THE STATE OR OF ANY STATE AGENCY IS PLEDGED TO THE PAYMENT OF ANY STATE PAYMENTS OR AGENCY PAYMENTS OR THE PRINCIPAL OR INTEREST EVIDENCED AND REPRESENTED BY THE CERTIFICATES. THE STATE WILL NOT BE OBLIGATED TO PAY THE SAME EXCEPT FROM AGENCY PAYMENTS AND OTHER AMOUNTS AS PROVIDED IN THE MASTER FINANCING AGREEMENTS.

**Non-appropriation and Executive Order Reduction**

ANY PAYMENTS BY THE TREASURER ON BEHALF OF A LOCAL AGENCY AND ANY PAYMENTS BY A STATE AGENCY ARE SUBJECT TO APPROPRIATION BY THE LEGISLATURE AND EXECUTIVE ORDER REDUCTION BY THE GOVERNOR. A DETERMINATION BY THE LEGISLATURE NOT TO APPROPRIATE, OR ANY EXECUTIVE ORDER REDUCTION BY THE GOVERNOR, WOULD NOT CONSTITUTE AN EVENT OF DEFAULT UNDER THE TRUST AGREEMENT, THE MASTER FINANCING AGREEMENTS OR ANY STATE AGENCY FINANCING ADDENDA OR ANY STATE AGENCY FINANCING LEASE ADDENDA.

An appropriation from the state General Fund to a State Agency for its operating budget (including Agency Payments under any Financing Lease or Agency Financing Contract) is made by the Legislature in an aggregate dollar amount and not specifically for each item in the State Agency's budget. In reducing budgeted expenditures to reflect reduced allotments of appropriations from the state General Fund in response to the Executive Order, a State Agency may choose to reduce its expenditures for certain purposes but not for others. Each State Agency in its Financing Lease or Agency Financing Contract covenants to use its best efforts to obtain allotments by the Office of Financial Management of appropriated funds sufficient to make all required Agency Payments thereunder, and, to the extent permitted by law, the State Agency agrees that, to the extent that any amounts are included in its budget for purposes or facilities served, or functions or operations supported or provided by Property acquired under a Financing Lease or Agency Financing Contract, the State Agency will allocate a sufficient portion of such amounts to the payment of the Agency Payments due under its Financing Lease or Agency

Financing Contract for the acquisition of that Property. See Appendix B—"DEFINITIONS AND SUMMARY OF CERTAIN LEGAL DOCUMENTS under the headings "FINANCING LEASES—Covenants and Agreements of the Agency" and "AGENCY FINANCING CONTRACTS—Covenants and Agreements of the Agency."

**Permitted Termination Events**

Under each State Agency Financing Addendum or State Agency Financing Lease Addendum, each of the following constitutes a "Permitted Termination Event":

(1) the Legislature determines not to appropriate sufficient funds within any biennial budget for the purpose of paying the Agency Payments due during the next occurring biennium, or

(2) the Governor issues an Executive Order mandating an emergency reduction in state funding; provided, that the State Agency delivers written notice thereof to the Treasurer as required by the State Agency Financing Addendum or State Agency Financing Lease Addendum.

Upon a Permitted Termination Event, subject to the provisions of the Master Financing Agreements, State Agency Financing Addenda and the State Agency Financing Lease Addenda, the state may terminate a State Agency Financing Addendum or State Agency Financing Lease Addendum and the related obligation of the Treasurer under the Master Financing Agreements.

The occurrence of a Permitted Termination Event does not constitute an Agency Event of Default, a Master Financing Agreement Event of Default or an Event of Default, and remedies of re-entry and re-letting of the Real Property during the term of the related Site Lease and the return of the Personal Property are the sole remedies available to the Treasurer and the Corporation upon such occurrence. See "Master Financing Lease—Permitted Termination Events," "Master Financing Contract—Permitted Termination Events," "Financing Leases—Permitted Termination Events" and "Financing Contracts—Permitted Termination Events" in Appendix B.

**Agency Payments**

Pursuant to each Agency Financing Agreement, the Agency is required to make its Agency Payments to the state with respect to its Property. Agency Payments are composed of principal and interest components and are payable, during the term of the applicable Agency Financing Agreement, on the first day of each month immediately preceding the related Certificate Payment Date. The Agency Payments in the aggregate are at least equal to the corresponding State Payment.

Each State Agency has covenanted in its Agency Financing Agreement to take such action as may be necessary to include all of its Agency Payments due thereunder in its biennial budget and to use its best efforts to obtain appropriations by the Legislature in amounts sufficient to make all such Agency Payments.

Each Local Agency has covenanted in its Agency Financing Agreement to take such action as may be necessary to include all of its Agency Payments due thereunder in its annual budget and to make the necessary annual appropriations for all such Agency Payments. The obligation of each Local Agency to make its Agency Payments is a direct and general obligation of the Local Agency to which the full faith and credit of such Local Agency is pledged. Each Local Agency executing an Agency Financing Agreement has covenanted and agreed that it will levy taxes, to the extent permitted by law, in such amounts and at such times necessary, within and as a part of the tax levy permitted to the Local Agency

without a vote of its electors, to provide funds, together with other money legally available for that purpose, to make its Agency Payments.

**Substitution of Real Property**

Under the Master Financing Lease and the corresponding provisions of the Financing Leases, the Treasurer may substitute and consent to the substitution, for a parcel of Property, of another parcel or parcels of real property by first filing with the Fiscal Agent, as Assignee of the Corporation:

(1) an Opinion of Counsel to the effect that such substitution (a) is permitted under the Master Financing Lease and (b) in and of itself, will not adversely effect the exclusion from gross income for federal income tax purposes of the Interest Component of the Certificates;

(2) an appraisal or other written evidence from an independent, disinterested real property appraiser acceptable to the Treasurer and the Fiscal Agent to the effect that such substitute Property has an estimated fair rental value for the remaining term of the respective Financing Lease equal to or greater than the Agency Rent Payments due thereunder from time to time thereafter;

(3) a certificate of the Agency to the effect that such substitute Property is free and clear of any mortgages, deeds of trust, liens, or other similar encumbrances, other than Permitted Encumbrances, and is essential to the Agency's ability to carry out its governmental functions and responsibilities; and

(4) written evidence from each Rating Agency then rating the Certificates that such substitution, in and of itself, will not result in the suspension, reduction or withdrawal of any ratings on the Certificates by such Rating Agency.

**Release of Real Property**

Under the Master Financing Lease and corresponding provisions of the Financing Leases, the Treasurer may release and consent to the release of a portion of the Property leased under any Site Lease, and subleased under and pursuant to the Master Financing Lease and the related Financing Lease, by first filing with the Fiscal Agent, as assignee of the Corporation:

(1) an Opinion of Counsel to the effect that such release (a) is permitted under the Master Financing Lease, and (b) in and of itself, will not adversely effect the exclusion from gross income for federal income tax purposes of the Interest Component of the Certificates;

(2) an appraisal or other written evidence from an independent, disinterested real property appraiser acceptable to the Treasurer and the Fiscal Agent to the effect that the remaining portion of the Property has an estimated fair rental value for the remaining term of the respective Financing Lease equal to or greater than the Agency Rent Payments due from time to time thereunder;

(3) provision by such Agency of any necessary easements, reciprocal agreements or other rights as may be necessary to provide comparable pedestrian and vehicular access, and other uses and amenities (including but not limited to water, sewer, electrical, gas, telephone, and other utilities) as existed prior to such release; and

(4) written evidence from each Rating Agency then rating the Certificates that such release, in and of itself, will not result in the suspension, reduction or withdrawal of any ratings on the Certificates by such Rating Agency.

**Substitution of Personal Property**

Under the Master Financing Contract and the corresponding provisions of the Agency Financing Contracts, the Treasurer may substitute and consent to the substitution for an item of Property acquired for and on behalf of an Agency of other personal property by filing with the Fiscal Agent, as assignee of the Corporation:

(1) a certificate of such Agency stating that such substitute Property:

(a) has a remaining useful life equal to or greater than the Property for which it is being substituted;

(b) has a fair market value equal to or greater than the fair market value of the item of Property for which it is being substituted;

(c) is free and clear of all liens and encumbrances except a first priority security interest in favor of the Fiscal Agent, as assignee of the Corporation, under the Master Financing Contract;

(d) is of equal usefulness and value as the Property for which it is being substituted;

(e) is essential to the Agency's ability to carry out its governmental functions and responsibilities; and

(f) is expected to be used by such Agency immediately and for the term of its Agency Financing Contract; and

(2) an Opinion of Counsel to the effect that the substitution will not cause the interest evidenced and represented by the Certificates to be includable in gross income for federal income tax purposes under the Code.

**State Payments and Agency Payments Not Subject to Abatement**

The State Payments payable by the state pursuant to the Master Financing Agreements, and the Agency Payments payable by the respective Agency pursuant to the Agency Financing Agreements, are *not* subject to abatement upon damage to or destruction of any of the Property, nor are such payments otherwise subject to diminution, reduction, postponement, counterclaim, defense, or set-off as a result of any dispute, claim or right of action by, against or among the state, the Corporation, the Fiscal Agent, any Agency, and/or any other Person, or for any other reason.

**Acceleration**

The Certificates may be subject to acceleration upon the occurrence of an Event of Default under the Master Financing Agreements. However, the Certificates are not subject to acceleration upon the occurrence of an Agency Event of Default under any related Agency Financing Agreement. See Appendix B—"DEFINITIONS AND SUMMARY OF CERTAIN LEGAL DOCUMENTS."

**Limitations on Exercise of Remedies**

***Real Property.*** Upon the occurrence of an Event of Default under the Master Financing Lease or the Financing Leases, the Fiscal Agent, as assignee of the Corporation, may pursue any available legal or

equitable remedy, which may include suing for rent as the same becomes due or re-entering the Real Property for the benefit of the owners of the Certificates, and terminating the Master Financing Lease or the Financing Leases, as appropriate, and accelerating the unpaid rent or suing for damages.

The remedies provided in the Master Financing Lease, the Financing Leases and/or the Trust Agreement, however, may be unenforceable under certain circumstances due to the application of principles of equity to state or federal laws relating to bankruptcy, moratorium, reorganization, and creditors' rights generally and to limitations on remedies against the state and the Agencies under the laws of the state. Moreover, due to the essential governmental nature of the Real Property or portions thereof, it is not certain whether a court would permit the exercise of the remedy of re-letting with respect thereto. In addition, the enforcement of remedies provided in the Master Financing Lease, the Financing Leases and the Trust Agreement could provide both expensive and time-consuming. In any event, although the Fiscal Agent has the right, upon the occurrence of an Event of Default or an Agency Event of Default, to re-enter and re-let the applicable Real Property, it is unknown whether any such re-entry, re-letting or other disposition would result in the collection of amounts sufficient to make the related Agency Rent Payments. Moreover, the Fiscal Agent would not be obligated to re-let the Real Property in the manner so as to preserve the tax-exempt nature of interest represented by the Certificates.

***Personal Property.*** Upon the occurrence of an Event of Default under the Master Financing Contract, the Fiscal Agent, as assignee of the Corporation, may pursue any available legal or equitable remedy against the state, which may include suing for Installment Payments then due and thereafter becoming due, or enforcing the observance or performance of any covenant, agreement or obligation of the state under the Master Financing Contract. Also, by written notice to the state, the Fiscal Agent may request the state to promptly return the item or items of Personal Property with respect to which such default occurred to the Fiscal Agent in good condition at the state's own expense. The state has covenanted in the Master Financing Contract to comply with such request.

Upon the occurrence of an Agency Event of Default under an Agency Financing Contract, the Fiscal Agent may pursue any available legal or equitable remedy against the related Agency, which may include suing for Agency Installment Payments then due and thereafter becoming due, or enforcing the observance or performance of any covenant, agreement or obligation of the Agency under the Master Financing Contract. Also, by written notice to the Agency, the Fiscal Agent may request the Agency to promptly return the item or items of Personal Property with respect to which such default occurred to the Treasurer in good condition at the Agency's own expense. In addition, the Fiscal Agent may declare an amount equal to all unpaid Agency Installment Payments to become due and payable under the Agency Financing Contract, including but not limited to the Agency Interest Components accrued and unpaid, to be immediately due and payable without further demand. However, the Fiscal Agent's remedies against the state upon the occurrence of an Agency Event of Default are limited to requiring the state to assemble the Personal Property and make it available to the Fiscal Agent.

The remedies provided in the Master Financing Contact, the Agency Financing Contracts and/or the Trust Agreement may be unenforceable under certain circumstances due to the application of principles of equity to state or federal laws relating to bankruptcy, moratorium, reorganization, and creditors' rights generally and to limitations on remedies against the state and the Agencies under the laws of the state of Washington. Moreover, due to the essential governmental nature of the Personal Property, it is not certain whether a court would permit the exercise of the remedies of repossession and re-sale of the Personal Property. In addition, the enforcement of remedies provided in the Master Financing Contract, the Agency Financing Contracts and the Trust Agreement could prove both expensive and time consuming. In any event, although the Fiscal Agent has the right, upon the occurrence of an Event of Default or an Agency Event of Default, to repossess and re-sell the applicable Personal Property, it is unknown whether such actions would result in the collection of amounts sufficient to make the related

Agency Installment Payments. Moreover, the Fiscal Agent would not be obligated to re-sell the Personal Property in a manner so as to preserve the tax-exempt nature of interest represented by the Certificates.

**Additional Certificates**

Each Agency may make additions or improvements to or alterations of the applicable Project so long as such additional improvements are constructed and installed in accordance with applicable laws and regulations and do not diminish the value or usefulness of the Real Property.

The Treasurer may enter into additional Master Financing Leases with the Corporation to finance all or any portion of the costs of such additions or improvements so long as such leases do not reduce the obligation of the state to make Base Rent Payments under the Master Financing Lease and will not, in the opinion of Certificate Counsel, adversely affect the tax-exempt status of the Interest Component of State Payments evidenced and represented by the Certificates. If the Treasurer enters into any additional Master Financing Lease for this purpose, the Corporation may be granted an interest in the Real Property under an additional Site Lease of all or any portion of the Real Property, which leasehold interest may be assigned to the Fiscal Agent for the benefit of owners of certificates of participation in such additional Master Financing Lease. The owners of certificates of participation in any additional Master Financing Lease will be secured proportionally, without preference, with the Owners with respect to any payments received by the Fiscal Agent in regards to the Real Property following the occurrence of an Event of Default or Permitted Termination Event.

The state may issue additional certificates of participation for other real and personal property by state and local agencies subject to the maximum authorized as described under "THE CERTIFICATES–Authorization."

## WASHINGTON FINANCE OFFICERS ASSOCIATION

The Washington Finance Officers Association is a Washington nonprofit corporation the members of which consist of state and local government finance officials in the state. The Corporation was formed primarily for educational purposes, including promoting the improvement of government finance in the state. The Corporation acts as the nominal purchaser, seller, lessee, and sublessor in connection with various certificate of participation financings undertaken by the Treasurer for the benefit of the state and local government agencies. In connection with the Certificates, the Corporation is acting as the lessee under each Site Lease, as lessor under the Master Financing Lease, as original purchaser of the Personal Property and as seller under the Master Financing Contract. As of the closing, the Corporation will irrevocably assign and transfer all of its right, title and interest in and to the Site Leases, the Master Financing Agreements and the Agency Financing Agreements, and thereafter will have no rights or interest with respect to the Certificates, the Projects, the Property, the Master Financing Agreements, the Agency Financing Agreements, or the Site Leases. The Corporation has not participated in the preparation of this Official Statement and is not responsible for any of the statements or information herein.

## FINANCIAL STATEMENTS

Audited basic financial statements for the state for the Fiscal Year ended June 30, 2010, are included as Appendix D. These statements have been audited by the Auditor, an independent elected state official. As described under "CONTINUING DISCLOSURE UNDERTAKING," the state is obligated to provide its audited financial statements to the Municipal Securities Rulemaking Board. In an effort to provide more timely reporting, the state successfully released its Fiscal Year 2010 audited financial statements within 150 days of the fiscal year-end.

## ECONOMIC AND REVENUE FORECASTS

Revenue, budgetary and economic information concerning the state government and Washington as a whole is contained in Appendix A–"GENERAL AND ECONOMIC INFORMATION." Pursuant to state law, the Office of Economic and Revenue Forecast Council (the "Forecast Council") provides state economic and revenue results and forecasts on a quarterly basis, generally in each March (February in even-numbered years), June, September and November. The Forecast Council's next economic and revenue forecast is scheduled to be released on or about November 17, 2011. As described in Appendix A, state law requires that state budgets and any necessary budgetary actions of the Governor during a fiscal period be based upon the Forecast Council's official economic and revenue forecasts. The Forecast Council's most recent forecast was released in September 2011, and that forecast is summarized in Appendix A. The Forecast Council also provides monthly updates of certain other information, including estimates of collections. In addition, the state prepares transportation forecasts, including forecasts of motor vehicle fuel excise tax collections, and forecasts about the state's entitlement caseloads. See Appendix A–"GENERAL FUND–General Fund-State Operating Budget" for a discussion of various actions and proposals to address the reduction in state revenue resulting from the continued economic downturn.

## LITIGATION

Based on an inquiry from the Attorney General's Office, there is no litigation now pending against the state in any way restraining or enjoining the sale, issuance or delivery of the Certificates, or in any manner challenging the validity of the Certificates, the security for the Certificates or the proceedings or authority pursuant to which they are to be sold and issued or the collection or application of any money pledged for the payment of the Certificates.

The state and its agencies are parties to routine legal proceedings that normally occur as a consequence of regular governmental operations. At any given point, there are lawsuits involving state agencies that could, depending on the outcome of the litigation or the terms of a settlement agreement, impact the state's or such agencies' budgets and expenditures to one degree or another. Some of these lawsuits are discussed in Appendix A and Appendix D. The state operates a self-insurance liability program for third-party claims against the state for injuries and property damage and purchases a limited amount of commercial insurance for these claims. The state maintains a risk management fund and is permitted to reserve up to 50 percent of total outstanding and actuarially determined liabilities. See Notes 7.E, 10 and 13.B in Appendix D—"THE STATE'S 2010 AUDITED BASIC FINANCIAL STATEMENTS" and "RISK MANAGEMENT" and "LITIGATION" in Appendix A—"GENERAL AND ECONOMIC INFORMATION."

## BALLOT MEASURES

Under the Constitution, the voters of the state have the ability to initiate legislation by initiative and to modify, approve or reject all or a part of recently existing statutes by referendum. Initiatives are new legislation proposed to the Legislature or for voter approval by petition of the voters. Referenda can be required on recently-enacted legislation through a petition of the voters, or a referendum on new legislation may be required by the Legislature itself. The Constitution may not be amended by initiative or referendum.

Any initiative or referendum approved by a majority of the voters may not be amended or repealed by the Legislature within a period of two years following enactment, except by a vote of two-thirds of all the members elected to each house of the Legislature. After two years, the relevant statute is subject to

amendment or repeal by the Legislature by a simple majority vote. See "GENERAL FUND–Revenue and Expenditure Limitations" in Appendix A.

***Initiatives.*** The Constitution requires an initiative petition to contain a number of signatures at least equal to 8 percent of all votes cast for Governor in the most recent gubernatorial election in the state. For 2011, the required number of signatures is 241,153. There are two types of initiatives: (1) initiatives to the people and (2) initiatives to the Legislature. Petitions for initiatives to the people must be filed not less than four months prior to the next state general election; for the November 2011 election petitions were due for certification on July 8, 2011. If certified to have sufficient signatures, initiatives to the people are submitted for a vote of the people at the next state general election. Petitions for initiatives to the Legislature must be filed not less than 10 days before the regular session of the Legislature; December 30, 2011, for the January 2012 regular session. If certified to have sufficient signatures, initiatives to the Legislature are submitted to the Legislature at its next regular session. The Legislature is required to either adopt the initiative, reject the initiative, or approve an alternative to the initiative. The latter two options require that the initiative or the initiative and the Legislature's alternative be placed on the ballot.

By statute, the Secretary of State is charged with verifying signatures and certifying whether sufficient signatures have been gathered to meet the constitutional requirement. Interpretation of initiatives is left to judicial court review.

The following three initiatives have been certified for the November 8, 2011 election:

1. Initiative 1125 ("I-1125") apparently is intended to amend various statutes to achieve the following purposes, among others: (1) prohibit the use of motor vehicle fuel taxes and tolls "for non-highway purposes;" (2) restrict the use of toll revenue to the facility on which those tolls are collected; (3) require that the Legislature serve as the tolling authority for the state; (4) require legislative action prior to the imposition of, increase in, or adjustment of tolls on most tolled facilities; (5) require that tolls be uniform and consistent, with no variable pricing; (6) require that tolls be removed "after the cost of the project is paid;" and (7) require that tolls imposed and collected on the I-90 floating bridge across Lake Washington be used exclusively for facilities and improvements to I-90, and for purposes "consistent with the eighteenth amendment to the Washington Constitution." (The Eighteenth Amendment to Washington's Constitution requires that motor vehicle fuel taxes and motor vehicle excise taxes "be used exclusively for highway purposes.")

2. Initiative 1163 would reinstate background checks, training and other requirements for long-term care workers and providers and would provide independent audits, increase fraud investigation, and cap administrative expenses for the long-term in-home care program.

3. Initiative 1183 would close state liquor stores and sell their assets. The state would license private parties to distribute spirits and sell spirits in retail stores and establish licensing fees for sale and distribution of spirits based on the licensee's sales revenues.

***Effect of New Legislation on Debt.*** Under current state law, including Washington State Supreme Court decisions, later enacted legislation, including initiatives, cannot impair the state's obligation or ability to comply with bond covenants and other similar contractual obligations in force prior to the effective date of that later enacted legislation.

***Referenda.*** The Constitution requires a petition for referendum to contain a number of signatures at least equal to 4 percent of all votes cast for Governor in the most recent gubernatorial election in the state. For 2011, the required number of signatures is 120,577. There are two types of referenda: (1) referendum

measures and (2) referendum bills. Referendum measures are laws recently passed by the Legislature that are placed on the ballot because of petitions signed by voters. Referendum bills are proposed laws referred to the voters by the Legislature. See Appendix A "GENERAL FUND–Budget Stabilization Account" for a description of a referendum on the November 2011 election.

## LEGAL MATTERS

Legal matters incident to the authorization, issuance and sale by the state of the Certificates are subject to the delivery of the approving legal opinion of Foster Pepper PLLC, Certificate Counsel to the state ("Certificate Counsel"). The proposed form of the legal opinion of Certificate Counsel is attached hereto as Appendix C. The opinions of Certificate Counsel are given based on factual representations made to Certificate Counsel, and under existing law, as of the date of initial delivery of the Certificates, and Certificate Counsel assumes no obligation to revise or supplement its opinions to reflect any facts or circumstances that may thereafter come to its attention, or any changes in law that may thereafter occur. The opinions of Certificate Counsel are an expression of its professional judgment on the matters expressly addressed in its opinions and do not constitute a guarantee of result. Certificate Council will be compensated only upon the issuance and sale of the Certificates.

## TAX MATTERS

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

***Continuing Requirements.*** The state is required to comply with certain requirements of the Code after the date of execution and delivery of the Certificates in order to maintain the exclusion of the interest evidenced and represented by the Certificates from gross income for federal income tax purposes, including, without limitation, requirements concerning the qualified use of Certificate proceeds and the facilities financed or refinanced with Certificate proceeds, limitations on investing gross proceeds of the Certificates in higher yielding investments in certain circumstances, and the requirement to comply with the arbitrage rebate requirement to the extent applicable to the Certificates. The state will covenant to comply with those requirements, but if the state fails to comply with those requirements, interest evidenced and represented by the Certificates could become taxable retroactive to the date of execution and delivery of the Certificates. Certificate Counsel has not undertaken and does not undertake to monitor the state's compliance with such requirements.

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

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

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

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

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

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

The state is a governmental unit that, together with all subordinate entities, has issued more than $10,000,000 of tax-exempt obligations during the current calendar year and has not designated the Certificates as "qualified tax-exempt obligations" for purposes of the 80 percent financial institution interest expense deduction. Therefore, no interest expense of a financial institution allocable to the Certificates is deductible for federal income tax purposes.

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

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

***Other Possible Federal Tax Consequences.*** Receipt of interest evidenced and represented by the Certificates may have other federal tax consequences as to which prospective purchasers of the Certificates may wish to consult their own tax advisors.

***Potential Future Federal Tax Law Changes.*** From time to time, there are legislative proposals in Congress which, if enacted, could require changes in the description of federal tax matters relating to the Certificates set forth above or adversely affect the market value of the Certificates. For example, on September 12, 2011, the President submitted to Congress a legislative proposal entitled the "American Jobs Act of 2011" (the "Jobs Act"), certain provisions of which, if enacted as proposed, would result in federal income tax being imposed on a portion of the interest on tax-exempt bonds (including the Certificates) received in taxable years beginning on or after January 1, 2013, by taxpayers with incomes above certain thresholds specified in the Jobs Act. It cannot be predicted whether the Jobs Act will be enacted as proposed or other future legislation may be proposed or enacted that would affect the federal tax treatment of interest received on the Certificates. Prospective purchasers of the Certificates should consult with their own tax advisors regarding any proposed or pending legislation that would change the federal tax treatment of interest on the Certificates, including the provisions of the Jobs Act.

## CONTINUING DISCLOSURE UNDERTAKING

In accordance with paragraph (b)(5) of Securities and Exchange Commission (the "SEC") Rule 15c2-12 promulgated under the Securities Exchange Act of 1934, as amended (the "Rule"), the Treasurer has agreed in the Master Financing Agreements to enter into a written undertaking in the form of a Disclosure Agreement for the benefit of the beneficial owners of the Certificates (the "Undertaking").

***Annual Disclosure Report.*** The state covenants and agrees in the Undertaking that not later than seven months after the end of each Fiscal Year (the "Submission Date"), beginning January 31, 2012, for the Fiscal Year ended June 30, 2011, the state will provide or cause to be provided either directly or through a designated agent, to the Municipal Securities Rulemaking Board (the "MSRB"), in an electronic format as prescribed by the MSRB, accompanied by identifying information as prescribed by the MSRB, an annual report (the "Annual Disclosure Report") that will consist of the following:

(1) audited financial statements of the state prepared (except as noted in the financial statements) in accordance with generally accepted accounting principles as promulgated by the Governmental Accounting Standards Board, as such principles may be changed from time to time, except that if the audited financial statements are not available by the Submission Date, the Annual Disclosure Report will contain unaudited financial statements in a format similar to the audited financial statements most recently prepared for the state, and the state's audited financial statements will be filed in the same manner as the Annual Disclosure Report when and if they become available;

(2) historical financial and operating data for the state of the type set forth in Appendix A; and

(3) a narrative explanation of any reasons for any amendments to the Undertaking made during the previous fiscal year and the effect of such amendments on the Annual Disclosure Report being provided.

Any or all of the items listed above may be included by specific reference to other documents available to the public on the Internet website of the MSRB or filed with the SEC. The state will identify clearly each document so included by reference. The MSRB has indicated that it intends to make continuing disclosure information submitted to it publicly available on the Internet on its Electronic Municipal Market Access system website.

The Annual Disclosure Report may be submitted as a single document or as separate documents comprising a package and may include by reference other information as provided herein; provided that any audited financial statements may be submitted separately from the balance of the Annual Disclosure Report and later than the Submission Date if such statements are not available by the Submission Date.

If the state's fiscal year changes, the state may adjust the Submission Date by giving notice of such change in the same manner as notice is to be given of the occurrence of a Listed Event.

The state agrees to provide or cause to be provided to the MSRB, in a timely manner, notice of its failure to provide the Annual Disclosure Report on or prior to the Submission Date.

***Listed Events.*** The state agrees to provide or cause to be provided, in a timely manner, not in excess of 10 business days after the occurrence of the event, to the MSRB notice of the occurrence of any of the following events with respect to the Certificates, if material (the "Material Events"): (1) principal and interest payment delinquencies; (2) nonpayment-related defaults, if material; (3) unscheduled draws on debt service reserves reflecting financial difficulties; (4) unscheduled draws on credit enhancements reflecting financial difficulties; (5) substitution of credit or liquidity providers, or their failure to perform; (6) adverse tax opinions, the issuance by the Internal Revenue Service of proposed or final determinations of taxability, Notice of Proposed Issue (IRS form 5701 – TEB) or other material notices or determinations with respect to the tax status of the Certificates; (7) modifications to rights of owners of the Certificates, if material; (8) Certificate calls (other than scheduled mandatory redemptions of Term Certificates), if material, and tender offers; (9) defeasances; (10) release, substitution or sale of property securing the repayment of the Certificates, if material; (11) rating changes; (12) bankruptcy, insolvency, receivership or similar event of the state, as such "Bankruptcy Events" are defined in the Rule; (13) the consummation of a merger, consolidation, or acquisition involving the state or the sale of all or substantially all of the assets of the state, other than in the ordinary course of business, the entry into a definitive agreement to undertake such an action or the termination of a definitive agreement relating to any such actions, other than pursuant to its terms, if material; and (14) appointment of a successor or additional trustee or the change of name of a trustee, if material.

***Termination or Modification of Undertaking.*** The state's obligations under the Undertaking will terminate upon the legal defeasance, prior prepayment or payment in full of all of the Certificates. The Undertaking, or any provision thereof, is to be null and void if the state:

(1) obtains an opinion of nationally recognized bond counsel to the effect that those portions of the Rule which require the Undertaking, or any such provision, have been repealed retroactively or otherwise do not apply to the Certificates; and

(2) notifies the MSRB, in a timely manner, of such opinion and the cancellation of the Undertaking.

The state may amend the Undertaking without the consent of any holder of any Certificate or any other person or entity under the circumstances and in the manner permitted by the Rule. The Treasurer will give notice to the MSRB of the substance of any such amendment, including a brief statement of the reasons therefor.

If the amendment changes the type of Annual Disclosure Report to be provided, the Annual Disclosure Report containing the amended financial information will include a narrative explanation of the effect of that change on the type of information to be provided (or in the case of a change of accounting principles, the presentation of such information). In addition, if the amendment relates to the accounting principles to be followed in preparing financial statements:

(1) notice of such change will be given in the same manner as for a Listed Event, and

(2) the Annual Disclosure 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.

***Remedies.*** The right to enforce the provisions of the Undertaking will be limited to a right to obtain specific enforcement of the state's obligations thereunder, and any failure by the state to comply with the provisions of the Undertaking will not be a default with respect to the Certificates.

***Additional Information.*** Nothing in the Undertaking will be deemed to prevent the state from disseminating any other information, using the means of dissemination set forth in the Undertaking or any other means of communication, or including any other information in any Annual Disclosure Report or notice of occurrence of a Listed Event, in addition to that which is required by the Undertaking. If the state chooses to include any information in any Annual Disclosure Report or notice of the occurrence of a Listed Event in addition to that specifically required by the Undertaking, the state will have no obligation to update such information or to include it in any future Annual Disclosure Report or notice of occurrence of a Listed Event.

***Prior Compliance.*** The state has complied in all material respects with all prior written undertakings under the Rule.

## RATING

Moody's Investors Service, Inc. ("Moody's") has assigned a rating of "Aa2" to the Certificates. The state has furnished certain information and materials to Moody's regarding the Certificates and the state. Such rating reflects only the view of such rating agency and is not be a recommendation to buy, sell or hold the Certificates. Generally, rating agencies base their ratings on the information and materials furnished to them and on their own investigations, studies and assumptions. An explanation of the significance of such rating may be obtained from Moody's Investors Service Inc., located at 7 World Trade Center, 250 Greenwich Street, New York, New York 10007.

There is no assurance that such rating will be maintained for any given period of time or that it may not be raised, lowered, suspended, or withdrawn entirely by the rating agency if, in its judgment, circumstances warrant. Any such downward change in or suspension or withdrawal of such rating may have an adverse effect on the market price of the Certificates. The state undertakes no responsibility to oppose any such change or withdrawal.

## UNDERWRITING

The Certificates are being purchased by _____ (the "Underwriter") at a price of $_____, representing the aggregate principal amount of the Certificates, [plus original issuance premium, less original issue discount and] less Underwriter's discount of $_____. The Underwriter has represented that the Certificates are to be reoffered at the prices or yields set forth on page i of this Official Statement. The Underwriter may offer and sell the Certificates to certain dealers (including dealers depositing Certificates into investment trusts) and others at prices lower than the initial offering prices set forth on page i hereof, and such initial offering prices may be changed from time to time by the Underwriter. After the initial public offering, the public offering prices may be varied from time to time.

## FINANCIAL ADVISOR

SDM Advisors, Inc. has served as financial advisor to the state in connection with the issuance and sale of the Certificates. The financial advisor has not audited, authenticated or otherwise verified the information set forth in this Official Statement or other information provided relative to the Certificates. SDM Advisors, Inc. makes no guaranty, warranty or other representation on any matter related to the information contained in this Official Statement. The financial advisor is an independent financial advisory firm and is not engaged in the business of underwriting, marketing, trading, or distributing municipal securities. The payment of compensation to the financial advisor is contingent upon the successful delivery of the Certificates to, and full payment for the Certificates by, the Underwriter.

## MISCELLANEOUS

Any statements made in this Official Statement involving matters of opinion, whether or not expressly so stated, are intended as such and not as representations of fact.

The state has duly authorized the execution and delivery of this Official Statement.

STATE OF WASHINGTON

By:_____

Deputy Treasurer–Debt Management

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# APPENDIX A

# GENERAL AND ECONOMIC INFORMATION

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# INTRODUCTION

## State Overview

The State of Washington (the "state" or "Washington"), the nation's 42nd state, was created in 1889 by an act of the U.S. Congress. The state is located on the Pacific Coast in the northwestern corner of the continental United States and comprises 71,303 square miles, including the more than 1,000 square miles of salt water known as Puget Sound.

Washington's population is 6,724,540 according to the 2010 U.S. Census, making the state the 13th most populous in the United States. The state's capital is Olympia at the southern end of Puget Sound, and the state's largest city, Seattle, is approximately 60 miles north of Olympia.

Washington is a geographically diverse state with two mountain ranges that divide the state's land area. The Olympic Mountains separate the Olympic Peninsula – generally regarded as the largest rain forest in the Northern hemisphere – from Puget Sound and the rest of the state. The Cascade Mountains extend from the northern border of the state with British Columbia, Canada, south to the State of Oregon. Mount Rainier, a 14.4 thousand-foot dormant volcano in the middle of the Cascade Range, is the fifth highest and most heavily glaciated peak in the lower 48 states.

Washington includes an international trade, manufacturing, technology, biotechnology and business service corridor that extends along Puget Sound from the City of Everett at the north end, south to Seattle and Tacoma. This corridor includes approximately 75 percent of the state's population and economic activity. A number of companies have chosen Washington as their headquarters or as a major center of operations, including Amazon, Amgen, Boeing Commercial Airplanes, Costco, F5 Networks, Microsoft, Nintendo America, Nordstrom, PACCAR, Starbucks and Weyerhaeuser. According to the U.S. Bureau of Economic Analysis, Washington ranked 14th in the United States in terms of real gross domestic product ("GDP") in 2010.

East of the Cascade Mountains is the center of dairy operations and production of crops such as wheat, potatoes, tree fruits and grapes within the state. Washington leads the nation in apple production and, on both sides of the Cascade Mountains, produces wine, flower bulbs and lumber, wood pulp, paper and other wood products. The Olympic Peninsula and the Puget Sound region include one of the country's primary aquaculture and fish- and shellfish-processing areas.

Washington is one of the most trade-intensive states in the nation, as measured by the dollar value of per capita exports, and is an important gateway for trade with Asia and Canada and for domestic trade with Alaska and Hawaii. The Ports of Seattle and Tacoma, the state's largest ports, are closer to Asian ports than any other continental port in the United States. Seattle-Tacoma International Airport is Washington's primary airport, serving the region's air passengers and cargo. Direct access to midwest and east-coast markets by land is via four major interstate highways and two transcontinental rail service providers.

The state's ferry system, the largest ferry system in the United States and the third-largest ferry system in the world, is owned and operated by the Washington State Department of Transportation ("WSDOT") and connects 15 islands and other areas within and along the coast of Puget Sound.

See "DEMOGRAPHIC AND ECONOMIC INFORMATION" for additional economic and demographic information about the state.

### State Government

Under the state Constitution (the "Constitution"), the legislative authority of the state is vested in the Legislature, and general elections are held on the first Tuesday in November in each even-numbered year. The state is divided into 49 legislative districts, each of which elects two representatives and one senator. Senators serve four-year terms, with one-half of the seats open in each general election. Representatives serve two-year terms, with every seat open in each general election. The Legislature convenes annual regular sessions of 105 days (beginning the second Monday in January) in odd-numbered years and 60 days (beginning the second Monday in January) in even-numbered years. The Governor may call an unlimited number of special sessions, each of which is limited to 30 days, and the Legislature itself may call special sessions with a two-thirds' vote of the members of each house.

Nine state executive officers are elected at-large to four-year terms at general elections held in the same years as elections for the President of the United States: the Governor, Lieutenant Governor, Secretary of State, Treasurer, Auditor, Attorney General, Superintendent of Public Instruction, Commissioner of Public Lands and Insurance Commissioner.

The nine justices of the state Supreme Court (the "Supreme Court") are elected at-large to six-year terms, with three seats open in each general election.

### State Finance Committee

The Legislature, by statute, has delegated to the State Finance Committee (the "Committee") authority to supervise and control the issuance of all state bonds and other state obligations, including financing leases, authorized by the Legislature. The Committee is composed of the Governor, Lieutenant Governor and Treasurer. The Treasurer is designated as Chairman of the Committee, and the Office of the State Treasurer provides administrative support to the Committee. A Deputy State Treasurer acts as recording officer for the Committee and is responsible for the administration of the Committee's official duties in accordance with prescribed policies of the Committee. See "INDEBTEDNESS AND OTHER OBLIGATIONS."

In 2010, the Legislature authorized the Committee to delegate to the State Treasurer the authority, by resolution, to (1) accept offers to purchase bonds, notes, or other evidences of indebtedness of the state and to sell and deliver such bonds, notes, or other evidences of indebtedness to the purchasers thereof; (2) determine the date or dates, price or prices, principal amounts per maturity, delivery dates, interest rate or rates (or mechanisms for determining the interest rate or rates); and (3) set other terms and conditions as the Committee may deem necessary and appropriate; with each such delegation to be limited to bonds, notes, or other evidences of indebtedness which the Committee has authorized to be issued.

## BUDGETING AND ACCOUNTING

### Budget and Appropriation Process

The state operates on a July 1 to June 30 fiscal year ("Fiscal Year") and is required under state law to budget on a biennial basis. State law requires that the Governor submit a balanced budget to the Legislature no later than December 20 in the year preceding the session during which the biennial budget is to be considered. The operating, capital and transportation budgets are prepared separately. As described below, the Governor is required to include, and the Legislature is required to appropriate, amounts sufficient to pay debt service on all of the state's outstanding general obligation bonds. See "GENERAL FUND–General Fund Expenditures–Payment of General Obligation Bonds" and

"TRANSPORTATION-RELATED REVENUES AND EXPENDITURES–Transportation Expenditures–Payment of Bonds Payable from Excise Taxes on Motor Vehicle and Special Fuels."

Formulation of the state's biennial budget begins in May of even-numbered years, when the Office of Financial Management ("OFM") distributes instructions to all state agencies, establishing budget guidelines and information requirements. Formal budget requests from agencies are sent to OFM in late summer, after which they are analyzed and revised by OFM as appropriate to match the Governor's policy choices. Alternative methods of delivering services are examined and evaluated, and recommended budget levels and program and policy choices are prepared for the Governor by the Director of OFM. As described below, state revenues and expenditures are limited by statutes enacted by the Legislature and sometimes also are limited by initiatives or referenda approved by the voters. See "GENERAL FUND–Revenue and Expenditure Limitations" below and "BALLOT MEASURES" in the front portion of this Official Statement.

Under state law, the Governor's budget submitted to the Legislature must include estimates of all anticipated revenues and all proposed operating and capital expenditures, including debt service requirements on state general obligation indebtedness. Revenues are estimated for a fiscal period from the sources, and at the rates, authorized by law at the time of submission of the budget document and are based upon entitlement caseload forecasts and quarterly economic and revenue forecasts as described below. A "fiscal period" is the Fiscal Year or biennium for which an appropriation is made as specified within the act making the appropriation.

The Governor must submit a balanced budget to the Legislature. Specifically, state law requires that in the Governor's proposed budget the total of the beginning undesignated fund balance and estimated revenues, less working capital and other reserves, equal or exceed the total of proposed expenditures without reliance upon increases in indebtedness, changes in existing tax rates or other statutory changes. The Governor also may submit a second, alternative budget for the same fiscal period to include expenditures from revenue sources derived from proposed changes in statutes.

Within a biennium, the Governor may submit supplemental budgets to the Legislature during the regular session or during any special session. See "GENERAL FUND–General Fund–State Operating Budget."

State law also provides that if for any applicable fund or account the estimated receipts for the next fiscal period, plus cash beginning balances, is less than the aggregate of estimated disbursements proposed by the Governor for the next ensuing fiscal period, the Governor must include proposals as to the manner in which the anticipated cash deficit is to be met, whether by an increase in state indebtedness, by the imposition of new taxes, by increases in tax rates or by an extension of existing taxes. The Governor also may propose planned elimination of the fund's or account's anticipated cash deficit over one or more fiscal periods. See "–Fiscal Monitoring and Controls."

The Legislature is obligated under the Constitution to appropriate money for debt service requirements on state general obligation indebtedness. Appropriations providing for the payment of bond principal and interest requirements on each series of bonds normally are included in an omnibus appropriation act.

The Legislature engages in extensive budget deliberations and committee hearings. After revenue and expenditure appropriation bills are passed by the House of Representatives and the Senate, the bills are transmitted to the Governor, who has constitutional authority to veto one or more sections of the bills.

Typically, the Legislature enacts three budgets: an operating budget, a capital budget and a transportation budget. The transportation budget includes both operating and capital transportation-related expenditures. Of the three state budgets, the operating budget is the largest. Sales and other excise taxes deposited to

the General Fund are the major state funding source for operating expenditures, and proceeds of state bonds have been the main source for capital expenditures. The transportation budget is funded primarily from bond proceeds, excise taxes on motor vehicle and special fuels, license fees and other state revenues, federal funds and local and private funds.

**Economic and Revenue Forecasting**

To assist the state in financial planning and budgeting, the state's Economic and Revenue Forecast Council (the "Forecast Council") prepares quarterly economic and revenue forecasts (other than forecasts of transportation revenues, which are prepared by the state's Transportation Revenue Forecast Council, and other than the state entitlement caseload forecasts, which are prepared by the state's Caseload Forecast Council, both described below). The Forecast Council is an independent state agency consisting of six members, two appointed by the Governor and one appointed by each of the two largest political caucuses of the Senate and House of Representatives. The Forecast Council approves the official economic and revenue forecasts for the state and reviews revenue collections monthly during each biennium. State law requires that the development of state budgets and any necessary budgetary actions of the Governor during a fiscal period be based upon the official economic and revenue forecasts of the Forecast Council and that the state's transportation budget be based upon the transportation forecast prepared by the Transportation Revenue Forecast Council. See "TRANSPORTATION-RELATED REVENUES AND EXPENDITURES–Transportation Revenue Forecast Council."

In mid-February (March in odd-numbered years), June, September and November, the Chief Economist prepares an official state economic and revenue forecast and two unofficial forecasts, one based upon optimistic economic and revenue assumptions and one based upon pessimistic economic and revenue assumptions. The forecasts are based in part upon forecasts of the United States economy and forecasts of state entitlement caseloads. See "GENERAL FUND–Economic and Revenue Forecast" and "–Caseload Forecast."

**Fiscal Monitoring and Controls**

When it enacts a biennial budget, the Legislature appropriates funding to state agencies for various purposes. Once the budget bills are signed by the Governor, OFM works with state agency fiscal staff to allot annual and biennial appropriations into monthly amounts. Revenues also are allotted for the biennium based upon forecasts prepared by the Forecast Council and for non-forecasted accounts, based upon information prepared by the administering agencies. Taken together, monthly allotments of expenditure authority and revenue form detailed monthly spending plans within the statutory maximums specified by appropriations in the biennial budget.

State agencies generally are prohibited from incurring cash deficits. State law does allow, however, for temporary negative cash balances in a specific fund or account if the temporary deficiency (1) results from disbursements under a spending plan approved by OFM; (2) was authorized by OFM within a fiscal period; (3) is in a fund or account neither in the state treasury nor in the custody of the Treasurer if the cash deficiency does not continue past the end of the biennium; or (4) is in a construction account and the deficiency is due to seasonal cash deficits pending receipt of proceeds from authorized bond or note sales.

OFM monitors spending plans on a monthly basis and recommends actions the Governor may take to adjust spending and revenue as appropriate. If at any time during the current fiscal period the Governor projects a cash deficit in a specific fund or account, the Governor may order across-the-board reductions in allotments to that fund or account to prevent the cash deficit. The Legislature may direct that a cash deficit in a particular fund or account be eliminated over one or more fiscal periods. Unused appropriation authority resulting from an across-the-board reduction in a fund or account is placed in

reserve status. Across-the-board reductions are not made to funding for basic education, pension benefits or general obligation debt service funding and can be made only within a fund with a cash deficit. In addition, the Governor may direct cabinet agencies to limit their discretionary spending. See "GENERAL FUND–State Operating Budget."

### Accounting and Auditing

State law requires expenditures and revenues to be based upon generally accepted accounting principles ("GAAP"), and revenues typically are treated on a modified accrual basis so that funds are recognized when they become measureable and available. The state also is required to maintain accounting records in conformance with GAAP. The accounting system generates monthly and other periodic financial statements at the state-wide combined level and at the agency, fund and program levels for use by OFM and state agencies in monitoring expenditures and in preparing budgets and the state's annual financial statements.

The Auditor, an independent elected official, audits the state-wide combined financial statements for each Fiscal Year. See Appendix D–"THE STATE'S 2010 AUDITED BASIC FINANCIAL STATEMENTS."

## GENERAL FUND

The state provides for most of its general operations through the General Fund. Most of the state's unrestricted revenues are deposited to the General Fund, and most of the state's general expenditures and general obligation debt service are paid from the General Fund. Debt service on general obligation bonds to which excise taxes on motor vehicle and special fuels are pledged is payable first from the state's Motor Vehicle Fund and, if those funds are insufficient, from the General Fund. As described below and in Appendix D–"THE STATE'S 2010 AUDITED BASIC FINANCIAL STATEMENTS," the state also maintains a number of other funds and several hundred accounts.

### General Fund Revenue

Most of the General Fund revenue is derived from state taxes and federal funds, with other charges, interest, license and other fees and miscellaneous income making up the remaining General Fund revenue. See "–General Fund-State Operating Budget" and Table 4.

General Fund tax revenues consist primarily of sales taxes, business and occupation taxes, other excise taxes and property taxes. There is no state income tax. Not all money deposited in the General Fund constitutes general state revenues or is available for the payment of general obligation debt service (e.g., restricted federal funds and local and private revenue). See "General Fund Expenditures–Payment of General Obligation Bonds" and "INDEBTEDNESS AND OTHER OBLIGATIONS–General Obligation Debt."

***Excise Taxes.*** The retail sales tax and its companion use tax represent the largest source of state tax revenue. Retail sales and use taxes are applied to a broad base of tangible personal property, certain digital products and selected services purchased by consumers, including construction (labor and materials), some machinery and supplies used by businesses, services and repair of real and personal property and other transactions not taxed in many other states. Unless waived or deferred by the Legislature, the state and local governments are obligated to pay the same retail sales and use taxes as other taxpayers. The Legislature, and the voters of the state through the initiative process, have changed the base of the state retail sales and use taxes on occasion, and this may occur again in the future. Among the various items not subject to the state retail sales and use taxes are most personal and professional services and motor vehicle and special fuels (all of which are subject to the separate excise taxes

described below), food and food ingredients (excluding prepared food), trade-ins, manufacturing machinery and purchases for resale. The state retail sales and use tax rate was last increased in 1983. Certain local taxing jurisdictions also are authorized to impose retail sales and use taxes. In some circumstances the Legislature has granted credits to local jurisdictions against the state sales tax for the local retail sales and use taxes. These credits have the effect of reducing the amount of state sales tax revenues retained by the state. Current state and local retail sales and use tax rates are shown in Table 1.

**Table 1**
**State and Local Retail Sales and Use Tax Rates**

| | General | New and Used Vehicles |
|---|---|---|
| **State** | 6.5% | 6.8% |
| **Local** | 0.5 to 3.0 | 0.5 to 3.0 |

*Source: Department of Revenue.*

The state business and occupation ("B&O") tax is applied to "gross receipts" (the value of products, gross income from sales or certain other income) from business activities conducted within the state. B&O tax rate reductions and tax credits for specific categories of businesses are enacted from time to time. Certain local taxing jurisdictions also are authorized to impose business and occupation taxes. The state's current B&O tax rates vary, depending upon the classification of business activities, and in general range from 0.138 percent to 1.8 percent of gross receipts; most are under 0.5 percent. See "General Fund–State Operating Budget" and Table 4.

The state imposes a real estate excise tax of 1.28 percent on sales of real property. Each county treasurer is required by statute to retain 1.3 percent of the proceeds of this tax to defray costs of collection and on a monthly basis to pay over to the Treasurer the balance of the proceeds. Of the proceeds received by the Treasurer, the Treasurer is required to deposit an amount equal to 6.1 percent into the Public Works Assistance Account and an amount equal to 1.6 percent to the City-County Assistance Account. The balance is deposited to the General Fund. Certain local taxing jurisdictions are authorized to impose real estate excise taxes. In most areas in which a local real estate excise tax is imposed, the maximum local rate is 0.5 percent of the sales price.

***Property Taxes.*** Property taxes apply to the assessed value of all taxable property, including all real and personal property located within the state, unless specifically exempted. Real property includes land, structures and certain equipment affixed to the structure. Personal property includes machinery, supplies, certain utility property and items owned by businesses and farmers that are generally movable.

The assessed value of most real property is determined by the county assessors, with the goal being to determine the fair market value of the property according to its highest and best use (unless an exemption applies that would permit a lower use to be considered). Property taxes for local taxing districts are levied against this assessed value. The state property tax is levied against the assessed value determined by the county assessors but then is adjusted to the state equalized value (a rate that would be equal across the state) in accordance with a ratio fixed by the Department of Revenue. For property taxes payable in 2010, assessed value against which property taxes were levied averaged 88.1 percent of fair market value as determined by the county assessors.

The Constitution provides that the aggregate of all regular (nonvoted) tax levies upon real and personal taxable property by the state and local taxing districts may not exceed 1.0 percent of the true and fair value of such property unless for the purpose of preventing the impairment of the obligation of a contract

when ordered to do so by a court of last resort. Excess property tax levies are subject to voter approval and are not subject to this limitation.

Increases in assessed values of property are not limited; however, by statute, the state property tax levy is limited to the limit factor (the lesser of 101 percent, or 100 percent plus inflation) multiplied by the amount of property taxes levied by the state in the highest of the three most recent years, plus an additional amount calculated by multiplying the increase in assessed value resulting from new construction and improvements by the property tax rate for the preceding year. The average state levy rate for taxes due in calendar year 2010 was $1.87 per $1,000 of true and fair property value.

By statute, all of the proceeds of the state's property tax levy are to be deposited to the General Fund and may be used only for the support of common schools (K-12), including debt service on bonds issued by the state for capital construction projects for common schools.

***Other State Tax Revenue.*** The state imposes a number of other taxes, including estate taxes, liquor taxes, rental car and telephone taxes, taxes on hazardous substances and taxes on cigarettes and other tobacco products. Together, these other taxes represent approximately 2.0 percent of state tax revenue.

***State Non-Tax Revenue.*** The largest components of state non-tax revenue include revenues derived from the sale of supplies, materials and services; fines and forfeitures; income from property; and income from liquor sales.

***Federal Revenue.*** Legislative appropriations for federal programs are designated specifically to be funded from federal revenue sources. To the extent that federal funds are not received, the appropriated expenditures may not be incurred. Use of federal funds is subject to audit, and often federal funds are payable only on a reimbursement basis. The state also may be required to appropriate and expend its own funds as a condition to receiving the federal revenue. As shown in Tables 4 and 5, federal funds for a variety of different programs increased significantly in Fiscal Years 2009, 2010 and 2011 as a result of federal funds made available under the American Recovery and Reinvestment Act of 2009 ("ARRA"). Federal revenues may be deposited into the General Fund, but are not "general state revenue." See "General Fund Expenditures–Payment of General Obligation Bonds" and "General Fund–State Operating Budget."

***Private and Local Revenues.*** Revenues provided to the state by private individuals, local governments (but not the federal government), commercial enterprises and foundations under agreements that restrict the use of such revenues and revenues received as payment for private or local purchases of goods or services or as reimbursement for expenditures by the state are separate from "general state revenues."

***Tax and Other Revenue Collection.*** Four state agencies are responsible for administering the major state taxes: the Department of Revenue, the Department of Licensing, the Liquor Control Board, and the Office of the Insurance Commissioner. The Treasurer receives the revenues from the collecting agencies and is required to deposit and distribute the funds as directed by law. Nearly all state agencies collect some form of revenue. See Table 4.

**General Fund Expenditures**

The state's largest General Fund expenditures are for education, social and health services and corrections. As described below, most of these expenditures are mandated either by state law (education, corrections and debt service) or by federal law (Medicaid and certain other human services). Federal funds are available to pay some of the federally-mandated costs.

***Education.*** The state's expenditures for public schools are mandated by the constitutional requirement that the state support the common schools, and as shown in Table 5, a significant portion of the General Fund budget is used for supporting public schools. The Supreme Court has interpreted the Constitution to require the state to ensure that each public school district receives the funds needed to provide a basic education.

In past legislative sessions, the Legislature enacted legislation intended to improve the stability and predictability of school funding, including legislation that (1) prescribes course offerings, teacher contract hours and core student/staff ratios; (2) limits local property tax levies and provides for the gradual equalization of levy capacity per student throughout the state; (3) limits local compensation increases to those authorized by the state; and (4) provides for state assistance to equalize tax rates for local levies, establishes a state-wide salary allocation schedule with mandated minimum salaries for teachers and requires school districts to maintain minimum teacher/student ratios. In the past, state voters, through the initiative process, have also affected school expenditures and current litigation may affect expenditures in the future. See "BALLOT MEASURES" in the front portion of this Official Statement and "LITIGATION" in this Appendix A. The Legislature has again temporarily suspended two initiatives relating to school expenditures as part of the amended 2009-11 Biennium Budget and the 2011-13 Biennium Budget. See "General Fund–State Operating Budget."

***Social and Health Services.*** The Department of Social and Health Services ("DSHS") provides services that include protective services for children, the aged and mentally disabled people and services for people in institutions and other residential care facilities.

While in the past the largest expenditure within DSHS was the Medical Assistance Program, as of July 1, 2011, this program became part of the Health Care Authority. Through this program, medical care is made available to recipients of cash assistance programs, beneficiaries of Supplemental Security Income and other eligible people with low incomes who do not qualify for income assistance. In addition to support from the General Fund, funding is received from the federal government for those people and for services covered under Medicaid. The Medical Assistance Program budget has grown significantly in recent years. Growth in the number of eligible recipient groups, rising health care costs and requirements to provide higher payments to hospitals have resulted in increased expenditures.

The Economic Services Program provides support to families with limited incomes and to disabled people who cannot work. The federal government provides funds for the Temporary Assistance for Needy Families Program and for several other, smaller programs.

DSHS is also responsible for supporting community mental health programs and for operating state psychiatric hospitals, institutions for the developmentally disabled, nursing homes, institutions for juvenile rehabilitation, child welfare service programs, child support enforcement activities, drug and substance abuse treatment programs, foster care programs and vocational rehabilitation services.

***Corrections.*** As of August 2011, the Department of Corrections ("DOC") had 12 correctional institutions and 15 work release facilities and leased 990 rental beds in-state. As of August 2011, the offender population was approximately 16,300 in the prison system and 662 at state work-release sites. In 2010, the state closed Ahtanum View Corrections Center in Yakima and the Pine Lodge Corrections Center for Women in Medical Lake. In 2011, the state closed McNeil Island Corrections Center in south Puget Sound.

***Employees and Employee Benefits.*** The state budgeted for 112,545 full-time equivalents ("FTEs") in Fiscal Year 2009, including Higher Education employees. Compensation for approximately 40 percent of these FTEs constituted expenditures of the General Fund in Fiscal Year 2009. In Fiscal Year 2010, the

state budgeted amounts for 109,969 FTEs. The 2011-2013 Budget budgets for 107,000 FTEs, which lower level reflects the series of cuts made in the past several legislative sessions. Approximately 53 percent of these FTEs are represented by collective bargaining organizations. There are 29 different collective bargaining organizations currently representing state employees. The largest, the Washington Federation of State Employees, represents approximately 31,000 state employees. State law provides that nothing in the state collective bargaining statute permits or grants to any employee the right to strike or refuse to perform his or her official duties.

The state, through the Public Employees Benefits Board program, provides medical, dental, life and long-term disability coverage to eligible state employees as a benefit of employment. Coverage is provided through private health insurance plans and self-insured products. The state's share of the cost of coverage for state employees is based on a per capita amount determined annually by the Legislature and allocated to state agencies. State employees self-pay for coverage beyond the state's contribution. The average benefit was $841 in 2010, with $755 paid by the state and $86 by the employee. State employees accrue vested vacation leave at a variable rate based on years of service, which in general cannot exceed 240 hours per year. It is the state's policy to liquidate unpaid compensated absences outstanding at June 30 with future resources. State employees accrue sick leave at the rate of one day per month without limitation. The state does not pay employees for unused sick leave upon termination except upon employee death or retirement. At death or retirement, the state is liable for 25 percent of the employee's accumulated sick leave. For a discussion of the state retirement plans and post employment benefits, see "RETIREMENT SYSTEMS."

***Payment of General Obligation Bonds.*** Statutes authorizing bonds and other general obligations of the state require the Committee to certify to the Treasurer on or before June 30 of each year the amount needed to provide for payment of debt service and require the Treasurer to deposit "general state revenues" in such amount into the Bond Retirement Accounts. The term "general state revenues" is defined in Article VIII of the Constitution and, as described below, not all money deposited in the General Fund constitutes "general state revenues" available for the payment of debt service (e.g., restricted federal funds or local and private revenue). See the description of general state revenues under "INDEBTEDNESS AND OTHER OBLIGATIONS–General Obligation Debt–Constitutional General Obligation Debt Limitation" and Table 4.

Some general obligation bond statutes provide that the General Fund will be reimbursed for bond debt service from discrete revenues that are not considered "general state revenues." For example, tuition fees charged by institutions of higher education must be used to reimburse the General Fund for payment of debt service for a number of higher education construction bond issues. Similar reimbursement requirements apply to hospital patient fees (for University of Washington hospital construction bonds) and to lease-rental proceeds (for Washington State University research center bonds). All of these required reimbursements have been made to date. In addition, a portion of net lottery and retail sales tax proceeds collected in King County reimburse the state for debt service payable on bonds issued to finance construction of a stadium and exhibition center in Seattle. See "INDEBTEDNESS AND OTHER OBLIGATIONS."

**Revenue and Expenditure Limitations**

From time to time the Legislature or state voters limit (by initiative or referendum) the state's authority to increase revenues. Initiative 601, approved by the voters in 1993, as amended by the Legislature and restored by subsequent initiatives in 2007 and 2010, requires that any action by the Legislature to raise taxes be approved either by a two-thirds' vote of the members of each house of the Legislature or by the voters or, in certain cases, by both, and that a fee may only be imposed or increased if approved by a majority vote of each house.

In addition to limiting the state's authority to generate revenues, from time to time state voters (by initiative or referendum) limit the state's authority to make expenditures. Initiative 601 prohibits the state from increasing expenditures from the General Fund during any Fiscal Year by more than the fiscal growth factor. The fiscal growth factor is calculated annually and is defined as the average growth in state personal income for the prior 10 Fiscal Years, adjusted for actual expenditures in the previous year and for certain money transfers and program cost shifts (to take into account federal and local revenue). Under current law, voter approval would be required to exceed the expenditure limit, except in case of an emergency. In the event revenues collected exceed the amount of revenues that may be expended under the expenditure limitation, the excess revenues are to be deposited to the Budget Stabilization Account as described in the next subsection. See "BALLOT MEASURES" in the front portion of this Official Statement.

**Budget Stabilization Account**

In 2008, the Constitution was amended to create a Budget Stabilization Account. By June 30 of each Fiscal Year, the Budget Stabilization Account receives 1.0 percent of the general state revenues that Fiscal Year. The Legislature may appropriate additional amounts to the Budget Stabilization Account. Money may be appropriated from the Budget Stabilization Account by a majority vote of the members of each house of the Legislature if (1) forecasted state employment growth for any Fiscal Year is estimated to be less than 1.0 percent or (2) the Governor declares an emergency resulting from a catastrophic event that necessitates government action to protect life or public safety. Amounts may be withdrawn from the Budget Stabilization Account at any time by the favorable vote of three-fifths of the members of each house of the Legislature. In addition, when the balance in the Budget Stabilization Account equals more than 10 percent of the estimated general state revenues in that Fiscal Year, the amount above 10 percent may be appropriated to the Education Construction Fund by a majority vote of the members of each house of the Legislature. The Legislature approved a measure to be submitted to the voters at the November 2011 election that if adopted will require that "extraordinary growth in state revenues," which is defined as the amount by which the growth in state revenues exceeds by one-third the average biennial growth in state revenues over the prior five biennia, be transferred to the Budget Stabilization Account at the end of each fiscal biennium.

**Economic and Revenue Forecast**

State law requires the Forecast Council to prepare an economic and revenue forecast on a quarterly basis. Additionally, the Forecast Council is required to publish monthly updates that include economic data releases and a report of revenue collections for the previous monthly collection period. This section describes the most recent economic forecast released on September 2, 2011 (the "September 2011 Forecast"), on which the latest revenue forecast (as of September 15, 2011) is based. The next revenue forecast is expected to be released on November 17, 2011.

***September 2011 Forecast.*** The September 2011 Forecast was based on the IHS Global Insight Model of the U.S. Economy issued in September 2011, modified according to the Forecast Council's standard practice to reflect the Blue Chip GDP forecast published in the Blue Chip Economic Indicators and NYMEX oil futures prices. Because the state's forecast must be based on current law, Global Insight's assumption that the payroll tax cut will be extended into next year was removed.

In the September 2011 Forecast, the Forecast Council noted that the near term economic outlook for Washington has weakened since the June 2011 Forecast. Revenues are forecasted to grow 7.5 percent from the 2009-11 Biennium to $30.31 billion in the 2011-13 Biennium. However, this is $1.4 billion less than the June 2011 Forecast. General Fund State revenue collections for the June 10, 2011, to September 10, 2011, collection period were $40 million (1.2 percent) less than the Forecast Council's

June 2011 Forecast, with $14 million in the 2009-2011 Biennium and $26 million in the 2011-13 Biennium.

The Washington economic recovery has slowed along with the slowdown in the global and national economies. Economic growth in Washington is no longer expected to pick up momentum later in 2011 as predicted in June 2011. The job growth forecast for 2011 is 1.1 percent and the employment growth in 2012 and 2013 is forecast at 1.4 percent and 2.1 percent, respectively. Personal income growth is forecast at 4.9 percent, 3.0 percent, and 4.5 percent in 2011, 2012 and 2013, respectively.

The employment recovery in Washington remains weak; the state's economy added 8,300 net new jobs in June, July and August 2011. In June, July and August, the manufacturing sector contributed 4,200 jobs, including 3,500 new aerospace jobs; construction added 600 jobs; and private service-providing industries, which account for two out of three jobs in the state, added 3,800 jobs. Federal government employment increased by 1,300 during June, July and August, but this was more than offset by the loss of 1,600 state and local government jobs. Washington's unemployment rate held steady at 9.3 percent.

Washington export growth is strong and is expected to help the state outperform in the recovery. Total exports were up by 31.5 percent year-over-year in the second quarter of 2011. The outlook for the state's aerospace sector is positive: Boeing has approximately seven years of commercial orders on the books and aerospace jobs in the state increased 9.5 percent from August 2010 to August 2011. Employment in the software sector in the state grew 4.3 percent from August 2010 to August 2011. Both Washington employment and personal income growth is expected to recover faster than that of the U.S.

The single family housing sector in Washington remains weak. The 12,600 single-family permits in the second quarter of 2011 were the lowest since the second quarter of 2009. Multi-family permits were a relatively strong 13,400 units in the quarter. The outlook for single-family construction is flat to negative through 2012, due to the backlog of foreclosed homes. The trend is positive in multi-family housing due to rising rents and declining apartment vacancies. A significant upturn in housing construction is not expected until the first quarter of 2013. Washington's housing market is expected to recover quicker than most other states because the foreclosure pipeline in the state is drying up. As of the second quarter, Washington ranked 47 out of 50 states in the number of mortgages that were 30 days past due.

Core inflation (excluding food and energy) in Seattle averaged an annual rate of 1.0 percent in the second quarter of 2011. Overall prices rose at an average annual rate of 3.0 percent over the same period, driven by rising energy costs. With energy costs easing since April 2011, more moderate inflation is expected going forward.

Table 2 summarizes some of the historical values and forecasts of the primary economic drivers upon which the September 2011 Forecast was based.

**Table 2**
**Summary of Economic Factors**
*(% Annual Change)*

| | | | | | Forecast | | |
|---|---|---|---|---|---|---|---|
| | **2007** | **2008** | **2009** | **2010** | **2011** | **2012** | **2013** |
| **Personal Income** | 8.1 | 6.0 | (2.7) | 2.6 | 4.9 | 3.0 | 4.5 |
| **Nonfarm Payroll Employment** | 2.6 | 0.9 | (4.6) | (1.4) | 1.1 | 1.4 | 2.1 |
| **Housing Units**[(1)] | (5.3) | (39.0) | (41.2) | 21.6 | (0.5) | 3.3 | 29.6 |

(1) Reflects single-family and multi-family units authorized by permits.

*Source: Washington Economic and Revenue Forecast Council Revenue Review: September 15, 2011.*

***Alternative September 2011 Economic Forecasts.*** As required by statute, the Forecast Council also adopts an optimistic and a pessimistic forecast. The level of uncertainty in the baseline forecast remains high; downside risks are still elevated and considerably higher than the upside risks.

Optimistic Scenario. In the optimistic scenario, underlying pent-up demand continues to drive the recovery, hiring picks up and the economy rebounds. In the optimistic scenario, 2011-13 Biennium revenues are more than $2.25 billion higher than the baseline forecast.

Pessimistic Scenario. In the pessimistic scenario, Congress fails to agree upon a deficit reduction plan, there is a sovereign debt default in Europe, and U.S. economic growth slows while rising wages in India and China boost inflationary pressures. In the pessimistic scenario, revenues for the 2011-13 Biennium fall $2.01 billion below the baseline forecast.

## Caseload Forecast

The Caseload Forecast Council is charged with forecasting the entitlement caseloads for the state. The forecast identifies the number of persons expected to qualify for and to require the services of public assistance programs, state correctional institutions, state correctional non-institutional supervision, state institutions for juvenile offenders, the common school system, long-term care, medical assistance, foster care and adoption support.

The Caseload Forecast Council meets three times per year in February, June and November and adopts a formal projection of caseloads for the current biennium. The November forecast is used in preparing the Governor's proposed budget and the March caseload forecast is used by the Legislature in the development of the omnibus biennial appropriations act. The Caseload Forecast Council consists of six members: two members appointed by the Governor and one member appointed by the Chair of each of the two largest political caucuses in the Senate and House of Representatives.

## General Fund-State Operating Budget

***General.*** The state's operating budget includes appropriations for the general day-to-day operating expenses of state agencies, colleges and universities and public schools. Employee salaries and benefits, leases, goods and services and public assistance payments are typical operating expenses. More than half of the operating budget is funded by unrestricted revenues from the General Fund, with the balance from federal and other funding sources.

Since the onset of the economic downturn in 2008, the Governor and Legislature have modified the state operating budget several times in response to lower actual and projected general state revenues and higher costs associated with growth in mandatory caseloads, school enrollment and medical assistance costs.

***2009-11 Biennium Budget.*** The 2009-11 Biennium Budget was originally adopted in the spring of 2009. During the course of the 2009-2011 Biennium, quarterly forecast updates of revenues declined while expenses increased due to the cost of providing services such as education, medical assistance and public safety. Several times during the Biennium, the Governor proposed and the Legislature adopted supplemental operating budgets to deal with the shortfalls. In addition, in the fall of 2010, the Governor issued an Executive Order directing across-the-board cuts of 6.3 percent for General Fund agencies beginning on October 1, 2010.

The supplemental budgets and across-the-board cuts reduced state expenditures in areas including health care and human services, natural resources, higher education, early learning, state prisons and K-12 education (other than basic education). Since the original enacted 2009-11 budget, General Fund expenditures have been reduced by $1.059 billion. The supplemental budgets did not reduce required spending on basic education, debt service or federally-mandated Medicaid. The General Fund benefited from $2.6 billion in ARRA funds as well as approximately $337 million in federal funds from the extension of the federal Medical Assistance percentage enhancement and $208 million in new education funding. In addition to the expenditure reductions, the budget was balanced by raising new revenue through a combination of permanent and temporary tax increases and transfers from the Budget Stabilization Account and other accounts. The supplemental budget passed by the Legislature in May 2011 for the 2009-11 Biennium approved General Fund expenditures at a maximum of $29.9 billion and an ending General Fund balance of $104 million. As a result of the September 2011 Revenue Forecast and other actions, OFM now expects General Fund resources of approximately $29.75 billion, and a projected negative ending General Fund balance of $109 million (including the Budget Stabilization Account). If agencies spend less than this maximum, or if revenues come in better than projected, the ending fund balance will change accordingly.

Beginning with the 2009-11 Biennium, the Legislature broadened the composition of revenue sources deposited into the General Fund by merging the Health Services, Public Safety and Education, Equal Justice, Student Achievement, Water Quality, and Violence Reduction and Drug Enforcement Accounts into the General Fund as of July 1, 2009. Though merging these accounts into the General Fund makes it appear that projected General Fund revenues increased by 4.1 percent compared with the General Fund in the 2007-09 Biennium, no new revenue was raised in this action. Similarly, the expenditures from these accounts were also merged into the General Fund, so a similar pattern of apparent growth is seen on the expenditure side, but this does not represent an increase in state spending by this action.

***2011-13 Budget.*** The Legislature adopted the budget for the 2011-13 Biennium that includes expenditures of $31.7 billion and total resources (including the beginning fund balance) of $31.9 billion, leaving a proposed ending General Fund-State Fund balance of $163 million (including the Budget Stabilization Account). The budget addresses the impact of increasing caseloads, rising costs, lower than expected state revenues, and substantially reduced federal stimulus funds.

The budget reflects extensive cuts in state spending of approximately $4.5 billion. The budget calls for a 3.0 percent reduction in compensation for state employees, increases to state employees' share for health insurance premiums, and increased pension contribution rates. In education, the budget reduces funds targeted to reduce class sizes, reduces K-12 teacher salaries by 1.9 percent and K-12 administrative staff salaries by 3.0 percent, and decreases state support of higher education through cuts in academic services and reductions in salary, although reductions are partially offset with tuition increases and financial aid. The budget again temporarily suspends two education initiatives that were approved by voters and that

allocated funds to reduce class sizes and extend programs and would have required an annual cost-of-living increase for school employees. The Legislature gave the state's universities the authority to raise tuition beyond the budgeted tuition increase. State funding for health and human services is cut back significantly, although the number of individuals who receive care is projected to increase. In particular, no new enrollment will be allowed in the state-subsidized Basic Health Plan and grants under the Disability Lifeline program will be eliminated. The budget eliminates automatic cost-of-living increases for retired workers in the PERS 1 and TRS 1 pension plans. The budget incorporates constitutionally-mandated contributions to the Budget Stabilization Account if approved at the November 2011 election, but also leaves a $281 million balance in the Budget Stabilization Account. The budget does not include tax increases; it does, however, include some fee increases and other transfers. The budget does not reduce required spending on basic education, debt service or federally-mandated Medicaid.

As a result of the September 2011 Revenue Forecast summarized under "Economic and Revenue Forecast," and other actions, OFM now expects General Fund revenues of approximately $30.2 billion for the 2011-13 Biennium. This produces a projected negative ending General Fund balance of $1.275 billion (including the Budget Stabilization Account) for the Biennium prior to any anticipated legislative action. If agencies spend less than this maximum, or if revenues come in better than projected, the ending fund balance will change accordingly. The Governor and the Legislature have begun planning for a possible early supplemental budget to reduce expenditures and bring the budget more in line with available resources. In August 2011, the Governor asked state agencies to prepare for additional cutbacks of 5 to 10 percent. The Governor has called a special legislative session commencing on November 28, 2011.

Table 3A and Table 3B summarize the actions taken by the Legislature and other adjustments made to develop a budget for the 2009-11 Biennium and the 2011-13 Biennium, respectively.

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## Table 3A
## 2009-11 General Fund-State Adjustments
## November 2009 through September 2011
*($ in millions)*

| | Adjustments |
|---|---|
| **Beginning Balance** | 189 |
| **Revenue** | |
| November 2009 Forecast | 28,843 |
| February 2010 Forecast[1] | (118) |
| June 2010 Forecast | (203) |
| September 2010 Forecast | (770) |
| November 2010 Forecast – Not including results of Initiative 1107 | (322) |
| November 2010 Forecast – Portion for Initiative 1107 | (63) |
| March 2011 Forecast | (80) |
| June 2011 Forecast | 25 |
| September 2011 Forecast | (25) |
| Transfer to Budget Stabilization Account | (247) |
| 2010 Revenue Legislation (Net Change) | 761 |
| 2011 Revenue Legislation (Net Change) | 146 |
| **Total Revenue** | 27,947 |
| **Other Resource Changes** | |
| Enacted Fund Transfers and Other Adjustments | 870 |
| 2009 Legislative Transfers from Budget Stabilization Account | 45 |
| 2010 Legislative Transfers from Budget Stabilization Account | 222 |
| 2010 Legislative Transfers to General Fund | 436 |
| 2010 Legislative Transfers from General Fund | (108) |
| Governor's Vetoes of Fund Transfers | (21) |
| Legislative Special Session December 2010 | 98 |
| Legislation Passed February 2011 | 126 |
| Prior Period Adjustments | 19 |
| Legislation Passed May 2011 | (74) |
| **Total Other Resource Changes** | 1,613 |
| **Total Resources** | 29,749 |
| **Spending** | |
| Enacted Budget | 30,918 |
| Legislative Supplemental Operating Budget | (45) |
| Legislative Maintenance Level Change[2] | 652 |
| Legislative 2010 Net Policy Level Changes[3] | (1,066) |
| Governor's Vetoes | 6 |
| Governor's Across-the-Board Cuts[4] | * |
| Legislative Special Session December 2010 | (488) |
| Legislation Passed February 2011 | (234) |
| Legislation Passed May 2011 | 116 |
| **Total Spending** | 29,859 |
| **Ending Balance and Reserves** | |
| Unrestricted Ending Fund Balance[5] | (110) |
| Budget Stabilization Account Balance | 1 |
| **Total Reserves** | (109) |

(1) Includes the effect of a decision by the Supreme Court in *DOT Foods, Inc. v. Department of Revenue*, which reinstated B&O tax exemptions for certain types of out-of-state companies.
(2) This change primarily reflects enrollment and caseload changes to the original budget, based upon the February 2010 Caseload Forecast.
(3) The 2010 supplemental budget cut existing programs and made some modest additions. This number reflects the netting of those changes.
(4) The Governor directed across-the-board cuts of 6.3 percent to the Fiscal Year 2011 budget beginning October 1, 2010. A portion of the Governor's 6.3 percent across-the-board cuts were included in the reductions adopted by the Legislature in the December, 2010, special session.
(5) The 2011 supplemental budget as passed by the Legislature and signed by the Governor in May 2011 left a positive fund balance for Fiscal Year 2011. Subsequently the September 2011 Revenue Forecast resulted in a negative ending fund balance for Fiscal Year 2011.

Totals may not add due to rounding.

*Source: Office of Financial Management.*

**Table 3B**
**2011-13 General Fund-State Adjustments**
**February 2010 through September 2011**
*($ in millions)*

| | Adjustments |
|---|---|
| **Beginning Balance** | (110) |
| **Revenue** | |
| February 2010 Forecast | 32,224 |
| June 2010 Forecast | 1,858 |
| September 2010 Forecast | (668) |
| November 2010 Forecast | (809) |
| March 2011 Forecast | (698) |
| June 2011 Forecast | (387) |
| September 2011 Forecast | (1,413) |
| Transfer to Budget Stabilization Account | (280) |
| 2011 Revenue Legislation (Net Change) | 146 |
| 2011 Budget Driven Revenue | 58 |
| **Total Revenue** | 30,031 |
| **Other Resource Changes** | |
| Enacted Fund Transfers and Other Adjustments | 245 |
| **Total Other Resource Changes** | 245 |
| **Total Resources** | 30,166 |
| **Spending** | |
| May 2011 Enacted Budget | 31,724 |
| Governor's Vetoes | (3) |
| **Total Spending** | 31,721 |
| **Ending Balance and Reserves** | |
| Unrestricted Ending Fund Balance | (1,555) |
| Budget Stabilization Account Balance | 280 |
| **Total Reserves** | (1,275) |

Totals may not add due to rounding.
*Source: Office of Financial Management.*

***Revenues and Expenditures.*** The state separates its General Fund revenues and expenditures into three categories: General Fund-State, General Fund-Federal and General Fund-Private/Local to indicate the general source of revenues. Tables 4 and 5 summarize such revenues and expenditures for the Fiscal Years 2006 through 2010, forecast revenues for the three Fiscal Years 2011 through 2013, and budgeted expenditures through Fiscal Year 2013. Table 4 is derived from the Forecast Council's forecast documents, which include forecasts of revenues through Fiscal Year 2013 (other than federal and local and private revenues and fund transfers, which are estimated through Fiscal Year 2013). The information in Table 5 is extracted from the state's budget documents.

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## Table 4
## General Fund Revenues and Resources[1]
Fiscal Years ended June 30
(Modified Accrual Basis)
*($ in millions)*

| | Actuals | | | | | Forecast | | |
|---|---|---|---|---|---|---|---|---|
| | **2006** | **2007** | **2008** | **2009** | **2010** | **2011[6]** | **2012[6]** | **2013[6]** |
| **Beginning General Fund Balance** | 999 | 1,271 | 1,372 | 805 | 279 | (561) | (110) | (1,069) |
| **General Fund-State Revenues[1]** | | | | | | | | |
| **State Tax Revenues** | | | | | | | | |
| Retail Sales Tax | 6,846 | 7,388 | 7,705 | 6,870 | 6,417 | 6,620 | 6,745 | 7,058 |
| Business and Occupation Taxes | 2,478 | 2,714 | 2,874 | 2,640 | 2,574 | 3,010 | 3,167 | 3,382 |
| Use Taxes (General Fund portion) | 465 | 504 | 511 | 460 | 423 | 534 | 503 | 535 |
| Property Taxes | 1,611 | 1,670 | 1,721 | 1,770 | 1,822 | 1,857 | 1,870 | 1,914 |
| Real Estate Excise Taxes | 933 | 1,070 | 663 | 389 | 380 | 373 | 356 | 382 |
| Other Excise Taxes[2] | 26 | 24 | 25 | 23 | 17 | 18 | 17 | 17 |
| Other Taxes[3] | 1,556 | 1,596 | 1,590 | 1,582 | 1,535 | 1,787 | 1,741 | 1,765 |
| **Subtotal State Tax Revenues** | 13,915 | 14,966 | 15,089 | 13,734 | 13,168 | 14,199 | 14,399 | 15,053 |
| **State Non-Tax Revenues** | | | | | | | | |
| Licenses, permits and other fees | 85 | 92 | 98 | 95 | 84 | 87 | 87 | 90 |
| Liquor profits and fees | 73 | 78 | 66 | 69 | 71 | 117 | 120 | 125 |
| Investment income | 68 | 110 | 125 | 63 | 2 | (12) | (10) | (9) |
| Lottery transfers | 2 | 8 | - | 11 | 13 | 9 | - | - |
| Other Non-Tax Revenue | 176 | 214 | 281 | 186 | 233 | 223 | 226 | 230 |
| **Subtotal State Non-Tax Revenues** | 404 | 502 | 570 | 424 | 403 | 424 | 423 | 436 |
| **Adjustments and Transfers** | | | | | | | | |
| Enacted Transfers/Prior Period Adjustments | 596 | 229 | (266) | 1,043 | 699 | 556 | 120 | 125 |
| Transfers from Budget Stabilization Account | - | - | - | - | 45 | 223 | - | - |
| Transfers to Emergency Reserve Account/Budget Stabilization Account[4] | - | (289) | - | (115) | (119) | (128) | (135) | (145) |
| **Subtotal Adjustment and Transfers** | 596 | (60) | (266) | 928 | 625 | 651 | (15) | (20) |
| **Total General Fund-State Resources** | 15,914 | 16,679 | 16,765 | 15,891 | 14,475 | 14,713 | 14,697 | 14,400 |
| **General Fund-State Resources** | 15,914 | 16,679 | 16,765 | 15,891 | 14,475 | 14,713 | 14,697 | 14,400 |
| **General Fund-Federal Revenues[5]** | 5,468 | 5,577 | 5,898 | 6,498 | 8,115 | 8,468 | 7,221 | 7,485 |
| **General Fund-Private/Local Revenues** | 158 | 178 | 207 | 220 | 252 | 275 | 287 | 277 |
| **Total General Fund Resources** | 21,540 | 22,434 | 22,870 | 22,609 | 22,842 | 23,456 | 22,205 | 22,162 |

(1) Includes revenues that before July 1, 2009, were deposited to the Public Safety and Education, Equal Justice, Water Quality, Health Services, Violence Reduction and Drug Enforcement and Student Achievement Accounts.
(2) Includes liquor, beer and wine, tobacco, boat and timber excise taxes, among others.
(3) Includes estate and inheritance taxes, public utility taxes and insurance premium and other taxes.
(4) The Emergency Reserve Account was abolished, and the Budget Stabilization Account was created effective July 1, 2009. See "GENERAL FUND—Budget Stabilization Account."
(5) Includes ARRA funding in 2009, 2010 and 2011 of $1.0 billion, $2.1 billion, and $1.9 billion, respectively.
(6) Based on September 2011 Forecast, December 2010 Special Session, and 2011 legislation.
Totals may not add due to rounding.

*Source: Compiled by the Office of Financial Management from forecast and budget documents.*

## Table 5
## General Fund Expenditures and Ending Fund Balance[1]
Fiscal Years ended June 30
(Modified Accrual Basis)
*($ in millions)*

| | Actuals | | | | | Forecast | | |
|---|---|---|---|---|---|---|---|---|
| | **2006** | **2007** | **2008** | **2009** | **2010** | **2011[6]** | **2012[6]** | **2013[6]** |
| **Education** | | | | | | | | |
| Public School | 5,654 | 6,006 | 6,326 | 6,409 | 6,512 | 6,334 | 6,840 | 6,893 |
| Higher Education | 1,442 | 1,503 | 1,588 | 1,593 | 1,396 | 1,355 | 1,187 | 1,215 |
| Other Education | 58 | 64 | 85 | 93 | 82 | 39 | 43 | 43 |
| **Total Education** | 7,154 | 7,573 | 7,999 | 8,095 | 7,990 | 7,728 | 8,070 | 8,151 |
| **Human Services** | | | | | | | | |
| Dept. Social and Health Services[2] | 4,224 | 4,471 | 4,796 | 4,433 | 4,303 | 4,425 | 2,853 | 2,878 |
| Dept. Corrections | 707 | 758 | 857 | 896 | 708 | 792 | 839 | 796 |
| Other Human Services[2] | 345 | 388 | 457 | 481 | 370 | 233 | 2,323 | 2,391 |
| **Total Human Services** | 5,276 | 5,617 | 6,110 | 5,810 | 5,381 | 5,450 | 6,015 | 6,065 |
| **Natural Resources Recreation** | 206 | 255 | 253 | 246 | 198 | 160 | 156 | 153 |
| **Government Operations** | 233 | 261 | 289 | 293 | 238 | 212 | 231 | 243 |
| **Transportation** | 41 | 39 | 43 | 38 | 40 | 34 | 40 | 38 |
| **Debt Service[3]** | 665 | 703 | 851 | 714 | 870 | 907 | 953 | 1,014 |
| **Other Expenditures[4]** | 1,067 | 860 | 416 | 416 | 319 | 332 | 301 | 291 |
| **Total General Fund-State Expenditures** | 14,642 | 15,308 | 15,961 | 15,612 | 15,036 | 14,823 | 15,766 | 15,955 |
| **Federal** | 5,468 | 5,577 | 5,898 | 6,498 | 8,115 | 8468 | 7,221 | 7,485 |
| **Private/Local[5]** | 158 | 178 | 207 | 220 | 252 | 275 | 287 | 277 |
| **Total General Fund Expenditures** | 20,268 | 21,063 | 22,066 | 22,330 | 23,403 | 23,566 | 23,274 | 23,717 |
| **Total General Fund Resources** | 21,540 | 22,434 | 22,870 | 22,609 | 22,842 | 23,456 | 22,205 | 22,162 |
| **Total General Fund Expenditures** | (20,268) | (21,063) | (22,066) | (22,330) | (23,403) | (23,566) | (23,274) | (23,717) |
| **Unrestricted General Fund Ending Balance** | 1,272 | 1,371 | 804 | 279 | (561) | (110) | (1,069) | (1,555) |
| **Emergency Reserve/Budget Stabilization Balance** | 4 | 293 | 303 | 21 | 95 | 1 | 135 | 280 |
| **Total Reserves** | 1,276 | 1,664 | 1,107 | 300 | (466) | (109) | (934) | (1,275) |

(1) Includes expenditures that before July 1, 2009, were made from the Public Safety and Education, Equal Justice, Water Quality, Health Services, Violence Reduction and Drug Enforcement and Student Achievement Accounts.
(2) The Medical Assistance Program moved from DSHS to the Health Care Authority beginning in Fiscal Year 2012.
(3) Does not include debt service payments reimbursed from sources that are not general state revenues, including tuition fees, patient fees, admission taxes, parking taxes and certain King County sales and use taxes. See Tables 11 and 12.
(4) Includes legislative and judicial agencies and other special appropriations.
(5) Includes spending from grants, contracts and other agreements from private/local sources.
(6) Based on September 2011 Forecast, December 2010 Special Session, and 2011 legislation.

Totals may not add due to rounding.

*Source: Office of Financial Management from forecast documents and 2010 and 2011 legislation.*

## Capital Budget

The capital budget includes appropriations for construction and repair of state office buildings, college and university buildings, prisons and juvenile rehabilitation facilities; parks; public schools; housing for low-income and disabled persons, farm workers and others; and for other capital facilities and programs. Approximately half of the capital budget typically is financed by state-issued bonds, while the rest is funded primarily from dedicated accounts, trust revenue and federal funding sources. The budget includes money re-appropriated from previous biennia when projects are not completed before the end of that biennium.

Table 6 summarizes the capital budget for the 2007-09 Biennium, the enacted capital budget for the 2009-11 Biennium and capital budgets enacted as part of the 2010 and 2011 supplemental budgets for the 2009-2011 Biennium, and the enacted capital budget for the 2011-13 Biennium.

In November 2010, voters rejected a proposal by the Legislature to issue up to $505 million of additional general obligation bonds to finance the costs of grants for construction of energy cost-saving improvements to schools and other public facilities.

**Table 6**
**Capital Budget**
(Modified Accrual Basis)
*($ in millions)*

| | 2007-2009 Final Budget | 2009-2011 Enacted Budget | 2010 Supplemental Budget | 2011 Supplemental Budget | 2011-13 Legislative Budget |
|---|---|---|---|---|---|
| **Education** | | | | | |
| Public Schools | 1,254 | 1,190 | 1,067 | 1,067 | 1,064 |
| Higher Education | 1,539 | 1,305 | 1,070 | 1,061 | 763 |
| Other Education | 45 | 30 | 34 | 33 | 19 |
| **Total Education** | 2,838 | 2,525 | 2,171 | 2,161 | 1,846 |
| **Human Services** | | | | | |
| Department of Social and Health Services | 85 | 44 | 44 | 44 | 30 |
| Other Human Services | 518 | 259 | 250 | 244 | 213 |
| **Total Human Services** | 603 | 303 | 294 | 288 | 243 |
| **Natural Resources and Recreation** | 1,721 | 1,568 | 1,771 | 1,762 | 1,799 |
| **General Government** | 1,952 | 1,270 | 1,318 | 1,292 | 1,092 |
| **Transportation**(1) | 17 | 10 | 10 | 7 | - |
| **Total Capital Budget Expenditures** | 7,131 | 5,676 | 5,564 | 5,510 | 4,980 |

(1) Transportation reflects the omnibus capital budget and not the transportation capital budget. See "TRANSPORTATION-RELATED REVENUES AND EXPENDITURES."

*Source: Office of Financial Management.*

## TRANSPORTATION-RELATED REVENUES AND EXPENDITURES

### Transportation Revenue

Transportation revenues include taxes and fees, ferry fares and concessions, toll revenue and federal funds. Most transportation revenues are deposited to the Motor Vehicle Fund. Revenues from excise taxes on motor vehicle and special fuels are restricted to highway purposes. Toll revenue from the

SR 520 Corridor is deposited into the SR 520 Corridor Account (also known as the Toll Facilities Account).

***Excise Taxes on Motor Vehicle and Special Fuels.*** The primary component of transportation revenue is excise taxes on motor vehicle and special fuels. In 1921, the Legislature established a motor vehicle fuel tax at a fixed rate of $0.01 per gallon. The tax rate has been increased several times since then. Table 7 lists the increases in the excise tax on motor vehicle fuel since April 1, 1990. The same rates are charged per gallon for diesel and alternative fuels.

**Table 7**
**Motor Vehicle Fuel Tax Rate History**
*(Per Gallon)*

| Effective Date of Change | Increase ($) | Per-Gallon Tax ($) |
|---|---|---|
| 4/1/1990 | 0.040 | 0.220 |
| 4/1/1991 | 0.010 | 0.230 |
| 7/1/2003 | 0.050 | 0.280 |
| 7/1/2005 | 0.030 | 0.310 |
| 7/1/2006 | 0.030 | 0.340 |
| 7/1/2007 | 0.020 | 0.360 |
| 7/1/2008 | 0.015 | 0.375 |

*Source: Washington State Department of Transportation.*

***Tolls.*** Currently the state is collecting tolls on two facilities, the Tacoma Narrows Bridge and State Route ("SR") 167 High Occupancy Toll ("HOT") Lanes Pilot Project. The Tacoma Narrows Bridge tolls are being collected to pay the bonds issued for the new bridge construction. Tolling on SR 167 is "dynamic"; cars with two or more people use the HOT lane for free and single occupant drivers have the option to pay the posted toll and use the carpool lane. The Legislature recently extended the SR 167 HOT Lanes Pilot Project through June 2013.

Tolling on the SR 520 Corridor is scheduled to begin in December 2011 in advance of the major construction of the SR 520 Floating Bridge and Eastside Project described below. Tolling will be variable depending on the time of day and number of axles and will be collected electronically.

***Transportation Revenue Forecast Council.*** The Transportation Revenue Forecast Council (the "Transportation Forecast Council"), comprised of technical staff of the Department of Licensing, WSDOT and the Forecast Council, prepares quarterly forecasts of transportation revenues (including revenues from excise taxes on motor vehicle and special fuels). The transportation forecast is based in part upon the separate economic and demographic forecasts and assumptions made by the Forecast Council. No increases in fuel tax rates are included in the forecast. Unlike the Forecast Council's quarterly forecasts, which generally extend over a three-year period, the Transportation Forecast Council forecasts are required to cover six years.

In its most recent forecast, released in September 2011, the Transportation Forecast Council projects that transportation revenues for the 2011-13 Biennium will total approximately $4.26 billion, an increase of 4.6 percent from the previous biennium's total revenue of $4.07 billion.

WSDOT hired Wilbur Smith Associates and Parsons Brinckerhoff to prepare traffic and toll revenue projections for the SR 520 Floating Bridge and Eastside Project.

**Transportation Expenditures**

***Transportation Excise Tax Revenue Distributions.*** The Constitution requires that all proceeds of the excise taxes on motor vehicle and special fuels be placed in the Motor Vehicle Fund, a special fund within the state treasury, and used exclusively for highway purposes, including the capital and operating costs of public highways, county roads, bridges and city streets and the operation of ferries that are part of any public highway, county road or city street and including the payment of state debt obligations for which excise taxes on the motor vehicle and special fuels have been legally pledged.

State statutes require that excise taxes on motor vehicle and special fuels be distributed to local governments and to certain state accounts, all to be used for highway purposes. The statutes provide, however, that nothing therein be construed to violate any terms or conditions contained in any highway construction bond issues then or thereafter authorized and to which such taxes are pledged. Excise taxes collected on motor vehicle and special fuels are distributed monthly. See Tables 8 and 9.

***Transportation Operating Budget.*** Highway and ferry operations and maintenance are the two largest components of the state's transportation operating budget. Ferry operations and maintenance is funded in part by ferry fares. Aviation, public transportation and rail operations are funded with other non-fuel tax revenues.

***Payment of Bonds Payable from Excise Taxes on Motor Vehicle and Special Fuels.*** Each legislative act that authorizes the issuance and sale of motor vehicle fuel tax bonds provides that the principal of and interest on such bonds are secured by a pledge of the excise taxes levied on motor vehicle and special fuels. That pledge constitutes a charge against the revenues from such motor vehicle and special fuels excise taxes equal to the charge of any other general obligation bonds of the state that have been and may thereafter be authorized that also pledge, on an equal basis, excise taxes on motor vehicle and special fuels for their payment. By state law, the Legislature also covenants to continue to levy those excise taxes in amounts sufficient to pay, when due, the principal of and interest on all of the bonds issued under those legislative authorizations. All motor vehicle fuel tax general obligation bonds of the state are further secured by a pledge of the full faith, credit and taxing power of the state. See "INDEBTEDNESS AND OTHER OBLIGATIONS–General Obligation Debt–Motor Vehicle Fuel Tax General Obligation Bonds." Statutes authorizing the issuance of refunding bonds require that if the bonds to be refunded are secured by motor vehicle fuel taxes, in addition to the pledge of the state's full faith, credit and taxing power, the refunding bonds must also be secured by the same taxes.

Under motor vehicle fuel tax bond statutes enacted before 1993, at least one year prior to the date any interest is due and payable on those bonds or prior to the maturity date of any such bonds, the Committee estimates, subject to the provisions of the pledge of revenue, the percentage of the monthly receipts of the motor vehicle fund resulting from collection of excise taxes on motor vehicle and special fuels that will be necessary to meet interest or bond payments when due. Each month, as such funds are paid into the Motor Vehicle Fund, the Treasurer must transfer such percentage of the monthly receipts from excise taxes on motor vehicle and special fuels in the Motor Vehicle Fund to the Highway Bond Retirement Fund and the Ferry Bond Retirement Fund. Money in the Ferry Bond Retirement Fund is to be used for payment when due of the principal of and interest on state ferry bonds. If in any month it appears that the estimated percentage of money to be transferred is insufficient to meet the requirements for interest and bond retirement, the Treasurer must notify the Committee, and the Committee must adjust its estimates so that all requirements for interest and principal of all bonds issued will be fully met at all times. Motor vehicle fuel tax bond statutes enacted in 1993 and thereafter require that such transfers from the Motor Vehicle Fund to the Highway Bond Retirement Fund be made in accordance with the bond proceedings, which generally provide that the transfers be made on the date a debt service payment is due, although in practice amounts are set aside monthly in the Motor Vehicle Fund for debt service. See Table 9.

***Payment of Bonds Payable from Toll Revenue and Other Funds.*** The state expects to finance the SR 520 Floating Bridge and Eastside Project as part of the SR 520 Corridor Program described below with a combination of general obligation bonds of the state first payable from toll revenue and excise taxes on motor vehicle and special fuels ("Triple Pledge Bonds"), and toll revenue bonds that do not pledge state excise taxes on motor vehicle and special fuels or the full faith and credit of the state. In addition, the state expects to issue Grant Anticipation Revenue Vehicle bonds to fund a portion of the SR 520 Corridor Program, which would be payable from Federal-aid highway formula funding and would not be secured by a pledge of toll revenue. The state is issuing the first series of bonds for the SR 520 Floating Bridge and Eastside Project in October 2011, as Triple Pledge Bonds. Under the authorizing legislation, "toll revenue" means only such toll revenue that is pledged to the payment of the bonds. The resolution authorizing the issuance of the Triple Pledge Bonds pledged to those bonds the toll revenue from the SR 520 Corridor and any other "Eligible Toll Facilities" that may become part of a system of Eligible Toll Facilities. If toll revenue is not sufficient to pay the Triple Pledge Bonds, the Triple Pledge Bonds are then payable first from excise taxes on motor vehicle and special fuels and then from other money of the state legally available therefor.

***Transportation Capital Program.*** The state's transportation capital plan includes several mega-projects, including the SR 520 Floating Bridge and Eastside Project, replacement of the Alaskan Way Viaduct (the "Viaduct Project"), and the Columbia River Crossing. Other major highway projects include the I-405 and SR 520 interchange in Bellevue, the U.S. 395 North Spokane corridor, and the I-5 and SR 16 interchange in Tacoma. Construction of approximately 200 smaller highway projects, including construction of new interchanges, lanes and bridges, is underway. For ferry capital projects, one 64-auto ferry boat was delivered in 2010, one in 2011 and a final 64-auto ferry boat will be delivered in Fiscal Year 2012. Federal funds made available under ARRA will support expansion of inner-city high-speed rail.

***The SR 520 Corridor Program.*** The SR 520 Corridor is 12.8 miles from I-5 in Seattle to the west and crossing Lake Washington to SR 202 in Redmond. The SR 520 floating bridge provides an east-west link across Lake Washington for approximately 100,000 daily vehicle trips. Built in the 1960s, the bridge currently is vulnerable to failure in severe windstorms and earthquakes. The SR 520 Floating Bridge and Eastside Project (a portion of the SR 520 Corridor Program) is underway and includes construction of a pontoon facility and pontoons for the new floating bridge, completion and reconfiguration of the HOV lane system on SR 520 to the east of Lake Washington, and construction of a new bridge to replace the Evergreen Point floating bridge.

The Legislature has authorized funding for the SR 520 Floating Bridge and Eastside Project. The state is issuing $518,775,000 in bonds in October 2011 for the project and expects to finance the remaining costs with approximately $1.2 billion in additional bonds, and from federal funds, toll revenue and excise taxes on motor vehicle and special fuels. Tolling on the SR 520 Corridor is scheduled to begin in December 2011. WSDOT is using the design-build methodology for the major components of the project and all major contracts have been awarded. The new bridge is expected to open to traffic in 2015. If funded by the Legislature, as part of the SR 520 Corridor Program, the state will construct the Westside Project consisting of a new six-lane corridor from I-5 to the new floating bridge, a new bridge, a new transit/HOV ramp to I-5 and other improvements.

***The Alaskan Way Viaduct.*** The Viaduct was built in the 1950s and includes an elevated 2.2-mile portion of SR 99 along the edge of Puget Sound in downtown Seattle. The Viaduct is a main north-south route through Seattle and carries 20 to 25 percent of the traffic through downtown. The elevated structure was damaged during the region's 2001 Nisqually earthquake. Studies indicate that the Viaduct may collapse if another major earthquake occurs.

The total cost of the Viaduct replacement project is estimated to be $3.1 billion, funded by state and federal investment totaling $2.4 billion and approximately $400 million in funding from tolls. An additional $300 million was committed from the Port of Seattle in an agreement with the state in April 2010. Road and bridge construction on a project to replace the southern end of the Viaduct with a side-by-side roadway started in July 2010. This part of the replacement is scheduled for completion in 2013. The Viaduct's downtown waterfront section will be replaced with a bored tunnel beneath downtown Seattle. Seattle Tunnel Partners – a joint venture between Tutor Perini and Dragados - was selected as the design-build contractor in December 2010. The tunnel project's record of decision and the notice to proceed for construction were issued in August 2011. The City of Seattle has approved the project through agreements between the city and state and a recent public vote. The SR 99 tunnel is scheduled to open in December 2015.

***Columbia River Crossing.*** Columbia River Crossing is a comprehensive five-mile project to improve safety, reduce congestion and enhance mobility on I-5 between SR 500 in Vancouver, Washington, and Columbia Boulevard in Portland, Oregon. The project will replace the current I-5 bridge, extend light rail to Vancouver, improve closely-spaced interchanges and access to the ports of Portland and Vancouver, and enhance the pedestrian and bicycle path between the two cities.

In April 2011, the governors of Oregon and Washington identified the deck truss bridge design as the best replacement structure for the I-5 bridge. The final environmental impact statement was published in September 2011, and the federal record of decision is expected by the end of 2011. Funding has not been secured, but likely funding sources include federal highway and transit sources, Washington and Oregon sources, and tolling. Once funding has been secured, project construction could begin as early as 2013. The new southbound bridge would open in 2018 and light rail service would begin in 2019. The cost estimate is between $3.1 and $3.5 billion (in year of expenditure dollars).

**Transportation Revenues and Expenditures**

Table 8 summarizes selected transportation-related revenues for the Fiscal Years 2007 through 2011 and selected forecast transportation-related revenues for the Fiscal Years 2012 and 2013. It includes forecast revenues and projected bond proceeds, based upon the current budget, and assumed federal and local funds. Not included in Table 8 are other, non-forecasted revenues, such as beginning balances, reserves, investment income, transfers, and other miscellaneous revenues. Table 9 summarizes transportation-related expenditures for Fiscal Years 2007 through 2011 and budgeted and projected expenditures for Fiscal Years 2012 and 2013.

## Table 8
## Selected Transportation Forecast Revenues and Other Transportation-Related Funding[1]

Fiscal Years ended June 30
(Modified Accrual Basis)
*($ in millions)*

| | Actuals | | | | | September 2011 Forecast | |
|---|---|---|---|---|---|---|---|
| | **2007** | **2008** | **2009** | **2010** | **2011** | **2012** | **2013** |
| **Forecast Transportation Revenues** | | | | | | | |
| Gross Fuel Tax Collections include Non-Highway | 1,161 | 1,244 | 1,247 | 1,234 | 1,255 | 1,256 | 1,265 |
| Refunds for Non-Highway Use | (44) | (73) | (79) | (57) | (62) | (63) | (67) |
| **Adjusted Gross Fuel Tax Collections** | 1,117 | 1,171 | 1,168 | 1,177 | 1,193 | 1,193 | 1,198 |
| WSDOT Portion of Licenses, Permits and Fees | 293 | 300 | 295 | 288 | 292 | 297 | 302 |
| Ferry Fares | 147 | 148 | 145 | 147 | 147 | 155 | 161 |
| Tolls[2] | - | 31 | 46 | 47 | 46 | 74 | 112 |
| Other Revenues | 77 | 106 | 107 | 58 | 65 | 64 | 67 |
| **Total Forecasted State Revenues** | 1,634 | 1,757 | 1,762 | 1,717 | 1,744 | 1,783 | 1,840 |
| **Other Transportation-Related Funding[3]** | | | | | | | |
| Bond Proceeds (Bonds sold in Fiscal Year) | 603 | 762 | 487 | 2,097 | 156 | 1,418 | 1,418 |
| Federal Funds | 516 | 505 | 453 | 582 | 537[4] | 823[4] | 823[4] |
| Local Funds | 39 | 30 | 45 | 48 | 54 | 75 | 75 |

(1) Does not include other non-forecasted revenues available to support appropriations (e.g., beginning balances, reserves, investment income, transfers and other miscellaneous revenues).
(2) Includes gross toll revenue (actual and forecast) for the Tacoma Narrows Bridge, HOT lanes on SR 167, as well as estimates for gross toll revenue for the SR 520 Corridor Program. SR 520 toll revenue forecasts assume six months of tolling in Fiscal Year 2012 and 12 months of tolling in Fiscal Year 2013.
(3) Bond proceeds and federal and local funds in Fiscal Years 2012 and 2013 have been annualized from a projected biennial total.
(4) Includes federal stimulus money.

Totals may not add due to rounding.

*Source: Washington State Department of Transportation.*

## Table 9
## WSDOT Transportation-Related Expenditures
Fiscal Years ended June 30
(Modified Accrual Basis)
*($ in millions)*

| | | | | 2009-11 Supplemental Budget | | 2011-13 Enacted Budget | |
|---|---|---|---|---|---|---|---|
| | **2007** | **2008** | **2009** | **2010** | **2011** | **2012** | **2013** |
| **Transfers and Distributions** | | | | | | | |
| Debt Service Transfers[1] | 208 | 278 | 314 | 350 | 418 | 450 | 566 |
| Fuel Tax Distribution to Cities and Counties | 245 | 245 | 233 | 235 | 238 | 237 | 238 |
| Fuel Tax Distribution to Local Users[2] | 135 | 134 | 127 | 128 | 130 | 129 | 130 |
| **Total Distributions and Transfers** | 588 | 657 | 675 | 713 | 786 | 817 | 935 |
| **WSDOT Operations** | | | | | | | |
| Toll Maintenance and Operations | 5 | 16 | 13 | 14 | 11 | 29 | 29 |
| Highway Maintenance & Operations | 183 | 209 | 232 | 198 | 214 | 220 | 220 |
| Ferries Maintenance & Operations | 205 | 228 | 215 | 209 | 225 | 234 | 234 |
| Aviation, Public Transportation and Rail | 73 | 60 | 74 | 73 | 82 | 75 | 75 |
| Local Programs and Economic Partnerships | 6 | 6 | 7 | 6 | 6 | 6 | 6 |
| Support Services | 149 | 155 | 156 | 149 | 149 | 157 | 157 |
| Compensation Adjustment | - | - | - | - | - | (11) | (11) |
| **Total Operations** | 620 | 673 | 696 | 648 | 687 | 710 | 709 |
| **WSDOT Capital** | | | | | | | |
| Highway Construction | 1,419 | 1,545 | 1,485 | 1,636 | 1,553 | 2,395 | 2,395 |
| Traffic Operations and Facilities | 11 | 7 | 10 | 6 | 8 | 9 | 9 |
| Ferry Construction | 91 | 65 | 91 | 131 | 158 | 142 | 142 |
| Rail Program | 41 | 30 | 59 | 59 | 35 | 213 | 213 |
| Local Programs | 26 | 37 | 30 | 50 | 34 | 47 | 47 |
| **Total Capital** | 1,589 | 1,684 | 1,675 | 1,882 | 1,788 | 2,805 | 2,805 |
| **Total WSDOT Transportation Expenditures** | 2,797 | 3,014 | 3,047 | 3,243 | 3,260 | 4,332 | 4,449 |

(1) Debt Service transfers to debt retirement accounts are done on a monthly basis assuring that enough money is set aside for future debt service payments. These transfers will not equal fiscal year debt service. Amounts shown here include estimates for the SR 520 Floating Bridge and Eastside Project debt service.

(2) Local Users include the following: The Rural Arterial Trust Account, the Urban Arterial Trust Account, the Transportation Improvement Board Account, the County Arterial Trust Account, and the Small City Pavement/Sidewalk Account.

Totals may not add due to rounding.

*Source: Washington State Department of Transportation.*

## INDEBTEDNESS AND OTHER OBLIGATIONS

All state general obligation debt and other evidences of indebtedness must be authorized by the Legislature and issued under the authority granted by the Legislature to the Committee. In addition to long-term bonds, the state may enter into financing contracts, including leases and installment purchase contracts, and notes. As described below, the state also may incur contingent obligations such as guarantees and may enter into payment agreements such as interest rate swaps (although to date it has not done so).

### Debt Issuance Policy

The Committee maintains a Debt Issuance Policy that addresses, among other things, the roles and responsibilities of the Committee and the Treasurer, debt structuring guidelines and standards of conduct and appointment of professional service providers. The Debt Issuance Policy addresses debt service structure, mode of interest, refunding savings thresholds and the average life of debt (shorter than or equal to the estimated useful life of the facility financed). The requirements may not apply in all cases.

### Debt Affordability Study

In December 2010, the Treasurer submitted the inaugural Debt Affordability Study to the Legislature as directed by the Legislature. The study was prepared to present information about the state's debt obligations to help guide policymakers as they make choices about the amounts, types and uses of debt financing undertaken in the state. The study describes issuance trends, borrowing costs and effective constraints on debt issuance and provides an assessment of the state's overall "debt affordability" by using demographic and financial indicators as well as peer analysis to measure the affordability of the state's existing and projected debt.

### 2011 Legislation

Through 2011 legislation, the Legislature created the Commission on State Debt to examine trends in the use of debt and other long term liabilities, compare debt service to other operating budget expenditures for similar policy objectives, and compare the state's debt limits and policies to other states. By December 1, 2011, this commission is required to recommend improvements in debt limits and policies to stabilize bond capacity, reduce growth in debt service relative to the General Fund, and to maintain and enhance the state's credit ratings.

The legislation further directs the State Finance Committee to recommend a working debt limit for purposes of budget development for various purpose capital bond appropriations, which is lower than the state constitutional debt limit in order to reserve capacity under the constitutional limit for emergencies and economic uncertainties. See "General Obligation Debt-Constitutional General Obligation Debt Limitation" below. The same legislation requires the Committee to recommend a working debt limit that phases down from 8.75 percent in 2016 to 7.75 percent by 2022. The Committee may recommend modified working debt limits in response to extraordinary economic conditions. The Committee is authorized to reduce or delay the issuance of bonds if an issuance would result in exceeding the recommended working debt limit.

### General Obligation Debt

***General Obligation Debt Authority.*** The Constitution and enabling statutes authorize different means of incurring state general obligation debt, the payment of which is secured by a pledge of the state's full faith, credit and taxing power.

General obligation bonds may be authorized:

(1) by the affirmative vote of three-fifths of the members of each house of the Legislature, without voter approval, in which case the amount of such debt is generally (but not always) subject to the constitutional debt limitation described below;

(2) when authorized by law for a distinct work or object and approved by a majority of the voters voting thereon at a general election, or a special election called for that purpose, in which case the amount of the debt so approved is not subject to the constitutional debt limitations described below;

(3) by a body designated by statute (currently the Committee) without limitation as to amount, and without approval of the Legislature or approval of the voters:

    (a) to refund outstanding state obligations; or

    (b) to meet temporary deficiencies of the state treasury, to preserve the best interests of the state in the conduct of the various state institutions and agencies during each Fiscal Year if such debt is discharged (other than by refunding) within 12 months of the date of incurrence and is incurred only to provide for appropriations already made by the Legislature.

The Constitution also permits the state to incur additional debt to repel invasion, suppress insurrection or to defend the state in war.

***Motor Vehicle Fuel Tax General Obligation Bonds.*** General obligation bonds that are payable from excise taxes on motor vehicle and special fuels may be issued for specified highway purposes and, as described below, such bonds are not subject to the constitutional general obligation debt limitation. Historically, excise taxes on motor vehicle and special fuels always have been used to pay such bonds. See "TRANSPORTATION-RELATED REVENUES AND EXPENDITURES–Transportation Expenditures–Payment of Bonds Payable from Excise Taxes on Motor Vehicle and Special Fuels."

***Bonds for SR 520 Corridor Program.*** The Legislature has authorized the issuance of $1.95 billion of bonds to provide the funds necessary for the location, design, right-of-way, and construction of the Floating Bridge and Eastside Project portion of the SR 520 Corridor Program. The Legislature has designated the SR 520 corridor as an eligible toll facility, and, as authorized by the Legislature, the State Transportation Commission has set tolls for travel on the floating bridge portion of the SR 520 corridor. Bonds authorized for the Floating Bridge and Eastside Project are expected to be issued as a combination of general obligation bonds of the state first payable from toll revenue and excise taxes on motor vehicle and special fuels and toll revenue bonds that do not pledge state excise taxes on motor vehicle and special fuels or the full faith, credit and taxing power of the state. On October 31, 2011, the state will issue $518,775,000 in Motor Vehicle Fuel Tax General Obligation Bonds (SR 520 Corridor Program-Toll Revenue), Series 2012C, which will be the first series of bonds issued to finance the SR 520 Corridor Program.

***Constitutional General Obligation Debt Limitation.*** With certain exceptions noted below, the amount of state general obligation debt that may be incurred is limited by the Constitution. The constitutional debt limitation prohibits the issuance of new debt if the aggregate debt contracted by the state would exceed the amount for which payments of principal and interest in any Fiscal Year would require the state to expend more than 9.0 percent of the arithmetic mean of general state revenues for the three immediately

preceding Fiscal Years. This limitation restricts the incurrence of new debt and not the amount of debt service that may be paid by the state in future years.

Under the Constitution, "general state revenues" includes all state money received in the state treasury, with certain exceptions, including (1) fees and revenues derived from the operation of any undertaking, facility, or project; (2) moneys received as gifts, grants, donations, aid, or assistance when the terms require the application of such moneys otherwise then for general purposes of the state; (3) retirement system moneys and performance bonds and deposits; (4) trust fund moneys, including moneys received from taxes levied for specific purposes; and (5) proceeds from sale of bonds or other indebtedness.

Principal and interest requirements on the following types of obligations are excluded from the calculation of the constitutional debt limitation:

(1) obligations payable from excise taxes levied on motor vehicle fuels, license fees, income received from the investment of the permanent common school fund and revenue received from license fees on motor vehicles;

(2) debt that has been refunded or defeased;

(3) debt authorized by law for a single work or object and approved by a majority of those voting in a general or special election;

(4) certificates of indebtedness issued to meet temporary deficiencies in the state treasury (described above under "General Obligation Debt Authority");

(5) principal requirements of bond anticipation notes;

(6) financing contracts, including certificates of participation therein;

(7) obligations issued to pay "current expenses of state government";

(8) obligations payable solely from the revenues derived from the ownership or operation of any particular facility or project;

(9) obligations payable solely from gifts, grants, donations, aid or assistance that is limited to expenditure on specific purposes; and

(10) any state guarantee of voter-approved general obligation debt of school districts in the state.

In November 2010, the State's voters approved an amendment to the Constitution specifying that for the purpose of computing the amount required for payment of interest on outstanding debt subject to the constitutional limitation described above, "interest" is reduced by subtracting the amount scheduled to be received by the state as payments from the federal government in each year in respect of such debt.

***Debt Service Within Constitutional Debt Limitation.*** The aggregate debt projected to be contracted by the state as of November 9, 2011, does not exceed that amount for which payments of principal and interest in any Fiscal Year would require the state to expend more than 9.0 percent of the arithmetic mean of its general state revenues for the three immediately preceding Fiscal Years. The arithmetic mean of general state revenues for Fiscal Years 2009, 2010 and 2011 is $12,080,764,474. The debt service limitation, 9.0 percent of this mean, is $1,087,268,803. The state's maximum annual debt service as of

November 9, 2011, on debt service subject to the constitutional debt limitation is estimated to be $1,012,850,511 or $74,418,292 less than the debt service limitation.

***Use of Short-Term General Obligation Debt Authority (Certificates of Indebtedness and Bond Anticipation Notes).*** Article VIII of the Constitution, Chapter 39.42 RCW and the state's other bond statutes delegate to the Committee the authority to issue, in the name of the state, temporary notes in anticipation of the sale of bonds. Pursuant to statutory authority and resolution of the Committee, such notes would be general obligations of the state, but principal of those notes would be excluded from the constitutional debt limitation. The state has no bond anticipation notes currently outstanding and currently does not plan to issue bond anticipation notes.

Article VIII of the Constitution and Chapter 39.42 RCW also provide for the issuance of certificates of indebtedness to meet temporary deficiencies in the state treasury. Such indebtedness must be retired other than by refunding within 12 months after the date of issue. Principal and interest on certificates of indebtedness are excluded from the constitutional debt limitation. The state has no certificates of indebtedness currently outstanding and does not anticipate any short-term borrowing during Fiscal Year 2012.

Table 10 includes the total debt service requirements by pledge of revenues for the state general obligation bonds, and Table 11 includes a summary of the state's outstanding general obligation bonds.

# Table 10
## General Obligation Bonds – Total Debt Service Requirements by Pledge of Revenues
*(in dollars)*

| | Outstanding 11/9/2011[1] | | | | Series R-2012A Bonds[2] | | Series R-2012B Bonds[2] | | Series 2012C Bonds[2] | | Total Debt Service Requirements [2][3][4][5] |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | General State Revenues[3] | | Motor Vehicle Fuel Tax Revenues | | General State Revenues | | Motor Vehicle Fuel Tax Revenues | | Triple Pledge | | |
| June 30 | Principal | Interest[4] | Principal | Interest[5] | Principal | Interest | Principal | Interest | Principal | Interest | |
| 2012[6] | 264,625,000 | 259,442,858 | 97,578,614 | 149,954,004 | 5,085,000 | 3,067,859 | 645,000 | 283,628 | - | 15,253,527 | 795,935,490 |
| 2013 | 487,992,252 | 506,990,272 | 169,914,745 | 284,070,448 | 26,870,000 | 20,894,050 | - | 1,953,900 | - | 26,024,975 | 1,524,710,642 |
| 2014 | 503,083,999 | 480,902,828 | 220,742,541 | 280,875,824 | 33,720,000 | 19,950,950 | - | 1,953,900 | - | 26,024,975 | 1,567,255,018 |
| 2015 | 519,661,564 | 465,408,922 | 226,367,993 | 273,562,500 | 43,150,000 | 18,197,800 | 965,000 | 1,944,250 | - | 26,024,975 | 1,575,283,004 |
| 2016 | 526,027,077 | 441,887,785 | 238,244,493 | 269,488,598 | 45,425,000 | 15,983,425 | 1,005,000 | 1,919,525 | - | 26,024,975 | 1,566,005,878 |
| 2017 | 522,866,191 | 434,371,548 | 250,198,239 | 266,011,793 | 47,545,000 | 13,913,525 | 1,050,000 | 1,888,700 | 10,835,000 | 26,024,975 | 1,574,704,971 |
| 2018 | 506,539,950 | 406,268,146 | 254,389,188 | 258,071,822 | 49,960,000 | 11,730,250 | 1,095,000 | 1,851,050 | 11,375,000 | 25,483,225 | 1,526,763,630 |
| 2019 | 491,491,629 | 382,600,756 | 262,846,883 | 251,055,838 | 52,645,000 | 9,165,125 | 1,150,000 | 1,806,150 | 11,945,000 | 24,914,475 | 1,489,620,855 |
| 2020 | 498,758,868 | 362,637,937 | 268,918,119 | 242,587,201 | 36,685,000 | 6,931,875 | 1,205,000 | 1,759,050 | 12,540,000 | 24,317,225 | 1,456,340,275 |
| 2021 | 494,893,505 | 322,374,622 | 266,841,687 | 233,012,861 | 18,620,000 | 5,549,250 | 1,265,000 | 1,709,650 | 13,165,000 | 23,690,225 | 1,381,121,800 |
| 2022 | 486,880,000 | 274,449,938 | 272,642,106 | 226,040,912 | 19,575,000 | 4,594,375 | 1,315,000 | 1,658,050 | 13,825,000 | 23,031,975 | 1,324,012,356 |
| 2023 | 473,715,000 | 249,999,875 | 260,032,167 | 217,002,208 | 33,395,000 | 3,270,125 | 10,820,000 | 1,361,250 | 14,515,000 | 22,340,725 | 1,286,451,350 |
| 2024 | 483,585,000 | 226,852,250 | 264,784,322 | 209,505,074 | 23,740,000 | 1,841,750 | 11,390,000 | 806,000 | 15,240,000 | 21,614,975 | 1,259,359,371 |
| 2025 | 459,700,000 | 202,871,100 | 273,794,917 | 200,101,541 | 24,965,000 | 624,125 | 10,425,000 | 260,625 | 16,005,000 | 20,852,975 | 1,209,600,283 |
| 2026 | 471,695,000 | 178,965,350 | 293,340,654 | 188,444,865 | - | - | - | - | 16,805,000 | 20,052,725 | 1,169,303,594 |
| 2027 | 453,805,000 | 155,704,613 | 290,968,610 | 176,591,937 | - | - | - | - | 17,685,000 | 19,170,463 | 1,113,925,622 |
| 2028 | 435,855,000 | 134,463,175 | 280,041,468 | 166,572,160 | - | - | - | - | 18,615,000 | 18,242,000 | 1,053,788,803 |
| 2029 | 431,835,000 | 113,225,650 | 279,496,913 | 155,524,482 | - | - | - | - | 19,545,000 | 17,311,250 | 1,016,938,295 |
| 2030 | 404,700,000 | 91,880,475 | 272,025,835 | 143,487,108 | - | - | - | - | 20,525,000 | 16,334,000 | 948,952,419 |
| 2031 | 373,845,000 | 72,359,575 | 238,245,000 | 71,479,193 | - | - | - | - | 21,550,000 | 15,307,750 | 792,786,518 |
| 2032 | 355,195,000 | 54,059,025 | 216,785,000 | 59,807,173 | - | - | - | - | 22,625,000 | 14,230,250 | 722,701,448 |
| 2033 | 317,985,000 | 36,915,638 | 185,535,000 | 49,170,664 | - | - | - | - | 23,760,000 | 13,099,000 | 626,465,302 |
| 2034 | 235,725,000 | 22,324,350 | 140,290,000 | 40,270,493 | - | - | - | - | 24,945,000 | 11,911,000 | 475,465,843 |
| 2035 | 157,245,000 | 11,305,538 | 115,675,000 | 33,391,718 | - | - | - | - | 26,195,000 | 10,663,750 | 354,476,006 |
| 2036 | 88,345,000 | 4,307,513 | 91,535,000 | 28,000,518 | - | - | - | - | 27,505,000 | 9,354,000 | 249,047,031 |
| 2037 | 28,110,000 | 632,475 | 94,860,000 | 23,154,835 | - | - | - | - | 28,880,000 | 7,978,750 | 183,616,060 |
| 2038 | - | - | 98,265,000 | 18,163,500 | - | - | - | - | 30,325,000 | 6,534,750 | 153,288,250 |
| 2039 | - | - | 101,840,000 | 12,956,982 | - | - | - | - | 31,840,000 | 5,018,500 | 151,655,482 |
| 2040 | - | - | 105,585,000 | 7,528,756 | - | - | - | - | 33,430,000 | 3,426,500 | 149,970,256 |
| 2041 | - | - | 78,700,000 | 2,752,981 | - | - | - | - | 35,100,000 | 1,755,000 | 118,307,981 |
| 2042 | - | - | 14,805,000 | 370,125 | - | - | - | - | - | - | 15,175,125 |
| **Total** | 10,474,160,035 | 5,893,202,212 | 6,225,289,495 | 4,539,008,115 | 461,380,000 | 135,714,484 | 42,330,000 | 21,155,728 | 518,775,000 | 522,013,890 | 28,833,028,959 |

(1) Does not include the Series 2012C, Series R-2012A and Series R-2012B Bonds; does include the defeasance of the bonds refunded by the Series R-2012A and Series R-2012B Bonds.
(2) Offerings dated October 31, 2011 (Series 2012C, including capitalized interest,) and November 9, 2011 (Series R-2012A and R-2012B).
(3) The state may be reimbursed for some of these debt service payments from sources that are not general state revenues, including tuition fees, patient fees, admission taxes, parking taxes and certain King County sales and uses taxes. See Tables 11 and 12.
(4) Interest payments on certain variable rate bonds are only estimates and are subject to change from time to time as market conditions change; $117,800,000 in principal amount of variable rate bonds is outstanding as of November 9, 2011.
(5) Debt service does not take into account the receipts of the 35 percent federal credit payments applicable to bonds issued as Build America Bonds.
(6) Remaining debt service on outstanding bonds. Upon the issuance of the Series 2012C, Series R-2012A and Series R-2012B Bonds, debt service requirements for entire Fiscal Year 2012 are: principal $651,469,749; interest $835,180,320; total debt service $1,486,650,069.

Totals may not add due to rounding.

*Source: Office of the State Treasurer.*

## Table 11
## Summary of Outstanding General Obligation Bonds
*(in dollars)*

| | 6/30/2007 | 6/30/2008 | 6/30/2009 | 6/30/2010 | 6/30/2011 |
|---|---|---|---|---|---|
| **Outstanding** | | | | | |
| General State Revenues and Other Sources [1] | 8,304,968,946 | 9,003,114,410 | 9,831,964,833 | 10,410,327,277 | 10,763,996,170 |
| Motor Vehicle Fuel Tax Revenues | 3,368,311,634 | 4,004,259,674 | 4,285,988,810 | 6,189,623,828 | 6,004,454,495 |
| **Total – Outstanding** | 11,673,280,580 | 13,007,374,085 | 14,117,953,643 | 16,599,951,104 | 16,768,450,665 |
| **Annual Debt Service Requirements by Fiscal Year** | | | | | |
| General State Revenues and Other Sources Debt Service[1] | | | | | |
| Payable from General State Revenues | 704,171,887 | 747,270,056 | 816,725,594 | 866,032,566 | 904,457,910 |
| Reimbursed from Other Sources [1] | 93,587,241 | 95,960,521 | 91,360,751 | 91,743,874 | 88,239,461 |
| | 797,759,128 | 843,230,577 | 908,086,345 | 957,776,440 | 992,697,370 |
| Motor Vehicle Fuel Tax Revenue Debt Service | | | | | |
| Payable from Excise Taxes on Motor Vehicle and Special Fuels | 213,063,011 | 246,575,046 | 291,775,904 | 319,143,978 | 379,425,700 |
| Reimbursed from Tolls on the Tacoma Narrows Bridge | 2,580,419 | 14,388,752 | 26,915,419 | 34,925,419 | 42,200,419 |
| | 215,643,430 | 260,963,798 | 318,691,323 | 354,069,397 | 421,626,119 |
| **Total – Annual Debt Service by Fiscal Year** | 1,013,402,558 | 1,104,194,376 | 1,226,777,668 | 1,311,845,837 | 1,414,323,489 |

(1) The state may be reimbursed from sources that are not general state revenues, including tuition fees, patient fees, admission taxes, parking taxes and certain King County sales and use taxes.

Totals may not add due to rounding.

*Source: Office of the State Treasurer.*

## Table 12
## General Obligations by Source of Payment[1]
(Outstanding as of November 9, 2011)
*(in dollars)*

| | |
|---|---|
| **Various Purpose General Obligation Bonds** | |
| Payable from General State Revenues | 10,033,303,121 |
| Reimbursed from Other Sources[2] | 902,236,914 |
| **Sub Total** | 10,935,540,035 |
| **Motor Vehicle Fuel Tax General Obligation Bonds** | |
| Payable from Excise Taxes on Motor Vehicle and Special Fuels | 5,673,760,000 |
| Payable from Tolls on the SR-520 Corridor | 518,775,000 |
| Reimbursed from Tolls on the Tacoma Narrows Bridge | 593,859,495 |
| **Sub Total** | 6,786,394,495 |
| **Total General Obligation Bonds** | 17,721,934,530 |

(1) Includes offerings dated October 31, 2011 (Series 2012C) and November 9, 2011 (Series R-2012A and R-2012B) (after defeasance of the refunded bonds).

(2) The state may be reimbursed from sources that are not general state revenues, including tuition fees, patient fees, admission taxes, parking taxes and certain King County sales and use taxes.

Totals may not add due to rounding.

*Source: Office of the State Treasurer.*

**Certificates of Participation/Financing Contracts for State and Local Agencies**

***Financing Contracts and Leases for State Agencies.*** In 1989, the Legislature authorized the state to enter into financing contracts, including leases, installment purchase agreements and other interest-bearing contracts, for the acquisition by state agencies of personal and real property. The state's current program provides for the financing of essential equipment and real estate projects with proceeds received from the sale of certificates of participation in master financing contracts. By their terms, the master financing contracts are payable only from current appropriations and/or from funds that do not constitute "general state revenues," and are not "debt" under the Constitution. Unlike bonds, the state's obligations under the master financing contracts and state agencies' obligations under their financing addenda are subject to appropriation by the Legislature and Executive Order reduction by the Governor.

The Committee is charged with oversight of financing contracts entered into by the state and state agencies, and all financing contracts for state real estate projects require prior approval of the Legislature. At the start of each biennium, the Office of the State Treasurer, as staff to the Committee, reports on prior usage of financing contracts and presents a proposed financing plan for the upcoming biennium. In addition, the Committee is required by law to establish from time to time a maximum aggregate principal amount payable from payments to be made under financing contracts entered into by the state.

The state also has entered into two long-term leases with separate nonprofit corporations that issued "63-20" lease revenue bonds on behalf of the state. The first lease, entered into in 2004 with Tumwater Office Properties, is for an office building being used as offices by WSDOT and DOC (now known as the "Edna Lucille Goodrich Building" and formerly the "Tumwater Office Building"). The second lease, entered into in July 2009 with FYI Properties, is for a state data center and an office building in Olympia to be used by the Department of Information Services and several smaller agencies (the "Wheeler Building"). The state began making lease payments in July 2011. The state's payments under the leases have been assigned to separate trustees as security for the "63-20" bonds issued by each of the lessors. Under each lease, the state's obligation to make payments of rent is subject to appropriation by the Legislature and subject to Executive Order reduction by the Governor, and neither lease is a "debt" under the Constitution.

***Financing Contracts for Local Agencies.*** In 1998, the Legislature authorized the state to enter into financing contracts on behalf of certain local government agencies for the acquisition of essential real and personal property. Pursuant to that authorization, the Treasurer established the state's Local Capital Asset Lending Program under which certain local government agencies with taxing power enter into financing contracts with the state for the acquisition of real and personal property. The obligations of local agencies under financing contracts with the state are general obligations to which the local agencies pledge their full faith and credit to make required payments. Local agency payments received by the state are used to make payments under financing contracts of the state. The state incurs a contingent obligation to make payments on behalf of a local agency in the event a local agency fails to make its required payment. This contingent payment obligation of the state is subject to appropriation by the Legislature and to Executive Order reduction by the Governor. If any local agency fails to make a payment due, the Treasurer is obligated to withhold an amount sufficient to make such payment from the local agency's share, if any, of state revenues or other amounts authorized or required by law to be distributed by the state to such local agency, if otherwise legally permissible.

Table 13 summarizes by Fiscal Year payments to be made relating to outstanding certificates of participation, and Table 14 summarizes the "63-20" lease revenue bond payments by Fiscal Year.

## Table 13
## Payments of Certificates of Participation in State Financing Contracts for State and Local Agencies by Fiscal Year[(1) (2)]
(Outstanding as of October 12, 2011)
*(in dollars)*

| | State | | | | Local | | | | State and Local Real Estate & Equipment Total Payments[(2)] |
|---|---|---|---|---|---|---|---|---|---|
| | Real Estate | | Equipment | | Real Estate | | Equipment | | |
| Fiscal Year | Principal | Interest | Principal | Interest | Principal | Interest | Principal | Interest | |
| 2012 | 11,801,409 | 8,005,735 | 15,908,252 | 2,138,857 | 1,853,349 | 777,454 | 4,984,906 | 744,860 | 46,214,821 |
| 2013 | 31,429,190 | 15,540,881 | 28,318,579 | 3,490,028 | 3,189,553 | 1,459,528 | 8,201,568 | 1,233,485 | 92,862,811 |
| 2014 | 31,781,083 | 14,402,669 | 21,377,649 | 2,552,268 | 3,150,364 | 1,346,221 | 6,785,349 | 940,918 | 82,336,521 |
| 2015 | 29,288,057 | 13,193,260 | 15,189,391 | 1,853,803 | 3,069,247 | 1,230,779 | 5,334,925 | 698,874 | 69,858,335 |
| 2016 | 30,404,795 | 12,008,266 | 9,270,163 | 1,319,314 | 3,144,867 | 1,114,050 | 3,707,689 | 516,504 | 61,485,648 |
| 2017 | 23,535,000 | 10,759,697 | 8,226,378 | 947,508 | 2,896,682 | 993,852 | 2,957,150 | 377,946 | 50,694,213 |
| 2018 | 22,680,000 | 9,831,432 | 3,767,881 | 696,074 | 2,197,758 | 887,621 | 2,530,096 | 264,220 | 42,855,083 |
| 2019 | 22,170,000 | 8,903,655 | 3,314,917 | 554,628 | 2,065,027 | 802,234 | 1,883,137 | 172,653 | 39,866,250 |
| 2020 | 21,600,000 | 8,009,559 | 2,795,395 | 433,706 | 1,965,013 | 721,244 | 1,467,239 | 105,418 | 37,097,574 |
| 2021 | 21,355,000 | 7,119,307 | 2,448,982 | 328,803 | 1,810,000 | 644,065 | 622,552 | 59,426 | 34,388,135 |
| 2022 | 20,410,000 | 6,240,913 | 1,085,000 | 241,250 | 1,565,000 | 572,208 | 175,000 | 39,400 | 30,328,770 |
| 2023 | 20,250,000 | 5,372,141 | 1,120,000 | 203,275 | 1,635,000 | 503,988 | 185,000 | 33,275 | 29,302,679 |
| 2024 | 18,635,000 | 4,515,599 | 1,175,000 | 152,875 | 1,695,000 | 432,475 | 190,000 | 24,950 | 26,820,900 |
| 2025 | 15,925,000 | 3,732,521 | 1,225,000 | 100,000 | 1,775,000 | 357,693 | 200,000 | 16,400 | 23,331,613 |
| 2026 | 15,680,000 | 3,032,013 | 1,275,000 | 51,000 | 1,860,000 | 276,278 | 210,000 | 8,400 | 22,392,690 |
| 2027 | 15,430,000 | 2,326,735 | - | - | 1,755,000 | 194,588 | - | - | 19,706,323 |
| 2028 | 11,880,000 | 1,671,974 | - | - | 1,800,000 | 113,441 | - | - | 15,465,415 |
| 2029 | 11,025,000 | 117,024 | - | - | 695,000 | 29,419 | - | - | 12,866,443 |
| 2030 | 11,210,000 | 561,183 | - | - | 90,000 | 3,293 | - | - | 11,864,475 |
| 2031 | 5,095,000 | 173,313 | - | - | 20,000 | 450 | - | - | 5,288,763 |
| **Total** | 391,584,533 | 136,517,874 | 116,497,585 | 15,063,390 | 38,231,860 | 12,460,878 | 39,434,612 | 5,236,729 | 755,027,461 |

(1) Excludes payments on state leases supporting "63-20" lease revenue bonds. See Table 14.
(2) Does not include principal and interest requirements on current offering dated November 9, 2011.
(2) Total payments for 2012 are $98,999,112.
Totals may not add due to rounding.
*Source: Office of the State Treasurer.*

**Table 14**
**Payments Under "63-20" Lease Revenue Bonds by Fiscal Year**
(Outstanding as of November 9, 2011)
*(in dollars)*

| Fiscal Year | E.L. Goodrich Building | | Wheeler Building | | Total Lease Revenue Bonds |
|---|---|---|---|---|---|
| | Principal | Interest | Principal | Interest | |
| 2012 | - | 1,351,344 | 1,300,000 | 16,233,375 | 18,884,719 |
| 2013 | 1,240,000 | 2,671,688 | 5,455,000 | 16,181,375 | 25,548,063 |
| 2014 | 1,360,000 | 2,606,688 | 5,725,000 | 15,908,625 | 25,600,313 |
| 2015 | 1,540,000 | 2,534,188 | 6,015,000 | 15,622,375 | 25,711,563 |
| 2016 | 1,740,000 | 2,450,013 | 6,310,000 | 15,321,625 | 25,821,638 |
| 2017 | 1,955,000 | 2,353,019 | 6,630,000 | 15,006,125 | 25,944,144 |
| 2018 | 2,180,000 | 2,244,475 | 6,965,000 | 14,674,625 | 26,064,100 |
| 2019 | 2,420,000 | 2,123,725 | 7,310,000 | 14,326,375 | 26,180,100 |
| 2020 | 2,685,000 | 1,989,719 | 7,675,000 | 13,960,875 | 26,310,594 |
| 2021 | 2,960,000 | 1,841,538 | 8,060,000 | 13,577,125 | 26,438,663 |
| 2022 | 3,260,000 | 1,678,263 | 8,460,000 | 13,174,125 | 26,572,388 |
| 2023 | 3,570,000 | 1,498,975 | 8,885,000 | 12,751,125 | 26,705,100 |
| 2024 | 3,905,000 | 1,302,756 | 9,350,000 | 12,284,663 | 26,842,419 |
| 2025 | 4,265,000 | 1,093,625 | 9,845,000 | 11,793,788 | 26,997,413 |
| 2026 | 4,640,000 | 871,000 | 10,360,000 | 11,276,925 | 27,147,925 |
| 2027 | 5,035,000 | 629,125 | 10,905,000 | 10,733,025 | 27,302,150 |
| 2028 | 5,480,000 | 366,250 | 11,450,000 | 10,187,775 | 27,484,025 |
| 2029 | 4,585,000 | 114,625 | 12,035,000 | 9,600,963 | 26,335,588 |
| 2030 | - | - | 12,665,000 | 8,969,125 | 21,634,125 |
| 2031 | - | - | 13,360,000 | 8,272,550 | 21,632,550 |
| 2032 | - | - | 14,095,000 | 7,537,750 | 21,632,750 |
| 2033 | - | - | 14,870,000 | 6,762,525 | 21,632,525 |
| 2034 | - | - | 15,690,000 | 5,944,675 | 21,634,675 |
| 2035 | - | - | 16,555,000 | 5,081,725 | 21,636,725 |
| 2036 | - | - | 17,465,000 | 4,171,200 | 21,636,200 |
| 2037 | - | - | 18,425,000 | 3,210,625 | 21,635,625 |
| 2038 | - | - | 19,440,000 | 2,197,250 | 21,637,250 |
| 2039 | - | - | 20,510,000 | 1,128,050 | 21,638,050 |
| **Total** | 52,820,000 | 29,721,013 | 305,810,000 | 295,890,363 | 684,241,375 |

Totals may not add due to rounding.
*Source: Office of the State Treasurer.*

## School Bond Guarantee Program

In 1999, the Legislature authorized a state school district credit enhancement program. The program's purpose is to provide savings to state taxpayers by pledging the full faith, credit and taxing power of the state to the payment of voter-approved school district general obligation bonds. The proposed law was approved by a vote of the electorate as a constitutional amendment.

Each school district is responsible for paying in full the principal of and interest on its bonds guaranteed by the state under the guarantee program. If sufficient money to make any scheduled debt service payment on guaranteed bonds of a school district has not been transferred to the paying agent in a timely manner, the Treasurer is required to transfer sufficient money to the paying agent for such payment. The Treasurer is entitled to recover from the school district any funds paid by the state on behalf of a school district under the guarantee program in a manner consistent with Chapter 39.98 RCW. The state has not been called upon to pay debt service on any school debt.

As of September 1, 2011, the aggregate total principal amount outstanding on 494 voter-approved bond issues guaranteed under the program is $8.44 billion. The bonds were issued by 190 school districts.

**Washington Guaranteed Education Tuition Program**

The Washington Guaranteed Education Tuition Program ("GET program") is a 529 prepaid college tuition plan that allows Washington residents or individuals opening accounts for Washington residents to prepay for future college tuition. Individual accounts are guaranteed by the state to keep pace with rising college tuition, based on the highest tuition at Washington's public universities. The after-tax contributions to a GET account grow tax-free and can be withdrawn tax-free when used for eligible higher education expenses. GET funds are held in the state treasury and invested by the Washington State Investment Board.

According to the 2010 Actuarial Valuation, the market value of program assets as of June 30, 2010, totaled $1.6 billion, or 86.2 percent of the "best estimate" of the actuarially determined present value of obligations for future payments of $1.85 billion. The 2011 Legislature transferred limited tuition-setting authority to some institutions of higher education ("new tuition-setting policy"). The new tuition-setting policy lowered the funded status, as of June 30, 2010, to 69.9 percent. However, the decrease in funded status due to the new tuition-setting policy will be partially offset by better than expected investment returns since the 2010 Actuarial Valuation. The June 30, 2011 Actuarial Valuation is expected to be issued in late September 2011 or early October 2011, and will include the full impact of the new tuition-setting policy and current assets. The market value of program assets as of June 30, 2009, totaled $1.26 billion, or 84.2 percent of the "best estimate" of the actuarially determined present value of obligations for future payments of $1.49 billion. The 2008 Actuarial Valuation showed the program to be fully funded, with an actuarial reserve of $104.5 million. The deterioration in the actuarially funded status of the program shown in the 2009 Actuarial Valuation primarily reflected Fiscal Year 2009 investment losses, an unexpected increase in tuition rates for the 2009-2010 academic year and an assumption of higher future tuition increases. The GET program has a goal to gradually rebuild a stabilization reserve, which as of June 30, 2010, had a deficit of $255.7 million or 13.8 percent of obligations.

There is no generally accepted standard of practice within the actuarial profession addressing prepaid tuition programs. This best estimate of the actuarial value of the obligations uses methodologies applicable to retirement systems and depends on certain assumptions regarding the rate of increase in tuition, investment returns and expense inflation. A 2010 report and a March 2011 solvency analysis completed by the Office of the Washington State Actuary ("OSA") concluded that under the status quo, the likelihood that the state will need to make required contributions to meet GET program tuition obligations over the next 50 years is low, but should it occur, the dollar amount would be high. OSA released a new analysis in August 2011 with the results of the new tuition-setting policy. Based on this analysis, the GET Committee approved a plan to recover from the unexpected past losses, which includes adopting a price that amortizes the unfunded liability over 30 years.

## INVESTMENTS

The Treasurer manages and invests two distinct sets of funds: state funds and Local Government Investment Pool ("LGIP") funds. State funds include funds in the state treasury that are subject to legislative appropriation and funds in the Treasurer's Trust, which are accounts placed in the custody of the Treasurer and not typically subject to legislative appropriation. Separately, the Treasurer manages the LGIP funds, a voluntary investment option for local governments.

Both the state funds and funds in the LGIP are managed by the Office of the State Treasurer pursuant to state laws that govern the permissible investments for each and to investment policies that provide further restrictions. For a description of permitted investments, see Note 3 in Appendix D–"THE STATE'S 2010 AUDITED BASIC FINANCIAL STATEMENTS." Historically, the Treasury and Treasurer's Trust

Funds and the LGIP have had sufficient liquidity to meet all cash flow demands. In keeping with state law, funds within the Treasury and Treasurer's Trust Funds are comingled for investment and cash management purposes.

Separately, the Washington State Investment Board manages and invests state retirement plan funds, state injured-worker insurance funds and various permanent funds. Its 15-member board consists of 10 voting members and five non-voting members. The 10 voting members include the Director of the Department of Labor and Industries and the Director of Retirement Systems, the Treasurer, five representatives of the public employee retirement systems and two legislators (one from each chamber).

**Treasury and Treasurer's Trust Funds**

The Treasury and Treasurer's Trust Funds are separated into sub-portfolios, a Liquidity Portfolio and a Core Portfolio, each managed by a separate portfolio manager within the Office of the State Treasurer. Earnings on the two sub-portfolios are calculated and distributed to individual funds on an accrued basis. Objectives are set for each portfolio as described below.

***Liquidity Portfolio.*** The objective of the Liquidity Portfolio is to meet daily cash requirements of all Treasury and Treasurer's Trust Funds (which include state operating and capital accounts). Additionally, the Liquidity Portfolio serves as a short-term investment fund for any cash holdings of the Core Portfolio. Balances in the Liquidity Portfolio fluctuate within a wide range (from near zero to more than $1.0 billion), increasing sharply with the receipt of seasonal tax payments and bond proceeds and declining with the pace of operating and capital expenditures. Investment holdings of this portfolio are generally repurchase agreements, reverse repurchase agreements, U.S. agency discount notes and deposits with qualified depositaries. Performance of this portfolio is measured against benchmarks used for the LGIP described below.

***Core Portfolio.*** Cash not anticipated to be needed to meet cash flow requirements for the foreseeable future is invested in the Core Portfolio. The maximum maturity for this portfolio is 10 years with a target duration of about 1.75 years. Investment holdings of this portfolio include obligations of the U.S. Government, U.S. agencies and bank notes guaranteed by the FDIC under the temporary liquidity guarantee program (the "TLGP"). Performance benchmarks of the Core Portfolio are the total return and accrued yield of the Bank of America/Merrill Lynch 1-3 Treasury/Agency Index and the accrued yield of a blended ladder of two- and five-year U.S. Treasuries.

**Table 15**
**Treasury and Treasurer's Trust Funds**
**Average Daily Balances by Security Class**
*($ in thousands)*

| | August 2011 | | September 2010-August 2011 | |
|---|---|---|---|---|
| | **$** | **%** | **$** | **%** |
| Agency | 1,239,325 | 38.4 | 1,166,345 | 41.1 |
| Treasury | 162,203 | 5.0 | 267,067 | 9.4 |
| Repurchase Agreements | 1,267,724 | 39.3 | 1,007,818 | 35.5 |
| Reverse Repo | - | - | - | - |
| Bank Deposits | 535,365 | 16.6 | 370,266 | 13.0 |
| NOW Accounts | - | - | - | - |
| TLGP Bonds | 19,987 | 0.6 | 26,021 | 0.9 |
| | 3,224,604 | 100.0 | 2,837,517 | 100.0 |
| Weighted Average Maturity: | 384 days | | | |

*Source: Office of the State Treasurer.*

## Local Government Investment Pool Funds

The LGIP, authorized by the Legislature in 1986, is a voluntary pool that provides its participants the opportunity to take advantage of the economies of scale inherent in pooling. The LGIP also is intended to offer participants safety of principal and the ability to achieve a higher investment yield than otherwise would be available to them. The more than 450 local governments that participate in the LGIP are allowed 100 percent liquidity on a daily basis. Although not regulated by the U.S. Securities and Exchange Commission (the "SEC"), the LGIP closely follows the SEC guidelines for Rule 2a-7 money market funds; for example, currently a maximum weighted average maturity ("WAM") of 60 days, a maximum weighted average life of 120 days. The maximum final maturity is 397 days except for floating- and variable-rate securities and securities that are used for repurchase agreements. The WAM of the LGIP generally ranges from 30 to 60 days. Typical investment holdings of the LGIP are repurchase agreements, U.S. Treasury bills and notes, U.S. agency discount notes, coupons, floating- and variable-rate notes, reverse repurchase agreements and bank deposits. The benchmarks utilized for the LGIP are the Government and Agency money market net and gross yields reported by iMoneyNet. The net yield is utilized for external comparisons while the gross yield is used internally to assess portfolio manager performance.

**Table 16**
**Local Government Investment Pool Funds**
**Average Daily Balances by Security Class**
*($ in thousands)*

| | August 2011 | | September 2010-August 2011 | |
|---|---|---|---|---|
| | **$** | **%** | **$** | **%** |
| Agency | 5,410,215 | 60.9 | 5,071,800 | 56.1 |
| Treasury | 777,700 | 8.8 | 1,419,606 | 15.7 |
| Repurchase Agreements | 2,130,301 | 24.0 | 1,673,503 | 18.5 |
| Reverse Repo | (254,838) | (2.9) | (44,366) | (0.5) |
| Bank Deposits | 701,567 | 7.9 | 826,762 | 9.1 |
| NOW Accounts | 115,461 | 1.3 | 97,286 | 1.1 |
| | 8,880,406 | 100.0 | 9,044,591 | 100.0 |
| Weighted Average Maturity: | 43 days | | | |

*Source: Office of the State Treasurer.*

## LITIGATION

The state and its agencies are parties to numerous routine legal proceedings that occur as a consequence of regular government operations. At any given point, there are numerous lawsuits involving state agencies which could, depending on the outcome of the litigation or the terms of a settlement agreement, impact revenue or expenditures of the state. There are risk management funds reserved by the state for these claims and insurance is available to pay all or a portion of most damages for most types of claims. There has been a trend in recent years of higher jury verdicts on certain types of damage claims. The collective impact of these claims, however, is not likely to have a material impact on state revenues or expenditures.

In addition to the regular damages claims, there are currently a number of lawsuits challenging the management and administration of state programs, some arising as a result of recent state budget cuts. The potential impact of this type of litigation is the most difficult to predict. Conceivably, a court could order the restructuring or expansion of certain entitlement programs that would result in a major restructuring of state budgeting and expenditures. No such ruling has yet to occur nor is such a court ruling currently anticipated. Most of these cases involve programs administered by the Department of Social and Health Services ("DSHS"). Only a few of these cases are called out specifically because it is not possible to quantify with exactitude what the fiscal impact of such claims could ultimately be, and it is not possible to know ahead of time what state or federal legislative responses could be taken to mitigate such impacts.

Those cases, which may raise potentially significant, but specifically incalculable, fiscal impacts, are described below.

In *McCleary v. State of Washington*, judgment for petitioners was entered on February 24, 2010, by the King County Superior Court. The court found that the state is not meeting its constitutional mandate to make ample provision for the education of all K-12 public school children. The court ordered the Legislature to conduct a study of what state funding was needed to "amply provide" all Washington public school students with the "education" required by Article IX of the Constitution. The court also ordered the Legislature to indicate how the state will fund that cost with "stable and dependable" state funding sources. The court set no deadlines or parameters for determining those costs and funding sources, other than a mandate that the Legislature make "real and measurable progress," nor did the court order a deadline for the implementation of new or increased state funding. Prior to the trial, in the 2009

legislative session, the Legislature enacted a sweeping reform of the substance of and funding for K-12 education. The court's decision leaves it to the Legislature to determine how to comply with its decision. That program of reform is scheduled to be fully implemented no later than 2018. The *McCleary* decision, by itself, does not translate into immediate or short-term impacts on the state budget. The 2009 legislation, though, could increase state funding for K-12 public education by billions of dollars. The state has appealed this decision to the Washington State Supreme Court and respondents filed their opposition on September 20, 2010, including a cross-appeal urging the Supreme Court to set a firm deadline (end of the school year following the Supreme Court's ultimate decision). If a deadline is set, that could conceivably accelerate the process of studying amounts of funding needed. However, it is not expected to interfere with the reforms initiated by the Legislature, still scheduled for full implementation by 2018. Oral argument was heard on June 28, 2011, and a decision is pending.

*Solis v. Washington Department of Social and Health Services* is a U.S. Department of Labor ("USDOL") lawsuit filed in U.S. District Court seeking back overtime wages and liquidated damages on behalf of approximately 2,000 social workers with the Children's Administration of DSHS. The court entered judgment for DSHS on May 3, 2010, after granting DSHS's motion for summary judgment. The USDOL has appealed to the Ninth Circuit Court of Appeals. Oral argument before a three-judge panel of the Ninth Circuit took place on August 1, 2011. If the Ninth Circuit reverses the district court and remands for trial, the estimated potential liability for back wages as of May 25, 2010, if all issues were construed in plaintiff's favor, is $40 million. Liquidated damages would double this to approximately $80 million.

**Programs and Services**

In the matter of *Rekhter v. DSHS* and two other consolidated cases (*Pfaff* and *SEIU* 775NW), plaintiffs argue that pursuant to DSHS's methodology ("shared living rule") for computing the number of hours of paid care available to the recipient class, those with live-in providers received approximately 15 percent less than those recipients who use live-out providers. This rule was invalidated by the Supreme Court ruling (*Jenkins v. DSHS*) issued on May 3, 2007, and was subsequently repealed by DSHS. Plaintiffs seek reimbursement by way of "money damages" for the recipient and provider classes for the approximately 15 percent fewer authorized hours, and injunctive relief barring application of the rule in the future. The Thurston County Superior Court has ruled that the recipient class is entitled to "retroactive compensatory relief" and ruled that the recipient class can go back to April 2003 for any award of money damages. The state argued that the recipient class could only go back, at most, 90 days from the date the complaint was filed on May 4, 2007. The trial for the provider class breach of contract claims concluded on December 20, 2010. The jury found that DSHS had not breached the express terms of the contracts, but did find violation of the "duty of good faith and fair dealing" when entering into the contracts. The jury awarded the provider class plaintiffs $57 million. Subsequently, the trial court granted plaintiffs' motion for pre- and post-judgment interest. The court has not ruled on the amount of interest that will be awarded, but plaintiffs will likely argue that it is $33 million, with post-judgment interest continuing to accrue on that amount. The court has provided the parties with a draft of the court's findings of fact and conclusions of law on the client class claims and it is anticipated that this pleading along with the final judgment will be entered soon. Following entry of the final judgment, any appeal will be due within 30 days and the plaintiffs will also need to file their motion for attorneys' fees and costs.

The matter of *Freeman v. DSHS* involves five plaintiffs who are adult recipients of Medicaid in-home personal care services from DSHS, together with their home care providers and "others similarly situated." The lawsuit challenges the reductions for in-home personal care services for adults required by the Legislature in 2009 and seeks a court order restoring those services and compensating plaintiffs for services that were not provided. Plaintiffs claim that DSHS cannot reduce in-home personal care services that recipients have been assessed to need, and that in doing so DSHS violated Medicaid law and the

supremacy clause of the U.S. Constitution. They claim that Medicaid law does not permit reductions for budgetary purposes, and that because there is an entitlement to needed services DSHS must provide notice and appeal rights prior to any reductions in services. They further claim that a 1978 consent decree in the *Mead v. Burdman* case obligates DSHS to provide all services that recipients are assessed to need, including in-home personal care services. Plaintiffs also claim that the reductions at issue constitute an impairment of contract for service providers in violation of the state Constitution. The case was originally filed in state court but removed to federal court by DSHS. In September 2010, the district court granted defendants' motion for summary judgment on all federal claims but declined to exercise supplemental jurisdiction over the remaining state claims, instead remanding them back to Thurston County Superior Court. A status conference was held on January 21, 2011. The case has been set for trial on December 19, 2011. Summary judgment motions have been filed by both parties and will be heard in October 2011.

*MR v. Dreyfus* was filed in federal district court in Seattle on December 21, 2010, challenging reductions in personal care services for adults scheduled for implementation on January 1, 2011. The plaintiffs include 14 individuals who receive in-home personal care services. The reductions at issue were implemented as a result of the Governor's September 2010 directive for an across-the-board budget reduction of 6.3 percent for all state agencies, and they are projected to save the General Fund-State almost $4 million per month or $117 million over the remainder of Fiscal Year 2011 and the next biennium. Plaintiffs allege violations of Medicaid law, the Americans with Disabilities Act, and due process requirements. They further claim that client notices were inadequate, that reduced services will lead to institutionalization, and that approval from the Centers for Medicare and Medicaid Services was necessary. Plaintiffs moved for a temporary restraining order ("TRO") to stop the reductions, which was denied by the trial court. Plaintiffs filed an emergency appeal with the Ninth Circuit seeking to overturn the denial of the TRO. On January 14, the Ninth Circuit panel issued an emergency order stopping the reductions pending the district court's ruling on plaintiffs' motion for preliminary injunction. As a result DSHS sent notices to all recipients and providers notifying them that hours reduced January 1 were being reauthorized pending further order of the court. On February 9, 2011, the U.S. District Court denied plaintiffs' motion for preliminary injunction. DSHS then reinstated the reductions effective March 1, 2011. Plaintiffs appealed the preliminary injunction denial to the Ninth Circuit and sought a second emergency injunction staying the reductions until the Ninth Circuit rules on the appeal. On February 18, 2011, the Ninth Circuit denied plaintiffs' request for the emergency stay. The Ninth Circuit heard oral argument on plaintiffs' appeal on June 9, 2011, and a decision is pending.

*Braam v. State of Washington* was filed as a class action lawsuit seeking damages for named-plaintiffs and injunctive relief on behalf of all foster children with three or more placements. Following settlement of damages claims, the case was tried to a jury, which rendered a verdict favoring plaintiffs. On appeal, the verdict was set aside and the case was remanded for a new trial. Following mediation, a settlement was reached that included an improvement plan and oversight by an expert panel. The expert panel was formed, and it developed an implementation plan for systemic improvements to the foster care system. The panel issues monitoring reports twice a year. The mediated settlement requires DSHS's Children's Administration to supplement its foster care system in six areas identified in plaintiffs' complaint, the implementation of which is to be monitored by the panel. Plaintiffs filed an enforcement motion in January 2008. The court found that DSHS had failed to comply with specific provisions of the settlement agreement. The deadline for DSHS to show significant progress towards implementing the new compliance plans by December 31, 2008, was met. DSHS and plaintiffs have settled the issue of plaintiffs' demands for attorneys' fees and costs for the enforcement motion. The original settlement agreement expires by its terms on July 31, 2011, unless there are enforcement actions pending at that time before a court or the panel. In June 2010, plaintiffs' counsel approached the Office of Attorney General and DSHS to initiate discussions on extending (and possibly modifying) the settlement agreement. In

July, the parties agreed to a short extension of the current agreement through the end of October to allow continued negotiations to occur.

*TR v. Dreyfus* is a class action lawsuit "to enforce the rights of Washington's Medicaid eligible children under the age of 21, with mental health needs, to receive the intensive home and community-based mental health services necessary to correct or ameliorate their mental health conditions." The suit claims violations of the (1) Medicaid Act-EPSDT/Comparability/Due Process provisions; (2) 14th Amendment due process under the U.S. Constitution; and (3) the Americans with Disabilities Act and Section 504 of the Rehabilitation Act. Plaintiffs seek sweeping and extraordinarily expensive changes to the service delivery system for children's mental health care. The parties agreed to engage in a formal mediation process with the goal of developing a plan for improvements to the system or, at a minimum, narrowing the issues for trial. Formal mediation began on January 6, 2011. In April 2011, by mutual agreement, the parties began mediating directly without the assistance of a mediator. Mediation was initially set to continue through the summer of 2011 with the goal of finalizing a settlement agreement at the end of August 2011. The date to finalize the agreement has been extended by court order to October 31, 2011. Progress is being made toward settlement. If a settlement is not reached, the trial date will be March 11, 2013.

**Taxes**

The Department of Revenue ("DOR") routinely has claims for refunds in various stages of administrative and legal review. In addition, the state is defending cases challenging the constitutionality of certain taxes that fund discrete state programs.

In the matter of *Automotive United Trades Organization v. State of Washington*, a fuel distributor and a nonprofit corporation filed a lawsuit against the state and the Treasurer challenging the Hazardous Substance Tax under Article I, Section 40 of the Washington Constitution (Amendment 18). In April 2011, King County Superior Court granted summary judgment to the state and dismissed the lawsuit on two grounds: (1) the lawsuit was untimely filed and (2) the plaintiffs did not meet their burden of proving that the tax violates the state Constitution. The plaintiffs have appealed and seek direct review in the Supreme Court. On May 31, 2011, the state filed an answer opposing direct review. All briefing is expected to be filed by the middle of November 2011, after which time the Supreme Court will decide whether to take the case or whether to refer it to the Court of Appeals. If the appeal is successful, the revenue generated by this tax would be diverted to the Motor Vehicle Fund and its uses would be limited to highway purposes only.

In the matter of *Dot Foods, Inc. v. Dep't of Revenue*, Dot Foods challenges 2010 legislation that retroactively amended the direct seller's exemption, RCW 82.04.423, with respect to tax periods before May 1, 2010. The 2010 legislation also repealed the exemption effective May 1, 2010, but Dot Foods does not challenge the repeal. Dot Foods alleges the retroactive portion of the legislation violates the federal due process clause and the constitutional separation of powers doctrine. Dot Foods further alleges that, even if the retroactive portion of the 2010 legislation is valid with respect to other taxpayers, section 1706 of the legislation preserves the *res judicata* effect of Dot Food's judgment in *Dot Foods, Inc. v. Dep't of Revenue*, 166 Wn.2d 912, 215 P.3d 185 (2009) (Dot Foods I), through the effective date of the repeal of the exemption. In Dot Foods I, the Supreme Court expansively construed the direct seller's exemption to grant Dot Foods a business and operation ("B&O") tax refund for the period January 2000 through April 2006. This case is stayed pending the Washington Supreme Court's decision in *Tesoro v. Dep't of Revenue*.

In *Estate of Bracken*, personal representatives of the estate (petitioners) object to DOR findings that assert additional state estate tax is due. Petitioners seek relief under RCW 11.96A.080 and .090, claiming that

the estate has paid all estate tax that is due under state law. This is one of a number of estate tax refund actions that have been filed against DOR in various superior courts. The petitioners in these actions argue that a Washington QTIP (qualified terminable interest property) election under RCW 83.100.047 was not made in the estates of the decedents' predeceased spouses and, therefore, DOR has erroneously included the marital trust assets left for the decedents' benefit in the decedents' taxable estates for purposes of Washington's estate tax. DOR estimates the potential refunds and lost revenues at risk based on the QTIP issue is approximately $25 million. Some of the petitioners also seek costs and attorneys' fees under RCW 11.96A.150. This case was consolidated with two other cases (*Estate of Toland* and *Estate of Nelson*) because each raises the same legal issue. On November 13, 2009, the Court granted summary judgment to DOR, holding that QTIP is not deductible and must be included in the decedents' Washington estates. On December 11, 2009, the *Estate of Nelson* filed an appeal in the Court of Appeals. On January 4, 2010, the *Estate of Bracken* filed a direct appeal in the Washington Supreme Court. The *Estate of Toland* did not file an appeal. Subsequently, the appeal in *Estate of Nelson* was transferred to the Washington Supreme Court and consolidated with *Estate of Bracken*. The Washington Supreme Court held oral arguments on May 19, 2011, and a decision is pending.

In *Tesoro Refining and Telemarketing Company,* Taxpayer contends that the manufacturing B&O tax does not apply on bunker fuel it sold for consumption outside the territorial waters of the United States by vessels used in foreign commerce, arguing that its manufacturing activity qualifies for a deduction provided by RCW 82.04.433(1) and WAC 458-20-175. DOR contends that the deduction is limited to selling B&O taxes, namely the wholesaling B&O tax and the retailing B&O tax. Taxpayer further contends that a retroactive amendment to RCW 82.04.433, enacted in 2009, that expressly limits the deduction to taxes imposed under RCW 82.04.250 (retailing B&O tax) and RCW 82.04.270 (wholesaling B&O tax), violates due process. DOR contends the 2009 amendment clarified the scope of the deduction and, moreover, the due process clause does not prevent retroactive tax legislation that either clarifies or changes a deduction as long as the legislation is rationally related to a legitimate state interest. In December 2010, the Court of Appeals issued a published decision in favor of the Taxpayer. DOR filed a petition for review in the Washington Supreme Court. The Court accepted review on April 26, 2011. Supplemental briefs in the Washington Supreme Court were filed in June 2011. Oral argument was heard on October 11, 2011, and a decision is expected in early to mid-2012.

In the matter of *Lamtec Corp.*, DOR assessed Lamtec (an out-of-state manufacturer) after concluding that its sales to Washington customers were subject to Washington's B&O tax and that it had sufficient nexus with Washington to be subject to Washington's B&O tax. Lamtec eventually paid the assessment and brought a refund action in Thurston County Superior Court. The superior court granted summary judgment to DOR. The Court of Appeals affirmed in a published decision. The Washington Supreme Court affirmed in a January 2011 opinion. Lamtec has filed a petition for certiorari to the U.S. Supreme Court, which remains pending. A decision of whether the court will accept the case is expected in late September 2011. Lamtec's refund claim is relatively small ($71,566.12 for the period 1997 through 2004). However, an adverse decision by the U.S. Supreme Court would potentially impact the economic nexus standards recently established by the Legislature during the 2010 legislative session through 2ESSB 6143. It also would potentially expose the state to significant refund claims filed by similarly-situated taxpayers.

In the matter of *Sprint Spectrum LLC v. Dep't of Revenue*, the Thurston County Superior Court issued a letter decision on May 16, 2011, that reversed a Board of Tax Appeal ("BTA") decision in favor of DOR. The BTA had upheld DOR's long-standing position that sales of cell phone service do not qualify for the sales tax exemption provided by RCW 82.08.0289 for service "provided to an individual subscribing to a residential class of telephone service." The superior court concluded that the exemption applies to both wireline and wireless telephone service provided to non-business customers. An adverse ruling could

result in potentially substantial refunds and loss of revenues. DOR has appealed and its opening brief was filed in October 2011.

**Employment and Pension**

In *WEA, et al. v. Department of Retirement Services and State of Washington*, a King County Superior Court was asked to overturn the Legislature's repeal of "gain sharing" benefits for various retirement system plans based on alleged constitutional impairment of contracts, due process, and estoppel theories. Four separate lawsuits were filed, which were consolidated under one case; one of those lawsuits was voluntarily dismissed in June 2009 leaving only three cases in the consolidated case. Summary judgment arguments were heard in July 2010. The plaintiff's motion for summary judgment was granted on the contract and estoppel claims, and the state's cross-motion was denied. There is a second phase of the case to be litigated before the end of 2011, which addresses benefits provided in replacement of gainsharing. If plaintiffs ultimately prevail on all issues before the court, there could be a significant fiscal impact potentially requiring the Legislature to pursue additional funding of the plans or other remedies. See "RETIREMENT SYSTEMS."

The matter of *Moore v. Washington Health Care Authority* is a class action lawsuit alleging that the state has wrongfully denied medical benefits to current and former non-permanent employees by inconsistently applying eligibility standards, misclassifying employees to deny them benefits in alleged violation of the applicable statutes and regulations. A comprehensive ruling for plaintiffs on all issues in dispute could have a potentially significant impact. The trial court has ruled against the state on most liability issues. Currently, trial is set for September 2012.

*Washington Federation of State Employees v. State of WA/Dept of Retirement Systems* and *Washington Education Association v. State of WA/Dept of Retirement Systems* were filed in Thurston County Superior Court on October 11 and 12, 2011. Both plaintiff groups challenge the 2011 Legislature's repeal of what is termed the Uniform Cost of Living Adjustment ("COLA") as described under "RETIREMENT SYSTEMS–Actuarial Valuation and Funding–2011 Legislation." This COLA was provided to retirees of Public Employees Retirement System (PERS) Plan 1 and Teachers Retirement System (TRS) Plan 1 on an annual basis by increasing the retirees' monthly retirement benefit in July of every year. Plaintiffs ask for declaratory and injunctive relief seeking, inter alia, the restoration of the COLA.

**Other**

In *US v. WA* (culverts/phase II), plaintiff Tribes and the United States allege that state-owned culverts that block fish passage violate Tribes' treaty rights. The state is awaiting the court's decision and is assessing potential issues for appeal in anticipation of the court's decision.

*Washington State Hospital Association v. State* was filed in King County Superior Court on July 18, 2011. The plaintiff is seeking to prevent the Health Care Authority from implementing House Bill ("HB") 2069, which the Legislature enacted in 2011. The plaintiff asserts that HB 2069 establishes a tax in violation of Article VII, Section 5 of the Washington Constitution by failing to set forth the purpose of the revenues generated from the Hospital Safety Net Assessment fund. HB 2069 reduces the state's payment rates to hospitals for the services they provide to Medicaid recipients, although the rates still would exceed the levels that existed before the Safety Net Assessment was enacted, and increases the amounts from the Safety Net Assessment fund that can be used to support Medicaid payments to hospitals. The state filed its answer to the complaint on August 4, 2011. The plaintiff filed a motion for summary judgment on September 2, 2011, which the court considered at a hearing on September 30, 2011.

## RISK MANAGEMENT

### Insurance

The state operates a self-insurance liability program (the "SILP") for third-party claims against the state for injuries and property damage up to $10 million for each occurrence. An excess insurance policy is also purchased for these risks, which covers amounts above a self-insured retention (the "SIR") up to an annual limit of $40 million. The current SIR is $10 million for all agencies except DSHS and DOC, each of which has an $18 million SIR. Insurance is procured annually, and the SIR may change. The SILP is administered by OFM with money available in a statutorily-based Liability Account. The Liability Account is funded by annual premiums assessed to state agencies based on each agency's loss history (paid claims over the most recent five years and open reserves for pending claims). State statutes do not permit the Liability Account to exceed 50 percent of the state's outstanding liabilities as determined bi-annually by an independent actuary. General and auto claims are investigated and settled through the coordinated efforts of OFM, the Office of the Attorney General and WSDOT with consultation and agreement of the affected agency. Approved claims (including judgments, settlements and related defense costs) are paid by OFM from the Liability Account.

The SILP covers the state, its agencies, governing bodies, boards and commissions, including all state employees, elected and appointed officials, members of boards or commissions, volunteers and reserve officers, all while acting within the scope of their employment or assigned volunteer activities. Students in state four-year universities and in the community and technical colleges are not covered by the SILP unless they otherwise qualify as state employees or volunteers. The University of Washington does not participate in SILP but operates its own self-insurance program and purchases a variety of commercial insurance, including excess and property policies. See Notes 7(E), 10 and 13(B) in Appendix D–"THE STATE'S 2010 AUDITED BASIC FINANCIAL STATEMENTS."

The Ferries Division of WSDOT does not participate in the SILP, so the state purchases a marine policy that covers the vessels and operations of the Washington State Ferry System and several small vessels owned by DOC to transport individuals to the McNeil Island Corrections Center. The policy combines general liability, pollution liability, vessel hull and machinery and property in a master policy. It provides coverage up to $250 million annually for liability, $250 million for pollution, approximately 60 percent of the value of the ferries ($879 million) and all terminals, docks and shore-side facilities ($400 million). There is a single $1.0 million deductible per occurrence. The policy also has a special protection for war risk for selected vessels and routes, which provides the above coverage for losses as a result of foreign or domestic terrorism. This is needed because acts of war are excluded from the general marine policy.

The state also purchases other commercial insurance such as aviation insurance covering aircraft and airport liability coverage for agencies and colleges with aviation exposures, a master property policy covering all risks for selected buildings, contents and electronic data processing equipment (replacement value insurance including earthquakes and floods), a fidelity policy covering fraudulent or dishonest acts of all state officers and employees, and special policies covering specific buildings such as certain buildings at Washington State University, as well as for the Tacoma Narrows Bridge, including all risk property coverage that covers the possible loss of toll revenues for the new span of the bridge.

### Workers' Compensation Program

The Workers' Compensation Program insures payment of benefits for approximately 70 percent of the work force in the state, excluding self-insured employers and their employees. The Workers' Compensation Program provides time-loss, medical, vocational, disability and pension benefits to qualifying individuals who sustain work-related injuries or illness.

The main benefits plans of the Workers' Compensation Program are funded based on rates that are designed to keep these plans solvent in accordance with recognized actuarial principles and to limit fluctuations in premium rates. The accrual of these future payments for workers that were injured as of June 30, 2010, was estimated to be approximately $11.2 billion as of June 30, 2010, without any cost-of-living adjustments ("COLA"). The accrual of future payments for workers that were injured as of June 30, 2010, was estimated to be approximately $24 billion as of June 30, 2010, with COLA. There are $11.9 billion of invested assets, mainly long-term fixed income securities, to help fund these accrued benefits.

The supplemental pension plan supports COLA granted for time-loss and disability payments for all injured workers, including those of self-insured employers. The supplemental pension component covers both state funded and self-insured employees. By statute, the state is permitted to collect only enough revenue to fund the current COLA payments. No assets are allowed to accumulate for the future funding of claims' COLA benefits payable. The programs' actuaries estimate these rates so that yearly premium payments will be sufficient to make these current payments.

In the 2011 legislative session, the Legislature adopted two bills designed to improve return-to-work outcomes and reduce the cost of the Workers' Compensation Program. One bill directs the Department of Labor and Industries to create a single, statewide provider network for injured workers and expands access to the state's Centers of Occupation Health Education, which are community-based organizations that use occupational health best practices. The second bill, among other provisions, (1) eliminates the Fiscal Year 2012 cost-of-living adjustment with no future catch-up and delays the first adjustment for future claims by one year, (2) allows certain workers to resolve all but the medical portion of their claims with a claim resolution structured settlement agreement that provides a periodic payment schedule, (3) provides that if a pension is awarded after a permanent partial disability award, all permanent partial disability compensation must be either deducted from the worker's monthly pension benefits or deducted from the pension reserve, and (4) authorizes state fund employers to receive a wage subsidy and certain reimbursements for employing an injured worker at light duty or transitional work.

See Note 7(E) in Appendix D–"THE STATE'S 2010 AUDITED BASIC FINANCIAL STATEMENTS."

**State Unemployment Compensation Fund**

The Washington State Unemployment Insurance Program provides weekly unemployment insurance payments for workers who lose their jobs through no fault of their own. The unemployment insurance program is a partnership among federal and state governments. Employers pay unemployment insurance through unemployment taxes to both the state and the federal government. Workers in Washington State do not pay unemployment taxes.

Federal unemployment tax revenues are used to finance specific purposes related to running the states' unemployment insurance programs, such as state employment security staff salaries, equipment, software, and supplies that are used in direct support of the Unemployment Insurance, Employment Services, and Labor Market Information programs. The federal tax also provides benefit reserve funds for possible extended benefits programs and provides a loan fund for states that deplete their benefit accounts.

State unemployment tax revenues are directed to the state's benefit trust fund, which can only be used to pay unemployment benefits. This trust fund is held in the national unemployment insurance trust fund of the U.S. Treasury. According to state statute, tax rates are intended to maintain fund balances sufficient to cover at least 12 months of unemployment benefits during a severe recession. By statute, the state may add an additional solvency tax of 0.2 percent to an employer's rate if the balance in the trust fund drops

below a level needed to pay seven months of benefits. The state has not borrowed from the federal government to pay unemployment benefits since the mid-1980s.

There are two major components of state unemployment taxes, an experience-rated tax based on a rolling four-year average of the employer's layoff history and a social-cost tax based on benefit costs from the previous year that are not attributed to a specific employer.

The average combined unemployment tax rates as a percentage of taxable wages for Fiscal Years 2005 to 2011 are shown in the following table.

**Table 17**
**Average Combined Unemployment Tax Rates**
(Fiscal Year ended June 30)

| Year | Average Tax Rate[1] |
|---|---|
| 2005 | 2.8% |
| 2006 | 2.8 |
| 2007 | 2.38 |
| 2008 | 1.97 |
| 2009 | 1.66 |
| 2010 | 1.40 |
| 2011 | 2.25 |

(1) Average Tax Rate on taxable wages as of second quarter of the year.

*Source: U.S. Department of Labor-Unemployment Insurance Data Summary.*

The balance in the trust fund as of August 2011 is $2.7 billion, which is calculated to provide 15.2 months of benefits. The following table shows the unemployment compensation balances for Fiscal Years 2005 through 2011.

**Table 18**
**Unemployment Compensation Fund Balance[1]**
(Fiscal Year ended June 30)
*($ in millions)*

| Year | Balance |
|---|---|
| 2005 | 1,638 |
| 2006 | 2,528 |
| 2007 | 3,321 |
| 2008 | 4,000 |
| 2009 | 3,398 |
| 2010 | 2,316 |
| 2011 | 2,545 |

(1) The state trust fund is held in an account for the state in the national unemployment trust fund of the U.S. Treasury.

*Source: TreasuryDirect®.*

In August 2011, approximately 178,000 unemployed workers received benefits under the program. Beginning July 3, 2011, new claimants entering the program are entitled to up to 26 weeks of regular

unemployment insurance benefits from the state with a maximum state liability of $15,158 (which is the maximum weekly benefit amount times 26). The maximum weekly benefit amount is calculated based on 63 percent of Washington's average weekly wage per unemployed worker.

Beginning September 24, 2011, all workers who had applied or will apply for unemployment between March 6, 2011, and November 5, 2011, will receive an additional $25 per week. This will be in addition to the calculated weekly benefit amount, which will bring the maximum state liability to $15,808.

In December 2010, the federal government again extended the Emergency Unemployment Compensation program. This program potentially adds up to 53 weeks of unemployment insurance to unemployed workers. This program was initially effective through March 2009, and has since been extended six times, currently until the end of December 2011. The federal government pays for the total cost of these benefits.

In February 2009, the state qualified for the federal Extended Benefits Program that allowed up to an additional 20 weeks of benefits. The qualification triggers are based upon unemployment rates and those rates compared to prior years. The two levels available, one for up to 13 weeks of benefits and one for up to 20 weeks, depend upon the seasonally adjusted total unemployment rate - the higher number of weeks are available when the rate is high. Extended benefits are funded 100 percent by federal money until December 2011. Thereafter the funding for these benefits will return to 50 percent from the state trust fund and 50 percent from the federal government.

### Seismic Activity and Other Natural Disasters

The state is in an area of seismic activity, with frequent small earthquakes and occasionally moderate and larger earthquakes. Certain soil types and property in certain areas of the state could become subject to liquefaction (the transformation of soil from a solid state to a liquid state) following a major earthquake, to landslides caused by an earthquake and to ongoing shaking that could follow a major earthquake. The state contains identified geologic faults. In addition to various faults beneath the state, the state is within the Cascadia subduction zone, a fault beneath the Pacific Ocean, which produced a large earthquake several hundred years ago and is thought to be capable of causing extensive damage if another such earthquake occurs. The most recent notable earthquake in the state, which measured 6.8 on the Richter Scale, occurred in 2001. Areas of the state also could experience the effects of a tsunami following a major earthquake on the West Coast or in areas outside the United States. WSDOT has determined that, among other infrastructure, the seawall between downtown Seattle and Puget Sound; the Alaskan Way Viaduct, an elevated highway adjacent to the seawall; and the SR 520 Evergreen Point Bridge, one of only two bridges that cross Lake Washington, are likely to be damaged if another major earthquake occurs. Other natural disasters, including volcanic eruptions and tsunamis, are possible. The loss of life and property damage that could result from a major earthquake or other major natural disasters could have a material and adverse impact on the state and its economy and financial condition. See "TRANSPORTATION-RELATED REVENUES AND EXPENDITURES–Transportation Expenditures–The SR 520 Corridor Program" and "–The Alaskan Way Viaduct."

## RETIREMENT SYSTEMS

### Overview

The state administers 13 defined benefit retirement plans, three of which contain hybrid defined benefit/defined contribution options. As of June 30, 2009, the plans covered approximately 500,070 eligible state and local government employees. These plans are administered through the Department of Retirement Systems and the Board for Volunteer Fire Fighters. See Table 19.

The state's retirement plans are funded by a combination of funding sources: (1) contributions from the state; (2) contributions from employers (including the state as employer and other governmental employers); (3) contributions from employees; and (4) investment returns.

Retirement funds are invested by the Washington State Investment Board, a 15-member board created by the Legislature in 1981. Additional information regarding retirement funds can be found in Note 11 of Appendix D–"THE STATE'S 2010 AUDITED BASIC FINANCIAL STATEMENTS."

The Office of the State Actuary ("OSA") is statutorily required to perform biennial actuarial valuations, although in practice actuarial valuations are performed annually. The final audited actuarial valuation report is typically released in the fall. OSA also is required to recommend contribution rates and to provide actuarial services to the Legislature, the Governor, and to certain boards and state agencies. OSA recommendations are non-binding.

See "LITIGATION" for a discussion of certain litigation concerning the state's retirement plans.

**Rate-Setting Process**

Contribution rates for the upcoming biennium are adopted during even-numbered years according to a statutory rate-setting process. The process begins with OSA's actuarial valuation of each plan and a determination of recommended contribution rates. OSA provides preliminary results to the Select Committee on Pension Policy ("SCPP") and the Pension Funding Council ("PFC"). The SCPP then recommends contribution rates to the PFC, which in turn is required to adopt contribution rates no later than the end of July in even-numbered years. The rates adopted by the PFC are subject to revision by the Legislature, and during the years 2001 through 2011 the rates adopted by the Legislature were lower than those that would have been required to produce actuarially required contributions to two closed plans, Plan 1 of the Public Employees Retirement System ("PERS 1") and Plan 1 of the Teachers Retirement System ("TRS 1") in those years.

The 20-member SCPP is made up of legislators, state agency representatives, and stakeholders. The six-member PFC consists of the Director of the Department of Retirement Systems, the Director of OFM, the chair and ranking minority member of the House of Representatives Ways and Means Committee, and the chair and ranking minority member of the Senate Ways and Means Committee. The Law Enforcement Officers' and Fire Fighters' Retirement System 2 ("LEOFF 2") is the single exception to this process. OSA's preliminary valuation is presented to the LEOFF 2 Board, which is also required to adopt contribution rates no later than the end of July in even-numbered years.

## Retirement Plans

A summary of each of the state retirement plans as of June 30, 2010, the period reported on in the last actuarial valuation dated September 2011, is provided below.

**Table 19**
**Overview of Retirement Plans**
**(**As of June 30, 2010)

| Retirement System/Plan | Administered by | Benefit Type | Active & Terminated Vested Members | Members Receiving Benefits | Closed in |
|---|---|---|---|---|---|
| **Public Employees' Retirement System ("PERS")** was established in 1947 and is a cost-sharing multiple-employer retirement system. | | | | | |
| PERS 1 | Dept of Retirement Systems | Defined Benefit | 10,986 | 53,742 | 1977 |
| PERS 2/3 | | Defined Benefit/ Hybrid | 174,400 | 23,157 | Open |
| **Teachers' Retirement System ("TRS")** was established in 1938 and is a cost-sharing multiple-employer retirement system comprised principally of non-state employees. | | | | | |
| TRS 1 | Dept of Retirement Systems | Defined Benefit | 5,291 | 36,015 | 1977 |
| TRS 2/3 | | Defined Benefit/Hybrid | 69,983 | 4,555 | Open |
| **School Employees' Retirement System ("SERS")** was established in 2000 and is a cost-sharing multiple-employer retirement system comprised principally of non-state employees. | | | | | |
| SERS 2/3 | Dept of Retirement Systems | Defined Benefit/Hybrid | 62,039 | 5,384 | Open |
| **Law Enforcement Officers' and Fire Fighters' Retirement System ("LEOFF")** was established in 1970 and is a cost-sharing multiple-employer retirement system comprised primarily of non-state employees, with the Department of Fish and Wildlife enforcement officers as the major exception. | | | | | |
| LEOFF 1 | Dept of Retirement Systems | Defined Benefit | 302 | 8,008 | 1977 |
| LEOFF 2 | | Defined Benefit | 17,556 | 1,639 | Open |
| **Washington State Patrol Retirement System ("WSPRS")** was established in 1947 and is a single employer retirement system. | | | | | |
| WSPRS 1 | Dept of Retirement Systems | Defined Benefit | 872 | 851 | 2002 |
| WSPRS 2 | | Defined Benefit | 287 | 0 | Open |
| **Public Safety Employees' Retirement System ("PSERS")** was established in 2006 and is a cost-sharing multiple-employer retirement system. | | | | | |
| PSERS 2 | Dept of Retirement Systems | Defined Benefit | 4,210 | 7 | Open |
| **Judicial Retirement System ("JRS")** was established in 1971 and is an agent multiple-employer retirement system. | | | | | |
| JRS | Dept of Retirement Systems | Defined Benefit | 5 | 125 | 1988 |
| **Judges' Retirement Fund ("Judges")** was established in 1937 to provide retirement benefits to judges of the Supreme Court, Court of Appeals, and Superior Courts. It is an agent multiple-employer retirement system. Judges are now covered under PERS. | | | | | |
| Judges | Dept of Retirement Systems | Defined Benefit | 0 | 13 | 1971 |
| **Volunteer Fire Fighters' and Reserve Officers' Relief and Pension Act ("VFFRPF")** was established in 1945 and is a cost-sharing multiple-employer retirement system. | | | | | |
| VFFRPF | Board for Volunteer Fire Fighters | Defined Benefit | 16,931 | 3,712 | Open |

*Source: Department of Retirement Systems.*

A table in Appendix D under Note 11 C. lists the contribution rates for employers and employees for the retirement plans at the close of Fiscal Year 2010 expressed as a percentage of current year covered payroll. The PFC adopted increased 2011 contribution rates for some plans; the Legislature did not revise the rates and, therefore, the rates adopted by the PFC were effective as of July 1, 2011, or September 1, 2011. The rates that increased from those shown in Appendix D are: (1) for PERS Plans 1 and 2, state agencies and local governments rates increased to 7.25 percent and to 10.8 percent for state elected officials and the employee rate for Plan 2 increased to 4.64 percent, (2) for SERS Plan 2, state agency and local government employer rates increased to 7.59 percent and the employee rate to 4.09 percent, (3) for WSPRS Plans 1 and 2, state agencies rates increased to 8.07 percent and the employee rate to 6.59 percent, (4) for PSERS Plan 2, state agency and local government rates increased to 8.86 percent and the employee rate to 6.36 percent and (5) for JRS, the employer and employee rate increased to 7.5 percent.

**State Contributions**

Table 20 summarizes the state's contributions to the retirement plans, as adopted by the Legislature.

**Table 20**
**State's Contributions**
*($ in millions)*

| | 2008 | 2009 | 2010 |
|---|---|---|---|
| PERS Plan 1 | 115.5 | 169.0 | 78.2 |
| PERS Plan 2/3 | 159.6 | 217.6 | 160.4 |
| TRS Plan 1 | 4.3 | 8.0 | 5.6 |
| TRS Plan 2/3 | 0.5 | 0.8 | 0.8 |
| SERS Plan 2/3 | - | - | - |
| PSERS Plan 2 | 5.9 | 7.7 | 7.8 |
| LEOFF Plan 1 | - | - | - |
| LEOFF Plan 2 | 46.8 | 52.0 | 52.2 |
| VFFRPF | 5.7 | 5.9 | 5.7 |
| WSPRS Plan 1 | 5.2 | 5.2 | 4.2 |
| WSPRS Plan 2 | 0.9 | 1.2 | 1.1 |
| JRS | 9.6 | 10.3 | 11.6 |
| Judges | - | - | - |
| **Total** | 354.0 | 477.7 | 327.6 |

*Source: Department of Retirement Systems.*

***Contribution Ratios.*** In addition to the state's required contributions, employees and local government employers must meet their required contributions. Participating governmental employers include, but are not limited to, school districts, counties, municipalities, and political subdivisions.

**Table 21**
**Estimated State and Local Government**
**Employer Contribution Ratios by Funding Source[1]**
*(in percents)*

| System | General Fund-State | Non-General Fund-State | Local Government |
|---|---|---|---|
| PERS | 19.9 | 28.4 | 51.7 |
| TRS | 66.3 | 0.0 | 33.7 |
| SERS | 44.6 | 0.0 | 55.4 |
| PSERS | 71.0 | 7.6 | 21.4 |
| LEOFF 1[2] | 0.0 | 0.0 | 0.0 |
| LEOFF 2 | 40.0 | 0.0 | 60.0 |
| WSPRS | 8.0 | 92.0 | 0.0 |

(1) These splits are used by OSA to model approximate cost allocations for employers by fund or type of employer in actuarial fiscal notes. The reader should exercise caution when using numbers provided in this table for any other purpose. Note these splits are based upon the June 30, 2008, actuarial valuation.
(2) No contributions required when the plan is fully funded. The plan has been fully funded since 2000.
*Source: Office of the State Actuary.*

## Actuarial Valuation and Funding

***Actuarial Reporting.*** The State Actuary is required, pursuant to Chapter 41.45 RCW, to provide an actuarial valuation of PERS, TRS, SERS, PSERS, LEOFF, and WSPRS plans every two years. In practice, valuations are provided annually but only valuations for odd-numbered years are used to determine contribution rates. The demographic assumptions were last updated in the 2007 Actuarial Valuation Report based upon the 2001-2006 Experience Study Report. The next review of the demographic assumptions is expected to be completed in 2014.

The results shown in Table 22 reflect the following assumptions, adopted by the PFC and the LEOFF 2 Board, respectively, which went into effect in 2009:

(1) Rate of investment return: 8.0 percent per annum;

(2) General salary increases: 4.0 percent per annum (4.5 percent in LEOFF 2); and

(3) Rate of Consumer Price Index increase: 3.5 percent (where applicable).

The State Actuary issued a report in August 2011 that recommends that the PFC adopt new long-term economic assumptions, including decreasing the inflation assumption from 3.5 percent to 3.0 percent, the annual investment return assumption from 8.0 percent to 7.5 percent, and the general salary growth assumption from 4.0 percent to 3.75 percent and to phase in the recommended change to the assumed rate of return over the next five biennia. The PFC is expected to consider the recommendations in the fall of 2011.

***Valuation Method.*** The state uses two funded status measures. The first funded status measure compares the Actuarial Value of Assets ("AVA") to the Projected Unit Credit ("PUC") liabilities. The PUC cost method projects future benefits using salary growth and other assumptions and applies the service that has been earned as of the valuation date to determine accrued liabilities. The asset valuation method smoothes the inherent volatility in the Market Value of Assets ("MVA") by deferring a portion of the annual investment gains or losses over a period of up to eight years. This method is consistent with governmental accounting standards. This smoothing method, which the state has followed in all actuarial

valuations since July 1, 2003, helps to limit fluctuations in contribution rates and funded status that would otherwise arise from short-term changes in MVA. For example, portions of investment gains in 2004 through 2007 were deferred for recognition in later years, and one-eighth of investment losses in 2008-2009 were recognized in that Fiscal Year, with the result that the remaining unrecognized losses will continue to put downward pressure on the funded status of all plans for seven more years as the remainder of 2008-2009 losses are recognized.

The state also uses a second measure, comparing the MVA to the PUC liabilities calculated using a short-term interest rate assumption. This measure is used for the closed plans, PERS 1, TRS 1, and LEOFF 1. Additional information on this measure is provided in the 2010 Actuarial Valuation Report.

***Funded Status.*** The following table displays the funded status on an actuarial value basis for the PERS, TRS, SERS, PSERS, LEOFF and WSPRS plans discussed above. The June 30, 2010, actuarial valuation showed that the funded status of all of the state-administered plans combined is 102 percent. Two funds – PERS 1 and TRS 1 – are underfunded with an unfunded liability of $4.7 billion as of June 30, 2010, approximately $2.4 billion of which is the responsibility of the state and the remainder a liability of local governments. Assets from one plan may not be used to fund benefits for another plan. However, all employers in PERS, PSERS and SERS are required to make contributions at a rate (percentage of payroll) determined by OSA every two years for the sole purpose of amortizing the PERS 1 Unfunded Actuarial Accrued Liability ("UAAL") within a rolling ten-year period. In addition, all employers in TRS are required to make contributions at a rate (percentage of payroll) determined by OSA every two years for the sole purpose of amortizing the TRS 1 UAAL within a rolling ten-year period. For this purpose, the Legislature has established certain maximum contribution rates that began in 2009 and will continue until 2015 and certain minimum contribution rates that are to become effective in 2015 and remain in effect until the actuarial value of assets in PERS 1 and TRS 1 equals 100 percent of the actuarial accrued liability of PERS 1 and TRS 1, respectively. Upon completion of each biennial actuarial valuation, OSA is to recommend to the PFC any adjustments in the minimum contribution rates that may be needed as a result of material changes in benefits or actuarial assumptions, methods or experience. Any changes adopted by the PFC are subject to revision by the Legislature.

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## Table 22
## Funded Status on an Actuarial Value Basis[1]

| | PERS | | TRS | | SERS | PSERS | LEOFF | | WSPRS | Total[2] |
|---|---|---|---|---|---|---|---|---|---|---|
| | Plan 1 | Plan 2/3 | Plan 1 | Plan 2/3 | Plan 2/3 | Plan 2 | Plan 1 | Plan 2 | Plan 1/2 | |
| **PUC Liability[3]** | 12,531 | 17,272 | 9,231 | 5,708 | 2,368 | 80 | 4,381 | 4,863 | 782 | 57,216 |
| **Valuation Assets[3]** | 9,293 | 19,474 | 7,791 | 6,593 | 2,664 | 103 | 5,561 | 6,043 | 920 | 58,442 |
| **Unfunded Liability[3]** | 3,238 | (2,202) | 1,439 | (886) | (296) | (23) | (1,180) | (1,179) | (137) | (1,226) |
| **Funded Ratio (%)** | | | | | | | | | | |
| 2000[4] | 98 | 190 | 100 | 196 | 170 | n/a | 136 | 161 | 152 | 131 |
| 2001[4] | 97 | 179 | 100 | 197 | 197 | n/a | 129 | 154 | 147 | 126 |
| 2002 | 92 | 158 | 98 | 182 | 169 | n/a | 119 | 137 | 135 | 118 |
| 2003 | 82 | 142 | 89 | 155 | 138 | n/a | 112 | 125 | 123 | 107 |
| 2004 | 81 | 134 | 88 | 153 | 137 | n/a | 109 | 117 | 118 | 105 |
| 2005[4] | 74 | 127 | 80 | 134 | 122 | n/a | 114 | 114 | 113 | 99 |
| 2006[4] | 74 | 121 | 80 | 133 | 125 | 99 | 117 | 116 | 114 | 100 |
| 2007[4] | 71 | 120 | 76 | 130 | 126 | 120 | 123 | 129 | 118 | 99 |
| 2008[4] | 71 | 119 | 77 | 125 | 121 | 127 | 128 | 133 | 121 | 100 |
| 2009 | 70 | 116 | 75 | 118 | 116 | 128 | 125 | 128 | 119 | 99 |
| 2010[5][6] | 74 | 113 | 84 | 116 | 113 | 129 | 127 | 124 | 118 | 102 |

(1) Liabilities have been valued using the Projected Unit Credit ("PUC") cost method at an interest rate of 8.0 percent while assets have been valued using the actuarial value of assets.
(2) Assets from one plan may not be used to fund benefits for another plan.
(3) Dollars in millions. Based on actuarial valuation as of June 30, 2010.
(4) Actuarial assumptions changed.
(5) Includes results of 2011-13 legislation that eliminated the annual adjustment increase for retirees in PERS 1 and TRS 1.
(6) 2010 Funded ratio for PERS 1 and TRS 1 would drop to 63 percent for PERS 1 and 70 percent for TRS 1 if both gainsharing and the annual adjustment were reinstated.
Totals may not add due to rounding.

*Source: Office of the State Actuary.*

***Alternative Methodology.*** In August 2010, OSA released the "2010 Risk Assessment" of the state's pension plans to assist the Legislature in proactively addressing pension plan funding levels. This report uses a dynamic risk assessment model with a stochastic (or probabilistic) component to quantify the likelihood and magnitude of possible future outcomes for pensions taking into account the variability of investment returns and revenue growth. It also differentiates between model outcomes in which (1) all actuarially recommended contributions are made and there are no future improvements in benefits, and (2) drawing on past practice, contributions are made at less than actuarially recommended rates and future benefits are improved. This differs from the traditional reporting methodology which provides funded status information at a single point in time based on what is expected to occur. OSA expects to use both methodologies in future reports on the financial condition of the pension systems.

Using this alternative methodology, the funded status of two closed plans (PERS 1 and TRS 1) is expected to decline to the 50 percent range by 2016 (when asset value losses as of June 2009 will be fully realized) and then rise thereafter provided that the plans are fully funded going forward and benefits are not further improved. If, instead, contribution rates and decisions to improve benefits follow past practice, the funded status for these two plans is expected to decline to the 20-30 percent range by 2030 and then rise thereafter. Alternatively, the funded status of PERS 2/3, the largest open plan, is expected to be in or above the 90 percent range in the projected 50-year period assuming the plan is fully funded and benefits are not improved. If contribution rates are lower and benefits improve as seen in the past, the expected funded status for PERS 2/3 drops to the 80 percent range. The 2010 Risk Assessment also notes model outcomes for each pension plan in more optimistic and more pessimistic scenarios.

***Additional Information.*** Additional information on the state's defined benefit plans, including information on the state's smoothing method used in the rate setting process, the UAAL as a percentage of covered payroll of each plan, and annual required contribution ("ARC"), as of the latest valuation date is presented in Note 11 and in the Required Supplemental Information – Pension Plan Information in Appendix D—"THE STATE'S 2010 AUDITED BASIC FINANCIAL STATEMENTS." Note 3 in Appendix D—"THE STATE'S 2010 AUDITED BASIC FINANCIAL STATEMENTS" describes eligible investments for the state's pension plans.

***2011 Legislation.*** Since 1995, there has been an automatic, annual, service-based adjustment paid every July 1 for eligible PERS and TRS Plans 1 retirees. The budget adopted by the Legislature for the 2011-13 Biennium ends the future automatic annual increase, which is a fixed dollar amount that increases by 3.0 percent each year and is multiplied by the member's total years of service, for most retirees in the PERS and TRS Plans 1 except for the minimum benefits. The basic minimum benefit amount for retirees in those plans will continue to be increased by the annual increase amount and the alternative minimum benefit is raised to $1,545 per month. The unfunded accrued actuarial liability ("UAAL") in PERS and TRS Plans 1 reduced from $6.884 billion in 2009 to $4.439 billion in 2010 due in large part to the elimination of the annual increase. In addition, the minimum employer contribution rates for the PERS Plan 1 UAAL will be reduced from 5.75 percent to 3.5 percent and from 8.0 percent to 5.75 percent for TRS Plan 1.

**Other Post-Employment Benefits**

***PEBB Plan Overview.*** The state offers other post-employment benefits ("OPEB") including medical (which includes medical, prescription drug, and vision), dental, life, disability and long-term care insurance to retired employees. See "STATE GENERAL FUND—Employees" for a description of benefits for current state employees.

The Public Employee Benefits Board ("PEBB"), created within the Washington State Health Care Authority ("HCA"), offers retirees access to all of these OPEB benefits ("PEBB Plan"). Employers

participating in the PEBB plan include the state (general government agencies and higher education institutions) and K-12 school districts, numerous political subdivisions of the state and tribal governments. Employers subsidize a portion of the cost of some PEBB Plan benefits.

The relationship between the PEBB Plan and its member employers and their employees and retirees is not formalized in a contract or plan document; rather, the benefits are provided in accordance with a substantive plan, which the Governments Accounting Standards Board (GASB) defines as the plan as understood by employers or employees. For additional information on the state's PEBB Plan, see Note 12 in Appendix D—"THE STATE'S 2010 AUDITED BASIC FINANCIAL STATEMENTS."

***PEBB Membership.*** The PEBB Plan is available to employees who elect to continue coverage and pay the administratively established premiums at the time they retire under the provisions of the retirement system to which they belong. PEBB Plan members are covered in the following retirement systems: PERS, TRS, SERS, PSERS, WSPRS, and Higher Education retirement systems. See "RETIREMENT SYSTEMS—Retirement Plans." The following table shows PEBB Plan membership.

**Table 23**
**Membership in PEBB Plan**
*(As of June 30, 2010)*

| | Active Employees | Retirees[1] | Total |
|---|---|---|---|
| State | 111,374 | 26,181 | 137,555 |
| K-12 Schools and ESDs[2] | 2,198 | 27,378 | 29,576 |
| Political Subdivision | 11,554 | 1,116 | 12,670 |
| **Total** | 125,126 | 54,675 | 179,801 |

(1) Retirees include retired employees, surviving spouses, and terminated members entitled to a benefit.

(2) In Fiscal Year 2010, there were 99,239 full-time equivalent active employees in the 244 K-12 schools and ESDs that elected to limit participation in PEBB only to their retirees.

*Source: Washington State Comprehensive Annual Financial Report ("CAFR") for Fiscal Year Ended June 30, 2010.*

***OPEB Subsidies.*** PEBB Plan employers provide monetary assistance or subsidies to retirees only for medical and life insurance. Retirees pay the full cost of other benefits.

Participating employers provide two different types of medical insurance subsidies to retirees:

(1) Explicit Subsidy. Retirees enrolled in Medicare Parts A and B receive an explicit subsidy which lowers the monthly premium. The amount of the subsidy is determined annually by PEBB. For 2009 this amount was $182.89 monthly for each participant. This subsidy was reduced by the Legislature for the 2011-2013 Biennium to $150 monthly.

(2) Implicit Subsidy. Non-Medicare eligible retired members pay a premium based in part on a pool that includes claims experience for active employees that, on average, are younger and healthier. There is an implicit subsidy as the premiums are lower than they would be if the retirees were insured separately. The value of the implicit subsidy reflects the difference between the age-based claims cost and the premium paid by retirees.

PEBB also provides subsidized basic life insurance coverage to retirees. This is an explicit life insurance subsidy and is set up by the PEBB Board and approved as part of the budget process. In 2009 and 2010

that subsidy was $5 per month per retiree. This explicit benefit will be discontinued January 1, 2012. Retirees may elect to continue life insurance through the PEBB plan, but will pay the entire premium.

***Funding of OPEB Subsidies PEBB Plan.*** The explicit subsidy (retiree benefit) is set each biennium by the Legislature as part of the budget process. The implicit subsidy (retiree benefit) is indirectly set annually by HCA when it determines the premium of each of the non-Medicare health plans. These subsidies (contributions) are funded on a pay-go basis.

***GASB 45.*** GASB 45 requires each employer to calculate OPEB's actuarial accrued liability ("AAL") on the medical and life insurance explicit and implicit subsidies. It also requires a calculation of the annual required contribution ("ARC"), representing the annual contribution that will fund the current active and retired members' subsidies by the end of their working lifetimes. The net OPEB obligation ("NOO") is the cumulative difference between the annual OPEB cost and the actual contributions. The annual OPEB cost is the ARC, plus the interest on the NOO and the amortization of the NOO.

The most recent valuation for the PEBB Plan prepared by the Office of the State Actuary and published in January 2011, determined the plan's liabilities as of January 1, 2009 ("2009 OPEB Report"). Small changes in the assumptions or methods or changes in the plan provisions could result in relatively large changes in OPEB liabilities and the state's ARC, NOO and annual OPEB cost.

***Valuation Assumptions and Methods.*** Valuations in the 2009 OPEB Report are based on methods selected by the Office of Financial Management and on assumptions detailed in the 2009 OPEB Report and summarized below. The actuarial method chosen to allocate costs and the AAL for the 2009 OPEB Report is the Projected Unit Credit ("PUC"), one of six methods permitted by GASB. The PUC cost method is a standard actuarial funding method. The annual cost of benefits under the PUC is comprised of two components, normal cost (the estimated present value of projected benefits current plan members will earn in the year following the valuation date; represents today's value of one year of earned benefits) and amortization of the unfunded actuarial liability.

The assumed return on investment earnings and the discount rate used in calculating the AAL (4.5 percent) was selected in consultation with the Office of the State Treasurer to represent a long-term average of short-term investment rates, and annual inflation is assumed to be 3.5%. Annual growth in membership is assumed to be at a rate of 1.25 percent (0.90 percent for K-12 School and Education Service Districts), and annual salary increases were assumed to be at a rate of 4.5%. Assumptions underlying the medical inflation trend rates (ranging from 7.0–8.0 percent in 2009 to 5.0 percent through 2067) were provided by health care actuaries at Milliman, Incorporated. The unfunded AAL is amortized over a closed 30-year period as a level percent of payroll. Participation level is assumed to be 65 percent (50 percent for K-12 School and Education Service Districts) of eligible employees and 45 percent of spouses of eligible employees. It is assumed that all employees will get Medicare coverage after becoming eligible.

Table 24 summarizes key GASB 45 funded status for Fiscal Year 2010, based upon the PEBB Plan AAL as of January 1, 2009. Table 25 shows annual OPEB costs and net OPEB obligations for Fiscal Years ended June 30, 2009, and June 30, 2010.

**Table 24**
**Funded Status and Funding Progress of PEBB Plan**
*($ in thousands)*

| | 1/1/2008 | 1/1/2009 |
|---|---|---|
| Actuarial Accrued Liability (AAL) [1] | 4,014,270 | 3,786,869 |
| Actuarial Value of Plan Assets | - | - |
| Unfunded Actuarial Accrued Liability (UAAL) [2] | 4,014,270 | 3,786,869 |

(1) Actuarial Accrued Liability ("AAL"): Represents the portion of the present value of fully projected benefits attributable to service credit that has been accrued as of the valuation date.
(2) Unfunded Actuarial Accrued Liability (UAAL) is the excess, if any, of the actuarial accrued liability over the actuarial value of assets or the present value of benefits accrued to date not covered by plan assets.

*Source: Washington State Comprehensive Annual Financial Report ("CAFR") for Fiscal Year Ended June 30, 2010.*

**Table 25**
**Annual OPEB Cost and Net OPEB Obligation**
*($ in thousands)*

| | 2009 | 2010 |
|---|---|---|
| Beginning Net OPEB Obligation (NOO)[1] | 245,855 | 493,551 |
| Annual Required Contribution (ARC)[2] | 331,688 | 349,326 |
| Interest on the Net OPEB Obligation | 11,063 | 22,210 |
| Amortization of the Net OPEB Obligation | (8,377) | (17,116) |
| Annual OPEB Cost[3] | 334,374 | 354,420 |
| Contributions for Fiscal Year[4] | (86,678) | (70,099) |
| Net OPEB Obligation (NOO)[1] | 493,551 | 777,872 |

(1) Net OPEB Obligation ("NOO"). The GASB disclosure requirement on the balance sheet. It is the cumulative difference between the annual OPEB cost and the actual contributions.
(2) Annual Required Contribution ("ARC") is the annual contribution that will fund the current active and inactive members' subsidies by the end of their working lifetimes.
(3) Annual OPEB cost is the ARC less the amortization of the NOO plus the interest that would have been earned on the NOO if the state had funded the NOO.
(4) Contributions for Fiscal Year include the estimated explicit subsidies and implicit subsidies.

*Source: Office of State Actuary.*

## DEMOGRAPHIC AND ECONOMIC INFORMATION

### Business in Washington

A number of corporations have chosen Washington as their headquarters or as a major center of operations, including Amazon, Amgen, Boeing Commercial Airplanes, Costco, F5 Network, Microsoft, Nintendo America, Nordstrom, PACCAR, Starbucks and Weyerhaeuser. Key sectors in the state's economy include:

**Table 26**
**Gross Business Income by Industry Sector (NAICS[1])**
(Calendar Year 2010)
*(in dollars)*

| | Gross Business Income | Percent of Total |
|---|---|---|
| Business, Personal and Other Services | 122,015,096,483 | 20.8 |
| Wholesale Trade | 118,654,466,882 | 20.2 |
| Retail Trade | 115,723,136,869 | 19.7 |
| Manufacturing–General | 87,536,187,422 | 14.9 |
| Manufacturing–Aerospace | 35,638,654,845 | 6.1 |
| Construction | 33,378,030,430 | 5.7 |
| Finance, Insurance, Real Estate | 31,992,523,665 | 5.4 |
| Information | 16,553,387,959 | 2.8 |
| Utilities | 11,673,579,361 | 2.0 |
| Transportation | 10,424,434,762 | 1.8 |
| Agriculture, Forestry, Fishing | 3,000,873,169 | 0.5 |
| Warehousing & Storage | 642,425,082 | 0.1 |
| Mining | 541,496,964 | 0.1 |

(1) North American Industry Classification System.

*Source: Washington State Department of Revenue, "Quarterly Business Review Calendar Year 2010" Table 1.*

**Table 27**
**Twenty-Five Largest Employers in Washington[1]**
(as of August 2011)

| | | Full-Time Washington Employees[2] | | | Full-Time Washington Employees[2] |
|---|---|---|---|---|---|
| 1 | The Boeing Co. | 76,452 | 14 | Costco Wholesale Corp. | 8,224 |
| 2 | Joint Base Lewis-McChord | 51,000 | 15 | Group Health Cooperative | 8,125 |
| 3 | Navy Region Northwest[3] | 41,300 | 16 | Nordstrom Inc. | 7,343 |
| 4 | Microsoft Corp. | 40,311 | 17 | Swedish | 7,069 |
| 5 | University of Washington | 27,920 | 18 | Alaska Air Group Inc. | 6,253 |
| 6 | Providence Health & Services Washington | 19,091 | 19 | Fairchild Air Force Base | 5,835 |
| 7 | Wal-Mart Stores Inc. | 17,975 | 20 | United Parcel Service | 5,554 |
| 8 | Fred Meyer Stores | 13,495 | 21 | QFC – Quality Food Centers | 5,479 |
| 9 | King County Government | 13,382 | 22 | Washington State University | 5,297 |
| 10 | United States Postal Service | 12,367 | 23 | Virginia Mason Medical Center | 5,177 |
| 11 | City of Seattle | 10,627 | 24 | Seattle Public Schools | 5,048[4] |
| 12 | MultiCare Health System | 9,028 | 25 | Pacific Northwest National Laboratory | 4,900 |
| 13 | Franciscan Health System | 8,226 | | | |

(1) Amazon.com Inc. and Starbucks Corp. did not participate in the survey, but if they had participated, the Puget Sound Business Journal believes both companies would have been ranked in this list of 25 Largest Employers. The Book of Lists does not include total employment figure for state employees or federal employees.
(2) Employment totals are as of December 31, 2010.
(3) Includes Whidbey Naval Air Station and Everett Naval Air Station.
(4) Does not include substitutes.

*Source: Puget Sound Business Journal, August 12-18, 2011.*

## Trade

Washington is one of the most trade-intensive states in the nation and is an important gateway for trade with Asia and Canada and for domestic trade with Alaska and Hawaii. In 2010, based on the 2010 U.S. Census, Washington was the fifth largest exporter in the United States with a total of $53.2 billion in goods exported.

***Ports.*** Washington has seven deep-draft ports on the Puget Sound, one on the Pacific Coast and three on the Columbia River. The ports of Seattle and Tacoma, on Puget Sound, are the state's largest ports and are closer to Asian ports than is any other continental United States port. The ports of Seattle and Tacoma nationally ranked 9th and 13th, respectively, in 2010 when measured by total dollar value of imports and exports, according to the U.S. Department of Commerce Bureau of Census, and when combined, rank as the second-largest port complex on the West Coast measured by cargo volume.

***Airport.*** Seattle-Tacoma International Airport is Washington's primary airport and, measured by total passengers, was the 18th busiest airport in the country in 2010 according to a preliminary survey by Airport Council International-North America. The airport also ranks as the 20th busiest cargo airport in the United States.

## Aerospace

The aerospace industry represented approximately 7.5 percent of all taxable business income generated in the state in calendar year 2010 and accounted for approximately 43.5 percent of the total value of goods exported by the state in calendar year 2010. There are 153 aerospace companies in the state, with Boeing being the largest aerospace employer in the area, and more than 650 in the industry cluster (including machine shops, engineering and research firms, and other suppliers and supporting entities). Although Boeing has dominated manufacturing employment, other manufacturers also have experienced growth, thus reducing Boeing's percentage of total manufacturing jobs in the state. Boeing expects to deliver its first 787 by the end of 2011 after experiencing production delays. Boeing has opened a second 787 production line in South Carolina, which may affect the state in the long-run.

## Forest Products

Natural forests cover nearly 50 percent of the state's land area. Forest products, including lumber, paper products and other wood and pulp products, are a traditional manufacturing sector in the state, although overall production has declined in recent years. Weyerhaeuser is the state's largest forest products employer.

## Agriculture and Food Processing

In 2009 (the last year for which such data is available), the state's $35 billion food and agriculture industry employed approximately 160,000 people and contributed 11 percent to the state's economy. Nearly 300 agricultural commodities are produced commercially in Washington, and in 2009 the state's top 10 agricultural commodities (in value of production for 2009) were apples, milk, wheat, potatoes, cattle, hay, nursery/greenhouses, cherries, hops and grapes. Washington ranked first in United States production of apples, sweet cherries, pears, red raspberries and hops and second in United States production of potatoes and grapes. In 2009, Washington was the second-largest wine-producer in the nation, with more than 600 wineries.

In 2010, food processing was an $11.7 billion dollar industry employing 40,531 people supporting approximately 1,119 companies that take advantage of the state's production of crops, access to low-cost energy, inter-modal access and ability to ship products.

The agricultural and food processing sector is export-oriented. In 2010, nearly $10.9 billion in food and agricultural products were exported through Washington ports. Close to 90 percent of the state's agricultural exports is directed to Asia.

Several locally-based manufacturers of specialty food processing equipment and packaging support the food-processing sector in the state. Locally-based companies design and manufacture food processing equipment, such as sorters, scanners, conveyors, packaging and bottling technology, and freezing and refrigeration equipment for both ship- and land-based facilities.

**Information and Communications Technology**

The state's approximately 4,200 software companies make the state the largest employer of software publishing workers in the nation, according to the U.S. Departments of Employment Security and Commerce. The state ranks first in the nation in the creation of new software companies. The state also is a global center for gaming design and development, with approximately 55 companies involved in game development. California-based companies Adobe, Google, Hewlett Packard, Intel, Oracle and Yahoo! all have established engineering and operations bases in the state.

**Global Health and Biotechnology**

The state is a global center for the advancement of medicine and life sciences. More than 25,000 workers were directly employed in the life sciences sector in the state in 2009, and the life sciences industry in the state generated an estimated $6.4 billion in revenues in 2008. The life sciences sector in Washington includes the development and manufacture of medical devices, cancer research, therapeutics and the prevention and treatment of infectious diseases.

The University of Washington Medical Center is the largest public university recipient of federal research dollars, receiving approximately $1.0 billion in external funds for research each year, and is second nationally in National Institutes of Health research funding.

Washington is also home to some of the leading global health research institutes and non-profit organizations, including the Gates Foundation, PATH, Seattle BioMed and the Fred Hutchinson Cancer Research Center.

**Services/Tourism**

Tourism is important to Washington's economy. Tourists are drawn to the state's mountains, water, proximity to Canada and Alaska, and metropolitan areas. As the business, legal and financial center of the state, Seattle has the largest selection of hospitality and entertainment venues in the state. The Washington State Convention Center has the capacity for events involving as many as 11,000 people. There are more than 10,000 hotel rooms in downtown Seattle and nearby venues, and entertainment options include professional football and baseball stadiums, theatres and music halls, the historic Pike Place Market, the Space Needle and the Seattle Center landmark from the 1962 World's Fair, and the architecturally unique Seattle Public Library, among others. Seattle is an embarkation port for several cruiseship lines, primarily cruising to Canada and Alaska.

## Military

Washington has a number of major military bases and installations, including the Fort Lewis Army Base, Madigan Army Medical Center and McChord Air Force Base in Pierce County (known as Joint Base Lewis-McChord); Puget Sound Naval Shipyard, Naval Station Bremerton and Bangor Naval Submarine Base in Kitsap County; Fairchild Air Force Base in Spokane County; Everett Naval Station in Snohomish County; and Whidbey Island Naval Air Station in Island County. There are approximately 65,500 military personnel in Washington. Washington's military installations spent nearly $8 billion in 2009.

## Construction

Table 28 provides information on housing permits for the state and the United States. The number of housing units authorized by building permits started to increase in the second half of 2009 after falling to record lows earlier in that year. The collapse in housing resulted in permits falling over 60 percent from the peak in 2005.

**Table 28**
**Housing Units Authorized by Building Permits**
**in Washington and United States**

| | Washington | | | |
|---|---|---|---|---|
| **Year** | **Single Family** | **Multi-Family** | **Total** | **United States** |
| 2002 | 30,239 | 9,961 | 40,200 | 1,747,678 |
| 2003 | 33,091 | 9,734 | 42,825 | 1,889,214 |
| 2004 | 36,489 | 13,600 | 50,089 | 2,070,077 |
| 2005 | 41,407 | 11,581 | 52,988 | 2,155,316 |
| 2006 | 35,611 | 14,422 | 50,033 | 1,838,903 |
| 2007 | 30,390 | 17,007 | 47,397 | 1,398,415 |
| 2008 | 17,440 | 11,479 | 28,919 | 905,359 |
| 2009 | 12,991 | 4,020 | 17,011 | 582,963 |
| 2010 | 14,702 | 5,989 | 20,691 | 604,610 |

*Source: U.S. Bureau of the Census.*

## Federal Spending

Federal spending in Washington totaled approximately $66.5 billion in federal fiscal year ("FFY") ended September 30, 2009 (the last year for which such information is available). In addition to making grants to the state (approximately $15.3 billion in FFY 2009), the federal government paid salaries to military and other federal employees in Washington ($9.2 billion), retirement and disability payments ($19.7 billion), payments for equipment and other procurement ($9.2 billion) and other direct payments ($13.1 billion) in FFY 2009.

## Other Employment Information

**Table 29**
**Resident Civilian Labor Force and Employment in Washington State**
(Employment Numbers in Thousands)[1]

| | 2007 | 2008 | 2009 | 2010 |
|---|---|---|---|---|
| **Resident Civilian Labor Force** | 3,390.4 | 3,476.4 | 3,528.7 | 3,536.2 |
| **Unemployment** | 154.5 | 186.3 | 314.2 | 325.8 |
| **WA Unemployment Rate (Percent)[2]** | 4.6 | 5.4 | 8.9 | 9.2 |
| **U.S. Unemployment Rate (Percent)** | 4.6 | 5.8 | 9.3 | 9.6 |
| **Nonagricultural Wage and Salary Workers Employed in Washington** | | | | |
| Nonfarm Employment | 2,933.6 | 2,958.9 | 2,821.4 | 2,777.4 |
| Durable Manufacturing | 211.9 | 211.3 | 190.5 | 184.2 |
| Aerospace | 80.1 | 83.0 | 82.9 | 80.8 |
| Computer and Electronic Products | 22.7 | 22.5 | 20.1 | 19.0 |
| Nondurable Manufacturing | 81.4 | 79.9 | 74.9 | 73.6 |
| Natural Resources and Mining | 8.2 | 7.5 | 6.0 | 5.9 |
| Construction | 208.2 | 200.5 | 159.4 | 141.1 |
| Trade, Transportation, Communication, Utilities | 553.4 | 553.4 | 522.5 | 516.5 |
| Information | 102.5 | 105.6 | 103.9 | 102.9 |
| Software | 47.6 | 50.9 | 51.5 | 51.0 |
| Financial | 155.5 | 152.4 | 141.7 | 135.1 |
| Professional and Business Services | 344.6 | 348.6 | 324.4 | 326.0 |
| Education and Health Services | 348.3 | 362.1 | 372.4 | 375.2 |
| Leisure and Hospitality | 280.6 | 283.7 | 269.6 | 265.8 |
| Other Services | 105.3 | 107.7 | 106.3 | 104.5 |
| Government | 533.8 | 546.3 | 549.8 | 546.7 |

(1) Averages of monthly data.
(2) Not seasonally adjusted. As reported by Washington Department of Employment Security in August 2011, the July 2011 unemployment rate (seasonally adjusted) in Washington was 9.3 percent as compared with 9.1 percent in the U.S. as a whole.

*Source: Department of Employment Security and U.S. Bureau of Labor Statistics.*

**Table 30**
**Composition of Employment by Industry Sector[1]**
*(percents)*

| | State of Washington | | United States | |
|---|---|---|---|---|
| | **2000** | **2010** | **2000** | **2010** |
| **Manufacturing** | | | | |
| Nondurable Manufacturing | | | | |
| Food Manufacturing | 1.4 | 1.2 | 1.2 | 1.1 |
| Pulp and Paper | 0.5 | 0.3 | 0.5 | 0.3 |
| Other | 1.6 | 1.1 | 3.2 | 2.0 |
| **Subtotal** | 3.5 | 2.7 | 4.8 | 3.4 |
| Durable Manufacturing | | | | |
| Lumber and Wood | 0.8 | 0.5 | 0.5 | 0.3 |
| Primary and Fabricated Metals | 1.1 | 0.8 | 1.8 | 1.3 |
| Machinery | 0.7 | 0.6 | 1.6 | 1.0 |
| Computers | 1.3 | 0.7 | 1.4 | 0.8 |
| Transportation Equipment | 3.7 | 3.2 | 1.6 | 1.0 |
| Other | 1.1 | 0.9 | 1.5 | 1.0 |
| **Subtotal** | 8.7 | 6.6 | 5.3 | 5.4 |
| **Total Manufacturing** | 12.2 | 9.3 | 13.1 | 8.9 |
| **Nonmanufacturing** | | | | |
| Natural Resources and Mining | 0.4 | 0.2 | 0.5 | 0.5 |
| Construction | 5.9 | 5.1 | 5.2 | 4.3 |
| Trade, Transportation and Utilities | 19.6 | 18.6 | 19.9 | 19.0 |
| Information | 3.6 | 3.7 | 2.8 | 2.1 |
| Financial | 5.2 | 4.9 | 5.8 | 5.9 |
| Professional and Business Services | 11.2 | 11.7 | 12.6 | 12.8 |
| Education and Health Services | 10.8 | 13.5 | 11.5 | 15.1 |
| Leisure and Hospitality | 9.3 | 9.6 | 9.0 | 10.0 |
| Other Services | 3.9 | 3.8 | 3.9 | 4.1 |
| Government | 17.8 | 19.7 | 15.8 | 17.3 |
| **Total Nonmanufacturing** | 87.8 | 90.7 | 86.9 | 91.1 |
| **Total[2]** | 100.0 | 100.0 | 100.0 | 100.0 |

(1) Figures are calculated as a percentage of total wage-and-salary employment.
(2) Numbers may not add due to rounding.

*Source: Washington State Office of the Economic and Revenue Forecast Council.*

The state's population has increased approximately 14.1 percent since 2000. Based upon the 2010 Census, the state is the thirteenth most populous in the nation. The following table summarizes the state's population for 2000-2010.

**Table 31**
**State of Washington Population**

| April 1 | Population |
|---|---|
| 2000 | 5,894,143 |
| 2001 | 5,974,910 |
| 2002 | 6,041,710 |
| 2003 | 6,098,300 |
| 2004 | 6,167,800 |
| 2005 | 6,256,400 |
| 2006 | 6,375,600 |
| 2007 | 6,488,000 |
| 2008 | 6,587,600 |
| 2009 | 6,668,200 |
| 2010 | 6,724,540 |

*Source: Office of Financial Management; 2000 and 2010 from U.S. Census.*

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## Income Characteristics

The state's per capita income consistently has exceeded the national level and has increased approximately 24 percent since 2001. Table 32, derived from U.S. Bureau of Economic Analysis ("BEA") statistics, provides a comparison of personal income and per capita income for the state and the nation. BEA also calculates that per capita disposable personal income (personal income less personal taxes) in Washington ($40,312 in 2010) has consistently been higher than the average per capita disposable personal income in the United States as a whole ($36,808 in 2010).

**Table 32**
**Personal Income Comparisons**
**Washington and United States**

| | Total Income ($ in billions) | | | | Per Capita Income (in dollars) | |
|---|---|---|---|---|---|---|
| | Washington | | United States | | | |
| Year | Amount | Percent Change | Amount | Percent Change | Washington | United States |
| 2001 | 197.3 | -- | 8,878.8 | -- | 32,954 | 31,145 |
| 2002 | 200.5 | 1.6 | 9,054.8 | 1.9 | 33,105 | 31,461 |
| 2003 | 206.9 | 3.1 | 9,369.1 | 3.4 | 33,858 | 32,271 |
| 2004 | 222.4 | 7.0 | 9,928.8 | 5.6 | 35,966 | 33,881 |
| 2005 | 230.1 | 3.3 | 10,476.7 | 5.2 | 36,743 | 35,424 |
| 2006 | 252.1 | 8.7 | 11,256.5 | 6.9 | 39,561 | 37,698 |
| 2007 | 272.6 | 7.5 | 11,900.6 | 5.4 | 42,169 | 39,461 |
| 2008 | 287.0 | 5.0 | 12,380.2 | 3.9 | 43,711 | 40,674 |
| 2009 | 285.7 | (0.5) | 12,168.2 | (1.7) | 42,870 | 39,635 |
| 2010 | 293.1 | 2.5 | 12,527.2 | 2.9 | 43,564 | 40,584 |
| 2011[1] | 304.1 | 3.7 | 12,915.0 | 3.0 | N/A | N/A |

(1) Through 1st quarter only.

*Source: U.S. Department of Commerce, Bureau of Economic Analysis, 2001-2009 as of April 21, 2011; 2010 and 2011 statistics as of June 22, 2011.*

# APPENDIX B

## DEFINITIONS AND SUMMARY OF CERTAIN LEGAL DOCUMENTS

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## DEFINITIONS AND SUMMARY OF CERTAIN LEGAL DOCUMENTS

The following is a summary of certain provisions of the Master Financing Agreements, Trust Agreement, Site Leases, Master Assignments, and Financing Agreements, including certain defined terms used within this Official Statement. Reference is directed to each of such documents for the complete text thereof. Copies of such documents are available from the Office of the Treasurer.

## CERTAIN DEFINITIONS

The following are definitions of certain terms used in this Appendix B and elsewhere in the Official Statement.

***Acquisition Costs*** means all costs incurred by or on behalf of the Corporation, or by the State or any Agency, as agent of the Corporation, on, prior to or after the effective date of the Master Financing Contract in connection with the acquisition of the Property thereunder, and shall include, but not be limited to, (1) the cost of such Property (including, but not limited to, charges for installation, delivery, preparation, testing and similar charges); (2) the expenses of the Corporation, the Treasurer and any Agency in connection with the acquisition of the Property, including but not limited to the Costs of Issuance; (3) any taxes, assessments and other charges, if any, payable in connection with the acquisition of the Property; and (4) any amounts required to reimburse the Corporation, the Treasurer or any Agency for advances or payments made prior to the effective date of the Master Financing Contract for any of the above costs.

***Acquisition Fund*** means the "State of Washington Certificates of Participation, Series 2011D Acquisition Fund" established by the Treasurer pursuant to the Trust Agreement and the Master Financing Contract.

***Act*** means Chapter 365 of the Laws of Washington, 1989, codified as Chapter 39.94 RCW, as supplemented and amended.

***Additional Costs*** means all costs, expenses, insurance premiums, Impositions and other payments, including Administrative Fees and Expenses, that are the obligations of the Treasurer or the Agency pursuant to the terms of the Master Financing Contract or the Agency Financing Contract, as the case may be.

***Additional Financing Lease Agreements*** means, collectively, any Additional Local Agency Financing Lease, Additional State Agency Financing Lease Addendum, Additional Site Lease, Additional Master Financing Lease and Additional Master Assignment.

***Additional Local Agency Financing Lease*** means any future Local Agency Financing Lease entered into by a Local Agency for the purpose of financing additions, betterments and improvements to the Property pursuant to Section 2.2(c) of the Local Agency Financing Lease.

***Additional Master Assignment*** means any future Master Assignment relating to an Additional Master Financing Lease.

***Additional Master Financing Lease*** means any future Master Financing Lease entered into for the purpose of financing additions, betterments and improvements to the Property.

***Additional Rent*** means all costs, expenses, insurance premiums, Impositions and other payments, including Administrative Fees and Expenses, that are the obligations of the Treasurer or the Agency pursuant to the terms of the Master Financing Lease or each Financing Lease, as the case may be.

***Additional Site Lease*** means any future lease of a Site by an Agency in connection with an Additional Local Agency Financing Lease or an Additional State Agency Financing Lease Addendum.

***Additional State Agency Financing Lease Addendum*** means any future State Agency Financing Lease Addendum entered into by a State Agency for the purpose of financing additions, betterments and improvements to the Property pursuant to Section 2.2(c) of the State Agency Financing Lease Addendum.

***Administrative Fees and Expenses*** means all application, commitment, financing or similar fees charged, or administrative or other expenses incurred, with respect to the administration and maintenance of the Certificates and the Series 2011D Agreements.

***Agency*** means a State Agency or Local Agency.

***Agency Event of Default*** has the meaning given such term in the related Agency Financing Agreement.

***Agency Financing Agreement*** means each Financing Lease and Agency Financing Contract.

***Agency Financing Contract*** means the Local Agency Financing Contract or the State Agency Financing Addendum.

***Agency Installment Payment Dates*** means each December 1 and June 1, as specified in the Agency Financing Contracts, on which an Agency Installment Payment is due.

***Agency Installment Payment Fund*** means the fund of that name maintained by the Treasurer pursuant to the Master Financing Contract.

***Agency Installment Payments*** means the installment payments to be made by each Agency as set forth in the related Agency Financing Contract.

***Agency Interest Component*** means that portion of each Agency Payment denominated as and comprising interest as set forth in each Agency Financing Agreement.

***Agency Payment*** means each Agency Rent Payment and Agency Installment Payment.

***Agency Principal Component*** means that portion of each Agency Payment denominated as and comprising principal as set forth in each Agency Financing Agreement.

***Agency Rent Payment Dates*** means each December 1 and June 1, as specified in each Financing Lease, on which an Agency Rent Payment is due.

***Agency Rent Payment Fund*** means the fund of that name maintained by the Treasurer pursuant to the Master Financing Lease.

***Agency Rent Payments*** means the rent payments to be made by each Agency as set forth in the related Financing Lease.

***Authorized Agency Representative*** means the natural person (a) designated on the certificate of the Agency in the form set forth in the related Agency Financing Agreement and shall include any other officer appointed by the chief elected official or administrative official of the Agency and (b) whose signature is on file with the Fiscal Agent and the Treasurer Representative.

***Authorized Corporation Representative*** means the President from time to time of the Corporation, unless such President shall have designated another officer of the Corporation, in which case "Authorized Corporation Representative" shall mean such other officer.

***Authorized Denomination*** means $5,000 and any integral multiple thereof.

***Base Rent Payment*** means a rent payment to be made by the Treasurer as set forth in the Master Financing Lease.

***Base Rent Payment Date*** means each January 1 and July 1, as specified in the Master Financing Lease, on which a Base Rent Payment evidenced and represented by the Certificates is due.

***Beneficial Owner*** means any Person that has or shares the power, directly or indirectly, to make investment decisions concerning ownership of any Certificates (including Persons holding Certificates through nominees, depositories or other intermediaries).

***Biennium*** means the fiscal period of the State.

***Business Day*** means any day other than (1) a Saturday, (2) a Sunday, (3) a day on which banking institutions located in the state of Washington are authorized or required by law to remain closed, or (4) a day on which the Principal Office of the Fiscal Agent or the New York Stock Exchange is closed.

***Certificate Counsel*** means a firm of attorneys appointed by the Treasurer of recognized national standing in the field of law relating to the issuance of certificates of participation, bonds and other obligations by states and their political subdivisions, and the exclusion of interest thereon from gross income for federal income tax purposes.

***Certificate Fund*** means the "State of Washington Certificates of Participation, Series 2011D Certificate Fund" established pursuant to the Trust Agreement.

***Certificate of the State Treasurer***, ***Written Request of the State Treasurer*** and ***Written Order of the State Treasurer*** each mean an instrument in writing signed by a Treasurer Representative.

***Certificate Payment Date*** means each Principal Payment Date and each corresponding Interest Payment Date on which a Principal Component and the corresponding Interest Component are due as set forth in the Master Financing Agreements.

***Certificate Register*** means the records for the registration of the Certificates maintained by the Fiscal Agent.

***Certificates*** means the certificates of participation in the State Payments executed and delivered by the Fiscal Agent pursuant to the Trust Agreement in the Initial Principal Amount and designated as the "State of Washington Certificates of Participation, Series 2011D (State and Local Agency Real and Personal Property)."

***Closing Date*** means the date on which the Certificates are delivered to the Underwriter in exchange for payment therefor.

***Code*** means the Internal Revenue Code of 1986, as amended, together with all regulations promulgated by the United States Department of the Treasury thereunder.

***Corporation*** means the Washington Finance Officers Association or any other Washington nonprofit corporation selected by the Treasurer's Office from time to time, and any successors and permitted assigns thereof, including without limitation the Fiscal Agent as assignee pursuant to the Master Assignment.

***Costs of Issuance*** means administrative expenses, legal, accounting, financial and printing expenses, and all other expenses incurred in connection with the preparation, execution and delivery of the Series 2011D Agreements and the Certificates.

***Dated Date*** means November 16, 2011, the date of initial delivery of the Certificates.

***Disclosure Agreement*** means an agreement for ongoing disclosure in compliance with the Rule, dated as of the Dated Date, executed and delivered by the Treasurer Representative and/or by the Authorized Agency Representative with respect to the Certificates.

***DTC*** means The Depository Company, New York, New York, a limited purpose trust company organized under the laws of the State of New York, as depository for the Certificates, or any successor or substitute depository for the Certificates.

***Event of Default*** means an Event of Default as set forth in Section 7.1 of the Master Financing Agreements.

***Executive Order***, for purposes of the Master Financing Agreements, means an order issued by the Governor of the State pursuant to sections 43.88.050 and 43.88.110 RCW, as amended or re-enacted.

***Financing Lease*** means each Local Agency Financing Lease or State Agency Financing Lease Addendum.

***Fiscal Agent*** means The Bank of New York Mellon, a banking corporation duly organized and existing under and by virtue of the laws of the State of New York, and its successors and assigns, or any other bank or trust company which may at any time be substituted in its place pursuant to the Trust Agreement.

***Fitch*** means Fitch IBCA, Inc., and its successors and assigns, and, if such organization shall be dissolved or liquidated or shall no longer perform the functions of a securities rating agency, "Fitch" shall be deemed to refer to any other nationally recognized securities rating agency (other than Moody's and S&P) designated by the Treasurer Representative.

***Government Obligations*** means obligations described in paragraph (1) of the definition of Qualified Investments below.

***Impositions*** means all federal, state and local real and personal property taxes and assessments (including assessments for public improvements), license and permit fees, charges for public utilities, leasehold excise taxes, other excise taxes, levies, use and occupancy taxes, privilege taxes, business and occupation taxes and all other governmental impositions and charges of every kind and nature, general and special, ordinary and extraordinary, foreseen and unforeseen, which are imposed, levied upon or assessed against or which arise with respect to the applicable Property (or any portion thereof), any State Payments, Agency Payments, Prepaid Site Lease Rent, Additional Rent, Additional Costs or other sums payable under the Master Financing Agreements, the Agency Financing Agreements or the Site Leases, the leasehold estates created by the Site Leases, the Master Financing Lease or the applicable Financing Leases, or the operation, use or possession of the applicable Property, and all income, gross receipts or similar taxes imposed, levied upon, assessed against or measured by any Agency Payments, State

Payments, Prepaid Site Lease Rent, Additional Rent, Additional Costs or other sums payable under the applicable Site Leases, the Master Financing Agreements or the applicable Agency Financing Agreements, and all sales, value added, *ad valorem*, use and similar taxes levied, assessed or payable on account of the leasing, use, possession, control or operation of the Property, and all charges, fees and assessments for utilities, communications and similar services provided to the Property.

***Initial Principal Amount*** means the aggregate initial Principal Components evidenced and represented by the Certificates as set forth in the Trust Agreement.

***Installment Payment Date*** means each January 1 and July 1, as specified in the Trust Agreement, on which an Installment Payment evidenced and represented by the Certificates is due.

***Installment Payments*** means the installment payments to be made by the State as set forth in Exhibit A to the Master Financing Contract.

***Interest Account*** means the account by that name established pursuant to the Trust Agreement.

***Interest Component*** means that portion of each State Payment denominated as and comprising interest as set forth in the Master Financing Agreements.

***Interest Payment Date*** means each January 1 and July 1 on which an Interest Component is due as set forth in the Master Financing Agreements.

***Land Lease*** means that certain lease between the State Department of Natural Resources as lessor, and the State Department of Social and Health Services, a State Agency, as lessor, granting that State Agency a leasehold interest in one of the Sites through the term of its Financing Lease.

***Letter of Representation*** means the blanket issuer letter of representations from the Treasurer to DTC.

***LGIP*** means the Local Government Investment Pool administered by the Office of the Treasurer.

***Local Agency*** means any "other agency" as that term is now or hereafter defined in the Act.

***Local Agency Financing Contract*** means each Local Agency Financing Contract, dated as of the Dated Date, by and between the State, acting by and through the Treasurer, and the Local Agency which is a Party thereto.

***Local Agency Financing Lease*** means each Local Agency Financing Lease, dated as of the Dated Date, by and between the State, acting by and through the Treasurer, and the Local Agency which is a Party thereto.

***Master Assignment*** means each Master Assignment dated as of the Dated Date, executed and delivered in connection with the Certificates.

***Master Financing Agreements*** means the Master Financing Contract and the Master Financing Lease.

***Master Financing Contract*** means the Master Financing Contract, dated as of the Dated Date, by and between the Corporation and the State, acting by and through the Treasurer, as supplemented and amended.

***Master Financing Lease*** means the Master Financing Lease, dated as of the Dated Date, by and between the Corporation and the State, acting by and through the Treasurer, as supplemented and amended.

***Moody's*** means Moody's Investors Service, and its successors and assigns, and, if such organization shall be dissolved or liquidated or shall no longer perform the functions of a securities rating agency, "Moody's" shall be deemed to refer to any other nationally recognized securities rating agency (other than Fitch and S&P) designated by the Treasurer Representative.

***MSRB*** means the Municipal Securities Rulemaking Board or any successor to its functions.

***Notice of Intent*** means the Notice of Intent in the form attached to each Agency Financing Agreement.

***OFM*** means the State Office of Financial Management established in the Office of the Governor of the State pursuant to Chapter 43.41 RCW, or any successor to the functions of the OFM, charged with responsibility of submitting budgets to the State Legislature.

***Opinion of Counsel*** means a written opinion of Certificate Counsel satisfactory to the Treasurer and the Fiscal Agent.

***Outstanding*** means all Certificates executed and delivered pursuant to the Trust Agreement, except:

(1) Certificates theretofore canceled by the Fiscal Agent, or delivered to the Fiscal Agent for cancellation;

(2) Certificates for which the payment or prepayment of the State Payments evidenced and represented thereby has been made or duly provided for pursuant to Section 4.1(b) of the Master Financing Agreements and Article X of the Trust Agreement; and

(3) Certificates in lieu of or in substitution for which other Certificates have been executed and delivered pursuant to Article II of the Trust Agreement.

***Owner*** means the registered owner of a Certificate as set forth on the Certificate Register.

***Parties*** means, as the context requires, the State, the Corporation, each Agency, and/or the Fiscal Agent.

***Paying Agent*** means any paying agent for the Certificates appointed pursuant to the Trust Agreement.

***Permitted Encumbrances*** means, as of any particular time:

(1) Liens for general *ad valorem* taxes and assessments, if any, that are not then delinquent;

(2) The Land Lease;

(3) The Property Lease;

(4) The Site Leases;

(5) The Master Financing Lease;

(6) The Master Assignment (Real Property);

(7) The Financing Leases;

(8) Any Additional Financing Lease Agreements;

(7) Any right or claim of any mechanic, laborer, materialmen, supplier or vendor filed or perfected in the manner provided by law;

(8) Easements, rights of way, mineral rights, drilling rights, and other rights, reservations, covenants, conditions or restrictions which (a) exist of record as of the Dated Date and which the respective Agency certifies in writing will not materially impair the use of the Property by such Agency, and (b) arise thereafter and to which the Treasurer and the Corporation consent in writing; and

(9) Exceptions shown on the respective title insurance policies issued with respect to the Property as of the date of execution and delivery of the Certificates.

***Permitted Termination Date*** means with respect to a Permitted Termination Event occurring as a result of an election by the State Legislature not to appropriate, the end of the last Biennium for which funding has been provided; or, with respect to a Permitted Termination Event occurring as a result of an Executive Order reduction in funding, the end of the last month for which funding is available to pay Agency Payments due from State Agencies.

***Permitted Termination Event*** means, with respect to a State Agency: (1)(a) sufficient funds have not been appropriated within any biennial budget for the purpose of paying Agency Payments in the next occurring Biennium or (b) the Governor of the State has issued an Executive Order mandating an emergency reduction in State funding; and (2) the Treasurer Representative has delivered written notice to the Fiscal Agent, within five Business Days following the enactment of such budget or within 30 days following such an emergency reduction in State funding, as the case may be, describing the election not to appropriate the necessary funds or the insufficiency of funds as a result of an emergency reduction in funding and stating the Permitted Termination Date.

***Person*** or ***persons*** means an individual, corporation, firm, association, partnership, trust, or other legal entity or group of entities, including a governmental entity or any agency or political subdivision thereof.

***Personal Property Certificate*** means the Personal Property Certificate (in the form attached to the Local Agency Financing Contract and State Agency Financing Addendum) delivered by the Agency to the Treasurer with respect to items of Property.

***Prepaid Site Lease Rent*** has the meaning given such term in Section 4 of each Site Lease.

***Prepayment Account*** means the account by that name established pursuant to the Trust Agreement.

***Prepayment Date*** means each date, other than a Principal Payment Date, on which a Principal Component evidenced and represented by the Certificates is to be prepaid.

***Prepayment Price*** means the price payable pursuant to each Master Financing Agreement upon any optional or mandatory prepayment of Principal Components evidenced and represented by the Certificates.

***Principal Account*** means the account by that name established pursuant to the Trust Agreement.

***Principal Component*** means that portion of each Base Rent Payment or Installment Payment denominated as and comprising principal as set forth in the Master Financing Agreements.

***Principal Office*** means, with respect to the Treasurer, the office in Olympia, Washington, designated in writing by the Treasurer to the Fiscal Agent, and, with respect to the Fiscal Agent, the corporate trust

office of the Fiscal Agent located in New York, New York, designated in writing by the Fiscal Agent to the Treasurer, or solely for purposes of the presentation of Certificates for payment, transfer or exchange, the designated corporate trust agency office of the Fiscal Agent.

***Principal Payment Date*** means each January 1 on which a Principal Component is due as set forth in the Master Financing Agreements.

***Project*** means the improvements acquired or constructed on each Site, if any, pursuant to each respective Financing Lease.

***Project Costs*** means all costs incurred by or on behalf of the Corporation, or the State or the Agency, as agent of the Corporation, on, prior to or after the effective date of the Master Financing Lease in connection with the acquisition or construction of the Property or the Project thereunder, as applicable, and shall include, but not be limited to, (1) the cost of such Property or the Project (including, but not limited to, charges for design, testing and similar charges); (2) the expenses of the Treasurer and the Agency in connection with the acquisition or construction of the Property or the Project, including but not limited to the Costs of Issuance; (3) any taxes, assessments and other charges, if any, payable in connection with the acquisition or construction of the Property or the Project; and (4) any amounts required to reimburse the Treasurer or the Agency for advances or payments made prior to the effective date of the Master Financing Lease for any of the above costs.

***Project Fund*** means the "State of Washington Certificates of Participation, Series 2011D Project Fund" established by the Treasurer pursuant to the Trust Agreement and the Master Financing Lease.

***Property*** means, (1) with respect to each Financing Lease, the Site and the Project leased by the Treasurer to the Agency, and, with respect to the Master Financing Lease, means collectively all of such Property, and (2) collectively, all personal property the Acquisition Costs of which are being financed or refinanced pursuant to the Master Financing Contract, as set forth in Exhibit B to the Master Financing Contract, together with all replacements parts, repairs, additions, attachments and accessories thereof, therefor and thereto, licenses, permits and capitalized maintenance agreements with respect thereto, and any replacements of or substitutes therefor as permitted by the Agency Financing Contracts.

***Property Lease*** means that certain College/City Library Lease between the State Board for Community and Technical Colleges, Yakima Valley Community College, as lessor, and the City of Grandview, Washington, a Local Agency, as lessee, granting to that Local Agency a leasehold interest in one of the Sites through the term of its Financing Lease.

***Purchase Price*** means the aggregate amount of the Principal Components of the Installment Payments with respect to the Property, as set forth in the Master Financing Contract.

***Qualified Investments*** shall include the following:

(1) Any securities (including obligations held or issued in book-entry form on the books of the Department of the Treasury of the United States of America) which constitute direct obligations of, or the timely payment of the principal of and interest on which is unconditionally guaranteed by, the United States of America;

(2) Federal Home Loan Bank Bonds and Discount Notes; Federal National Mortgage Association Bonds and Discount Notes; Federal Farm Credit Banks Consolidated System-Wide Bonds and Discount Notes; Federal Home Loan Mortgage Corporation Bonds and Discount Notes; Government National Mortgage Association Bonds; Student Loan Marketing Association Bonds

and Discount Notes; Small Business Administration Bonds; Export-Import Bank Bonds; Maritime Administration Bonds; and Obligations of any other Government Sponsored Corporation whose obligations are or may become eligible as collateral for advances to member banks as determined by the Board of Governors of the Federal Reserve System;

(3) Bankers acceptances, which are eligible for purchase by the Federal Reserve System, drawn on and accepted by a commercial bank (which may include the Fiscal Agent) having a combined capital and surplus of not less than $100,000,000, which bank has at the time of investment one of the two highest ratings of a Rating Agency;

(4) Commercial paper having original maturities of not more than 365 days which has at the time of investment one of the two highest ratings of a Rating Agency, which is issued by a corporation organized and operating in the United States with total assets in excess of $100,000,000;

(5) Bonds of the State and any local government in the State, which bonds have at the time of investment one of the three highest credit ratings of a Rating Agency;

(6) General obligation bonds of a state other than the State and general obligation bonds of a local government of a state other than the State, which bonds have at the time of investment one of the three highest credit ratings of a Rating Agency;

(7) Any investments authorized by law for the Treasurer or any local government of the State;

(8) Shares of money market funds with portfolios consisting of only U.S. Treasury and agency securities or repurchase agreements, which have at the time of investment one of the three highest ratings of a Rating Agency;

(9) Any repurchase agreement with any bank or trust company organized under the laws of any state of the United States or any national banking association (including the Fiscal Agent) or government bond dealer reporting to, trading with, and recognized as a primary dealer by the Federal Reserve Bank of New York, which agreement is secured by any one or more of the securities described in clauses (1) or (2) above;

(10) The LGIP; and

(11) Any other legal investment for funds held by the Treasurer.

***RCW*** means the Revised Code of Washington, as supplemented and amended.

***Rating Agency*** means Fitch, Moody's or S&P.

***Rating Category*** means the generic rating categories of the Rating Agency, without regard to any refinement or gradation of such rating category by a numerical modifier or otherwise.

***Rebate Fund*** means the "State of Washington Certificates of Participation, Series 2011D Rebate Fund" which may be established pursuant to the Master Financing Agreements.

***Rebate Requirement*** has the meaning given to such term in the Tax Certificate.

***Record Date*** means the 15th day of the month immediately preceding each Interest Payment Date and Principal Payment Date.

***Resolution*** means Resolution No. 987 adopted by the State Finance Committee on October 7, 2003.

***Rule*** means Rule 15c2-12 promulgated by the SEC under the Securities Exchange Act of 1934, as the same may be amended from time to time.

***S&P*** means Standard & Poor's Ratings Group, and its successors and assigns, and, if such organization shall be dissolved or liquidated or shall no longer perform the functions of a securities rating agency, "S&P" shall be deemed to refer to any other nationally recognized securities rating agency (other than Fitch and Moody's) designated by the Treasurer Representative.

***SEC*** means the Securities and Exchange Commission.

***Securities Depositories*** means: The Depository Trust Company, 711 Stewart Avenue, Garden City, New York 11530, Fax-(516) 227-4039 or 4190, or, in accordance with then-current guidelines of the SEC, such other addresses and/or such other securities depositories as the Treasurer may designate in a Certificate of the Treasurer delivered to the Fiscal Agent.

***Series 2011D Agreement*** means, as the context requires, the Trust Agreement, the Site Leases, the Master Financing Agreements, the Agency Financing Agreements, the Master Assignments or the Disclosure Agreement, and collectively means all such agreements in connection with the Certificates.

***Site*** means the real property legally described in Exhibit A to the Site Lease, including the improvements thereon as of the Dated Date.

***Site Lease*** means each Site Lease, dated as of the Dated Date, by and between the Agency and the Corporation for the lease of a parcel or parcels of the Property by the Agency to the Corporation.

***State*** means the state of Washington.

***State Agency*** means any state agency permitted to enter into financing contracts under the Act.

***State Agency Financing Addendum*** means each State Agency Financing Addendum to the Master Financing Contract, dated as of the Dated Date, executed by the Treasurer Representative and the State Agency.

***State Agency Financing Lease Addendum*** means each State Agency Financing Lease Addendum to the Master Financing Lease, dated as of the Dated Date, executed by the Treasurer Representative and the State Agency.

***State Finance Committee*** means the state finance committee as constituted from time to time pursuant to Chapter 43.33 RCW.

***State Legislature*** means the Legislature of the state of Washington.

***State Payment*** means each Installment Payment and each Base Rent Payment.

***State Reimbursement Rate*** means the average rate of return on the LGIP over the period the reimbursement payment by the Local Agency to the Treasurer is delinquent, as determined by the Treasurer, which determination shall be binding and conclusive against the Local Agency absent manifest error.

***State Sublease Termination Date*** has the meaning given such term in the Master Financing Lease.

***Supplemental Agreement*** means any agreement duly authorized and entered into following the Closing Date between or among the Treasurer, the Corporation, and the Fiscal Agent (in the case of the Trust Agreement, the Master Financing Agreements, or the Master Assignments), or the Agency (in the case of the Agency Financing Agreements or the Site Leases) supplementing, modifying or amending the Trust Agreement, a Site Lease, a Master Financing Agreement, a Master Assignment or an Agency Financing Agreement.

***Tax Certificate*** means the Tax Certificate executed and delivered by the Treasurer Representative and/or Authorized Agency Representatives regarding compliance with applicable provisions of the Code in connection with the Site Leases, the Master Financing Agreements, the Agency Financing Agreements and the Certificates.

***Term Certificates*** means the Certificates identified as such in the Trust Agreement.

***Toxic or Hazardous Substances*** shall be interpreted broadly to include, but not be limited to, any material or substance that is defined or classified under federal, State or local laws as: (1) a "hazardous substance" pursuant to Section 101 of the Comprehensive Environmental Response, Compensation and Liability Act, 42 U.S.C. § 9601(14) or Section 311 of the Federal Water Pollution Control Act, 33 U.S.C. § 1321, each as now or hereafter amended; (2) a "hazardous waste" pursuant to Section 1004 or Section 3001 of the Resource Conservation and Recovery Act, 42 U.S.C. § 6903, 42 U.S.C. § 6921, as now or hereafter amended; (3) a toxic pollutant under Section 307(1)(a) of the Federal Water Pollution Control Act, 33 U.S.C. § 1317(1)(a); (4) a "hazardous air pollutant" under Section 112 of the Clean Air Act, 42 U.S.C. § 7412, as now or hereafter amended; (5) a "hazardous material" under the Hazardous Material Transportation Act, 49 U.S.C. § 1802(2), as now or hereafter amended; (6) toxic or hazardous pursuant to regulations promulgated now or hereafter under the aforementioned laws; or (7) presenting a risk to human health or the environment under other applicable federal, State or local laws, ordinances, or regulations, as now or as may be posed or promulgated in the future. "Toxic or Hazardous Substances" shall also mean any substance that after release into the environment and upon exposure, ingestion, inhalation or assimilation, either directly from the environment or indirectly by ingestion through food chains, will or may reasonably be anticipated to cause death, disease, behavior abnormalities, cancer or genetic abnormalities. "Toxic or Hazardous Substances" specifically includes, but is not limited to, asbestos, polychlorinated biphenyls (PCBs), petroleum and petroleum-based derivatives, flammable explosives, radioactive materials and urea formaldehyde.

***Treasurer*** means the State Treasurer of the state of Washington.

***Treasurer Representative*** means the Treasurer, the Assistant Treasurer or the Deputy Treasurer of the State, and shall include any other natural person who at the time and from time to time may be designated by a Certificate of the Treasurer delivered to the Party relying thereon. Such Certificate shall contain the specimen signature of such person, and shall be signed on behalf of the State by the Treasurer, the Assistant Treasurer or the Deputy Treasurer.

***Trust Agreement*** means the Trust Agreement, dated as of the Dated Date, by and among the Treasurer, the Corporation and the Fiscal Agent, as supplemented and amended in accordance therewith.

***Underwriter*** means the original purchaser of the Certificates.

## MASTER FINANCING LEASE

### Sublease of Property

The Corporation subleases to the State, and the State hires from the Corporation, upon the terms and conditions set forth in the Master Financing Lease, the real property and all improvements thereon, including but not limited to the Projects, described in the Master Financing Lease, subject to all easements, covenants, conditions and restrictions existing as of the Dated Date. The State agrees to pay in consideration thereof the Base Rent Payments and Additional Rent therefor in accordance with the Master Financing Lease, and all other amounts required to be paid by the State thereunder. The Corporation reserves the right for any of its duly authorized representatives to enter upon the Property at any reasonable time (or in an emergency at any time) to inspect the same, or to make any repairs, improvements or changes necessary for the preservation thereof, or otherwise in connection with the Corporation's rights and obligations thereunder. The State and its authorized assignees and sublessees at all times during the term of the Master Financing Lease may peaceably and quietly have, hold and enjoy all of the Property without suit, trouble or hindrance from the Corporation.

### Appointment of Agents; Acquisition and Construction of Projects; Changes to Projects; Additions to Property; Substitution and Release of Property

***Appointment of Agents.*** The Corporation appoints, and ratifies, approves and confirms its appointment of, the Treasurer and the respective Agencies pursuant to the Notice of Intent as its agents in connection with the disbursement of the proceeds of the Certificates and the design, acquisition and/or construction and financing or refinancing of the Projects, respectively, and the Treasurer accepts and agrees to such designation and appointment.

***Acquisition and Construction of Projects.*** The Treasurer agrees that it has caused or will cause each Project to be designed, acquired and/or constructed and financed or refinanced with all reasonable dispatch by the respective Agency, as agent for the Corporation, in accordance with the plans, specifications, bidding documents, and construction and other contracts approved by such Agency, and in accordance with applicable laws and regulations. The State further agrees that it will pay or cause to be paid the Project Costs solely from funds available to it pursuant to the Master Financing Lease, the Trust Agreement and the Financing Leases. The appointment of the Treasurer and the respective Agencies to act as agents of the Corporation in connection with the disbursement of the proceeds of the Certificates and the design, acquisition and/or construction and financing or refinancing of the Projects, respectively, and all authority conferred is made and conferred irrevocably by the Corporation, and will not be terminated by any act of the State, any Agency, the Corporation or otherwise.

***Changes to Projects; Additions to Property.*** The Treasurer may revise or consent to the revision of any Project to be acquired, constructed, financed or refinanced with proceeds of the Certificates, or the description thereof; *provided*, that: (1) such Project as so revised must satisfy the requirements under the Master Financing Lease with respect to the substitution of Property previously acquired, constructed, financed or refinanced; (2) the Project Costs must not be materially reduced thereby; and (3) any such revision will not relieve the State or any Agency of its obligation to design, acquire, construct, finance or refinance the Project in accordance therewith and with the Financing Lease with respect thereto.

The Treasurer has the right during the term of the Master Financing Lease, at the cost and expense of the State or the Agency, to make or permit additions, betterments and improvements to the Property, and to attach fixtures, structures and signs thereto; *provided*, that such additions, betterments and improvements and fixtures, structures and signs (1) must be constructed and installed in accordance with applicable laws

and regulations, and not in violation of any easements, restrictions, conditions or covenants affecting title to the Property; and (2) must not diminish the value, capacity or usefulness of the Property.

The Treasurer also has the right during the term of the Master Financing Lease, without the consent of any Owners, to enter into Additional Master Financing Leases with the Corporation to finance all or any portion of the cost of such additions, betterments and improvements to the Property so long as such leases do not reduce the obligation of the State to perform its obligations under the Master Financing Lease, including without limitation its obligation to make Base Rent Payments, and will not, in an Opinion of Counsel, adversely affect the tax-exempt status of the Interest Component of Base Rent Payments evidenced and represented by the Certificates. If the Treasurer enters into any Additional Master Financing Lease for this purpose, the Corporation may be granted an interest in the Property under an Additional Site Lease of all or any portion of the Property, which leasehold interest may be assigned to the Fiscal Agent for the benefit of owners of certificates of participation in such Additional Master Financing Lease. The occurrence of an Event of Default or Permitted Termination Event with respect to the Master Financing Lease will constitute a like event under any Additional Master Financing Lease, and the occurrence of any such like event under any Additional Master Financing Lease will constitute an Event of Default or Permitted Termination Event, as the case may be, under the Master Financing Lease. The owners of certificates of participation in any additional Master Financing Lease will be secured *pari passu* with the Owners with respect to any amounts received by the Fiscal Agent with respect to the Property following the occurrence of an Event of Default or Permitted Termination Event.

***Substitution of Property.*** After the acquisition, construction, financing or refinancing of any Project, the Treasurer may substitute and consent to the substitution, for a Property, another parcel or parcels of real property by first filing with the Fiscal Agent, as assignee of the Corporation:

(1) an Opinion of Counsel to the effect that such substitution (a) is permitted under the Master Financing Lease, and (b) in and of itself, will not adversely effect the exclusion from gross income for federal income tax purposes of the Interest Component of the Certificates;

(2) an appraisal or other written evidence from an independent, disinterested real property appraiser acceptable to the Treasurer to the effect that such substitute Property has an estimated fair rental value for the remaining term of the respective Financing Lease equal to or greater than the Agency Rent Payments due thereunder from time to time;

(3) a certificate of the Agency to the effect that such substitute Property (a) is free and clear of any mortgages, deeds of trust, liens or other similar encumbrances, other than Permitted Encumbrances, and (b) is essential to the Agency's ability to carry out its governmental functions and responsibilities; and

(4) written evidence from each Rating Agency then rating the Certificates that such substitution, in and of itself, will not result in the suspension, reduction or withdrawal of any ratings on the Certificates by such Rating Agency.

The Treasurer, the Fiscal Agent, as assignee of the Corporation, and the Agency will execute, deliver and record such amendments and modifications to the Site Leases, the Master Financing Lease, the Master Assignment, the Financing Leases, and such other documents, agreements and instruments, as the Treasurer deems necessary or desirable in connection with such substitution.

***Release of Property.*** After the acquisition, construction, financing or refinancing of any Project, the Treasurer may release and consent to the release of a portion of the Property leased under the related Site

Lease, and subleased under and pursuant to the Master Financing Lease and the related Financing Leases, by first filing with the Fiscal Agent, as assignee of the Corporation:

(1) an Opinion of Counsel to the effect that such release (a) is permitted under the Master Financing Lease, and (b) in and of itself, will not adversely effect the exclusion from gross income for federal income tax purposes of the Interest Component of the Certificates;

(2) an appraisal or other written evidence from an independent, disinterested real property appraiser acceptable to the Treasurer to the effect that the remaining portion of the Property has an estimated fair rental value for the remaining term of the related Financing Lease equal to or greater than the Agency Rent Payments due from time to time thereunder;

(3) provision by such Agency of any necessary easements, reciprocal agreements or other rights as may be necessary to provide comparable pedestrian and vehicular access, and other uses and amenities (including but not limited to water, sewer, electrical, gas, telephone and other utilities) as existed prior to such release; and

(4) written evidence from each Rating Agency then rating the Certificates that such release, in and of itself, will not result in the suspension, reduction or withdrawal of any ratings on the Certificates by such Rating Agency.

The Treasurer, the Fiscal Agent, as assignee of the Corporation, and the Agency will execute, deliver and record such amendments and modifications to the Site Lease, the Master Financing Lease, the Master Assignment or the applicable Financing Lease, and such other documents, agreements and instruments, as the Treasurer deems necessary or desirable in connection with such release.

**Title to the Property**

Fee title to or ownership of a leasehold interest in the Property, as applicable, subject to Permitted Encumbrances, and all additions, modifications, repairs and improvements thereto, remains and vests in the respective Agencies, subject to the respective leasehold estates under the Site Leases, the Master Financing Lease and the Financing Leases, without any further action by the State, the respective Agencies or the Corporation.

**Assignment; Attornment**

The State assigns and transfers to the Corporation the State's interest in the Financing Leases and all rentals, income and profits therefrom, including without limitation the Agency Rent Payments; *provided*, that until an Event of Default occurs and is continuing thereunder, the State may receive, collect, enjoy and apply the rents accruing under the Financing Leases as otherwise provided therein and in the Master Financing Lease. Upon the occurrence and continuance of an Event of Default under the Master Financing Lease, the Corporation may, at its option, either (1) terminate the respective Financing Lease; (2) elect to receive and collect, directly from the Agencies, the Agency Rent Payments and other amounts due and to become due under the Financing Leases, or (3) elect to succeed to the State's interest in the Financing Leases and cause the Agencies to attorn to the Corporation, as sublessor. The Corporation covenants to credit the State with any Agency Rent Payments received as a result of such assignment; *provided*, that the acceptance by the Corporation of any such payment should not be deemed to be (a) an attornment by the Corporation to the Agency, or by the Agency to the Corporation, or (b) a waiver by the Corporation of any provision of the Master Financing Lease or (c) a release of the State from any obligation or liability thereunder.

**Disclaimer of Warranties**

The State acknowledges and agrees that it has had adequate opportunity to inspect the Property, and that such Property, including but not limited to the structures and improvements thereon, is acceptable to the State in its present condition. The State subleases the Property in its present condition, "as is." THE CORPORATION MAKES NO WARRANTY OR REPRESENTATION, EITHER EXPRESS OR IMPLIED, AND ASSUMES NO RESPONSIBILITY, LIABILITY OR OBLIGATION, AS TO THE VALUE, DESIGN, STRUCTURAL OR OTHER CONDITION, USE, USABILITY, SUITABILITY, OCCUPANCY OR MANAGEMENT OF THE PROPERTY, AS TO THE INCOME FROM OR EXPENSE OF THE USE OR OPERATION THEREOF, AS TO TITLE TO THE PROPERTY, AS TO COMPLIANCE WITH APPLICABLE ZONING, SUBDIVISION, PLANNING, SAFETY, FIRE, HEALTH OR ENVIRONMENTAL LAWS, REGULATIONS, ORDINANCES, CODES OR REQUIREMENTS, OR AS TO COMPLIANCE WITH APPLICABLE COVENANTS, CONDITIONS OR RESTRICTIONS, OR ANY OTHER REPRESENTATION OR WARRANTY WITH RESPECT TO THE PROPERTY. IN NO EVENT SHALL THE CORPORATION BE LIABLE OR RESPONSIBLE FOR ANY INCIDENTAL, INDIRECT, SPECIAL OR CONSEQUENTIAL DAMAGES IN CONNECTION WITH OR ARISING OUT OF THE MASTER FINANCING LEASE OR THE CONSTRUCTION OR USE BY ANY AGENCY OF ANY ITEM OF PROPERTY.

**Rent Payments**

The State promises to pay to the Corporation, as rental for the use and occupancy of the Property, the following amounts at the following times:

***Base Rent Payments.*** On each Base Rent Payment Date, the Base Rent Payment, consisting of a Principal Component and/or an Interest Component; and

***Additional Rent.*** All Additional Rent incurred by the Corporation in connection with the lease of the Sites from the Agencies, the sublease of the Property to the State, the execution and delivery of the Certificates, and the observance and performance of the Series 2011D Agreements, within 30 days following receipt of an invoice from the Corporation with respect thereto which includes (1) a brief description of each item of such Additional Rent, (2) the party to whom payment is due, (3) the amount thereof, and (4) such additional information as the Treasurer may reasonably request.

Such payments of Base Rent Payments and Additional Rent for each rental payment period during the term of the Master Financing Lease should constitute the total rental due for such period, and should be paid for and in consideration of the use and occupancy and continued quiet enjoyment of the Property for such period. The Parties to the Master Financing Lease have determined and agreed that such total rental does not exceed the fair rental value of the Property for each such rental period, given the purposes, terms and provisions of the Master Financing Lease. Anything in the Master Financing Lease to the contrary notwithstanding, the State waives any right that it may have under the laws of the State to a rebate or repayment of any portion of such rental in the event that there is substantial interference with the use or right to possession by the State of the Property or any portion thereof as a result of material damage, destruction or condemnation.

Each Base Rent Payment consists of a Principal Component and/or an Interest Component as set forth in the Master Financing Lease. Interest accrues and is calculated as provided in the Trust Agreement. Each Base Rent Payment consists of the aggregate of the Agency Rent Payments payable by each Agency pursuant to its Financing Lease. Each Base Rent Payment payable thereunder is required to be paid by electronic funds transfer in lawful money of the United States of America. Payments of Additional Rent

should be made to or upon the order of the Corporation. Each Base Rent Payment should be applied first to the Interest Component due thereunder, and then to the Principal Component due thereunder.

The Corporation directs the Treasurer, and the Treasurer agrees, to make all Base Rent Payments directly to the Fiscal Agent, as assignee of the Corporation.

**Sources of Payment of Base Rent Payments**

***State Agency Financing Lease Addenda.*** The State is subleasing certain Property for and on behalf of the State Agencies set forth in the Master Financing Lease. Concurrently with the execution of the Master Financing Lease, each State Agency shall execute and deliver a State Agency Financing Lease Addendum pursuant to which such Agency shall agree to sublease its Property and to make Agency Rent Payments therefor. Such Agency Rent Payments shall be sufficient in the aggregate to pay, on each Base Rent Payment Date, the Base Rent Payment for the Property subleased under the Master Financing Lease by the State from the Corporation for and on behalf of such State Agencies.

The Base Rent Payments shall be payable by the State solely from the Agency Rent Payments to be made by the State Agencies. The obligation of each State Agency to make its Agency Rent Payments shall be subject to appropriation by the State Legislature and Executive Order reduction by the Governor. The State shall not be obligated to pay the Base Rent Payments other than from appropriated funds of the State Agencies.

***Local Agency Financing Leases.*** The State is subleasing certain Property for and on behalf of the respective Local Agencies set forth in the Master Financing Lease. Concurrently with the execution of the Master Financing Lease, each such Local Agency covenants to execute and deliver a Local Agency Financing Lease pursuant to which such Local Agency agrees to sublease its respective Property and to make Agency Rent Payments therefor, at such times and in such amounts as provided therein. Such Agency Rent Payments must be sufficient to pay, on each Base Rent Payment Date, the Base Rent Payment for the Property subleased thereunder by the State from the Corporation for and on behalf of such Local Agencies.

The Base Rent Payments allocable to Agency Rent Payments of each Local Agency is payable by the State solely from the Agency Rent Payments to be made by such Local Agency, except as otherwise provided in the Master Financing Lease. The obligation of each Local Agency to make its Agency Rent Payments is a direct and general obligation of such Local Agency to which the full faith and credit of such Local Agency is pledged. The State is not obligated to pay the Base Rent Payments other than from Agency Rent Payments paid by the respective Local Agencies, except as otherwise provided in the Master Financing Lease.

***Intercept of Local Agency Share of State Revenues.*** In the event that any Local Agency fails to make any payment due under its Local Agency Financing Lease, the Treasurer is required to withhold an amount sufficient to make such payment from such Local Agency's share of State revenues or other amounts authorized or required by law to be distributed by the State to such Local Agency, including but not limited to leasehold excise taxes, sales and use taxes, excise taxes, property taxes and liquor control board receipts; provided, that the use of any such revenues or amounts to make such payments is otherwise authorized or permitted by State law. Such withholding should continue until all such payments due thereunder have been made. Amounts withheld by the Treasurer should be applied to make any such payment due under the Local Agency Financing Lease on behalf of such Local Agency, or to reimburse the Treasurer for any such payment made pursuant to the Master Financing Lease.

***Conditional Payment of Local Agency Rent Payments.*** Upon the failure of any Local Agency to make any Agency Rent Payment at such time and in such amount as required pursuant to its Local Agency Financing Lease, the Treasurer covenants, to the extent of legally available appropriated funds and subject to any Executive Order reduction, make such payment into the Agency Rent Payment Fund on behalf of such Local Agency within 10 Business Days after such Agency Rent Payment was due. The Treasurer is entitled to reimbursement for any such payments made on behalf of such Local Agency as provided in the Local Agency Financing Lease.

**Agency Rent Payments; Deposit and Investment**

Agency Rent Payments are payable on each Agency Rent Payment Date and are to be deposited in a special fund or funds maintained by the Treasurer (the "Agency Rent Payment Fund"). The Agency Rent Payments due on each Agency Rent Payment Date are at least sufficient, in the aggregate, to make the Base Rent Payment next coming due thereunder. Amounts in the Agency Rent Payment Fund, including investment earnings thereon, are to be used and applied, first, to make the Base Rent Payment next coming due, and thereafter, but prior to the next Agency Rent Payment Date, to the extent that amounts remain in such Fund after such Base Rent Payment is made, to pay Additional Rent or for any other lawful purpose of the Treasurer. Amounts in the Agency Rent Payment Fund must be invested in Qualified Investments, and must be separately accounted for, but may be commingled with other moneys on deposit with the Treasurer solely for investment purposes.

**Net Lease**

The Master Financing Lease should be deemed and construed to be a "triple net lease," and the State is required to pay absolutely net during the term of the Master Financing Lease the Base Rent Payments, Additional Rent and all other amounts due thereunder, without notice or demand, and free of any charges, assessments, impositions or deductions whatsoever, and without any diminution, reduction, postponement, abatement, counterclaim, defense or set-off as a result of any dispute, claim or right of action by, against among the State, the Corporation, the Fiscal Agent, any Agency, and/or any other Person, or for any other reason; *provided*, that nothing in this provision should be construed to release or excuse the Corporation from the observance or performance of its obligations thereunder. If the Corporation fails to observe or perform any such obligation, the State may institute such legal action and pursue such other remedies against the Corporation as the State deems necessary or desirable, including, but not limited to actions for specific performance, injunction and/or the recovery of damages.

**Limited Obligation**

THE MASTER FINANCING LEASE CONSTITUTES A SPECIAL, LIMITED OBLIGATION OF THE STATE PAYABLE SOLELY FROM THE SOURCES AND SUBJECT TO THE LIMITATIONS SET FORTH THEREIN. THE MASTER FINANCING LEASE DOES NOT CONSTITUTE A DEBT OR A GENERAL OBLIGATION OF THE STATE, THE CONTRACTING OF AN INDEBTEDNESS BY THE STATE, OR A PLEDGE OF THE FAITH AND CREDIT OR TAXING POWER OF THE STATE, FOR PURPOSES OF ANY CONSTITUTIONAL OR STATUTORY LIMITATION UPON DEBT OR THE CONTRACTING OF INDEBTEDNESS. THE OBLIGATION OF THE STATE TO MAKE AGENCY RENT PAYMENTS ON BEHALF OF THE AGENCIES IS SUBJECT TO APPROPRIATION AND TO EMERGENCY REDUCTION IN FUNDING UNDER CERTAIN CIRCUMSTANCES, ALL AS SET FORTH IN THE MASTER FINANCING LEASE. NOTHING IN THE MASTER FINANCING LEASE SHOULD BE CONSIDERED AS OR CONSTRUED TO IMPLY A MORAL OBLIGATION ON THE PART OF THE STATE TO MAKE THE BASE RENT PAYMENTS DUE THEREUNDER.

**Assignment**

Concurrently with the execution and delivery of the Master Financing Lease, the Corporation will unconditionally grant, sell, assign, transfer and convey to the Fiscal Agent pursuant to the Master Assignment (Real Property), without recourse, (1) all of its rights to the Sites pursuant to the Site Leases, (2) all of its rights to receive the Base Rent Payments and any Additional Rent under and pursuant to the Master Financing Lease; (3) its right to take all actions, exercise all remedies, and give all consents under and pursuant to the Site Leases and the Master Financing Lease; (4) all of its remaining right, title and interest in, to and under the Site Leases, the Master Financing Lease, the Financing Leases, and in and to the Property (including any security interest therein) and any rents or profits generated therefrom; and (5) its right of access more particularly described in the Master Financing Lease, all in consideration for the payment by the Fiscal Agent to the Treasurer, as agent of the Corporation, of the proceeds of the sale of the Certificates.

The Treasurer and the Corporation acknowledge and agree that such grant, sale, assignment, transfer and conveyance by the Corporation is intended to be a true sale of the Corporation's right, title and interest, and that upon such grant, sale, assignment, transfer and conveyance, the Corporation ceases to have any rights, duties or obligations under the Site Leases, the Master Financing Lease, the Financing Leases, or with respect to the Property, and the Fiscal Agent should thereafter have all the rights, duties and obligations of the Corporation thereunder as if the Fiscal Agent had been the original party thereto, and every reference therein and in the Master Financing Lease to the Corporation is deemed and construed to refer to the Fiscal Agent, except where the context otherwise requires. Anything in the Master Financing Lease to the contrary notwithstanding, such grant, sale, assignment, transfer and conveyance does not confer any rights or impose any duties or obligations on the Fiscal Agent other than as expressly set forth in the Trust Agreement and the Master Assignment (Real Property).

**Optional Prepayment**

The State may at its option, and shall upon the optional prepayment of Agency Rent Payments by any Agency pursuant to its Financing Lease, prepay all or any portion of the Principal Components then unpaid, in whole or in part on any date on or after January 1, 2021, in Authorized Denominations from any source of available funds, at the times and at the Prepayment Price of 100 percent of the Principal Components prepaid, plus accrued interest, if any, evidenced and represented thereby to the Prepayment Date.

The State may at its option, and shall upon the optional prepayment of Agency Rent Payments by any Agency pursuant to its Financing Lease, provide for the payment of all or any portion of the Base Rent Payments then unpaid, in whole or in part on any date, by causing to be deposited with the Fiscal Agent, as assignee of the Corporation, (1) moneys and/or Government Obligations in accordance with the Trust Agreement; and (2) an Opinion of Counsel to the effect such actions are permitted under the Master Financing Lease and will not cause interest evidenced and represented by the Certificates to be includable in gross income for federal income tax purposes under the Code.

**Mandatory Prepayment; Special Prepayment**

***Eminent Domain; Loss of Title.*** The State covenants to, upon the special mandatory prepayment of Agency Rent Payments by any Agency pursuant to its Financing Lease, prepay or cause to be prepaid from eminent domain awards or sale proceeds received pursuant to the Master Financing Lease, and from the net proceeds of title insurance, if any, pursuant to the Master Financing Lease, the Principal Components of Base Rent Payments then unpaid, in whole or in part on any date, in Authorized Denominations, so that the aggregate annual Base Rent Payments for the related Property from and after

such Prepayment Date are in approximately equal amounts, at a Prepayment Price equal to the sum of the Principal Components so prepaid, without premium, plus accrued interest evidenced and represented thereby to the Prepayment Date.

***Insurance Proceeds.*** The State covenants to, upon the special optional prepayment of Agency Rent Payments by any Agency pursuant to its Financing Lease, prepay or cause to be prepaid from net insurance proceeds received pursuant to the Master Financing Lease, the Principal Components of Base Rent Payments then unpaid, in whole or in part on any date, in Authorized Denominations, so that the aggregate annual Base Rent Payments for the related Property from and after such Prepayment Date are in approximately equal amounts, at a Prepayment Price equal to the sum of the Principal Components so prepaid, without premium, plus accrued interest evidenced and represented thereby to the Prepayment Date.

***Provision for Payment in Accordance with Trust Agreement.*** To the extent such award, sale proceeds or net proceeds are not sufficient, in whole or in part, to prepay or cause the prepayment of Principal Components of Base Rent Payments in Authorized Denominations, such amounts must be applied by the Treasurer to provide for the payment thereof pursuant to the Master Financing Lease.

**Notice to Fiscal Agent**

The Treasurer is required to provide the Fiscal Agent, as assignee of the Corporation, with not less than 45 days' prior written notice of its intention (1) to prepay any Principal Components, which notice is required to specify the reason for such prepayment, the Prepayment Date, and the amount and the Principal Payment Dates of the Principal Components to be prepaid, and (2) to provide for the payment of any Base Rent Payments pursuant to the Master Financing Lease.

**Revision of Base Rent Payments upon Prepayment**

The Principal Components and Interest Components due on each Base Rent Payment Date on and after a Prepayment Date pursuant to the Master Financing Lease may be reduced by the Fiscal Agent, as assignee of the Corporation, to reflect such prepayment, in Authorized Denominations, in such amounts and on such Base Rent Payment Dates as the Treasurer elects in a written notice to the Fiscal Agent, as assignee of the Corporation; *provided*, that the aggregate reduction in such Principal Components is equal to the aggregate Principal Components prepaid by the Treasurer; and *provided further*, that the reduction in Principal Components and Interest Components due on each Base Rent Payment Date is equal to the corresponding reduction in the Agency Rent Payments due on each Agency Rent Payment Date.

**Discharge of Master Financing Lease**

All right, title and interest of the Corporation in the Master Financing Lease and all obligations of the State thereunder cease, terminate, become void and are completely discharged and satisfied (except for the right of the Fiscal Agent, as assignee of the Corporation, and the obligation of the State to have the moneys and Government Obligations so set aside applied to make the remaining Base Rent Payments) when either:

(1) all Base Rent Payments and all Additional Rent and other amounts due thereunder have been paid in accordance therewith; or

(2) (a) the Treasurer has delivered a written notice to the Corporation and the Fiscal Agent of its intention to prepay all of the Base Rent Payments remaining unpaid; (b) the Treasurer causes to be deposited with the Fiscal Agent, as assignee of the Corporation, (i) moneys and/or

Government Obligations in accordance with the Trust Agreement; and (ii) an Opinion of Counsel to the effect that such actions are permitted thereunder and will not cause interest evidenced and represented by the Certificates to be includable in gross income for federal income tax purposes under the Code; and (c) for so long as any Base Rent Payments remain unpaid, provision has been made satisfactory to the Corporation and the Fiscal Agent for payment of all Additional Rent, including but not limited to the fees and expenses of the Fiscal Agent.

**Eminent Domain**

If all of the Property subleased to the State pursuant to the Master Financing Lease and to any Agency pursuant to a Financing Lease, or so much thereof so as to render the remainder unsuitable for the purposes for which it was used by the Agency at the time of such taking, should be taken under the power of eminent domain (or sold under threat of condemnation), the sublease of such Property pursuant to the Master Financing Lease and the Financing Lease ceases as of the day that the State and the Agency is required to vacate such Property. If less than all of such Property is taken under the power of eminent domain (or sold under threat of condemnation), and the remainder is suitable for the purposes for which it was used by the Agency at the time of such taking, as reasonably determined by the Treasurer, then the sublease thereof pursuant to the Master Financing Lease and the Financing Lease continues in full force and effect as to such remainder, and the Parties waive any benefits of the law to the contrary. In such event, there should be no abatement of the rental due under the Master Financing Lease or Financing Lease. So long as any Agency Rent Payments under the Financing Lease remain unpaid, any eminent domain award and any proceeds of sale under threat of condemnation for all or any part of the Property should be applied to the prepayment of Agency Rent Payments and Base Rent Payments as provided in the Financing Lease and the Master Financing Lease. Any award or proceeds in excess of the amount necessary to prepay such Agency Rent Payments due under such Financing Lease, and thereby to prepay or provide for the payment of the corresponding portion of the Base Rent Payments under the Master financing Lease, should be paid to the Corporation, the State and the Agency as their respective interests may appear.

**Loss of Title**

If there is a loss of title to the Property subleased to the State pursuant to the Master Financing Lease and to any Agency pursuant to a Financing Lease which is insured under a policy or policies of title insurance, or so much thereof so as to render the remainder unsuitable for the purposes for which it was used by the State and the Agency at the time of such loss, the sublease of such Property pursuant to the Master Financing Lease and the Financing Lease ceases as of the day that the State and the Agency is required to vacate such Property. If there is a loss of title to less than all of such Property, and the remainder is suitable for the purposes for which it was used by the Agency at the time of such loss, as reasonably determined by the Treasurer, then the sublease thereof pursuant to the Master Financing Lease and the Financing Lease continues in full force and effect as to such remainder, and the Parties waive any benefits of the law to the contrary. In such event, there will be no abatement of the rental due thereunder or thereunder. So long as any Agency Rent Payments under the related Financing Lease remain unpaid, any payments under such title insurance policy or policies with respect to such Property are to be applied to the prepayment of Agency Rent Payments and Base Rent Payments as provided in the Financing Lease and the Master Financing Lease. Any payment in excess of the amount necessary to prepay such Agency Rent Payments due under such Financing Lease, and thereby to prepay or provide for the payment of the corresponding portion of the Base Rent Payments due under the Master Financing Lease, is to be paid to the Corporation, the State and the Agency as their respective interests may appear.

**Damage or Destruction**

If all or any portion of the Property subleased to the State pursuant to the Master Financing Lease and to any Agency pursuant to its Financing Lease is damaged or destroyed by fire or other casualty, the sublease thereof pursuant to the Master Financing Lease and the Financing Lease will not terminate, nor will there be any abatement of the rent payable under the Master Financing Lease or the Financing Lease. So long as any Agency Rent Payments under the related Financing Lease remain unpaid, any payments under the property insurance policy or policies with respect to such Property may be applied to the prepayment of Agency Rent Payments and Base Rent Payments as provided in the Financing Lease and the Master Financing Lease, or may be paid to the Treasurer and applied as provided in the Trust Agreement.

**Permitted Termination Event**

Upon the occurrence of a Permitted Termination Event with respect to any State Agency Financing Lease Addendum, the Treasurer shall immediately deliver written notice thereof to the Corporation, which notice shall state the election not to appropriate the necessary funds or the Executive Order reduction in State funding as set forth in such State Agency Financing Lease Addendum as the reason for cancellation thereof. The Treasurer shall, if practicable, request a supplemental appropriation in the event that an appropriation has not been made to the State Agency. In the event of an Executive Order reduction, the Treasurer shall determine whether or not the Property and the obligations of the Agency under the State Agency Financing Lease Addendum may be transferred to the office of the Treasurer or to another agency or department of the State authorized under the Act to enter into financing agreements. No Permitted Termination Event following an Executive Order reduction in funding shall be effective unless or until the Treasurer has determined that neither the Treasurer nor any other agency or department of the State authorized under the Act to enter into financing agreements is willing and able to assume the rights and obligations of the Agency under the State Agency Financing Lease Addendum. The Treasurer shall, at the beginning of the period for which funds have not been appropriated or for which funding has been reduced, transfer said Property to the Corporation for the remaining term of the related Site Lease for the account of the State and thereupon be released of its obligations to make payments in an amount equal to the then unpaid balance of Agency Rent Payments with respect to such Property. Upon the occurrence and effectiveness of a Permitted Termination Event, the Corporation shall be entitled to retain for the benefit of the Owners of the Certificates all sums theretofore transmitted to the Fiscal Agent, as assignee of the Corporation, by the Treasurer, and thereafter take possession of and relet the Property for the remaining term of the related Site Lease or assign its leasehold interest in the Property under the related Site Lease for the account of the State Agency and the benefit of the Owners of the Certificates. The occurrence of a Permitted Termination Event with respect to one State Agency Financing Lease Addendum shall not affect any rights, duties or obligations with respect to any other State Agency Financing Lease Addendum with respect to which no Permitted Termination Event has occurred.

**Covenants and Agreements of the State**

***Budget.*** The Treasurer covenants to: (1) include in its biennial budget all scheduled Agency Rent Payments under Local Agency Financing Leases due during such Biennium; (2) submit such budget to OFM at such times and in such manner as required by law; (3) use its best efforts to obtain appropriations by the State Legislature in amounts sufficient to make any such payments; (4) include all such payments in its statements of proposed expenditures for each fiscal period required by law to be submitted to OFM; and (5) use its best efforts to obtain allotments by OFM of appropriated funds sufficient to make all such payments.

***Financing Lease.*** Concurrently with the execution and delivery of the Master Financing Lease, the Treasurer covenants to enter into a Local Agency Financing Lease with each Local Agency with respect to the sublease of the respective Property and the acquisition and/or construction of the related Project. Concurrently with the execution and delivery of the Master Financing Lease, the Treasurer is required to enter into a State Agency Financing Lease Addendum with each State Agency with respect to the sublease of the respective Property and the acquisition and/or construction of the related Project. Each State Agency Financing Lease Addendum constitutes a part of the Master Financing Lease.

***Tax-Exemption.*** The State shall not make any use of the proceeds of the Master Financing Lease or the Certificates or of any other amounts, regardless of the source, or of any Property, and shall not take or refrain from taking any action, that would cause the Master Financing Lease or the Certificates to be "arbitrage bonds" within the meaning of Section 148 of the Code. The State shall not use or permit the use of the Property or any part thereof by any Person other than a "governmental unit" as that term is defined in Section 141 of the Code, in such manner or to such extent as would result in the loss of the exclusion from gross income for federal income tax purposes of the Interest Component of the Base Rent Payments under Section 103 of the Code. The State shall not make any use of the proceeds of the Master Financing Lease or the Certificates or of any other amounts, and shall not take or refrain from taking any action, that would cause the Master Financing Lease or the Certificates to be "federally guaranteed" within the meaning of Section 149(b) of the Code, or "private activity bonds" within the meaning of Section 141 of the Code, or "hedge bonds" within the meaning of Section 149 of the Code. To that end, for so long as any Base Rent Payments remain unpaid, the State, with respect to such proceeds and other amounts, will comply with all requirements under such Sections and all applicable regulations of the United States Department of the Treasury promulgated thereunder. The State will at all times do and perform all acts and things permitted by law which are necessary or desirable in order to assure that the Interest Components of the Base Rent Payments will not be included in gross income of the Owners of the Certificates for federal income tax purposes under the Code, and will take no action that would result in such interest being so included. The State shall comply with the provisions of the Tax Certificate.

The Treasurer may establish and maintain a separate account designated as the "State of Washington Certificates of Participation, Series 2011D Rebate Fund" (the "Rebate Fund"). The State shall deposit in the Rebate Fund the Rebate Requirement as provided in the Tax Certificate. Subject to the other provisions of this covenant regarding tax exemption of the Certificates, moneys held in the Rebate Fund are pledged to secure the rebate payments to the United States, and the State, the Agencies, the Corporation, the Fiscal Agent and the Owners shall have no rights in or claim to such moneys.

Without limiting the generality of the foregoing, the State agrees that there shall be paid from time to time all amounts required to be rebated to the United States pursuant to Section 148(f) of the Code. This covenant shall survive the discharge of the Master Financing Lease and the payment in full or defeasance of the Certificates. The State specifically covenants to pay or cause to be paid to the United States at the times and in the amounts determined to comply with the Rebate Requirement as provided by the Tax Certificate.

Notwithstanding any provision of the covenant regarding tax exemption, if the State shall provide to the Fiscal Agent an Opinion of Counsel to the effect that any specified action required under the covenant regarding tax exemption is no longer required or that some further or different action is required to maintain the tax-exempt status of interest evidenced and represented by the Certificates, the Fiscal Agent may conclusively rely on such opinion, and the covenants of the State thereunder shall be deemed to be modified to that extent.

***Duties Imposed by Law.*** To the extent permitted by law, the covenants, agreements and other obligations on the part of the State contained in the Master Financing Lease shall be deemed and construed to be

ministerial and non-discretionary duties imposed by law, and it shall be the duty of the State and each and every public official to take such actions in the performance of the official duties of such officials to enable the State to observe and perform the covenants, agreements, terms, conditions and other obligations contained in the Master Financing Lease and in the other Series 2011D Agreements to which the State is a party to be observed and performed by the State.

***Liens.*** The State shall not create, incur, assume or suffer to exist any mortgage, pledge, lien, charge, encumbrance or claim on or with respect to the Property or any part thereof, except for Permitted Encumbrances. The State shall promptly, at its own expense, take such action as may be necessary to duly discharge any such mortgage, pledge, lien, charge, encumbrance or claim if the same shall arise at any time.

***Assignments and Subleases.*** The State shall not (and shall not permit any Agency to) grant, sell, assign, pledge, transfer, convey, mortgage, pledge, sublet or otherwise dispose any of its right, title or interest in, to or under the Master Financing Lease or the Property other than to the respective Agencies pursuant to the Financing Leases or as otherwise provided in the Master Financing Lease or therein, and any such attempted grant, sale, transfer, assignment, pledge, conveyance or disposal shall be void. The Corporation consents to the sublease of the Property pursuant to the Financing Leases. Such subleases shall be subject and subordinate to the Master Financing Lease. Such subleases shall not release or alter the obligations or liability of the State under the Master Financing Lease. Upon the occurrence and continuance of an Agency Event of Default with respect to any Property, the Treasurer shall have the right, pursuant to the Financing Lease, to sublease all or any portion of such Property.

***Performance.*** The State shall punctually pay the Base Rent Payments and Additional Rent in strict conformity with the terms and provisions of the Master Financing Lease, and will faithfully observe and perform all the covenants, agreements, terms, conditions and other obligations contained in the Master Financing Lease required to be observed and performed by the State. Except for Permitted Termination Events, the State will not suffer or permit any default to occur thereunder, or do or permit anything to be done, or omit or refrain from doing anything, in any case where any such act done or permitted to be done, or any such omission or refraining from doing anything, would or might be ground for cancellation or termination of the Master Financing Lease.

***Corporation Not Liable.*** The Corporation and its directors, officers and employees shall not be liable to the State or to any other Person whomsoever for any death, injury or damage that may result to any Person or property by or from any cause whatsoever in, on, about or relating to the Property.

***Accounting Records and Report.*** The Treasurer will keep or cause to be kept proper accounting records in which complete and correct entries shall be made of all transactions relating to the receipt, investment, deposit, application and disbursement of the Agency Rent Payments, and such accounting records shall be available for inspection by the Fiscal Agent, as assignee of the Corporation, or its agent duly authorized in writing at reasonable hours and under reasonable conditions.

***Further Assurances.*** The State will preserve and protect the rights of the Corporation and the Fiscal Agent, as assignee of the Corporation, thereunder, and will warrant and defend such rights against all claims and demands of all Persons. The Treasurer will promptly execute, make, deliver, file and record any and all further assurances, instruments and agreements, and do or cause to be done such other and further things, as may be necessary or proper to carry out the intention or to facilitate the performance of the Master Financing Lease and for the better assuring and confirming to the Corporation the rights and benefits provided to it thereunder.

***Disclosure Agreement.*** Concurrently with the execution and delivery of the Master Financing Lease, the Treasurer will execute and deliver the Disclosure Agreement in order to assist the Underwriter in complying with the requirements under the Rule. The Treasurer shall comply with the requirements of the Disclosure Agreement; *provided*, that failure to so comply shall not constitute a default under the Master Financing Lease.

**Events of Default**

Each of the following shall constitute an "Event of Default" under the Master Financing Lease:

(1) Failure by the State (other than as a result of a Permitted Termination Event) to pay or cause to be paid any Base Rent Payment required to be paid thereunder at the time set forth in the Master Financing Lease; and

(2) Failure by the State (other than as a result of a Permitted Termination Event) to observe or perform any covenant, agreement, term or condition on its part to be observed or performed thereunder, other than as set forth in paragraph (1), above, for a period of 30 days after written notice from the Corporation, or from the Owners of not less than 25 percent in aggregate Principal Component evidenced and represented by the Certificates then Outstanding, to the Treasurer specifying such failure and requesting that it be remedied; *provided, however*, that such period shall be extended for not more than 60 days if such failure cannot be corrected within such period, and corrective action is commenced by the State within such period and diligently pursued until the failure is corrected; and

(3) If the State's interest under the Master Financing Lease or any part of the Master Financing Lease shall be assigned, sublet or transferred other than as provided in the Master Financing Lease, either voluntarily or by operation of law; and

(4) The occurrence of an Agency Event of Default.

Notwithstanding the provisions summarized above, if by reason of *force majeure* the State is unable in whole or in part to carry out the covenants, agreements, terms and conditions on its part contained in the Master Financing Lease, the State shall not be deemed in default during the continuance of such inability. The term "*force majeure*" means the following: acts of God; strikes; lockouts or other industrial disturbances or disputes; acts of public enemies; orders or restraints of any kind of the government of the United States of America or any of its departments, agencies or officials, or of its civil or military authorities; orders or restraints of the State or of any of its departments, agencies or officials or civil or military authorities of the State; wars, rebellions, insurrections; riots; civil disorders; blockade or embargo; landslides; earthquakes; fires; storms; droughts; floods; explosions; or any other cause or event not within the control of the State.

The Corporation may, at its election, waive any default or Event of Default and its consequences under the Master Financing Lease and annul any notice thereof by written notice to the Treasurer to such effect, and thereupon the respective rights of the Parties thereunder shall be as they would have been if such default or Event of Default had not occurred.

ANYTHING IN THE MASTER FINANCING LEASE TO THE CONTRARY NOTWITHSTANDING, A PERMITTED TERMINATION EVENT SHALL NOT CONSTITUTE AN EVENT OF DEFAULT UNDER THE MASTER FINANCING LEASE.

**Remedies**

Whenever an Event of Default under the Master Financing Lease shall have occurred and be continuing, the Corporation shall have the following rights and remedies:

(1) ***Continuation; Reentry and Reletting.*** The Corporation may continue the Master Financing Lease in full force and effect, and (a) collect rent and other amounts as they become due thereunder, (b) enforce every other term and provision of the Master Financing Lease to be observed or performed by the State, and (c) exercise any and all rights of entry and reentry upon the Property. In the event that the Corporation does not elect to terminate the Master Financing Lease in the manner summarized in paragraph (2) below, the State agrees to observe and perform all terms and provisions in the Master Financing Lease to be observed or performed by it, and, if the Property is not relet, to pay the full amount of the rent and other amounts due thereunder for the term of the Master Financing Lease, or, if the Property or any part thereof is relet, to pay any deficiency that results therefrom, in each case at the same time and in the same manner as otherwise provided in the Master Financing Lease, and notwithstanding any reentry or reletting by the Corporation, or suit in unlawful detainer or otherwise brought by the Corporation for the purpose of effecting such re-entry or obtaining possession of all or any part of the Property. Should the Corporation elect to re-enter or obtain possession of all or any part of the Property, the State irrevocably appoints the Corporation as the State's agent and attorney-in-fact (a) to relet the Property, or any part thereof, from time to time, either in the name of the Corporation or otherwise, upon such terms and conditions and for such use and period as the Corporation may determine in its discretion, (b) to remove all persons in possession thereof and all personal property whatsoever situated upon the Property, and (c) to place such personal property in storage in any warehouse or other suitable place for the State in the county in which such personal property is located, for the account of and at the expense of the State. The State shall be liable for, and agrees to pay the Corporation, the Corporation's costs and expenses in connection with reentry of the Property, removal and storage of any personal property, and reletting of the Property. The State agrees that the terms of the Master Financing Lease constitute full and sufficient notice of the right of the Corporation to reenter and relet the Property or any part thereof without effecting a surrender or termination of the Master Financing Lease. Termination of the Master Financing Lease upon an Event of Default shall be effected solely as summarized in paragraph (2) below. The State further waives any right to, and releases, any rental obtained by the Corporation upon reletting in excess of the rental and other amounts otherwise due under the Master Financing Lease.

(2) ***Termination.*** The Corporation may terminate the Master Financing Lease, but solely upon written notice by the Corporation to the Treasurer of such election. No notice to pay rent, notice of default, or notice to deliver possession of the Property or of any part thereof, nor any entry or reentry upon the Property or any part thereof by the Corporation, nor any proceeding in unlawful detainer or otherwise brought by the Corporation for the purpose of effecting such reentry or obtaining possession, nor any other act shall operate to terminate the Master Financing Lease, and no termination of the Master Financing Lease on account of an Event of Default shall be or become effective by operation of law or acts of the Parties to the Master Financing Lease or otherwise, unless and until such notice of termination shall have been given by the Corporation. The State agrees that no surrender of the Property or any part thereof, nor any termination of the Master Financing Lease by the State shall be valid or effective in any manner or for any purpose whatsoever unless such notice of termination shall have been given by the Corporation. Upon such termination, the Corporation may (1) reenter the Property or any part thereof and remove all persons in possession thereof and all personal property whatsoever situated upon the Property, and (2) to place such personal property in storage in any warehouse or other suitable place for the

State in the county in which such personal property is located, for the account of and at the expense of the State. Upon such termination, the State's right to possession of the Property shall terminate, and the State shall surrender possession thereof to the Corporation. In the event of such termination, the State shall remain liable to the Corporation for damages in an amount equal to the rent and other amounts that would have been due thereunder for the balance of the term of the Master Financing Lease, less the net proceeds, if any, of any reletting of the Property or any part thereof by the Corporation subsequent to such termination, after deducting the expenses incurred by the Corporation in connection with any such reentry, removal and storage of personal property, and reletting. The Corporation shall be entitled to collect damages from the State on the respective Base Rent Payment Dates, or alternatively, the Corporation may accelerate the State's obligations under the Master Financing Lease and recover from the State (a) the worth at the time of award of the unpaid rental which had been earned at the time of termination, (b) the worth at the time of award of the amount by which the unpaid rental which would have been earned after the termination until the time of award exceeds the amount of such rental loss that the State proves could have been reasonably avoided, (c) the worth at the time of award by which the unpaid rental for the balance of the term of the Master Financing Lease after the time of award exceeds the amount of rental loss that the State proves could reasonably have been avoided, and (d) any other amount necessary to compensate the Corporation for all the detriment proximately caused by the State's failure to perform its obligations thereunder, or which in the ordinary course would be likely to result therefrom, including but not limited to the Corporation's expenses in connection with reentry of the Property, removal and storage of any personal property, and reletting of the Property. The worth at the time of award shall be computed using a discount rate equal to the composite Interest Component evidenced and represented by the Certificates.

(3) ***Other Remedies.*** In addition to the other remedies summarized under this subheading, upon the occurrence and continuance of an Event of Default, the Corporation shall be entitled to proceed to protect and enforce the rights vested in them by the Master Financing Lease or by law. The terms and provisions of the Master Financing Lease and the duties and obligations of the State thereunder, and the officers and employees thereof, shall be enforceable by the Corporation by an action at law or in equity, for damages or for specific performance, or for writ of mandate, or by other appropriate action, suit or proceeding in any court of competent jurisdiction. Without limiting the generality of the foregoing, the Corporation shall have the right to bring the following actions:

(a) Accounting. By action or suit in equity to require the State or any Agency and its officers and employees to account as the trustee of an express trust;

(b) Injunction. By action or suit in equity to enjoin the violation of the rights of the Corporation; and

(c) Mandate. By writ of mandate or other action, suit or proceeding at law or in equity to enforce the Corporation's rights against the State or any Agency and its officers and employees, and to compel the State to perform and carry out its duties and obligations under the law and its covenants and agreements with the Corporation as provided in the Master Financing Lease.

In the event that the Corporation shall prevail in any action, suit or proceeding brought to enforce any of the terms or provisions of the Master Financing Lease, the State shall be liable for the reasonable attorneys' fees of the Corporation in connection therewith.

The State waives any and all claims for damages caused or which may be caused by the Corporation in reentering and taking possession of the Property or any part thereof as provided in the Master Financing Lease, and all claims for damages that may result from the destruction of or injury to the Property or any part thereof, and all claims for damages to or loss of any personal property that may be in or upon the Property.

ANYTHING IN THIS MASTER FINANCING LEASE TO THE CONTRARY NOTWITHSTANDING, IF THE EVENT OF DEFAULT CONSISTS OF AN AGENCY EVENT OF DEFAULT, THE REMEDIES OF THE CORPORATION SHALL BE LIMITED TO THOSE SET FORTH IN THE RELATED FINANCING LEASE AND THE MASTER FINANCING LEASE.

**No Remedy Exclusive; Non-Waiver**

No remedy conferred upon or reserved to the Corporation under the Master Financing Lease or under applicable law is intended to or shall be exclusive, and every such remedy shall be cumulative and shall be in addition to every other remedy given under the Master Financing Lease or now or existing at law or in equity. No delay or omission to exercise any right or remedy accruing upon a default or an Event of Default thereunder shall impair any such right or remedy or shall be construed to be a waiver of such default or Event of Default, but any such right or remedy may be exercised from time to time and as often as may be deemed necessary or expedient. In order to exercise any remedy reserved to the Corporation thereunder, it shall not be necessary to give any notice, other than such notice as may be required thereunder. A waiver by the Corporation of any default or Event of Default thereunder shall not constitute a waiver of any subsequent default or Event of Default thereunder, and shall not affect or impair the rights or remedies of the Corporation in connection with any such subsequent default or Event of Default.

No acceptance of less than the full amount of a rental payment due thereunder shall constitute an accord and satisfaction or compromise of any such payment unless the Corporation specifically agrees to such accord and satisfaction or compromise in writing.

**Default by the Corporation**

Anything in the Master Financing Lease to the contrary notwithstanding, the Corporation shall not be in default in the observance or performance of any of the covenants, agreements, terms or conditions to be observed or performed by it thereunder unless and until the Corporation shall have failed to observe or perform such covenant, agreement, term or condition for a period of 60 days after written notice by the Treasurer to the Corporation specifying such failure and requesting that it be remedied; *provided, however*, that such period shall be extended for such additional time as shall be reasonably required to correct such failure if corrective action is commenced by the Corporation within such period and diligently pursued until the failure is corrected.

**Term**

The term of the Master Financing Lease shall commence on the Dated Date, and shall end on the final Principal Payment Date thereunder, unless such term is extended or sooner terminated as provided in the Master Financing Lease. If on such date, all amounts due thereunder shall not have been paid or the payment thereof duly provided for pursuant to the Master Financing Lease, then the term of the Master Financing Lease shall be extended until 10 days after all amounts due thereunder shall have been paid or the payment thereof so provided for, except that the term of the Master Financing Lease shall in no event be extended beyond the date five years after such final Principal Payment Date. If prior to the final Principal Payment Date thereunder, all amounts due thereunder shall have been paid or the payment

thereof so provided for, the term of the Master Financing Lease shall end 10 days thereafter or 10 days after written notice by the Treasurer to the Corporation, whichever is earlier.

Anything in the Master Financing Lease to the contrary notwithstanding, the lease of any parcel of Property pursuant to the Master Financing Lease shall terminate when all Agency Rent Payments and other amounts due under the respective Financing Lease have been paid or the payment thereof duly provided for pursuant thereto.

**Termination**

The State agrees, upon the termination or expiration of the Master Financing Lease as to any parcel of Property, to quit and surrender such Property in the same good order, condition and repair as the same was in at the time of commencement of the term thereunder, except for acts of God, reasonable wear and tear, and any actions by any Agency in accordance therewith and with its Financing Lease that affect the condition of such Property. The State agrees that any permanent improvements and structures existing upon the Property at the time of such termination or expiration of the Master Financing Lease shall remain thereon. The State shall thereafter execute, acknowledge and deliver to the Corporation such instruments of further assurance as are necessary or desirable to confirm the Corporation's leasehold right, title and interest in and to such Property.

## MASTER FINANCING CONTRACT

**Sale and Purchase of Property**

The Corporation agrees to sell, assign and convey, and does sell, assign and convey, to the State, and the State agrees to purchase, acquire and assume, and does purchase, acquire and assume, from the Corporation, upon the terms and conditions set forth in the Master Financing Contract, all of the Corporation's right, title and interest in and to the Property sold thereunder and all proceeds and profits thereof and therefrom, subject to the security interest created pursuant to the Master Financing Contract, and the State agrees to pay in consideration thereof the Purchase Price therefor and interest thereon and the Additional Costs in accordance with the Master Financing Contract, and all other amounts required to be paid by the State under the Master Financing Contract.

**Appointment of Agents; Acquisition of Property; Revision and Substitution**

***Appointment of Agents.*** The Corporation appoints, and ratifies, approves and confirms its appointment of, the Treasurer and the respective Agencies pursuant to the Notices of Intent as its agents in connection with the disbursement of the proceeds of the Certificates and the acquisition of the respective items of Property, respectively, and the Treasurer accepts and agrees to such designation and appointment.

***Acquisition of Property.*** The Treasurer agrees that (1) it has caused or will cause the Property to be acquired by the respective Agencies, as agents for the Corporation, with all reasonable dispatch; and (2) it will pay or cause to be paid the Costs of Acquisition of the Property solely from funds available to it pursuant to the Master Financing Contract, the Trust Agreement and the Agency Financing Contracts. The appointment of the Treasurer and the respective Agencies to act as agents of the Corporation in connection with the disbursement of the proceeds of the Certificates and the acquisition of the Property, respectively, and all authority conferred is made and conferred irrevocably by the Corporation, and shall not be terminated by any act of the Treasurer, any Agency or the Corporation or otherwise.

***Revision and Substitution of Property.*** The Treasurer may revise or consent to the revision of any item of Property to be acquired with proceeds of the Certificates, or the description thereof; provided, that (1)

such item of Property as so revised shall satisfy the requirements under the Master Financing Contract with respect to the substitution of Property previously acquired; (2) the Costs of Acquisition of such item of Property shall not be materially reduced thereby; and (3) any such revision shall not relieve the State or any Agency of its obligation to acquire the Property in accordance therewith and with the Agency Financing Contract with respect thereto.

After acquisition of an item of Property, the Treasurer may substitute or consent to the substitution for an item of Property acquired for and on behalf of an Agency other personal property by filing with the Fiscal Agent, as assignee of the Corporation:

(1) a certificate of such Agency stating that such substitute Property:

(a) has a remaining useful life equal to or greater than the Property for which it is being substituted;

(b) has a fair market value equal to or greater than the fair market value of the item of Property for which it is being substituted;

(c) is free and clear of all liens and encumbrances except a first priority security interest in favor of the Fiscal Agent, as assignee of the Corporation, under the Master Financing Contract;

(d) is of equal usefulness and value as the Property for which it is being substituted;

(e) is essential to the Agency's ability to carry out its governmental functions and responsibilities; and

(f) is expected to be used by such Agency immediately and for the term of its Agency Financing Contract; and

(2) an Opinion of Counsel to the effect that such substitution will not cause interest evidenced and represented by the Certificates to be includable in gross income for federal income tax purposes under the Code.

**Title to the Property**

All right, title and interest in and to the Property shall transfer to and vest in the State from the Corporation without any further action by the State or the Corporation immediately upon the acquisition thereof or reimbursement to the State or the Agency for the Acquisition Costs thereof; *provided*, that the Treasurer and the Corporation shall take such action and execute such documents (including without limitation bills of sale and other title documents) as may be deemed necessary or desirable by the Treasurer or the Corporation to evidence and confirm such transfer of title pursuant to the Master Financing Contract.

Title to any and all additions, modifications, improvements, repairs or replacements to any Property shall be vested in the State, subject to the security interest of the Corporation until payment of all amounts due and owing with respect to such Property under the Master Financing Contract.

Any Property constituting a motor vehicle subject to registration with the State Department of Licensing shall be registered with the Agency as the registered and legal owner thereof.

**Security Interest**

In order to secure the payment and performance by the State of its obligations under the Master Financing Contract, the State pledges, grants, assigns and conveys to the Corporation a lien on and security interest in all right, title and interest of the State, whether now owned or acquired, in and to the Property and the Agency Financing Contracts, including without limitation the Agency Installment Payments and all proceeds thereof. Accordingly, the Master Financing Contract constitutes a security agreement. The State acknowledges and agrees that each provision of the Master Financing Contract is also a provision of the security agreement and that an Agency Event of Default under the Master Financing Contract is also a default under the security agreement.

The State further agrees that the Corporation may: (1) commingle Property which comes into its possession; (2) re-pledge such Property upon terms which impair the State's right to redeem such Property; and (3) require the State to assemble the Property and make it available to the Corporation in a manner which is reasonably convenient to both Parties. To the extent the Corporation is required for any reason to provide commercially reasonable notice to the State, the State agrees that notice mailed by first class mail five days before the event of which notice is given is commercially reasonable notice. The standard by which the Corporation's rights and duties with respect to such security agreement shall be measured is gross negligence or willful misconduct.

If required by the Corporation or the Fiscal Agent, as assignee of the Corporation, at any time during the term of the Master Financing Contract, the State will execute and deliver to the Corporation or the Fiscal Agent, as the case may be, in form satisfactory to the Corporation or the Fiscal Agent, such security agreements, financing statements and/or other instruments covering the Property and all accessions thereto.

**Disclaimer of Warranties**

The State acknowledges and agrees that the Property is of a nature, size, design and capacity selected by the respective Agencies pursuant to their own specifications, and not by the Corporation, and that the Corporation is not a manufacturer, supplier or a vendor of such personal property. THE CORPORATION MAKES NO WARRANTY OR REPRESENTATION, EITHER EXPRESS OR IMPLIED, AND ASSUMES NO RESPONSIBILITY, LIABILITY OR OBLIGATION, AS TO THE VALUE, DESIGN, CONDITION, MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR FITNESS FOR USE OF THE PROPERTY, OR AS TO THE TITLE THERETO, OR FOR THE ENFORCEMENT OF THE MANUFACTURERS', SUPPLIERS' OR VENDORS' REPRESENTATIONS, WARRANTIES OR GUARANTIES, OR ANY OTHER REPRESENTATION OR WARRANTY WITH RESPECT TO THE PERSONAL PROPERTY.

**Installment Payments**

The State promises to pay to the Corporation, as rental for the use and occupancy of the Property, the following amounts at the following times:

(1) On each Installment Payment Date, the Installment Payment, consisting of a Principal Component and/or an Interest Component; and

(2) All Additional Costs incurred by the Corporation in connection with the sale of the Property to the State, the execution and delivery of the Certificates, and the observance and performance of the Series 2011D Agreements, within 30 days following receipt of an invoice from the Corporation with respect thereto which includes (a) a brief description of each such Additional

Cost, (b) the party to whom payment is due, (c) the amount thereof, and (d) such additional information as the Treasurer may reasonably request.

Each Installment Payment shall consist of a Principal Component and/or an Interest Component as set forth in the Master Financing Contract. Interest shall accrue and be calculated as provided in the Trust Agreement. Each Installment Payment shall consist of the aggregate of the Agency Installment Payments payable by each Agency pursuant to its Agency Financing Contract. Each Installment Payment payable under the Master Financing Contract shall be paid by electronic funds transfer in lawful money of the United States of America. Payments of Additional Costs shall be made to or upon the order of the Corporation. Each Installment Payment shall be applied first to the Interest Component due under the Master Financing Contract, and then to the Principal Component due under the Master Financing Contract.

The Corporation directs the Treasurer, and the Treasurer agrees, to make all Installment Payments directly to the Fiscal Agent, as assignee of the Corporation, from the sources set forth in the Master Financing Contract and subject to the terms and conditions of the Master Financing Contract.

**Sources of Payment of Installment Payments**

***State Agency Financing Addenda.*** The State is acquiring the State Agency Property for and on behalf of the respective State Agencies set forth in Exhibit B to the Master Financing Contract. Concurrently with the execution of the Master Financing Contract, each such State Agency shall execute and deliver a State Agency Financing Addendum pursuant to which such State Agency shall agree to acquire its respective Property and to make Agency Installment Payments therefor, at such times and in such amounts as provided in the Master Financing Contract, which will be sufficient in the aggregate to pay the Purchase Price of the Property to be acquired by the State for and on behalf of such State Agency and interest thereon. Each State Agency Financing Addendum is incorporated in the Master Financing Contract and made a part of the Master Financing Contract by reference therein.

That portion of the Installment Payments that is allocable to the Purchase Price of State Agency Property and interest thereon shall be payable by the State solely from Agency Installment Payments to be made by the respective State Agencies. The obligation of each State Agency to make its Agency Installment Payments shall be subject to appropriation by the State Legislature and Executive Order reduction by the Governor. The State shall not be obligated to pay that portion of the Installment Payments that is allocable to the Purchase Price of State Agency Property and interest thereon other than from appropriated funds of the respective State Agencies.

***Local Agency Financing Contracts.*** The State is acquiring the Local Agency Property for and on behalf of the respective Local Agencies set forth in Exhibit B to the Master Financing Contract. Concurrently with the execution of the Master Financing Contract, each such Local Agency shall execute and deliver a Local Agency Financing Contract pursuant to which such Local Agency shall agree to acquire its respective Property and to make Agency Installment Payments, at such times and in such amounts as provided in the Master Financing Contract. Such Agency Installment Payments shall be sufficient in the aggregate to pay, on each Installment Payment Date, the Purchase Price of the Property to be acquired by the State for and on behalf of such Local Agency, and interest thereon.

That portion of the Installment Payments that is allocable to the Purchase Price of Local Agency Property and interest thereon shall be payable by the State solely from Agency Installment Payments to be made by the respective Local Agencies, except as otherwise provided in the two succeeding paragraphs immediately below. The obligation of each Local Agency to make its Agency Installment Payments shall be a direct and general obligation of the Local Agency to which the full faith and credit of such Local

Agency is pledged. The State shall not be obligated to pay that portion of the Installment Payments that is allocable to the Purchase Price of Local Agency Property and interest thereon other than from Agency Installment Payments paid by the respective Local Agencies, except as otherwise provided in the Master Financing Contract.

***Intercept of Local Agency Share of State Revenues.*** In the event that any Local Agency fails to make any payment due under its Local Agency Financing Contract, the Treasurer shall withhold an amount sufficient to make such payment from the Local Agency's share of State revenues or other amounts authorized or required by law to be distributed by the State to such Local Agency, including but not limited to leasehold excise taxes, sales and use taxes, excise taxes, property taxes and liquor control board receipts; provided, that the use of any such revenues or amounts to make such payments is otherwise authorized or permitted by State law. Such withholding shall continue until all such payments due under the Master Financing Contract have been made. Amounts withheld by the Treasurer shall be applied to make any such payment due under the Local Agency Financing Contract on behalf of the Local Agency, or to reimburse the Treasurer for any such payment made pursuant to the Master Financing Contract.

***Conditional Payment of Local Agency Installment Payments.*** Upon the failure of any Local Agency to make any Agency Installment Payment at such time and in such amount as required pursuant to its Local Agency Financing Contract, the Treasurer shall, to the extent of legally available appropriated funds and subject to any Executive Order reduction, make such payment into the Agency Installment Payment Fund on behalf of such Local Agency within 10 Business Days after such Agency Installment Payment was due. The Treasurer shall be entitled to reimbursement for any such payments made on behalf of the Local Agency as provided in the Local Agency Financing Contract.

**Agency Installment Payments; Deposit and Investment**

Agency Installment Payments shall be payable on each Agency Installment Payment Date and shall be deposited in a special fund or funds maintained by the Treasurer (the "Agency Installment Payment Fund"). Payments of Agency Installment Payments from State Agencies shall be accounted for separately from payments from Local Agencies. The Agency Installment Payments due on each Agency Installment Payment Date shall be at least sufficient, in the aggregate, to make the Installment Payment next coming due under the Master Financing Contract. Amounts in the Agency Installment Payment Fund, including investment earnings thereon, shall be used and applied, first, to make the Installment Payment next coming due, and thereafter, but prior to the next Agency Installment Payment Date, to the extent that amounts remain in such Fund after such Installment Payment is made, to pay Additional Costs or for any other lawful purpose of the Treasurer. Amounts in the Agency Installment Payment Fund shall be invested in the Qualified Investments, and shall be separately accounted for, but may be commingled with other moneys on deposit with the Treasurer solely for investment purposes.

**No Set Off**

The obligation of the State to make Installment Payments from the sources set forth in the Master Financing Contract and to perform its other obligations under the Master Financing Contract shall be absolute and unconditional, subject, however, to the right of any Agency to cease making Agency Installment Payments upon the occurrence of a Permitted Termination Event. The State shall make Installment Payments as and when the same shall become due without diminution, reduction, postponement, abatement, counterclaim, defense or set-off as a result of any dispute, claim or right of action by, against or diminution, among the State, the Corporation, the Fiscal Agent, any Agency, and/or any other Person, or for any other reason; provided, that nothing in the Master Financing Contract shall be construed to release or excuse the Corporation from the observance or performance of its obligations under the Master Financing Contract. If the Corporation shall fail to observe or perform any such

obligation, the State may institute such legal action and pursue such other remedies against the Corporation as the State deems necessary or desirable, including, but not limited to actions for specific performance, injunction and/or the recovery of damages.

**Limited Obligation**

THE MASTER FINANCING CONTRACT SHALL CONSTITUTE A SPECIAL, LIMITED OBLIGATION OF THE STATE PAYABLE SOLELY FROM THE SOURCES AND SUBJECT TO THE LIMITATIONS SET FORTH THEREIN. THE MASTER FINANCING CONTRACT SHALL NOT CONSTITUTE A DEBT OR A GENERAL OBLIGATION OF THE STATE OR OF ANY STATE AGENCY, THE CONTRACTING OF AN INDEBTEDNESS BY THE STATE OR BY ANY STATE AGENCY, OR A PLEDGE OF THE FAITH AND CREDIT OR TAXING POWER OF THE STATE OR OF ANY STATE AGENCY, FOR PURPOSES OF ANY CONSTITUTIONAL OR STATUTORY LIMITATION UPON DEBT OR THE CONTRACTING OF INDEBTEDNESS. THE OBLIGATION OF THE STATE TO MAKE AGENCY INSTALLMENT PAYMENTS, BOTH FOR STATE AGENCY PROPERTY AND ON BEHALF OF LOCAL AGENCIES FOR LOCAL AGENCY PROPERTY, IS SUBJECT TO APPROPRIATION AND TO EMERGENCY REDUCTION IN FUNDING UNDER CERTAIN CIRCUMSTANCES, ALL AS SET FORTH IN THE MASTER FINANCING CONTRACT. NOTHING IN THE MASTER FINANCING CONTRACT SHOULD BE CONSIDERED AS OR CONSTRUED TO IMPLY A MORAL OBLIGATION ON THE PART OF THE STATE OR ANY AGENCY TO MAKE THE INSTALLMENT PAYMENTS DUE THEREUNDER.

**Assignment**

Concurrently with the execution and delivery of the Master Financing Contract, the Corporation will grant, sell, assign, transfer and convey (1) all of its rights to receive the Installment Payments, and (2) all of its remaining right, title and interest in, to and under the Master Financing Contract and the Agency Financing Contracts, and in and to the Property to the Fiscal Agent pursuant to the Master Assignment (Equipment) in consideration for the payment by the Fiscal Agent to the Treasurer, as agent of the Corporation, of the proceeds of the sale of the Certificates. The Treasurer, the State Agencies and the Corporation acknowledge and agree that such grant, sale, assignment, transfer and conveyance by the Corporation is intended to be a true sale of the Corporation's right, title and interest, and that upon such grant, sale, assignment, transfer and conveyance, the Corporation shall cease to have any rights, duties or obligations under the Master Financing Contract or with respect to the Property, and the Fiscal Agent shall thereafter have all the rights, duties and obligations of the Corporation under the Master Financing Contract as if the Fiscal Agent had been the original party thereto, and every reference in the Master Financing Contract to the Corporation shall be deemed and construed to refer to the Fiscal Agent, except where the context otherwise requires. Anything in the Master Financing Contract to the contrary notwithstanding, such grant, sale, assignment, transfer and conveyance shall not confer any rights or impose any duties or obligations on the Fiscal Agent other than as expressly set forth in the Trust Agreement and in the Master Assignment (Equipment).

**Optional Prepayment**

The State may at its option, and shall upon the optional prepayment of Agency Installment Payments by any Agency pursuant to its Financing Contract, prepay all or any portion of the Principal Components then unpaid, in whole or in part on any date on or after January 1, 2021, in Authorized Denominations from any source of available funds, at the times and at the Prepayment Price of 100 percent of the Principal Components prepaid, plus accrued interest, if any, evidenced and represented thereby to the Prepayment Date.

The State may at its option, and shall upon the optional prepayment of Agency Installment Payments by any Agency pursuant to its Financing Contract, provide for the payment of all or any portion of the Installment Payments then unpaid, in whole or in part on any date, by causing to be deposited with the Fiscal Agent, as assignee of the Corporation, (1) moneys and/or Government Obligations in accordance with the Trust Agreement; and (2) an Opinion of Counsel to the effect such actions are permitted under the Master Financing Lease and will not cause interest evidenced and represented by the Certificates to be includable in gross income for federal income tax purposes under the Code.

**Notice to Fiscal Agent**

The Treasurer is required to provide the Fiscal Agent, as assignee of the Corporation, with not less than 45 days' prior written notice of its intention (1) to prepay any Principal Components, which notice is required to specify the reason for such prepayment, the Prepayment Date, and the amount and the Principal Payment Dates of the Principal Components to be prepaid, and (2) to provide for the payment of any Installment Payments pursuant to the Master Financing Contract.

**Revision of Installment Payments upon Prepayment**

The Principal Components and Interest Components due on each Installment Payment Date on and after a Prepayment Date pursuant to the Master Financing Contract may be reduced by the Fiscal Agent, as assignee of the Corporation, to reflect such prepayment, in Authorized Denominations, in such amounts and on such Installment Payment Dates as the Treasurer elects in a written notice to the Fiscal Agent, as assignee of the Corporation; *provided*, that the aggregate reduction in such Principal Components is equal to the aggregate Principal Components prepaid by the Treasurer; and *provided further*, that the reduction in Principal Components and Interest Components due on each Installment Payment Date is equal to the corresponding reduction in the Agency Installment Payments due on each Agency Installment Payment Date.

**Discharge of Master Financing Contract**

All right, title and interest of the Corporation in the Master Financing Contract and all obligations of the State under the Master Financing Contract shall cease, terminate, become void and be completely discharged and satisfied (except for the right of the Fiscal Agent, as assignee of the Corporation, and the obligation of the State to have the moneys and Government Obligations so set aside applied to make the remaining Installment Payments) when either:

(1) all Installment Payments and all Additional Costs and other amounts due under the Master Financing Contract have been paid in accordance therewith; or

(2) (a) the Treasurer shall have delivered a written notice to the Fiscal Agency, as assignee of the Corporation, of its intention to prepay all of the Installment Payments remaining unpaid; (b) the Treasurer shall cause to be deposited with the Fiscal Agent, as assignee of the Corporation, (i) moneys and/or Government Obligations in accordance with the Trust Agreement; and (ii) an Opinion of Counsel to the effect that such actions are permitted under the Master Financing Contract and will not cause interest evidenced and represented by the Certificates to be includable in gross income for federal income tax purposes under the Code; and (c) for so long as any Installment Payments remain unpaid, provision shall have been made satisfactory to the Corporation and the Fiscal Agent for payment of all Additional Costs, including but not limited to the fees and expenses of the Fiscal Agent.

**Permitted Termination Event**

Upon the occurrence of a Permitted Termination Event with respect to any State Agency Financing Addendum, the Treasurer shall immediately deliver written notice thereof to the Corporation, which notice shall state the election not to appropriate the necessary funds or the Executive Order reduction in State funding as set forth in said State Agency Financing Addendum as the reason for cancellation thereof. The Treasurer shall, if practicable, request a supplemental appropriation in the event that an appropriation has not been made to the State Agency. In the event of an Executive Order reduction, the Treasurer shall determine whether or not the Property and the obligations of the State Agency under the State Agency Financing Addendum may be transferred to the office of the Treasurer or to another agency or department of the State authorized under the Act to enter into financing agreements. No Permitted Termination Event following an Executive Order reduction in funding shall be effective unless or until the Treasurer has determined that neither the Treasurer nor any other agency or department of the State authorized under the Act to enter into financing agreements is willing and able to assume the rights and obligations of the State Agency under the Master Financing Contract. The Treasurer shall, at the beginning of the period for which funds have not been appropriated or for which funding has been reduced, return said Property to the Corporation for the account of the State and thereupon be released of its obligations to make payments in an amount equal to the then unpaid balance of Agency Installment Payments with respect to such Property; provided, that the State delivers such Property in good repair, working order and condition (ordinary wear and tear excepted) and its unencumbered title to the Corporation at a location in the United States designated by the Corporation as of the end of the last month for which funding has been provided or the end of the last month for which funding is available in the event of an Executive Order reduction in funding. Upon the occurrence and effectiveness of a Permitted Termination Event, the Corporation shall be entitled to retain for the benefit of the Owners of the Certificates all sums theretofore transmitted to the Fiscal Agent, as assignee of the Corporation, by the Treasurer. The occurrence of a Permitted Termination Event with respect to one State Agency Financing Addendum shall not affect any rights, duties or obligations with respect to any other State Agency Financing Addendum with respect to which no Permitted Termination Event has occurred.

**Covenants and Agreements of the State**

***Budget.*** The Treasurer shall (1) include in its biennial budget all scheduled Local Agency Installment Payments due during such Biennium; (2) submit such budget to OFM at such times and in such manner as required by law; (3) use its best efforts to obtain appropriations by the State Legislature in amounts sufficient to make any such payments; (4) include all such payments in its statements of proposed expenditures for each fiscal period required by law to be submitted to OFM; and (5) use its best efforts to obtain allotments by OFM of appropriated funds sufficient to make all such payments.

***Agency Financing Contracts.*** Concurrently with the execution and delivery of the Master Financing Contract, the Treasurer shall enter into a Local Agency Financing Contract with each Local Agency set forth in Exhibit B to the Master Financing Contract with respect to the acquisition of the item or items of Property set forth in the Master Financing Contract substantially in the form set forth in Exhibit C to the Master Financing Contract. Concurrently with the execution and delivery of the Master Financing Contract, the Treasurer shall also enter into a State Agency Financing Addendum with each State Agency set forth in Exhibit B to the Master Financing Contract with respect to the acquisition of the item or items of Property set forth in the Master Financing Contract substantially in the form set forth in Exhibit D to the Master Financing Contract. Each State Agency Financing Addendum shall constitute a part of the Master Financing Contract.

***Tax-Exemption.*** The State shall not make any use of the proceeds of the Master Financing Contract or the Certificates or of any other amounts, regardless of the source, or of any Property, and shall not take or

refrain from taking any action, that would cause the Master Financing Contract or the Certificates to be "arbitrage bonds" within the meaning of Section 148 of the Code. The State shall not use or permit the use of the Property or any part thereof by any Person other than a "governmental unit" as that term is defined in Section 141 of the Code, in such manner or to such extent as would result in the loss of the exclusion from gross income for federal income tax purposes of the Interest Component of the Installment Payments under Section 103 of the Code. The State shall not make any use of the proceeds of this Master Agency Financing Contract or the Certificates or of any other amounts, and shall not take or refrain from taking any action, that would cause the Master Financing Contract or the Certificates to be "federally guaranteed" within the meaning of Section 149(b) of the Code, or "private activity bonds" within the meaning of Section 141 of the Code, or "hedge bonds" within the meaning of Section 149 of the Code. To that end, for so long as any Installment Payments remain unpaid, the State, with respect to such proceeds and other amounts, will comply with all requirements under such Sections and all applicable regulations of the United States Department of the Treasury promulgated under the Master Financing Contract. The State will at all times do and perform all acts and things permitted by law which are necessary or desirable in order to assure that the Interest Components of the Installment Payments will not be included in gross income of the Owners of the Certificates for federal income tax purposes under the Code, and will take no action that would result in such interest being so included. The State shall comply with the provisions of the Tax Certificate and Agreement.

The Treasurer shall establish and maintain a separate account designated as the "State of Washington Certificates of Participation, Series 2011D Rebate Fund" (the "Rebate Fund"). The State shall deposit in the Rebate Fund the Rebate Requirement as provided in the Tax Certificate. Subject to the other provisions of the covenant regarding tax exemption of the Certificates summarized above, moneys held in the Rebate Fund are pledged to secure the rebate payments to the United States, and the State, the Agencies, the Corporation, the Fiscal Agent and the Owners shall have no rights in or claim to such moneys.

Without limiting the generality of the foregoing, the State agrees that there shall be paid from time to time all amounts required to be rebated to the United States pursuant to Section 148(f) of the Code. This covenant shall survive the discharge of the Master Financing Contract and the payment in full or defeasance of the Certificates. The State specifically covenants to pay or cause to be paid to the United States at the times and in the amounts determined as required to comply with the Rebate Requirement as provided by the Tax Certificate.

Notwithstanding any provision of the covenant regarding tax exemption, if the State shall provide to the Fiscal Agent an Opinion of Counsel to the effect that any specified action required under the covenant regarding tax exemption is no longer required or that some further or different action is required to maintain the tax-exempt status of interest evidenced and represented by the Certificates, the Fiscal Agent may conclusively rely on such opinion, and the covenants of the State under the Master Financing Contract shall be deemed to be modified to that extent.

***Duties Imposed by Law.*** To the extent permitted by law, the covenants, agreements and other obligations on the part of the State contained in the Master Financing Contract shall be deemed and construed to be ministerial and non-discretionary duties imposed by law, and it shall be the duty of the State and each and every public official to take such actions and to do such things as are required by law in the performance of the official duties of such officials to enable the State to observe and perform the covenants, agreements, terms, conditions and other obligations contained in the Master Financing Contract and in the other Series 2011D Agreements to which the State is a party to be observed and performed by the State.

***Liens.*** The State shall not create, incur, assume or suffer to exist any mortgage, pledge, lien, charge, encumbrance or claim on or with respect to the Property, except the rights of the Corporation and the

respective Agencies as provided in the Master Financing Contract and in the Agency Financing Contracts. The State shall promptly, at its own expense, take such action as may be necessary to duly discharge any such mortgage, pledge, lien, charge, encumbrance or claim if the same shall arise at any time. The State shall not (and shall not permit any Agency) to grant, sell, transfer, assign, pledge, convey or otherwise dispose of any of the Property other than to the respective Agencies pursuant to the Agency Financing Contracts or as otherwise provided in the Master Financing Contract, and any such attempted grant, sale, transfer, assignment, pledge, conveyance or disposal shall be void.

***Performance.*** The State shall punctually pay the Installment Payments in strict conformity with the terms and provisions of the Master Financing Contract, and will faithfully observe and perform all the covenants, agreements, terms, conditions and other obligations contained in the Master Financing Contract required to be observed and performed by the State. Except for Permitted Termination Events, the State will not suffer or permit any default to occur under the Master Financing Contract, or do or permit anything to be done, or omit or refrain from doing anything, in any case where any such act done or permitted, or any such omission or refraining from doing anything, would or might be grounds for acceleration or termination of the Master Financing Contract. Except for Permitted Termination Events, the State will not terminate the Master Financing Contract for any cause, including but not limited to any acts or circumstances that may constitute failure of consideration, destruction of or damage to the Property, commercial frustration of purpose, any change in the tax or other laws of the United States of America or of the State or any political subdivision of the State, or any failure by the Corporation to observe or perform any covenant, agreement, term, condition or other obligation contained in the Master Financing Contract required to be observed and performed by it, whether express or implied, or the bankruptcy, insolvency, liquidation or reorganization of the Corporation. The State assumes the entire risk of loss, from any and every cause whatsoever, to the Property.

***Accounting Records and Report.*** The Treasurer will keep or cause to be kept proper accounting records in which complete and correct entries shall be made of all transactions relating to the receipt, investment, deposit, application and disbursement of the Agency Installment Payments, and such accounting records shall be available for inspection by the Fiscal Agent, as assignee of the Corporation, or its agent duly authorized in writing at reasonable hours and under reasonable conditions.

***Further Assurances.*** The State will preserve and protect the rights of the Corporation and the Fiscal Agent, as assignee of the Corporation, under the Master Financing Contract, and will warrant and defend such rights against all claims and demands of all Persons. The State will promptly execute, make and deliver any and all further assurances, instruments and agreements, and do or cause to be done such other and further things, as may be necessary or proper to carry out the intention or to facilitate the performance of the Master Financing Contract and for the better assuring and confirming to the Corporation the rights and benefits provided to it under the Master Financing Contract.

***Disclosure Agreement.*** Concurrently with the execution and delivery of the Master Financing Contract, the Treasurer will execute and deliver the Disclosure Agreement in order to assist the Underwriter in complying with the requirements under the Rule. The Treasurer shall comply with the requirements of the Disclosure Agreement; provided, that failure to so comply shall not constitute a default under the Master Financing Contract.

**Events of Default**

Each of the following shall constitute an “Event of Default” under the Master Financing Contract:

(1) Failure by the State (other than as a result of a Permitted Termination Event) to pay or cause to be paid any Installment Payment required to be paid under the Master Financing Contract at the time set forth in the Master Financing Contract;

(2) Failure by the State (other than as a result of a Permitted Termination Event) to observe or perform any covenant, agreement, term or condition on its part to be observed or performed under the Master Financing Contract, other than as set forth in paragraph (1), above, for a period of 30 days after written notice from the Corporation, or from the Owners of not less than 25 percent in aggregate Principal Component evidenced and represented by the Certificates then Outstanding, to the Treasurer specifying such failure and requesting that it be remedied; provided, however, that such period shall be extended for not more than 60 days if such failure cannot be corrected within such period, and corrective action is commenced by the State within such period and diligently pursued until the failure is corrected; and

(3) The occurrence of an Agency Event of Default.

Notwithstanding the provisions summarized above, if by reason of *force majeure* the State is unable in whole or in part to carry out the covenants, agreements, terms and conditions on its part contained in the Master Financing Contract, the State shall not be deemed in default during the continuance of such inability. The term "*force majeure*" means the following: acts of God; strikes; lockouts or other industrial disturbances or disputes; acts of public enemies; orders or restraints of any kind of the government of the United States of America or any of its departments, agencies or officials, or of its civil or military authorities; orders or restraints of the State or of any of its departments, agencies or officials or civil or military authorities of the State; wars, rebellions, insurrections; riots; civil disorders; blockade or embargo; landslides; earthquakes; fires; storms; droughts; floods; explosions; or any other cause or event not within the control of the State.

The Corporation may, at its election, waive any default or Event of Default and its consequences under the Master Financing Contract and annul any notice thereof by written notice to the Treasurer to such effect, and thereupon the respective rights of the Parties under the Master Financing Contract shall be as they would have been if such default or Event of Default had not occurred.

ANYTHING IN THE MASTER FINANCING CONTRACT TO THE CONTRARY NOTWITHSTANDING, A PERMITTED TERMINATION EVENT SHALL NOT CONSTITUTE AN EVENT OF DEFAULT UNDER THE MASTER FINANCING CONTRACT.

**Remedies**

Whenever an Event of Default under the Master Financing Contract shall have occurred and be continuing, the Corporation has the right, without any further demand or notice, to:

(1) take whatever action at law or in equity may appear necessary or desirable to collect the Installment Payments then due and thereafter becoming due, or to enforce the observance or performance of any covenant, agreement or obligation of the State under the Master Financing Contract;

(2) by written notice to the State, request the State to (and the State agrees that it shall), at the State's expense, promptly return the item or items of Property with respect to which such default occurred in good condition (ordinary wear and tear excepted) to any location in the United States specified by the Corporation;

(3) exercise all rights of a secured party under the State Uniform Commercial Code with respect to the item or items of Property with respect to which such default occurred; and

(4) exercise any other rights or remedies it may have under the Master Financing Contract or under applicable law.

ANYTHING IN THE MASTER FINANCING CONTRACT TO THE CONTRARY NOTWITHSTANDING, IF THE EVENT OF DEFAULT CONSISTS OF AN AGENCY EVENT OF DEFAULT, THE REMEDIES OF THE CORPORATION SHALL BE LIMITED TO THOSE SET FORTH IN THE MASTER FINANCING CONTRACT AND THE RELATED AGENCY FINANCING CONTRACT, RESPECTIVELY.

**No Remedy Exclusive; Non-Waiver**

No remedy conferred upon or reserved to the Corporation under the Master Financing Contract or under applicable law is intended to or shall be exclusive, and every such remedy shall be cumulative and shall be in addition to every other remedy given under the Master Financing Contract or now or existing at law or in equity. No delay or omission to exercise any right or remedy accruing upon a default or an Event of Default under the Master Financing Contract shall impair any such right or remedy or shall be construed to be a waiver of such default or Event of Default, but any such right or remedy may be exercised from time to time and as often as may be deemed necessary or expedient. In order to exercise any remedy reserved to the Corporation under the Master Financing Contract, it shall not be necessary to give any notice, other than such notice as may be required under the Master Financing Contract. A waiver by the Corporation of any default or Event of Default under the Master Financing Contract shall not constitute a waiver of any subsequent default or Event of Default under the Master Financing Contract, and shall not affect or impair the rights or remedies of the Corporation in connection with any such subsequent default or Event of Default.

**Term**

The Master Financing Contract shall terminate on the date on which all amounts due under the Master Financing Contract shall have been paid or the payment thereof duly provided for pursuant to the Master Financing Contract.

## TRUST AGREEMENT

**Project Fund**

The Treasurer shall establish and maintain the Project Fund as agent for the Corporation. The moneys in the Project Fund shall be held by the Treasurer in trust for the benefit of the Owners and applied to the payment of the Project Costs (including reimbursement to the Corporation, or to the Treasurer or any Agency, in its capacity as agent of the Corporation, for any such costs theretofore paid by such Party), including but not limited to the Costs of Issuance. Moneys in the Project Fund shall be invested by the Treasurer in Qualified Investments. Disbursements by the Treasurer from the Project Fund to pay or reimburse the Project Costs of the related Property or the Projects to be acquired, constructed, financed or refinanced by each Agency shall not exceed the amount in the Project Fund for such Agency, as determined by the Treasurer. When the Projects and the related Property have been acquired, constructed, financed, or refinanced and all of the Project Costs and Costs of Issuance have been paid, the Treasurer shall transfer any remaining balance in the Project Fund to the Agency Rent Payment Fund.

**Acquisition Fund**

The Treasurer shall establish and maintain the Acquisition Fund as agent for the Corporation. The moneys in the Acquisition Fund shall be held by the Treasurer in trust for the benefit of the Owners and applied to the payment of the Acquisition Costs (including reimbursement to the Corporation, or to the Treasurer or any Agency, in its capacity as agent of the Corporation, for any such costs theretofore paid by such Party), including but not limited to the Costs of Issuance. Moneys in the Acquisition Fund shall be invested by the Treasurer in Qualified Investments. Disbursements by the Treasurer from the Acquisition Fund to pay or reimburse the Acquisition Costs of Property to be acquired by each Agency shall not exceed the amount in the Acquisition Fund allocable to such Agency, as determined by the Treasurer. When the Property has been acquired or refinanced and all of the Acquisition Costs and Costs of Issuance have been paid, the Treasurer shall transfer any remaining balance in the Acquisition Fund to the Agency Installment Payment Fund.

**State Payments; Funds and Accounts; Investments**

***State Payments Held in Trust.*** The State Payments are irrevocably pledged and shall be applied to pay the Principal Component and Interest Component evidenced and represented by the Certificates when due, and shall not be used or applied for any other purpose while any of the Certificates remain Outstanding. The pledge shall constitute a first and exclusive lien on and security interest in the State Payments for the benefit of the Owners of the Certificates.

All State Payments shall be paid directly by the Treasurer to the Fiscal Agent, as assignee of the Corporation, and if received by the Corporation at any time shall be deposited by the Corporation with the Fiscal Agent within one Business Day after the receipt thereof. All State Payments shall be immediately deposited by the Fiscal Agent in the appropriate funds provided in the Trust Agreement, whereupon they shall be applied immediately to the payment or prepayment, as appropriate, of Certificates except as otherwise expressly provided in the Trust Agreement, but if for any reason not so applied, held in trust by the Fiscal Agent in such fund for the benefit of the Owners from time to time.

***Deposit of State Payments.*** The Fiscal Agent agrees to establish, maintain and hold in trust the Certificate Fund for so long as any Certificates remain Outstanding. The Fiscal Agent shall deposit all State Payments, including prepayments, in the following Accounts within the Certificate Fund, each of which the Fiscal Agent agrees to establish and maintain, at the times, in the manner and in the order of priority as set forth below, and the moneys in each of such Accounts shall be disbursed only for the purposes and uses authorized.

(1) Interest Account. On each Interest Payment Date, the Fiscal Agent shall deposit in the Interest Account that amount of moneys evidencing the Interest Components due on such Interest Payment Date. Moneys in the Interest Account shall be withdrawn and used by the Fiscal Agent solely for the purpose of paying the interest evidenced and represented by the Certificates due and payable on such Interest Payment Date.

(2) Principal Account. On each Principal Payment Date and Prepayment Date, the Fiscal Agent shall deposit in the Principal Account that amount of moneys evidencing the Principal Components due on such Principal Payment Date or Prepayment Date. Moneys in the Principal Account shall be withdrawn and used by the Fiscal Agent solely for the purpose of paying the principal evidenced and represented by the Certificates due and payable on such Principal Payment Date or Prepayment Date.

(3) Prepayment Account. On each date on which the Treasurer makes a prepayment of Principal Components at the Prepayment Price therefor (and related payments of Interest Components, if any) pursuant to the Master Financing Agreements, the Fiscal Agent shall deposit in the Prepayment Account the amount of such prepayment and related payments. Moneys in the Prepayment Account shall be withdrawn and used by the Fiscal Agent solely for the purpose of paying the Prepayment Price evidenced and represented by Certificates prepaid on such date pursuant to the Trust Agreement and the accrued interest, if any, evidenced and represented by the Certificates so prepaid.

***Application of Insurance Proceeds and Eminent Domain Awards.*** The proceeds of any casualty insurance with respect to any of the Property, if received by the State or any Agency, shall immediately be paid to the Fiscal Agent. Within 90 days of payment of such proceeds to the Fiscal Agent, the respective Agency shall notify the Fiscal Agent in writing as to whether it elects to repair or replace such Property. In the event that the Agency elects to repair or replace such Property, such amounts shall be disbursed by the Fiscal Agent to pay the costs of such repair or replacement. In the event that the Agency elects not to repair or replace the property damaged, destroyed or taken, the Fiscal Agent shall transfer all such amounts to the Prepayment Account and apply such amounts to the prepayment of Outstanding Certificates pursuant to the Trust Agreement at the earliest possible Prepayment Date. Any eminent domain award, the proceeds of any sale under threat of condemnation, and the net proceeds of any title insurance in connection with a loss of title with respect to any Property, if received by the State or an Agency, shall immediately be paid to the Fiscal Agent. The Fiscal Agent shall transfer all such amounts to the Prepayment Account and apply such amounts to the prepayment of Outstanding Certificates pursuant to the Trust Agreement at the earliest possible Prepayment Date. To the extent that such amounts are not sufficient, in whole or in part, to prepay Principal Components evidenced and represented by the Certificates in Authorized Denominations, such amounts shall be applied to provide for the payment thereof pursuant to the Trust Agreement.

***Investment of Moneys.*** All moneys in any of the funds or accounts established and maintained by the Fiscal Agent pursuant to the Trust Agreement shall be invested by the Fiscal Agent, at the written direction of the Treasurer, solely in Qualified Investments. The written investment instruction to the Fiscal Agent shall contain a statement that such investments are Qualified Investments as required by the Trust Agreement. The Fiscal Agent may rely on the investment instructions of the Treasurer as to the suitability and legality of the instructed investments, and the Fiscal Agent shall not be responsible for losses incurred in making investments in accordance with the Treasurer's investment instructions.

Qualified Investments may be purchased at such prices as the Fiscal Agent may in its discretion determine or as may be directed by the Treasurer. All investment instructions to the Fiscal Agent shall be subject to the limitations set forth in the Trust Agreement and such additional limitations or requirements consistent with the foregoing as may be established by the Treasurer.

Moneys in all funds and accounts maintained by the Fiscal Agent shall be invested in Qualified Investments maturing not later than the date on which such moneys will be required for the purposes specified in the Trust Agreement. Notwithstanding any provisions in the Trust Agreement to the contrary, any moneys held for the payment of Certificates pursuant to the Trust Agreement shall be invested only at the written direction of the Treasurer and only in Government Obligations (or in shares of a taxable government money market fund restricted to Government Obligations rated in the highest rating category applicable to such funds by at least one Rating Agency) which mature not later than the date on which it is estimated that such moneys will be required to pay such Certificates (but in any event maturing in not more than 30 days).

All interest, profits and other income received from the investment of moneys in any fund or account established pursuant to the Trust Agreement shall be deposited in the fund or account which gave rise to the investment earnings. For the purpose of determining the amount in any fund or account, all Qualified Investments credited to such fund or account shall be valued at the lesser of cost or par value.

Subject to any written instruction from the Treasurer pursuant to the Trust Agreement, moneys in any and all funds and accounts may be commingled for investment purposes; provided, that the Fiscal Agent shall at all times account for such investments strictly in accordance with the funds and accounts to which they are credited and otherwise as provided in the Trust Agreement. The Fiscal Agent and its affiliates may act as principal or agent in the making or disposing of any investment. The Fiscal Agent may sell or present for redemption any Qualified Investments so purchased whenever it shall be necessary to provide moneys to meet any required payment, transfer, withdrawal or disbursement from the fund or account to which such Qualified Investment is credited, and the Fiscal Agent shall not be liable or responsible for any loss resulting from such investment or disposition. The Fiscal Agent and its affiliates may act as sponsor, advisor or depository with regard to any Qualified Investments.

***Non-Presentment of Certificates.*** In the event that any Certificates shall not be presented for payment when the principal or Prepayment Price evidenced and represented thereby becomes due, either at a Principal Payment Date, Prepayment Date or otherwise, if moneys sufficient to pay such principal or Prepayment Price shall have been deposited in the Principal Account or the Prepayment Account, as applicable, all liability of the Fiscal Agent and the State to the Owner thereof for payment with respect to such Certificate shall forthwith cease, terminate and be completely discharged, and thereupon it shall be the duty of the Fiscal Agent to hold such moneys (subject to the Trust Agreement), without liability for interest thereon, for the benefit of the Owner of such Certificate who shall thereafter be restricted exclusively to such moneys, for any claim of whatever nature on his or her part under the Trust Agreement or on or with respect to such Certificate.

***Repayment to Treasurer.*** When there are no longer any Certificates Outstanding, and all fees, charges and expenses of the Fiscal Agent and any Paying Agents have been paid or provided for, and all expenses of the Corporation and the Treasurer relating to the Master Financing Lease and the Trust Agreement have been paid or provided for, and all other amounts payable under the Trust Agreement and under the Master Financing Lease have been paid, and the Trust Agreement has been discharged and satisfied, the Fiscal Agent shall pay to the Treasurer any amounts remaining in any fund or account established and held under the Trust Agreement.

**Covenants of the Corporation, the State and the Fiscal Agent**

***Compliance with Trust Agreement.*** The Fiscal Agent will not execute or deliver any Certificates in any manner other than in accordance with the provisions of the Trust Agreement. The Corporation, the State and the Fiscal Agent will faithfully comply with, keep, observe and perform all the agreements, conditions, covenants and terms of the Trust Agreement required to be complied with, kept, observed and performed by each of them.

***Compliance with and Amendment of the Master Financing Agreement.*** The Corporation, the State and the Fiscal Agent, as assignee of the Corporation, will faithfully comply with, keep, observe and perform all the agreements, conditions, covenants and terms contained in the Master Financing Agreements required to be complied with, kept, observed and performed by each of them, and the Fiscal Agent will, to the extent required under the Trust Agreement, enforce such agreement against the State in accordance with its terms.

The State will not alter, amend or modify the Master Financing Agreements without the prior written consent of the Fiscal Agent. Such consent of the Fiscal Agent shall be given only (1) if the Fiscal Agent receives an Opinion of Counsel to the effect that such alterations, amendments or modifications will not have a material adverse effect on the interests of the Owners of the Certificates, or (2) if the Fiscal Agent first obtains the written consent of the Owners of a majority in aggregate Principal Component evidenced and represented by the Certificates then Outstanding to such alterations, amendments or modifications; provided, that no such alteration, amendment or modification shall reduce the amount or extend the time for payment of any State Payment without the prior written consent of the Owners of the Certificates evidencing and representing any portion thereof.

***Other Liens.*** So long as any Certificates are Outstanding, the Corporation, the State and the Fiscal Agent will not create or suffer to be created any pledge of, lien on or security interest in the State Payments other than the pledge and lien of the Trust Agreement and security interest under the Trust Agreement.

***Prosecution and Defense of Suits.*** The State will defend against every action, suit or other proceeding at any time brought against the Corporation, the Fiscal Agent or any Owner upon any claim arising out of the receipt, deposit or disbursement of any of the State Payments or involving the rights or obligations of the Corporation, the Fiscal Agent or any Owner under the Trust Agreement; *provided, however*, that the Corporation or any Owner, at its election and at its sole cost and expense, and the Fiscal Agent (at the reasonable cost and expense of the Corporation or the State, but only if (1) the employment of such counsel has been authorized by the Corporation or the State, or (2) the Corporation and the State shall have failed promptly after receiving notice of such action from the Fiscal Agent to assume the defense of such action and employ counsel reasonably satisfactory to the Fiscal Agent, or (3) the State, the Corporation and the Fiscal Agent shall have agreed, or a court of competent jurisdiction shall have determined, that there is a conflict of interest between the Fiscal Agent and the Corporation or the State on any legal issue pertaining to such action, or (4) the Fiscal Agent has received the written legal opinion of outside counsel to the Fiscal Agent that there is a conflict of interest between the Fiscal Agent and the Corporation or the State on any legal issue pertaining to such action, and such action does not involve an action, suit or proceeding between the Fiscal Agent and the Corporation or the State), may appear in and defend any such action, suit or other proceeding.

***Accounting Records and Statements.*** The Fiscal Agent will keep proper accounting records in accordance with corporate trust accounting standards in which complete and correct entries shall be made of all transactions relating to the receipt, investment, deposit, application and disbursement of the State Payments, and such accounting records shall be available for inspection by the Treasurer or any Owner or agent duly authorized in writing at reasonable hours and under reasonable conditions. Not later than December 1 in each year, commencing on December 1, 2011, and continuing for so long as any Certificates are Outstanding, the Fiscal Agent will furnish, or cause to be furnished to the Treasurer and any Owner who may so request (at the expense of such Owner) a complete statement covering the receipts, investment, deposits, application and disbursements of the State Payments for the twelve-month period ending on the preceding July 1.

Such records shall specify the fund or account to which each investment (or portion thereof) held pursuant to the Trust Agreement is to be allocated and shall set forth, in the case of each Qualified Investment, (1) its purchase price, (2) identifying information, including par amount, coupon rate, and payment dates, (3) the amount received at maturity or its sale price, as the case may be, (4) the amounts and dates of any payments made with respect thereto, and (5) such other documentation as is required by the Treasurer in writing.

***Recording and Filing.*** The Fiscal Agent, upon receipt of a Written Request of the State Treasurer, shall execute, and the State or the Corporation shall file, record, register, renew, refile and rerecord all such

documents, including but not limited to the Site Leases, the Master Financing Agreements, the Financing Agreements, and the Master Assignments, as may be required by law in order to maintain a security interest in the State Payments, all in such manner, at such times and in such places as may be required and to the extent permitted by law in order to fully perfect, preserve and protect the security of the Owners and the rights and interests of the Fiscal Agent; *provided, however*, that the Fiscal Agent will not be required to execute a special or general consent to service of process, or to qualify as a foreign corporation in connection with any such filing, recording, registration, refiling or rerecording in any jurisdiction in which it is not now so subject.

***Further Assurances.*** Whenever and so often as requested to do so by the Fiscal Agent or any Owner, the Corporation and the Treasurer will promptly execute and deliver or cause to be executed and delivered all such other and further assurances, documents or instruments and promptly do or cause to be done all such other and further things as may be necessary or desirable in order to further and more fully vest in the Fiscal Agent and the Owners all advantages, benefits, interests, powers, privileges and rights conferred upon them and by the Master Financing Agreements.

**Events of Default; Remedies**

***Events of Default; Remedies; Waiver.*** If an Event of Default shall occur and be continuing, then such Event of Default shall constitute a default under the Trust Agreement, and in each and every such case during the continuance of such Event of Default, the Fiscal Agent may, and upon the written request of the Owners of not less than a majority in aggregate Principal Component evidenced and represented by the Certificates then Outstanding and receipt of indemnity satisfactory to it shall, exercise the remedies provided to the Corporation and the Fiscal Agent, as assignee of the Corporation, under the Trust Agreement and under the Master Financing Agreements.

The Fiscal Agent may, in its discretion, waive any default or Event of Default and its consequences under the Trust Agreement and annul any notice thereof by written notice to the Treasurer to such effect, and thereupon the respective rights of the Parties under the Trust Agreement shall be as they would have been if such default or Event of Default had not occurred.

***Other Remedies of the Fiscal Agent.*** The Fiscal Agent may, and upon the written request of the Owners of not less than a majority in aggregate Principal Component evidenced and represented by the Certificates then Outstanding and receipt of indemnity satisfactory to it, shall:

(1) by mandamus or other action or proceeding or suit, action or proceeding at law or in equity enforce its rights against the State or any Agency or any officer or employee thereof, and to compel the State or any Agency or any such officer or employee to perform or carry out its duties under law and the agreements and covenants required to be performed by it or him or her contained in the Trust Agreement and in the Master Financing Agreements;

(2) by suit in equity to enjoin any acts or things which are unlawful or violate the rights of the Fiscal Agent; or

(3) by suit in equity upon the happening of any default under the Trust Agreement to require the State or any Agency and its officers and employees to account as the trustee of an express trust.

Nothing in the Trust Agreement shall be deemed to authorize the Fiscal Agent to authorize or consent to or accept or adopt on behalf of any Owner any plan of reorganization, arrangement, adjustment, or composition affecting the Certificates or the rights of any Owner thereof, or to authorize the Fiscal Agent

to vote in respect of the claim of any Owner in any such proceeding without the approval of the Owners so affected.

***Application of Moneys.*** If an Event of Default shall have occurred and be continuing, all moneys received by the Fiscal Agent shall be applied, first, to the payment of the reasonable fees, costs and expenses incurred by the Fiscal Agent and the Owners in connection with such default (including but not limited to the reasonable fees and expenses of their counsel and agents); second, to the payment of the Interest Components evidenced and represented by the Certificates accrued to the date of application thereof *pro rata* among the Owners entitled thereto; third, to the payment of the Principal Components evidenced and represented by the Certificates and the Prepayment Price, if any, then due under the Trust Agreement *pro rata* among the Owners entitled thereto; and fourth, when no Certificates remain Outstanding, to pay or reimburse the State for its costs and expenses, including reasonable attorneys' fees, incurred in connection with the Certificates, the Master Financing Agreements, the Financing Agreements, and the Trust Agreement.

***Non-Waiver.*** A waiver of any default or breach of duty or contract by the Fiscal Agent shall not affect any subsequent default or breach of duty or contract or impair any rights or remedies on any such subsequent default or breach of duty or contract. No delay or omission by the Fiscal Agent to exercise any right or remedy accruing upon any default or breach of duty or contract shall impair any such right or remedy or shall be construed to be a waiver of any such default or breach of duty or contract or an acquiescence therein, and every right or remedy conferred upon the Fiscal Agent by law or by such article may be enforced and exercised from time to time and as often as shall be deemed expedient by the Fiscal Agent.

If any action, proceeding or suit to enforce any right or to exercise any remedy is abandoned or determined adversely to the Fiscal Agent, the Fiscal Agent, the Corporation and the Treasurer shall be restored to their former positions, rights and remedies as if such action, proceeding or suit had not been brought or taken.

***Remedies Not Exclusive.*** No remedy in the Trust Agreement conferred upon or reserved to the Fiscal Agent is intended to be exclusive of any other remedy, and each such remedy shall be cumulative and shall be in addition to every other remedy given under the Trust Agreement or now or existing in law or in equity or by statute or otherwise and may be exercised without exhausting and without regard to any other remedy conferred by any law.

***Fiscal Agent May Enforce Claims Without Possession of Certificates.*** All rights of action and claims under the Trust Agreement or the Certificates may be prosecuted and enforced by the Fiscal Agent without the possession of any of the Certificates or the production thereof in any proceeding relating thereto, and any such proceeding instituted by the Fiscal Agent shall be brought in its own name as trustee of an express trust, and any recovery of judgment shall, after provision for the payment of the reasonable compensation, expenses, disbursements and advances of the Fiscal Agent, its agents and counsel, be for the ratable benefit of the Owners of the Certificates in respect of which such judgment has been recovered.

***Limitation on Actions by Owners.*** The Owners of not less than a majority in aggregate Principal Component evidenced and represented by the Certificates then Outstanding shall have the right to direct the method and place of conducting any proceeding or remedy available to the Fiscal Agent, or exercising any trust or power conferred on the Fiscal Agent, under the Trust Agreement or under the Master Financing Agreements in connection with the enforcement of the covenants, agreement, terms, and conditions of the Trust Agreement and thereof; *provided*, that any such direction shall not be contrary to law, the Trust Agreement or the Master Financing Agreements, and is not unduly prejudicial to the

interest of the Owners not joining in such direction; and *provided further*, that the Fiscal Agent may take any other action which it deems necessary or appropriate and not inconsistent with such direction.

No Owner shall have the right to institute any action, suit or proceeding for the enforcement of the Trust Agreement or of the Master Financing Agreements, or to pursue any remedy available under the Trust Agreement or under such Master Financing Agreements, unless:

(1) the Fiscal Agent shall have been given written notice of an Event of Default by such Owner;

(2) the Owners of at least a majority in aggregate Principal Component evidenced and represented by the Certificates then Outstanding respecting which there has been an Event of Default shall have requested the Trustee, in writing, to exercise the powers granted by the Trust Agreement or the Master Financing Agreements, or to institute such action, suit or proceeding, or to pursue such remedy in it or their name or names;

(3) the Fiscal Agent shall have been offered indemnity satisfactory to it against its costs, expenses and liabilities in connection therewith; and

(4) the Fiscal Agent shall have failed to comply with such request within 60 days, or such shorter period as shall be reasonable under the circumstances.

***No Liability by the Corporation to the Owners.*** Except for the observance and performance of the agreements and covenants required to be observed and performed by it contained in the Trust Agreement, the Corporation shall not have any obligation or liability to the Owners with respect to the Trust Agreement, or the payment when due of the State Payments by the State, or with respect to the observance or performance by the State of the other agreements and covenants required to be observed and performed by the State contained in the Master Financing Agreements or in the Trust Agreement, or with respect to preparation, execution, delivery, or transfer of the Certificates or the disbursement of the State Payments by the Fiscal Agent to the Owners, or with respect to the observance or performance by the Fiscal Agent of any agreements, covenants, terms or obligations required to be performed or observed by it contained in the Trust Agreement.

***No Liability by the State to the Owners.*** Except for the payment when due of the State Payments and the observance and performance of the other agreements and covenants required to be observed and performed by it contained in the Master Financing Agreements and in the Trust Agreement, the State shall not have any obligation or liability to the Owners with respect to the Trust Agreement, or the preparation, execution, delivery or transfer of the Certificates or the disbursement of the State Payments by the Fiscal Agent to the Owners, or with respect to the observance or performance by the Fiscal Agent of any agreements, covenants, terms or obligations required to be observed or performed by it contained in the Trust Agreement.

***No Liability by the Fiscal Agent to the Owners.*** Except as expressly provided in the Trust Agreement, the Fiscal Agent shall not have any obligation or liability to the Owners with respect to the payment when due of the State Payments by the State, with respect to the observance or performance by the State of the other agreements and covenants required to be observed and performed by it contained in the Master Financing Agreements or in the Trust Agreement or with respect to the observance or performance by the Corporation of the agreements and covenants required to be observed and performed by it contained in the Trust Agreement.

**Amendment or Supplement of Trust Agreement**

***Amendment or Supplement; Consents.*** The Trust Agreement and the rights and obligations of the State, the Owners, the Fiscal Agent or any Paying Agent under the Trust Agreement may be amended or supplemented at any time as provided in the Appendix of the Trust Agreement. No such amendment or supplement shall:

(1) extend the stated Principal Payment Date of any Certificate, or reduce the rate of interest evidenced and represented thereby, or extend the time of payment of such interest, or reduce the amount of the Principal Component evidenced and represented thereby, or reduce any Prepayment Price evidenced and represented thereby, without the prior written consent of the Owner of the Certificate so affected; or

(2) reduce the percentage of Owners whose consent is required for the execution of any amendment of the Trust Agreement or supplement thereto; or

(3) modify any of the rights or obligations of the Fiscal Agent or any Paying Agent without its prior written consent thereto.

***Disqualified Certificates.*** Certificates owned or held by or for the account of the State (but excluding Certificates held in any pension or retirement fund of the State) or any Agency shall not be deemed Outstanding for the purpose of any consent or other action or any calculation of Outstanding Certificates provided in the Trust Agreement, and shall not be entitled to consent to or take any other action provided in the Trust Agreement, except that in determining whether the Fiscal Agent shall be protected in relying upon any consent or other actions of an Owner, or in calculating Outstanding Certificates under the Trust agreement, only Certificates which the Fiscal Agent actually knows to be owned or held by or for the account of the State or any Agency shall be disregarded unless all Certificates are so owned or held by or for the account of the State or any Agency, in which case such Certificates shall be considered Outstanding for the purpose of such determination. The Fiscal Agent may adopt appropriate regulations to require each Owner, before consent provided for in the Trust Agreement shall be deemed effective, to reveal if the Certificates as to which such consent is given are disqualified as provided in the Trust Agreement.

***Endorsement or Replacement of Certificates After Amendment or Supplement.*** After the effective date of any action taken as provided above, the Fiscal Agent may determine that the Certificates may bear a notation by endorsement in a form approved by the Fiscal Agent as to such action, and in that case upon demand of the Owner of any Outstanding Certificate and presentation of such Owner's Certificate for such purpose at the Principal Office of the Fiscal Agent a suitable notation as to such action shall be made on such Certificate. If the Fiscal Agent shall so determine, new Certificates so modified as in the opinion of the Fiscal Agent shall be necessary to conform to such action shall be prepared, and in that case upon demand of the Owner of any Outstanding Certificates such new Certificates shall be exchanged at the Principal Office of the Fiscal Agent without cost to each Owner for Certificates then Outstanding upon surrender of such Outstanding Certificates.

***Amendment by Mutual Consent.*** The amendment provisions of the Trust Agreement shall not prevent any Owner from accepting any amendment to the particular Certificates held by it; provided, that due notation thereof is made on such Certificates.

**Defeasance of Certificates; Discharge of Trust Agreement**

***Discharge of Trust Agreement.*** When the obligations of the State under the Master Financing Agreements shall cease (except for the right of the Fiscal Agent and the obligation of the State to have the money and Qualified Investments referenced therein applied to the payment of State Payments as therein set forth), then and in that case the obligations created by the Trust Agreement shall thereupon cease, terminate, become void and be completely discharged except for the right of the Owners and the obligation of the Fiscal Agent to apply such moneys and Qualified Investments to the payment of the Certificates as in the Trust Agreement set forth and the right of the Fiscal Agent to collect any fees or expenses due or indemnities provided by Owners under the Trust Agreement. The Fiscal Agent shall turn over to the Treasurer, as an overpayment of State Payments, any surplus in the Certificate Fund and all balances remaining in any other funds or accounts other than moneys and Qualified Investments held for the payment of the Certificates on the Principal Payment Dates or Prepayment Dates thereof, which moneys and Qualified Investments shall continue to be held by the Fiscal Agent in trust for the benefit of the Owners and shall be applied by the Fiscal Agent to the payment, when due, of the principal, Prepayment Price and interest evidenced and represented by the Certificates, and after such payment, the Trust Agreement shall become void. The Fiscal Agent shall thereafter execute and deliver to the State such other documents and instruments as may be necessary or desirable, as requested by or on behalf of the State, to evidence such discharge and satisfaction of the Trust Agreement.

***Defeasance of Certificates.*** Any Outstanding Certificates shall be deemed to have been paid with the meaning and effect expressed in the immediately preceding paragraph if there shall be irrevocably deposited and held in trust by the Fiscal Agent moneys or Qualified Investments in the amount necessary to pay or prepay the principal or Prepayment Price and interest evidenced and represented thereby as provided in the Trust Agreement.

***Notice of Defeasance.*** If moneys or Qualified Investments are deposited with and held by the Fiscal Agent as described above, the Fiscal Agent shall within 30 days after such moneys or Qualified Investments shall have been deposited with it, mail a notice, first class postage prepaid, to the Owners of the Certificates that have been defeased at the addresses listed on the registration books kept by the Fiscal Agent pursuant to the Trust Agreement, setting forth (1) the date or dates fixed for payment or prepayment of the Certificates, (2) a description of the moneys or Qualified Investments so held by it, and (3) that such Certificates have been defeased and are no longer deemed to be Outstanding under the Trust Agreement, and/or that the Trust Agreement has been released and discharged in accordance with the provisions of the Trust Agreement.

***Deposit of Money or Securities with Fiscal Agent.*** Whenever in the Trust Agreement or the Master Financing Agreements it is provided or permitted that there be deposited with or held in trust by the Fiscal Agent money and/or securities (such money and/or securities certified to be sufficient by a report of an independent certified public accountant or firm of accountants, or an independent financial advisor or consultant or firm of such advisors or consultants) in the necessary amount to pay or prepay the principal and interest evidenced and represented by all or a portion of the Certificates, the money or securities to be so deposited or held may include money or securities held by the Fiscal Agent in the funds and accounts established pursuant to the Trust Agreement and shall be:

(1) lawful money of the United States of America in an amount equal to the principal amount evidenced and represented by such Certificates and all unpaid interest evidenced and represented thereby to the respective Principal Payment Dates thereof, except that, in the case of Certificates which are to be prepaid prior to their respective Principal Payment Dates and in respect of which notice of such prepayment shall have been given as in the Trust Agreement provided or provision satisfactory to the Fiscal Agent shall have been made for the giving of such notice, the amount to

be deposited or held shall be the Prepayment Price plus accrued interest to such date of prepayment, if any, evidenced and represented by such Certificates; or

(2) Government Obligations, the principal of and interest on which when due will provide money sufficient, without reinvestment, to pay the principal or Prepayment Price, and accrued interest to the Principal Payment Date or to the Prepayment Date, as the case may be, evidenced and represented by the Certificates to be paid or prepaid, as such amounts become due; *provided that*, in the case of Certificates which are to be prepaid prior to the Principal Payment Date thereof, notice of such prepayment shall have been given as in the Trust Agreement provided or provision satisfactory to the Fiscal Agent shall have been made for the giving of such notice;

*further provided*, in each case, that the Fiscal Agent shall have been irrevocably instructed (by the terms of the Trust Agreement and the Master Financing Agreements or by Written Request of the State Treasurer) to apply such money to the payment of such principal, Prepayment Price and interest, if any, evidenced and represented by such Certificates.

***Unclaimed Moneys.*** Any moneys held by the Fiscal Agent in trust for the payment and discharge of the principal, Prepayment Price or interest evidenced and represented by any of the Certificates which remain unclaimed for two years after the date when the principal, Prepayment Price or interest evidenced and represented by such Certificates have become payable, shall at the Written Request of the State Treasurer be repaid by the Fiscal Agent (without liability for interest) to the Treasurer as its property free from trust, and the Fiscal Agent shall thereupon be released and discharged with respect thereto and the Owners shall look only to the Treasurer for the payment of the principal, Prepayment Price or interest evidenced and represented by such Certificates.

**Miscellaneous**

***Funds and Accounts.*** Any fund required to be established and maintained in the Trust Agreement by the Fiscal Agent or the Treasurer may be established and maintained in the accounting records of the Fiscal Agent or the Treasurer, respectively, either as an account or a fund, and may, for the purposes of such accounting records, any audits thereof, and any reports or statements with respect thereto, be treated either as an account or a fund; but all such records with respect to all such funds shall at all times be maintained in accordance with prudent accounting practice and with due regard for the protection of the security of the Certificates and the right of the Owners.

***Notices to Rating Agencies.*** The Fiscal Agent shall provide to each Rating Agency then rating the Certificates prompt written notice of (1) the appointment of any successor Fiscal Agent or Paying Agent; (2) any amendment to the Trust Agreement or the Master Financing Agreements; (3) any prepayment of the Certificates; and (4) any defeasance or discharge of the Certificates or the Trust Agreement.

## MASTER ASSIGNMENT (REAL PROPERTY)

**Assignment**

The Corporation unconditionally grants, sells, assigns, transfers and conveys to the Fiscal Agent without recourse (1) all of its rights to the Sites pursuant to the Site Leases; (2) all of its rights to receive the Base Rent Payments and any Additional Rent under and pursuant to the Master Financing Lease; (3) its right to take all actions, exercise all remedies, and give all consents under and pursuant to the Site Leases and the Master Financing Lease; (4) all of its remaining right, title and interest in, to and under the Site Leases, the Master Financing Lease, and the Financing Leases, and in and to the Property and any rents or profits generated therefrom; and (5) its right of access more particularly described in the Master Financing Lease.

**Acceptance**

The Fiscal Agent accepts the grant, sale, assignment, transfer and conveyance for the benefit of the Owners of the Certificates, subject to the conditions and terms of the Trust Agreement, and all such Base Rent Payments and Additional Rent shall be applied and all of such right, title and interest shall be exercised by the Fiscal Agent as provided in the Trust Agreement. The Fiscal Agent agrees to keep, perform and observe all of the terms, conditions, covenants and agreements under the Site Leases and the Master Financing Lease from and after the Dated Date.

**Acknowledgement**

The Fiscal Agent and the Corporation acknowledge and agree that: (1) such grant, sale, assignment, transfer and conveyance by the Corporation is intended to be a true sale of the Corporation's right, title and interest in, to and under the Site Leases, the Master Financing Lease and in and to the Property; (2) the Corporation shall cease to have any rights, duties or obligations under the Site Leases, the Master Financing Lease or with respect to the Property; (3) the Fiscal Agent shall have all the rights, duties and obligations of the Corporation thereunder as if the Fiscal Agent had been the original party thereto; and (4) except where the context otherwise requires, every reference in the Site Leases and the Master Financing Lease to the Corporation shall be deemed and construed to refer to the Fiscal Agent.

## MASTER ASSIGNMENT (EQUIPMENT)

**Assignment**

The Corporation unconditionally grants, sells, assigns, transfers and conveys to the Fiscal Agent without recourse (1) all of its rights to receive the Installment Payments under and pursuant to the Master Financing Contract, and (2) all of its remaining right, title and interest in, to and under the Master Financing Contract, the Agency Financing Contracts, and in and to the Property (including any security interest therein), including but not limited to its right to take all actions and exercise all remedies under and pursuant to the Master Financing Contract.

**Acceptance**

The Fiscal Agent accepts the grant, sale, assignment, transfer and conveyance for the benefit of the Owners of the Certificates, subject to the conditions and terms of the Trust Agreement, and all such Installment Payments shall be applied and all of such right, title and interest shall be exercised by the Fiscal Agent as provided in the Trust Agreement. The Fiscal Agent agrees to keep, perform and observe all of the terms, conditions, covenants and agreements under the Master Financing Contract from and after the Dated Date.

**Acknowledgement**

The Fiscal Agent and the Corporation acknowledge and agree that: (1) such grant, sale, assignment, transfer and conveyance by the Corporation is intended to be a true sale of the Corporation's right, title and interest in, to and under the Master Financing Contract and in and to the Property; (2) the Corporation shall cease to have any rights, duties or obligations under the Master Financing Contract or with respect to the Property; (3) the Fiscal Agent shall have all the rights, duties and obligations of the Corporation thereunder as if the Fiscal Agent had been the original party thereto; and (4) every reference in the Master Financing Contract to the Corporation shall be deemed and construed to refer to the Fiscal Agent, except where the context otherwise requires.

## SITE LEASES

### Lease of the Site; Ownership

Under each Site Lease, the Agency leases to the Corporation and the Corporation hires from the Agency the real property and all improvements thereon described in the Site Lease, subject to all easements, covenants, conditions and restrictions existing as of the Dated Date. Under each Site Lease, the Agency represents and warrants that it is the owner in fee of or the owner of a leasehold interest in the Site, as applicable, subject only to Permitted Encumbrances.

### Term

The term of each Site Lease commences on the Dated Date, and ends on the termination date of the related Financing Lease, unless such term is extended or sooner terminated. If on such date, the Financing Lease shall not be discharged by its terms, then the term of the Site Lease shall be extended until 10 days after all amounts due under the Financing Lease shall have been paid and the Financing Lease shall have been discharged by its terms, except that the term of the Site Lease shall in no event be extended beyond five years after the term date indicated by the Agency. If, prior to scheduled termination date of the Site Lease, all amounts due under the Financing Lease shall have been paid and the Financing Lease shall have been discharged by its terms, the term of the Site Lease shall end 10 days thereafter or 10 days after written notice by such Agency to the Corporation, whichever is earlier.

### Assignments and Subleases

Under each Site Lease, the Corporation is not permitted to grant, sell, assign, mortgage, pledge, sublet or transfer any of its right, title or interest in, to or under the Site Lease or the Site except as expressly provided in the Master Assignment, the Master Financing Lease and the related Financing Lease, without the prior written consent of the Agency. Each Local Agency consents to the sublease of the applicable Property pursuant to the Master Financing Lease, and the assignment of the Corporation's right, title and interest under the Site Lease to the Fiscal Agent pursuant to the Master Assignment for the benefit of the Owners of the Certificates. Each State Agency consents to the sublease of the applicable Property pursuant to its related State Agency Finance Lease Addendum, and the assignment of the Corporation's right, title and interest under the Site Lease to the Fiscal Agent pursuant to the Master Assignment for the benefit of the Owners of the Certificates.

Upon the occurrence and continuance of an Event of Default or Permitted Termination Event with respect to the applicable Property, the Corporation has the right, pursuant to the Master Assignment, the Trust Agreement, the Master Financing Lease and each State Agency Financing Lease Addendum, to sublease all or any portion of such Property; provided, that the subtenant and the terms and provisions of the sublease shall be subject to the prior written approval of the Agency, which approval shall not be unreasonably withheld or delayed.

### Eminent Domain; Loss of Title

In the event the whole or any part of the applicable Property is taken permanently or temporarily under the power of eminent domain (or sold under threat of condemnation), or there is a loss of title to the whole or any part of such Property, the interest of the Corporation in such Property shall be recognized and is determined to be an amount not less than the then unpaid indebtedness incurred by each Agency under its Financing Lease. The term "unpaid indebtedness" includes all unpaid Agency Principal Components, Agency Interest Components and all other payments required to be made by an Agency pursuant to its Financing Lease. The amount of any such award, judgment or payment shall be paid by

the Corporation, and the balance, if any, in excess of the unpaid indebtedness shall be paid to the respective Agency.

## FINANCING LEASES

### Appointment of Agents; Changes to the Project; Additions to Property; Substitution and Release of Property

***Appointment of Agents.*** The Agency ratifies, approves and confirms, and accepts and agrees to, its designation and appointment as agent of the Corporation in connection with the refinancing of the Property.

***Changes to the Project; Additions to the Property.*** The Agency, with the prior written consent of the Treasurer, may revise the Project to be acquired, constructed, financed or refinanced pursuant the Financing Lease; provided, that: (1) such Project as so revised shall satisfy the requirements under the Financing Lease with respect to the substitution of Property; (2) the Project Costs shall not be materially reduced thereby; and (3) any such revision shall not relieve the Agency of any obligation to design, acquire, construct, finance or refinance the Project or the Property in accordance therewith. The appointment of a Local Agency as agent of the Corporation in connection with the design, acquisition and/or construction of a Project is made and conferred irrevocably by the Corporation, and shall not be terminated by any act of the Local Agency, the Treasurer or otherwise.

Each Agency shall have the right during the term of its Financing Lease, at its cost and expense, to make additions, betterments and improvements to the Property, and to attach fixtures, structures and signs thereto; *provided*, that such additions, betterments and improvements and fixtures, structures and signs (1) shall be constructed and installed in accordance with applicable laws and regulations, and not in violation of any easements, restrictions, conditions or covenants affecting title to the Property; and (2) shall not diminish the value, capacity or usefulness of the Property.

The Agency also shall have the right during the term of the Financing Lease, without the consent of any Owners, to enter into Additional State Agency Financing Lease Addenda or Additional Local Agency Financing Leases, as applicable (each an "Additional Financing Lease"), and Additional Site Leases with the Corporation to finance all or any portion of the cost of such additions, betterments and improvements to the Property so long as such leases do not reduce the obligation of the State to perform its obligations under the Master Financing Lease, including without limitation its obligation to make Base Rent Payments, and will not, in an Opinion of Counsel, adversely affect the tax-exempt status of the Interest Component of Base Rent Payments evidenced and represented by the Certificates. If the Agency enters into any Additional Financing Lease for this purpose, the Corporation may be granted an interest in the Property under an Additional Site Lease of all or any portion of the Property, which leasehold interest may be assigned to the Fiscal Agent for the benefit of owners of certificates of participation in the Additional Master Financing Lease to which such Additional Financing Lease is related. The occurrence of an Event of Default or Permitted Termination Event with respect to the Financing Lease shall constitute a like event under any Additional Financing Lease, and the occurrence of any such like event under any Additional Financing Lease shall constitute an Event of Default or Permitted Termination Event, as the case may be, under the Financing Lease. The owners of certificates of participation in any Additional Master Financing Lease shall be secured *pari passu* with the Owners with respect to any amounts received by the Fiscal Agent with respect to the Property following the occurrence of an Event of Default or Permitted Termination Event.

***Substitution of Property.*** After design, acquisition, construction, financing or refinancing of the Project or the Property, the Agency, with the prior written consent of the Treasurer and only upon the satisfaction

of the requirements set forth in the Master Financing Lease, may substitute for the Property, another parcel or parcels of real property. As a condition to any such substitution, the Agency shall deliver to the Treasurer:

(1) an appraisal or other written evidence from an independent, disinterested real property appraiser acceptable to the Treasurer and the Fiscal Agent to the effect that such substitute Property has an estimated fair rental value for the remaining term of the Financing Lease equal to or greater than the Agency Rent Payments due under the Financing Lease from time to time thereafter; and

(2) a certificate of the Agency to the effect that such substitute Property (a) is free and clear of any mortgages, deeds of trust, liens or other similar encumbrances, other than Permitted Encumbrances, and (b) is essential to the Agency's ability to carry out its governmental functions and responsibilities.

The Treasurer, the Fiscal Agent, as assignee of the Corporation, and the Agency shall execute, deliver and record such amendments and modifications to the Site Lease, the Master Financing Lease, the Master Assignment, and the Financing Lease, and such other documents, agreements and instruments, as the Treasurer or the Fiscal Agent deems necessary or desirable in connection with such substitution.

***Release of Property.*** After design, acquisition, construction, financing or refinancing of the Project, the Agency, with the prior written consent of the Treasurer and only upon the satisfaction of the requirements set forth in the Master Financing Lease, may release a portion of the Property leased under the Site Lease, and subleased under and pursuant to the Master Financing Lease and the Financing Lease. As a condition to any such release, the Agency shall:

(1) deliver to the Treasurer an appraisal or other written evidence from an independent, disinterested real property appraiser acceptable to the Treasurer and the Fiscal Agent to the effect that the remaining portion of the Property has an estimated fair rental value for the remaining term of the Financing Lease equal to or greater than the Agency Rent Payments due from time to time under the Financing Lease; and

(2) provide any necessary easements, reciprocal agreements or other rights as may be necessary to provide comparable pedestrian and vehicular access, and other uses and amenities (including but not limited to water, sewer, electrical, gas, telephone and other utilities) as existed prior to such release.

The Treasurer, the Fiscal Agent, as assignee of the Corporation, and the Agency shall execute, deliver and record such amendments and modifications to the Site Lease, the Master Financing Lease, the Master Assignment and the Financing Lease, and such other documents, agreements and instruments, as the Treasurer or the Fiscal Agent deems necessary or desirable in connection with such release.

**Title to the Property**

Fee title to or ownership of a leasehold interest in the Property, as applicable, and all additions, modifications, repairs and improvements thereto, shall remain and vest in the Agency, subject to the respective leasehold estates under the Site Lease, the Master Financing Lease and the Financing Lease, without any further action by the State, the Agency or the Corporation.

**Assignment**

In order to secure the payment and performance of the State of its obligations under the Master Financing Lease, the State has assigned and transferred to the Corporation the State's interest in each Agency Financing Lease and the rentals, income and profits therefrom, including without limitation the Agency Rent Payments. Each Agency acknowledges and agrees to such assignment and transfer. The Treasurer irrevocably authorizes and directs an Agency, upon receipt of written notice from the Fiscal Agent, as assignee of the Corporation, that an Event of Default has occurred and is continuing, to pay to the Fiscal Agent the Agency Rent Payments and other amounts due and to become due under its Financing Lease. The Treasurer shall not have any right or claim against such Agency for any Agency Rent Payments or other amounts so paid by the Agency to the Fiscal Agent.

**Disclaimer of Warranties**

Each Agency acknowledges and agrees that it has had adequate opportunity to inspect the Property, and that such Property, including but not limited to the structures and improvements thereon, is acceptable to the Agency in its present condition. Such Agency subleases the Property in its present condition, "as is." THE CORPORATION AND THE STATE MAKE NO WARRANTY OR REPRESENTATION, EITHER EXPRESS OR IMPLIED, AND ASSUMES NO RESPONSIBILITY, LIABILITY OR OBLIGATION, AS TO THE VALUE, DESIGN, STRUCTURAL OR OTHER CONDITION, USE, USABILITY, SUITABILITY, OCCUPANCY OR MANAGEMENT OF THE PROPERTY, AS TO THE INCOME FROM OR EXPENSE OF THE USE OR OPERATION THEREOF, AS TO TITLE TO THE PROPERTY, AS TO COMPLIANCE WITH APPLICABLE ZONING, SUBDIVISION, PLANNING, SAFETY, FIRE, HEALTH OR ENVIRONMENTAL LAWS, REGULATIONS, ORDINANCES, CODES OR REQUIREMENTS, OR AS TO COMPLIANCE WITH APPLICABLE COVENANTS, CONDITIONS OR RESTRICTIONS, OR ANY OTHER REPRESENTATION OR WARRANTY WITH RESPECT TO THE PROPERTY.

**Agency Rent Payments**

Each Agency Rent Payment shall consist of an Agency Principal Component and/or an Agency Interest Component as set forth in an exhibit to the Financing Lease. Interest shall accrue and be calculated as provided in the Trust Agreement. Each Agency Rent Payment payable under the Financing Lease shall be paid by electronic funds transfer in lawful money of the United States of America. Payments of Additional Rent shall be made to or upon the order of the Corporation. Each Agency Rent Payment shall be applied first to the Agency Interest Component due under the Financing Lease, and then to the Agency Principal Component due under the Financing Lease.

The Corporation directs the Treasurer, and the Treasurer agrees to transfer all Agency Rent Payments directly to the Fiscal Agent, as assignee of the Corporation; provided, however, that the Treasurer is not thereby agreeing to obligate its funds to make Agency Rent Payments.

Such payments of Agency Rent Payments and Additional Rent for each rental payment period during the term of the Financing Lease shall constitute the total rental due for such period, and shall be paid for and in consideration of the use and occupancy and continued quiet enjoyment of the Property for such period. The Parties to the Financing Lease have determined and agreed that such total rental does not exceed the fair rental value of the Property for each such rental period, given the purposes, terms and provisions of the Financing Lease. Anything in the Financing Lease to the contrary notwithstanding, the Agency waives any right that it may have under the laws of the State to a rebate or repayment of any portion of such rental in the event that there is substantial interference with the use or right to possession by the

Agency of the Property or any portion thereof as a result of material damage, destruction or condemnation.

**Sources of Payment of Agency Rent Payments**

***State Agency Financing Lease Addendum.*** Each State Agency acknowledges and agrees that the State is subleasing the respective Property from the Corporation for and on behalf of the State Agency. Concurrently with the execution of the State Agency Financing Lease Addendum, the State shall execute and deliver (1) the Master Financing Lease with the Corporation, pursuant to which the State shall agree to make Base Rent Payments for the sublease of the Property for and on behalf of the State Agency, at such times and in such amounts as provided therein; and (2) the State Agency Financing Lease Addendum, pursuant to which the State Agency shall agree to sublease its Property and to make Agency Rent Payments therefor, at such times and in such amounts as provided therein. Such Agency Rent Payments shall be an amount sufficient in the aggregate to pay the Agency Rent Payment of the Property to be subleased by the State from the Corporation for and on behalf of the State Agency under the Master Financing Lease.

***Obligation of State Agency Subject to Appropriation.*** That portion of the Base Rent Payments that is allocable to the Agency Rent Payments of the State Agency shall be payable by the State solely from Agency Rent Payments to be made by the State Agency. The obligation of the State Agency to make its Agency Rent Payments shall be subject to appropriation by the State Legislature and to Executive Order reduction. The State shall not be obligated to pay that portion of the Base Rent Payments that is allocable to the Agency Rent Payments of the State Agency and interest thereon other than from appropriated funds of the State Agency.

***Local Agency Financing Lease.*** Each Local Agency acknowledges and agrees that the State is subleasing the respective Property from the Corporation for and on behalf of such Local Agency. Concurrently with the execution of each Local Agency Financing Lease, the State shall execute and deliver (1) the Master Financing Lease with the Corporation, pursuant to which the State shall agree to make Base Rent Payments for the sublease of the Property for and on behalf of the corresponding Local Agency, at such times and in such amounts as provided therein; and (2) the Local Agency Financing Lease with each Local Agency, pursuant to which such Local Agency shall agree to sublease its Property and to make Agency Rent Payments therefor, at such times and in such amounts as provided therein. Such Agency Rent Payments shall be an amount sufficient in the aggregate to pay the Agency Rent Payment of the Property to be subleased by the State from the Corporation for and on behalf of each Local Agency under the Master Financing Lease.

The portion of the Base Rent Payments allocable to each Local Agency is payable by the State solely from Agency Rent Payments to be made by such Local Agency, except as otherwise provided in the Master Financing Lease. The obligation of each Local Agency to make its Agency Rent Payments is a direct and general obligation of such Local Agency to which the full faith and credit of such Local Agency is pledged. The State shall not be obligated to pay the Base Rent Payments allocable to each Local Agency other than from Agency Rent Payments paid by such Local Agency, except as otherwise provided in the Master Financing Lease.

***Intercept of Local Agency Share of State Revenues.*** In the event that a Local Agency fails to make any payment due under its Local Agency Financing Lease, the Treasurer shall withhold an amount sufficient to make such payment from such Local Agency's share of State revenues or other amounts authorized or required by law to be distributed by the State to such Local Agency, including but not limited to leasehold excise taxes, sales and use taxes, excise taxes, property taxes and liquor control board receipts; provided, that the use of any such revenues or amounts to make such payments is otherwise authorized or permitted

by State law. Such withholding shall continue until all such delinquent payments have been made. Amounts withheld by the Treasurer shall be applied to make any such payment due under the corresponding Local Agency Financing Lease on behalf of such Local Agency, or to reimburse the Treasurer for any such payment made pursuant to such Local Agency Financing Lease. Each Local Agency authorizes, approves and consents to any such withholding.

***Conditional Payment of Agency Rent Payments.*** Upon the failure of any Local Agency to make any Agency Rent Payment at such time and in such amount as required pursuant to the corresponding Local Agency Financing Lease, the Treasurer shall, to the extent of legally available appropriated funds and subject to any Executive Order reduction, make such payment into the Agency Rent Payment Fund, defined below, on behalf of such Local Agency within 10 Business Days after such Agency Rent Payment Date. Such Local Agency shall reimburse the State for such payments made on its behalf immediately thereafter and in any case not later than 10 Business Days after such Agency Rent Payment Date, together with interest thereon at a rate equal to the State Reimbursement Rate. Anything in the Local Agency Financing Lease to the contrary notwithstanding, failure of such Local Agency to reimburse the Treasurer for any such payment shall not constitute an Agency Event of Default under such Local Agency Financing Lease, but the State may institute such legal action and pursue such other remedies against such Local Agency as the State deems necessary or desirable including but not limited to actions for specific performance, injunction and/or the recovery of damages.

***Payments by Local Agency Treasurer.*** The treasurer of each Local Agency is authorized and directed to establish and/or maintain a special fund in the "bonds payable" category of accounts of such Local Agency for the purposes of paying such Local Agency's Agency Rent Payments and Additional Rent. The treasurer of such Local Agency is further authorized and directed to remit each payment of Agency Rent Payments to the Treasurer or its assignee on each Agency Rent Payment Date and any Additional Rent when due under the corresponding Local Agency Financing Lease. Such payment shall be made from any legally available funds of such Local Agency.

**Deposit and Investment of Agency Rent Payments**

Each Local Agency acknowledges and agrees that the Agency Rent Payments shall be deposited in a special fund or funds maintained by the Treasurer (the "Agency Rent Payment Fund"). The Agency Rent Payments due on each Agency Rent Payment Date shall be at least sufficient, in the aggregate, to make the Base Rent Payment next coming due under the Master Financing Lease. Amounts in the Agency Rent Payment Fund, including investment earnings thereon, shall be used and applied, first, to make the Base Rent Payment next coming due, and thereafter, but prior to the next Agency Rent Payment Date, to the extent that amounts remain in such Fund after such Base Rent Payment is made, to pay Additional Rent or for any other lawful purpose of the Treasurer. Amounts in the Agency Rent Payment Fund shall be invested in the Qualified Investments, and shall be separately accounted for, but may be commingled with other moneys on deposit with the Treasurer solely for investment purposes. The Agencies shall have no right, title or interest in or to the amounts on deposit from time to time in the Agency Rent Payment Fund.

**Net Lease**

The obligation of each Local Agency to make Agency Rent Payments from the sources set forth in the corresponding Local Agency Financing Lease and to perform its other obligations under such Local Agency Financing Lease shall be absolute and unconditional. Each Local Agency Financing Lease shall be deemed and construed to be a "triple net lease," and the corresponding Local Agency shall pay absolutely net during the term of such Local Agency Financing Lease the Agency Rent Payments, Additional Rent and all other amounts due under such Local Agency Financing Lease, without notice or demand, and free of any charges, assessments, Impositions or deductions whatsoever, and without any

diminution, reduction, postponement, abatement, counterclaim, defense or set-off as a result of any dispute, claim or right of action by, against among such Local Agency, the State, the Corporation, the Fiscal Agent, and/or any other Person, or for any other reason; provided, that nothing in the Local Agency Financing Lease shall be construed to release or excuse the State from the observance or performance of its obligations under such Local Agency Financing Lease. If the State shall fail to observe or perform any such obligation, such Local Agency may institute such legal action and pursue such other remedies against the State as such Local Agency deems necessary or desirable, including, but not limited to actions for specific performance, injunction and/or the recovery of damages.

Each State Agency Financing Lease Addendum shall be deemed and construed to be a "triple net lease," and the State shall pay absolutely net during its term the Agency Rent Payments, Additional Rent and all other amounts due thereunder, without notice or demand, and free of any charges, assessments, Impositions or deductions whatsoever, and without any diminution, reduction, postponement, abatement, counterclaim, defense or set-off as a result of any dispute, claim or right of action by, against or among the State, the Corporation, the Fiscal Agent, the State Agency, and/or any other Person, or for any other reason; provided, that nothing in such provision shall be construed to release or excuse the Corporation from the observance or performance of its obligations thereunder. If the Corporation shall fail to observe or perform any such obligation, the State may institute such legal action and pursue such other remedies against the Corporation as the State deems necessary or desirable, including, but not limited to actions for specific performance, injunction and/or the recovery of damages.

**Assignments by the Corporation**

Each Local Agency acknowledges and agrees that, concurrently with the execution and delivery of the corresponding Local Agency Financing Lease, the Corporation will unconditionally grant, sell, assign, transfer and convey to the Fiscal Agent pursuant to the Master Assignment, without recourse:

(1) all of its rights to the Site pursuant to the Site Lease,

(2) all of its rights to receive the Base Rent Payments and any Additional Rent under and pursuant to the Master Financing Lease;

(3) its right to take all actions, exercise all remedies, and give all consents under and pursuant to the Site Lease and the Master Financing Lease;

(4) all of its remaining right, title and interest in, to and under the Site Lease, the Master Financing Lease, and its Local Agency Financing Lease, and in and to the Property (including any security interest in each Local Agency Financing Lease) and any rents or profits generated therefrom; and

(5) its right of access more particularly described in the Master Financing Lease, all in consideration for the payment by the Fiscal Agent to the Treasurer, as agent of the Corporation, of the proceeds of the sale of the Certificates.

The Treasurer and the Corporation have acknowledged and agreed that such grant, sale, assignment, transfer and conveyance by the Corporation is intended to be a true sale of the Corporation's right, title and interest, and that upon such grant, sale, assignment, transfer and conveyance, the Corporation shall cease to have any rights, duties or obligations under the Site Leases, the Master Financing Lease and the Financing Leases, or with respect to the Property, and the Fiscal Agent shall thereafter have all the rights, duties and obligations of the Corporation under each Local Agency Financing Lease as if the Fiscal Agent had been the original party thereto, and, except where the context otherwise requires, every reference in each Local Agency Financing Lease to the Corporation shall be deemed and construed to refer to the

Fiscal Agent. Anything in each Local Agency Financing Lease to the contrary notwithstanding, such grant, sale, assignment, transfer and conveyance shall not confer any rights or impose any duties or obligations on the Fiscal Agent other than as expressly set forth in the Trust Agreement and the Master Assignment.

Concurrently with the execution and delivery of each State Agency Financing Lease Addenda, the Corporation will unconditionally grant, sell, assign, transfer and convey to the Fiscal Agent pursuant to the Master Assignment, without recourse:

(1) all of its rights to the Site pursuant to the Site Lease,

(2) all of its rights to receive the Agency Rent Payments and any Additional Rent under and pursuant to the State Agency Financing Lease Addenda;

(3) its right to take all actions, exercise all remedies, and give all consents under and pursuant to the Site Lease and the State Agency Financing Lease Addenda;

(4) all of its remaining right, title and interest in, to and under the Site Lease and the State Agency Financing Lease Addenda, and in and to the Property (including any security interest therein) and any rents or profits generated therefrom; and

(5) its right of access more particularly described in the State Agency Financing Lease Addenda, all in consideration for the payment by the Fiscal Agent to the Treasurer, as agent of the Corporation, of the proceeds of the sale of the Certificates.

The Treasurer, the State Agency and the Corporation have acknowledged and agreed that such grant, sale, assignment, transfer and conveyance by the Corporation is intended to be a true sale of the Corporation's right, title and interest, and that upon such grant, sale, assignment, transfer and conveyance, the Corporation shall cease to have any rights, duties or obligations under the Site Leases or the State Agency Financing Lease Addenda, or with respect to the Property, and the Fiscal Agent shall thereafter have all the rights, duties and obligations of the Corporation under the State Agency Financing Lease Addenda as if the Fiscal Agent had been the original party thereto, and, except where the context otherwise requires, every reference in the State Agency Financing Lease Addenda to the Corporation shall be deemed and construed to refer to the Fiscal Agent, except where the context otherwise requires. Anything in the State Agency Financing Lease Addenda to the contrary notwithstanding, such grant, sale, assignment, transfer and conveyance shall not confer any rights or impose any duties or obligations on the Fiscal Agent other than as expressly set forth in the Trust Agreement.

**Optional Prepayment**

The Agency may, at its option, prepay all or any portion of its Agency Rent Payments then unpaid, in whole or in part on any date, by causing to be deposited with the Treasurer money and/or Government Obligations in an amount sufficient for the Treasurer to prepay or defease the portion of its Base Rent Payments corresponding thereto in accordance with the Master Financing Lease and to pay any Additional Rent in connection therewith.

The Agency shall provide the Treasurer with not less than 60 days' prior written notice of its intention to prepay any of its Agency Rent Payments which notice shall specify the date of prepayment, and the amount and the Agency Rent Payment Dates of the Agency Rent Payments to be prepaid. The Treasurer shall notify the Agency within 15 Business Days after receipt of such notice from the Agency as to the amount required to be paid in connection with such prepayment or defeasance of the corresponding Base

Rent Payments, including any Additional Rent in connection therewith. The determination by the Treasurer of the amount to be paid by the Agency shall be binding and conclusive against the Agency, absent manifest error.

**Mandatory Prepayment; Special Prepayment**

***Eminent Domain; Loss of Title.*** The Agency shall prepay or cause to be prepaid from eminent domain awards or sale proceeds received pursuant to the Financing Lease, and from the net proceeds of title insurance received pursuant to the Financing Lease, the Agency Rent Payments then unpaid, in whole or in part on any date, so that the aggregate annual Agency Rent Payments for the related Property from and after such prepayment date shall be in approximately equal amounts, at a Prepayment Price equal to the sum of the Agency Rent Payments so prepaid, without premium, plus accrued interest evidenced and represented thereby to the date of prepayment.

***Insurance Proceeds.*** The Agency may, at its option, prepay or cause to be prepaid from net insurance proceeds received pursuant to the Financing Lease, the Agency Rent Payments then unpaid, in whole or in part on any date, so that the aggregate annual Agency Rent Payments for the related Property from and after such prepayment date shall be in approximately equal amounts, at a Prepayment Price equal to the sum of the Agency Rent Payments prepaid, without premium, plus accrued interest evidenced and represented thereby to the date of prepayment.

**Revision of Agency Rent Payments upon Prepayment**

The Agency Principal Components and Agency Interest Components of the Agency Rent Payments due on each Agency Rent Payment Date on and after the date of any prepayment pursuant to the Financing Lease shall be reduced by the Treasurer to reflect such prepayment, in Authorized Denominations, in such amounts and on such Agency Rent Payment Dates as the Agency shall elect in its written notice to the Treasurer pursuant to the Financing Lease.

**Discharge of Financing Lease**

All right, title and interest of the Corporation in the State Agency Financing Lease Addenda and of the State in the Local Agency Financing Lease and all obligations of any Agency under its Financing Lease shall cease, terminate, become void and be completely discharged and satisfied (except for the right of the Treasurer and the Fiscal Agent, as assignee of the Corporation, and the obligation of the Agency to have the moneys and Government Obligations so set aside applied to make the remaining Agency Rent Payments) when either:

(1) all Agency Rent Payments and all Additional Rent and other amounts due under the Financing Lease have been paid in accordance therewith; or

(2) (a) the Agency shall have delivered a written notice to the Treasurer of its intention to prepay all of the Agency Rent Payments remaining unpaid;

(b) the Agency shall have caused to be deposited with the Treasurer (i) moneys and/or Government Obligations in accordance with the Financing Lease; and (ii) an Opinion of Counsel to the effect that such actions are permitted under the Financing Lease, under the Master Financing Lease and under the Trust Agreement, and will not cause interest evidenced and represented by the Certificates to be includable in gross income for federal income tax purposes under the Code; and

(c) for so long as any Agency Rent Payments remain unpaid, provision shall have been made satisfactory to the Corporation and the Fiscal Agent for payment of all Additional Rent.

**Eminent Domain**

If the Property subleased to the Agency pursuant to the Financing Lease, or so much thereof so as to render the remainder unsuitable for the purposes for which it was used by the Agency at the time of such taking, shall be taken under the power of eminent domain (or sold under threat of condemnation), the sublease of such Property pursuant to the Financing Lease shall cease as of the day that the Agency is required to vacate such Property. If less than all of such Property is taken under the power of eminent domain (or sold under threat of condemnation), and the remainder is suitable for the purposes for which it was used by the Agency at the time of such taking, as reasonably determined by the Treasurer, then the sublease thereof pursuant to the Financing Lease shall continue in full force and effect as to such remainder, and the Parties waive any benefits of the law to the contrary. In such event, there shall be no abatement of the rental due under the Financing Lease. So long as any Agency Rent Payments under the Financing Lease remain unpaid, any eminent domain award and any proceeds of sale under threat of condemnation for all or any part of the Property shall be applied to the prepayment of Agency Rent Payments as provided in the Financing Lease. Any award or proceeds in excess of the amount necessary to prepay such Agency Rent Payments due under the Financing Lease, and thereby to prepay or provide for the payment of the corresponding portion of the Base Rent Payments under the Master Financing Lease, shall be paid to the Corporation, the State and the Agency as their respective interests may appear.

**Loss of Title**

If there is a loss of title to the Property subleased to the Agency pursuant to the Financing Lease which is insured under a policy or policies of title insurance, or so much thereof so as to render the remainder unsuitable for the purposes for which it was used by the Agency at the time of such loss, the sublease of such Property pursuant to the Financing Lease shall cease as of the day that the Agency is required to vacate such Property. If there is a loss of title to less than all of such Property, and the remainder is suitable for the purposes for which it was used by the Agency at the time of such loss, as reasonably determined by the Treasurer, then the sublease thereof pursuant to the Financing Lease shall continue in full force and effect as to such remainder, and the Parties waive any benefits of the law to the contrary. In such event, there shall be no abatement of the rental due under the Financing Lease. So long as any Agency Rent Payments under the Financing Lease remain unpaid, any payments under such title insurance policy or policies with respect to such Property shall be applied to the prepayment of Agency Rent Payments as provided in the Financing Lease. Any payment in excess of the amount necessary to prepay such Agency Rent Payments due under the Financing Lease, and thereby to prepay or provide for the payment of the corresponding portion of the Base Rent Payments due under the Master Financing Lease, shall be paid to the Corporation, the State and the Agency as their respective interests may appear.

**Damage or Destruction**

If all or any portion of the Property subleased to the Agency pursuant to the Financing Lease shall be damaged or destroyed by fire or other casualty, the sublease thereof pursuant to the Financing Lease shall not terminate, nor shall there be any abatement of the rent payable under the Financing Lease. So long as any Agency Rent Payments under the Financing Lease remain unpaid, any payments under the property insurance policy or policies with respect to such Property may be applied to the prepayment of Agency Rent Payments as provided in the Financing Lease, or may be paid to the Treasurer and applied as provided in the Trust Agreement.

**Permitted Termination Events for State Agency Financing Lease Addendum**

The following shall constitute a "Permitted Termination Event" under each State Agency Financing Lease Addendum:

(1) The State Legislature elects not to appropriate sufficient funds within any biennial budget for the purpose of paying the Agent Rent payments due under the State Agency Financing Lease Addendum during the next occurring biennium; or

(2) The Governor of the State issues an Executive Order mandating an emergency reduction in State funding;

*provided*, that the State Agency delivers written notice thereof to the Treasurer as provided in the following paragraph.

***Written Notice to Treasurer describing a Permitted Termination Event.*** If, as of five Business Days following (1) the enactment of each biennial budget by the State Legislature or (2) an Executive Order reduction in funding, the State Agency determines as a result of such legislation or Executive Order that sufficient funds will not be available to make its scheduled Agency Rent Payments for the Property in the next occurring Biennium or upon a reduction in funding in the manner as set forth above, the State Agency shall deliver written notice to the Treasurer not less than 45 days prior to the Permitted Termination Date, which notice shall describe the Permitted Termination Event, state the Permitted Termination Date and state that the State Agency has determined that such Permitted Termination Event will result in the cancellation of the applicable Financing Lease.

***Treasurer's Duties upon a Permitted Termination Event.*** Upon the occurrence of a Permitted Termination Event, the Treasurer shall immediately deliver written notice thereof to the Corporation and the Fiscal Agent, which notice shall identify the election not to appropriate the necessary funds or the Executive Order reduction as the reason for cancellation thereof. The Treasurer shall, if practicable, request a supplemental appropriation in the event that an appropriation has not been made to the State Agency. In the event of an Executive Order reduction, the Treasurer shall determine whether or not the Property and the obligations of the State Agency under its Financing Lease may be transferred to the office of the Treasurer or to another agency or department of the State authorized under the Act to enter into financing agreements. No Permitted Termination Event following an Executive Order reduction in funding shall be effective unless or until the Treasurer has determined that neither the Treasurer nor any other agency or department of the State authorized under the Act to enter into financing agreements is willing and able to assume the rights and obligations of the State Agency under its Financing Lease, as evidenced by a Certificate of the Treasurer.

***Remedies of the Corporation Upon a Permitted Termination Event.*** Upon the occurrence and effectiveness of a Permitted Termination Event, the State Agency shall, at the beginning of the period for which funds have not been appropriated or for which funding has been reduced, vacate said Property and deliver possession and control thereof to the Corporation for the remaining term of its Site Lease and thereupon be released of its obligations to make payments in an amount equal to the then unpaid balance of Agency Rent Payments with respect to the Property; provided, that the State Agency delivers the Property in good repair, working order and condition, ordinary wear and tear excepted, as of the end of the last month for which funding has been provided, or the end of the last month for which funding is available in the event of an Executive Order reduction in funding, and written notice is provided by the State Agency directly to the Treasurer as set forth in its Financing Lease. Upon the occurrence and effectiveness of a Permitted Termination Event, the Corporation (or the Fiscal Agent, as assignee of the Corporation) shall be entitled to retain all sums theretofore transmitted to the Corporation (or to the Fiscal

Agent as assignee of the Corporation) by or on behalf of the State Agency for the benefit of the Owners of the Certificates (including, without limitation, for use in administering the Property for the benefit of the Owners of the Certificates, including expenses of retaining accountants, consultants, attorneys, appraisers or other experts), and thereafter take possession of and relet the Property for the remaining term of the related Site Lease or assign its leasehold interest in the Property under the related Site Lease for the account of the State Agency and the benefit of the Owners of the Certificates.

The occurrence of a Permitted Termination Event shall not constitute an Event of Default, and the remedies relating to the return of the Property are the sole remedies available to the Corporation upon such occurrence. If the State Legislature provides a supplemental appropriation or the Executive Order is withdrawn prior to the expiration of the specified notice period and the Treasurer or the Corporation has not yet relet or otherwise disposed of the Property, the State Agency may, by written notice to the Corporation, revoke the notice of termination and continue its obligations under the Financing Lease.

**Covenants and Agreements of the Agency**

The Agency covenants and agrees as follows:

***Budget***. Each Local Agency shall take such action as may be necessary to include all the Agency Rent Payments and Additional Rent due under the corresponding Local Agency Financing Lease in its annual budget and to make the necessary annual appropriations for all such Agency Rent Payments and Additional Rent.

Each State Agency shall (1) include in its biennial budget any scheduled Agency Rent Payments that may be required to be made by the Agency during such Biennium; (2) submit such budget to OFM at such times and in such manner as required by law; (3) use its best efforts to obtain appropriations by the State Legislature in amounts sufficient to make any such payments; (4) include all such payments in its statements of proposed expenditures for each fiscal period required by law to be submitted to OFM; and (5) use its best efforts to obtain allotments by OFM of appropriated funds sufficient to make all such payments.

***Application of Appropriations.*** To the extent permitted by law, each State Agency agrees that, to the extent that any amounts are included in its budget for purposes or facilities served, or functions or operations supported or provided by the Property, the State Agency will allocate a sufficient portion of such amounts to the payment of the Agency Rent Payments and Additional Rent due under its Financing Lease.

***Tax-Exemption.*** The Agency shall not make any use of the proceeds of the Financing Lease or the Certificates or of any other amounts, regardless of the source, or of any property, and shall not take or refrain from taking any action, that would cause the Master Financing Lease or the Certificates to be "arbitrage bonds" within the meaning of Section 148 of the Code. The Agency shall not use or permit the use of the Property or any part thereof by any Person other than a "governmental unit" as that term is defined in Section 141 of the Code, in such manner or to such extent as would result in the loss of the exclusion from gross income for federal income tax purposes of the Interest Component of the Agency Rent Payments under Section 103 of the Code. The Agency shall not make any use of the proceeds of the Financing Lease or the Certificates or of any other amounts, and shall not take or refrain from taking any action, that would cause the Master Financing Lease or the Certificates to be "federally guaranteed" within the meaning of Section 149(b) of the Code or "private activity bonds" within the meaning of Section 141 of the Code, or "hedge bonds" within the meaning of Section 149 of the Code. To that end, for so long as any Agency Rent Payments remain unpaid, the Agency, with respect to such proceeds and other amounts, will comply with all requirements under such Sections and all applicable regulations of the

United States Department of the Treasury promulgated under the Financing Lease. The Agency will at all times do and perform all acts and things permitted by law which are necessary or desirable in order to assure that the Interest Components of the Agency Rent Payments will not be included in gross income of the Owners of the Certificates for federal income tax purposes under the Code, and will take no action that would result in such interest being so included. The Agency shall comply with the applicable provisions of the Tax Certificate.

***Liens; Assignments and Subleases.*** The Agency shall not create, incur, assume or suffer to exist any mortgage, pledge, lien, charge, encumbrance or claim on or with respect to the Property or any part thereof, except for Permitted Encumbrances. The Agency shall promptly, at its own expense, take such action as may be necessary to duly discharge any such mortgage, pledge, lien, charge, encumbrance or claim if the same shall arise at any time. The Agency shall not grant, sell, transfer, assign, pledge, convey, mortgage, pledge, sublet or otherwise dispose of any of the Property or any interest in the Financing Lease during the term of the Financing Lease, and any such attempted grant, sale, transfer, assignment, pledge, conveyance or disposal shall be void.

***Pledge of Funds and Credit of Local Agency.*** The obligations of each Local Agency under its Local Agency Financing Lease constitute a debt and a general obligation of such Local Agency, and a contracting of an indebtedness by such Local Agency, to which the full faith and credit of such Local Agency are pledged. If and to the extent authorized by law, each Local Agency covenants and agrees that it will levy taxes in such amounts and at such times as shall be necessary, within and as a part of the tax levy, if any, permitted to such Local Agency without a vote of its electors, to provide funds, together with other legally available moneys, sufficient to make the Agency Rent Payments and the other payments required under the corresponding Local Agency Financing Lease.

***Use of Property.*** During the term of each Financing Lease, the corresponding Agency will use the Property for the purposes of performing one or more of its essential governmental functions or responsibilities.

***Maintenance; Repairs.*** For so long as the Agency is in possession of the Property, such Agency shall be solely responsible for the maintenance and repair, both ordinary and extraordinary, thereof. The Agency will (1) keep and maintain the Property in good repair and condition, protect the same from deterioration other than normal wear and tear, and pay or cause to be paid all charges for utility services to the Property; (2) comply with the requirements of applicable laws, ordinances and regulations and the requirements of any insurance or self-insurance program required under the Financing Lease in connection with the use, occupation and maintenance of the Property; (3) obtain all permits and licenses, if any, required by law for the use, occupation and maintenance of the Property; and (4) pay all costs, claims, damages, fees and charges arising out of its possession, use or maintenance of the Property.

***Hazardous Substances.***

(1) Use. The Property does not currently violate, and neither the Agency nor its officers, agents, employees, contractors, or invitees, shall not use the Property in a manner that violates, any applicable federal, state or local law, regulation or ordinance, including, but not limited to, any such law, regulation or ordinance pertaining to air and water quality, the handling, transportation, storage, treatment, usage and disposal of Toxic or Hazardous Substances, air emissions, other environmental matters, and all zoning and other land use matters. The Agency shall not cause or permit the release or disposal of any Toxic or Hazardous Substances on or from the Property.

(2) Indemnity. The Agency, to the extent permitted by law, agrees to protect, indemnify, defend (with counsel satisfactory to the Agency) and hold the State (with respect to a Local Agency). the

Corporation and the Fiscal Agent, and their respective directors, officers, employees and agents harmless from any claims, judgments, damages, penalties, fines, expenses, liabilities or losses arising out of or in any way relating to the presence, release or disposal of Toxic or Hazardous Substances on or from the Property; provided, however, that the Agency shall not be obligated to provide such indemnification, in its capacity as Lessee under the Site Lease (with respect to the State Agency) or in its capacity as Lessor under the Financing Lease (with respect to a Local Agency), from any such claims, judgments, damages, penalties, fines, expenses, liabilities or losses relating to the presence, release or disposal of Toxic or Hazardous Substances on or from the Property occurring when the Agency is or was not in possession of the Property. Such indemnity shall include, without limitation, costs incurred in connection with: (a) Toxic or Hazardous Substances present or suspected to be present in the soil, groundwater or soil vapor on or under the Property; or (b) Toxic or Hazardous Substances that migrate, flow, percolate, diffuse, or in any way move onto or under the Property; or (c) Toxic or Hazardous Substances present on or under the Property as a result of any discharge, dumping, spilling (accidental or otherwise) onto the Property by any person, corporation, partnership, or entity other than the Agency, its officials, officers, employees or agents.

The indemnification summarized above covers, without limitation, costs incurred in connection with any investigation of site conditions or any cleanup, remedial, removal or restoration work required by any federal, state or local governmental agency or political subdivision or other third party because of the presence or suspected presence of Toxic or Hazardous Substances in the soil, groundwater, or soil vapor on or under the Property. Such costs may include, but not be limited to, damages for the loss or restriction on use of renewable or usable space or of any amenity of the Property, sums paid in settlements of claims, attorneys fees, consultants fees, and expert fees.

(3) Notification Requirements. The Agency shall promptly notify the other Parties in writing of all spills or releases of any Toxic or Hazardous Substances, all failures to comply with any federal, state, or local law, regulation or ordinance, all inspections of the Property by any regulatory entity concerning the same, all notices, orders, fines or communications of any kind from any governmental entity or third party that relate to the existence of or potential for environmental pollution of any kind existing on or resulting from the use of the Property or any activity conducted thereon, and all responses or interim cleanup action taken by or proposed to be taken by any government entity or private party on the Property.

Upon request by any Party, the Agency shall provide such Party with a written report (a) listing the Toxic or Hazardous Substances that were used or stored on the Property; (b) discussing all releases of Toxic or Hazardous Substances that occurred or were discovered on the Property and all compliance activities related to Toxic or Hazardous Substances, including all contacts with and all requests from third parties for cleanup or compliance; (c) providing copies of all permits, manifests, business plans, consent agreements or other contracts relating to Toxic or Hazardous Substances executed or requested during that time period; and (d) including such other information requested by such Party.

(4) Inspection Rights. The Parties, and their officers, employees and agents, shall have the right, but not the duty, to inspect the Property and the Agency's relevant environmental and land use documents at any time and to perform such tests on the Property as are reasonably necessary to determine whether the Agency is complying with the terms of the Financing Lease. The Agency shall be responsible for paying for any testing that is conducted if the Agency is not in compliance with the Financing Lease and such Party has reason to believe such noncompliance is due to the Agency's operations or use of the Property. If the Agency is not in compliance with the Financing Lease, such Party, without waiving or releasing any right or remedy it may have

with respect to such noncompliance, shall have the right to immediately enter upon the Property to remedy any contamination caused by the Agency's failure to comply notwithstanding any other provision of the Financing Lease. The Party shall use reasonable efforts to minimize interference with the Agency's business but shall not be liable for any interference caused thereby.

(5) Corrective Action. In the event any investigation, site monitoring, containment, cleanup, removal, restoration or other remedial work ("Remedial Work") of any kind is necessary under any applicable federal, state or local laws, regulations or ordinances, or is required by any governmental entity or other third person because of or in connection with the presence or suspected presence of Toxic or Hazardous Substances on or under the Property, each Agency shall assume responsibility for all such Remedial Work and shall promptly commence and thereafter diligently prosecute to completion all such Remedial Work. The Agency shall pay for all costs and expenses of such Remedial Work, including, without limitation, the Party's reasonable attorneys' fees and costs incurred in connection with monitoring or review of such Remedial Work. In the event the Agency shall fail to timely commence, or cause to be commenced, or fail to diligently prosecute to completion, such Remedial Work, such Party may, but shall not be required to, cause such Remedial Work to be performed and all costs and expenses thereof, or incurred in connection therewith, shall become immediately due and payable as Additional Rent due to the Corporation from the State Agency and the State from the Local Agency.

***Insurance.***

(1) The Agency shall maintain, or cause to be maintained, in full force and effect, comprehensive general liability insurance with respect to the Property in such amounts as may be reasonably determined by the Agency from time to time but in any event not less than $1,000,000 per occurrence. Such insurance may be carried under a blanket policy with umbrella coverage. Such insurance shall cover any and all liability of the Agency and its officials, officers, employees and volunteers. Such insurance shall include (a) coverage for any accident resulting in personal injury to or death of any person and consequential damages arising therefrom; and (b) comprehensive property damage insurance.

(2) The Agency shall maintain or cause to be maintained in full force and effect fire and extended coverage insurance with respect to the Property in such amounts as the Agency may reasonably determine from time to time, but in any event not less than the aggregate of the principal components of Agent Rent Payments due under the Financing Lease which remain unpaid. Such insurance may be carried under a policy or policies covering other property of the Agency. Such property insurance shall be "all risk" insurance, and shall cover physical loss or damage as a result of fire, lightning, theft, vandalism, malicious mischief, flood, earthquake, and boiler and machinery; provided, that the Treasurer may waive the requirement for earthquake or flood insurance if it determines, based on consultation with risk management or insurance advisors of the State, that the same is not available from reputable insurers and commercially reasonable rates. Such extended coverage insurance shall, as nearly as practicable, cover loss or damage by explosion, windstorm, riot, aircraft, vehicle damage, smoke and such other hazards as the Agency may reasonably determine from time to time. Such policies of insurance shall provide that all proceeds under the Financing Lease shall be payable to the Fiscal Agent, as assignee of the Corporation, pursuant to a lender's loss payable endorsement. The net proceeds of such insurance shall be applied as provided in the Trust Agreement. Such insurance may at any time include a deductible of not to exceed $500,000 for losses in any year with respect to a State

Agency and not to exceed $5,000 for losses in any year with respect to a Local Agency, or such greater amount as the Treasurer may approve in writing.

(3) The insurance required by the Financing Lease as summarized above (a) shall be provided by a financially responsible insurance company authorized to do business in the State; (b) shall name the Fiscal Agent, as assignee of the Corporation, as additional insured under the Financing Lease; (c) shall provide that the same may not be canceled or given notice of non-renewal, nor shall the terms of conditions thereof be altered, amended or modified, without at least 45 days' prior written notice being given by the insurer to the Treasurer and, for a State Agency, to the Fiscal Agent, as assignee of the Corporation; and (d) may be provided in whole or in part through a funded program of self-insurance reviewed at least annually by an insurance actuary.

(4) A certificate of insurance with respect to the required coverages shall be provided by the Agency to the Treasurer and, for a State Agency, to the Fiscal Agent, as assignee of the Corporation, annually on or prior to the December 1 with respect to any required insurance maintained pursuant to the Financing Lease.

(5) Unless otherwise provided by the State, the Local Agency shall obtain a policy or policies of title insurance on the Property, subject only to Permitted Encumbrances, in an amount equal to the aggregate amount of Agent Rent Payments to become due under the Financing Lease, payable to the State and the Fiscal Agent, in a form and from a provider approved in writing by the Treasurer, which approval shall not be unreasonably withheld or delayed. The proceeds received under any such policy shall be applied as provided in the Financing Lease.

(6) The Agency will pay or cause to be paid when due the premiums for all insurance policies required under the Financing Lease.

**Agency Event of Default**

Each of the following shall constitute an "Agency Event of Default" under the Financing Lease:

(1) Failure by the Agency to pay or cause to be paid any Agency Rent Payment required to be paid under the Financing Lease at the time set forth in the Financing Lease;

(2) Failure by the Agency to observe or perform any covenant, agreement, term or condition on its part to be observed or performed under the Financing Lease, other than as set forth in paragraph (1) above, for a period of 30 days after written notice from the Corporation, or from the Owners of not less than 25 percent in aggregate Principal Component evidenced and represented by the Certificates then Outstanding to the Treasurer (or in the case of a Local Agency from the Treasurer or the Fiscal Agent to the Local Agency) specifying such failure and requesting that it be remedied; provided, however, that such period shall be extended for not more than 60 days if such failure cannot be corrected within such period, and the corrective action is commenced by the Agency within such period and diligently pursued until the failure is corrected;

(3) If the statement, representation, or warranty made by the Agency in the Financing Lease or in any writing delivered by the Local Agency pursuant to its Financing Lease is false, misleading, or erroneous in any material respect;

(4) If the Agency's interest under the Financing Lease or any part thereof shall be assigned, sublet or transferred other than as provided in the Financing Lease, either voluntarily or by operation of law;

(5) If the Agency shall abandon or vacate the Property; and

(6) Inability of the Agency to generally pay its debts as such debts become due, or admission by the Agency, in writing, of its inability to pay its debts generally, or the making by the Agency of a general assignment for the benefit of creditors, or the institution of any proceeding by or against the Agency seeking to adjudicate it as bankrupt or insolvent, or seeking liquidation, winding-up, reorganization, reimbursement, adjustment, protection, relief or composition of it or its debts under any law relating to bankruptcy, insolvency or reorganization or relief of debtors, or seeking the entry of an order for relief or for appointment of a receiver, trustee, or other similar officer of it or any substantial part of its property, or the taking of any action by the Agency to authorize any of the actions summarized above in this paragraph;

(7) If an event of default shall occur under any Additional Financing Lease Agreement.

Notwithstanding the foregoing provisions of the Financing Lease, if by reason of *force majeure* the Agency is unable in whole or in part to carry out the covenants, agreements, terms and conditions on its part contained in the Financing Lease, the Agency shall not be deemed in default during the continuance of such inability. The term "*force majeure*" means the following: acts of God; strikes; lockouts or other industrial disturbances or disputes; acts of public enemies; orders or restraints of any kind of the government of the United States of America or any of its departments, agencies or officials, or of its civil or military authorities; orders or restraints of the State or of any of its departments, agencies or officials or civil or military authorities of the State; wars, rebellions, insurrections; riots; civil disorders; blockade or embargo; landslides; earthquakes; fires; storms; droughts; floods; explosions; or any other cause or event not within the control of the Agency.

The Treasurer, with the prior written consent of the Fiscal Agent, may, at its election, waive any default or Agency Event of Default and its consequences under the Financing Lease and annul any notice thereof by written notice to the Agency to such effect, and thereupon the respective rights of the Parties under the Financing Lease shall be as they would have been if such default or Agency Event of Default had not occurred.

ANYTHING IN A STATE AGENCY FINANCING LEASE ADDENDUM TO THE CONTRARY NOTWITHSTANDING, A PERMITTED TERMINATION EVENT SHALL NOT CONSTITUTE AN EVENT OF DEFAULT UNDER A STATE AGENCY FINANCING LEASE ADDENDUM.

**Rights of Treasurer Following Agency Event of Default**

***Continuation; Reentry and Reletting.*** The State may continue the Financing Lease in full force and effect, and (1) collect rent and other amounts as they become due under the Financing Lease, (2) enforce every other term and provision of the Financing Lease to be observed or performed by the Agency, and (3) exercise any and all rights of entry and reentry upon the Property. In the event that the State does not elect to terminate the Financing Lease in the manner summarized in the following paragraph, the Agency agrees to observe and perform all terms and provisions in the Financing Lease to be observed or performed by it, and, if the Property is not relet, to pay the full amount of the rent and other amounts due under the Financing Lease for the term of the Financing Lease, or, if the Property or any part thereof is relet, to pay any deficiency that results therefrom, in each case at the same time and in the same manner as otherwise provided in the Financing Lease, and notwithstanding any reentry or reletting by the State, or suit in unlawful detainer or otherwise brought by the State for the purpose of effecting such re-entry or obtaining possession of all or any part of the Property. Should the State elect to re-enter or obtain possession of all or any part of the Property, the Agency irrevocably appoints the State as the Agency's agent and attorney-in-fact (a) to relet the Property, or any part thereof, from time to time, either in the

name of the State or otherwise, upon such terms and conditions and for such use and period as the State may determine in its discretion, (b) to remove all persons in possession thereof and all personal property whatsoever situated upon the Property, and (c) to place such personal property in storage in any warehouse or other suitable place for the Agency in the county in which such personal property is located, for the account of and at the expense of the Agency. The Agency shall be liable for, and agrees to pay the State, the State's costs and expenses in connection with reentry of the Property, removal and storage of any personal property, and reletting of the Property. The Agency agrees that the terms of the Financing Lease constitute full and sufficient notice of the right of the Treasurer to reenter and relet the Property or any part thereof without effecting a surrender or termination of the Financing Lease. Termination of the Financing Lease upon an Agency Event of Default shall be effected solely as summarized in the following paragraph. The Agency further waives any right to, and releases, any rental obtained by the State upon reletting in excess of the rental and other amounts otherwise due under the Financing Lease.

***Termination.*** The State may terminate the Financing Lease, but solely upon written notice by the Treasurer to the Agency of such election. No notice to pay rent, notice of default, or notice to deliver possession of the Property or of any part thereof, nor any entry or reentry upon the Property or any part thereof by the Treasurer, nor any proceeding in unlawful detainer or otherwise brought by the Treasurer for the purpose of effecting such reentry or obtaining possession, nor any other act shall operate to terminate the Financing Lease, and no termination of the Financing Lease on an account of a Master Financing Lease Event of Default shall be or become effective by operation of law or acts of the Parties hereto or otherwise, unless and until such notice of termination shall have been given by the Treasurer. The Agency agrees that no surrender of the Property or any part thereof, nor any termination of the Financing Lease by the Agency shall be valid or effective in any manner or for any purpose whatsoever unless such notice of termination shall have been given by the Treasurer. Upon such termination, the State may (1) reenter the Property or any part thereof and remove all persons in possession thereof and all personal property whatsoever situated upon the Property, and (2) place such personal property in storage in any warehouse or other suitable place for the Agency in the county in which such personal property is located, for the account of and at the expense of the Agency. Upon such termination, the Agency's right to possession of the Property shall terminate, and the Agency shall surrender possession thereof to the State. In the event of such termination, the Agency shall remain liable to the State for damages in an amount equal to the rent and other amounts that would have been due under the Financing Lease for the balance of the term of the Financing Lease, less the net proceeds, if any, of any reletting of the Property or any part thereof by the State subsequent to such termination, after deducting the expenses incurred by the State in connection with any such reentry, removal and storage of personal property, and reletting. The State shall be entitled to collect damages from the Agency on the respective Agency Rent Payment Dates, or alternatively, the Treasurer may accelerate the Agency's obligations under the Financing Lease and recover from the Agency (a) the worth at the time of award of the unpaid rental which had been earned at the time of termination, (b) the worth at the time of award of the amount by which the unpaid rental which would have been earned after the termination until the time of award exceeds the amount of such rental loss that the Agency proves could have been reasonably avoided, (c) the worth at the time of award by which the unpaid rental for the balance of the term of the Financing Lease after the time of award exceeds the amount of rental loss that the Agency proves could reasonably have been avoided, and (d) any other amount necessary to compensate the State for all the detriment proximately caused by the Agency's failure to perform its obligations under the Financing Lease, or which in the ordinary course would be likely to result therefrom, including but not limited to the State's expenses in connection with reentry of the Property, removal and storage of any personal property, and reletting of the Property. The worth at the time of award shall be computed using a discount rate equal to (in the case of a State Agency) the composite Interest Component evidenced and represented by the Certificates or (in the case of a Local Agency) the composite Agency Interest Component of the unpaid Agency Rent Payments.

***Other Remedies.*** In addition to the other remedies set forth in the Financing Lease, upon the occurrence and continuance of an Agency Event of Default, the State shall be entitled to proceed to protect and enforce the rights vested in them by the Financing Lease or by law. The terms and provisions of the Financing Lease and the duties and obligations of the Agency under the Financing Lease, and the officers and employees thereof, shall be enforceable by the Treasurer by an action at law or in equity, for damages or for specific performance, or for writ of mandate, or by other appropriate action, suit or proceeding in any court of competent jurisdiction. Without limiting the generality of the foregoing, the State shall have the right to bring the following actions:

(1) Accounting. By action or suit in equity to require the Agency and its officers and employees to account as the trustee of an express trust.

(2) Injunction. By action or suit in equity to enjoin the violation of the rights of the Treasurer.

(3) Mandate. By writ of mandate or other action, suit or proceeding at law or in equity to enforce the Treasurer's rights against the Agency and its officers and employees, and to compel the Agency to perform and carry out its duties and obligations under the law and its covenants and agreements with the Treasurer as provided in the Financing Lease.

In the event that the State shall prevail in any action, suit or proceeding brought to enforce any of the terms of provisions of the Financing Lease, the Agency shall be liable for the reasonable attorneys' fees of the Treasurer in connection therewith.

The Agency waives any and all claims for damages caused or which may be caused by the Treasurer in reentering and taking possession of the Property or any part thereof as provided in its Financing Lease, and all claims for damages that may result from the destruction of or injury to the Property or any part thereof, and all claims for damages to or loss of any personal property may be in or upon the Property.

**No Remedy Exclusive; Non-Waiver**

No remedy conferred upon or reserved to the State under the Financing Lease or under applicable law is intended to or shall be exclusive, and every such remedy shall be cumulative and shall be in addition to every other remedy given under the Financing Lease or now or existing at law or in equity. No delay or omission to exercise any right or remedy accruing upon a default or an Event of Default under the Financing Lease shall impair any such right or remedy or shall be construed to be a waiver of such default or Event of Default, but any such right or remedy may be exercised from time to time and as often as may be deemed necessary or expedient. In order to exercise any remedy reserved to the Treasurer under the Financing Lease, it shall not be necessary to give any notice, other than such notice as may be required under the Financing Lease. A waiver by the Treasurer of any default or Event of Default under the Financing Lease shall not constitute a waiver of any subsequent default or Event of Default under the Financing Lease, and shall not affect or impair the rights or remedies of the Treasurer in connection with any such subsequent default or Event of Default.

No acceptance of less than the full amount of a rental payment due under the Financing Lease shall constitute an accord and satisfaction or compromise of any such payment unless the Treasurer specifically agrees to such accord and satisfaction or compromise in writing.

**Default by State**

Anything in the Financing Lease to the contrary notwithstanding, the State shall not be in default in the observance or performance of any of the covenants, agreements, terms or conditions to be observed or

performed by it under the Financing Lease unless and until the State shall have failed to observe or perform such covenant, agreement, term or condition for a period of 60 days after written notice by the Agency to the Treasurer specifying such failure and requesting that it be remedied; provided, however, that such period shall be extended for such additional time as shall be reasonably required to correct such failure if corrective action is commenced by the State within such period and diligently pursued until the failure is corrected.

**Indemnification of State and the Corporation**

To the extent permitted by law, each Local Agency releases the State and the Corporation from, agrees that the State and the Corporation shall not be liable for, and agrees to indemnify and hold the State and the Corporation and their respective directors, officers, officials, employees, and agents harmless from, any liability for any loss or damage to property or any injury to or death of any person that may be occasioned by any cause whatsoever arising out of the ownership or operation of the Property or the design, acquisition, construction, financing or refinancing thereof. To the extent permitted by law, each Local Agency agrees to indemnify and hold the State and the Corporation and their respective directors, officers, officials, employees, and agents harmless from any losses, costs, charges, expenses (including reasonable attorneys' fees), judgments and liabilities incurred by it or them, as the case may be, in connection with any action, suit or proceeding instituted or threatened in connection with the transactions contemplated by the corresponding Local Agency Financing Lease or the exercise of rights or the performance of duties of the State or the Corporation under such Local Agency Financing Lease, the Master Financing Lease or the other Series 2011D Agreements, except to the extent caused by the gross negligence or willful misconduct of such indemnified party. The indemnification provided in each Local Agency Financing Lease shall survive the final payment of the Agency Rent Payments and the termination of such Local Agency Financing Lease for any reason.

**Term**

If on the scheduled termination date for the Financing Lease as set forth in the Financing Lease, all amounts due under the Financing Lease shall not have been paid or the payment thereof duly provided for pursuant to the Financing Lease, then the term of the Financing Lease shall be extended until 10 days after all amounts due under the Financing Lease shall have been paid or the payment thereof so provided for, except that the term of the Financing Lease shall in no event be extended more than five years beyond such scheduled termination date. If prior to the scheduled termination date, all amounts due under the Financing Lease shall have been paid or the payment thereof so provided for, the term of the Financing Lease shall end 10 days thereafter or 10 days after written notice by the Agency to the Treasurer, whichever is earlier. Notwithstanding the foregoing, the payment of all amounts due under the Financing Lease shall not result in the termination of the Financing Lease prior to the scheduled termination of the related Site Lease.

**Termination**

The Agency agrees, upon the termination or expiration of the Financing Lease, to quit and surrender the Property (1) in the same good order, condition and repair as the same was in at the time of commencement of the term under the Financing Lease, except for acts of God, reasonable wear and tear and any actions by the Agency in accordance with the Financing Lease that affect the condition of the Property; and (2) free and clear of all leases, occupancies, liens and encumbrances, other than those existing as of the Dated Date. The Agency agrees that any permanent improvements and structures existing upon the Property at the time of such termination or expiration of the Financing Lease shall remain thereon. The Agency shall thereafter execute, acknowledge and deliver to the Treasurer (with respect to a Local Agency) and to the Corporation (with respect to a State Agency) such instruments of

further assurance as in the reasonable opinion of the Treasurer are necessary or desirable to confirm the Treasurer's leasehold right, title and interest in and to the Property.

## FINANCING CONTRACTS

### Appointment of Agents; Acquisition of Property, Substitution of Property

***Appointment of Agents.*** Under each Agency Financing Contract, the Agency ratifies, approves and confirms, and accepts and agrees to, its designation and appointment as agent of the Corporation in connection with the acquisition of the Property.

***Acquisition of Property.*** The Agency agrees that:

(1) it has caused or will cause the Property to be acquired, as agent for the Corporation, with all reasonable dispatch;

(2) it will make, execute, acknowledge and deliver any contracts, agreements, orders, receipts, documents, writings or instructions with or to any Person and do all other things that may be necessary or desirable to acquire the Property; and

(3) it will pay or cause to be paid the Costs of Acquisition of the Property from funds available to it pursuant to the Agency Financing Contract and the Master Financing Contract.

The appointment of the Agency to act as agent of the Corporation in connection with the acquisition of the Property is made and conferred irrevocably by the Corporation, and shall not be terminated by any act of the Agency, the Treasurer or otherwise.

The Agency shall negotiate or call for bids for the purchase of the Property in accordance with the requirements and limitations, if any, imposed by State or local law with respect to the purchase of such Property by such Agency. Neither the Corporation nor the State shall have any responsibility, liability or obligation with respect to the selection or procurement of any of the Property.

***Substitution of Property.*** The Agency, with the prior written consent of the Treasurer, may revise any item of Property to be financed or refinanced and acquired pursuant to the Agency Financing Contract, or the description thereof; *provided*, that:

(1) such item of Property as so revised shall satisfy the requirements under the Agency Financing Contract and the Master Financing Contract with respect to the substitution of Property previously acquired;

(2) the Costs of Acquisition of such item of Property shall not be materially reduced thereby; and

(3) any such revision shall not relieve the Agency of its obligation to acquire the Property in accordance therewith and with the Master Financing Contract.

After acquisition of an item of Property, the Agency, with the prior written consent of the Treasurer, may substitute for an item of Property acquired pursuant to the Agency Financing Contract other personal property by filing with the Treasurer:

(1) a certificate of the Agency stating that such substitute Property: (a) has a remaining useful life equal to or greater than the Property for which it is being substituted; (b) has a fair market value

equal to or greater than the fair market value of the item of Property for which it is being substituted; (c) is free and clear of all liens and encumbrances except a first priority security interest in favor of the Fiscal Agent, as assignee of the Corporation, under the Master Financing Contract; (d) is of equal usefulness and value as the Property for which it is being substituted; (e) is essential to the Agency's ability to carry out its governmental functions and responsibilities; and (f) is expected to be used by such Agency immediately and for the term of the Agency Financing Contract; and

(2) an Opinion of Counsel to the effect that such substitution will not cause interest evidenced and represented by the Certificates to be includable in gross income for federal income tax purposes under the Code.

**Title to the Property**

All right, title and interest in and to the Property shall transfer to and be vested in the Agency from the Corporation or the State, as applicable, without any further action by the Agency, the Corporation or the State immediately upon the acquisition thereof or reimbursement to the Agency for the Acquisition Costs thereof; *provided*, that the Treasurer and the Agency shall take such action and execute such documents (including without limitation bills of sale and other title documents) as may be deemed necessary or desirable by the Treasurer or the Agency to evidence and confirm such transfer of title pursuant to the Agency Financing Contract.

Title to any and all additions, modifications, improvements, repairs or replacements to the Property shall be vested in the Agency, subject to the security interest of the Corporation until payment of all amounts due and owing with respect to such Property under the Agency Financing Contract.

Any Property constituting a motor vehicle subject to registration with the State Department of Licensing shall be registered with the Agency as the registered and legal owner thereof.

**Security Interest**

***State Security Interest.*** In order to secure the payment and performance by the State of its obligations under the Master Financing Contract, the State has pledged, granted, assigned and conveyed to the Corporation a lien on and security interest in all right, title and interest of the State, whether now owned or acquired, in and to the Property and the Agency Financing Contract, including without limitation the Agency Installment Payments and all proceeds thereof. The Agency acknowledges and agrees to such pledge, grant, assignment and conveyance, and acknowledges that its right, title and interest in and to the Property is subject to such first priority lien and security interest.

***Agency Security Interest.*** In order to secure the payment and performance by the Agency of its obligations under the Agency Financing Contract, the Agency pledges, grants, assigns and conveys to the Corporation a lien on and security interest in all right, title and interest of the Agency, whether now owned or acquired, in and to the Property. Accordingly, the Agency Financing Contract constitutes a security agreement. The Agency acknowledges and agrees that each provision of the Agency Financing Contract is also a provision of the security agreement.

The Agency further agrees that the Corporation may: (1) commingle Property which comes into its possession; (2) re-pledge such Property upon terms which impair the Agency's right to redeem such Property; and (3) require the Agency to assemble the Property and make it available to the Corporation in a manner which is reasonably convenient to both Parties. To the extent the Corporation is required for any reason to provide commercially reasonable notice to the Agency, the State agrees that notice mailed

by first class mail five days before the event of which notice is given is commercially reasonable notice. The standard by which the Corporation's rights and duties with respect to such security agreement shall be measured is gross negligence or willful misconduct.

If required by the Corporation or the Fiscal Agent, as assignee of the Corporation, at any time during the term of the Agency Financing Contract, the Agency will execute and deliver to the Corporation or the Fiscal Agent, as the case may be, in form satisfactory to the Corporation or the Fiscal Agent, such security agreements, financing statements and/or other instruments covering the Property and all accessions thereto.

**Disclaimer of Warranties**

The Local Agency acknowledges and agrees that the Property is of a nature, size, design and capacity selected by the Local Agency pursuant to its own specifications, and not by the State or the Corporation, and that neither the State nor the Corporation is a manufacturer, supplier or a vendor of such Property. THE STATE AND THE CORPORATION MAKE NO WARRANTY OR REPRESENTATION, EITHER EXPRESS OR IMPLIED, AND ASSUME NO RESPONSIBILITY, LIABILITY OR OBLIGATION, AS TO THE VALUE, DESIGN, CONDITION, MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR FITNESS FOR USE OF THE PROPERTY, OR AS TO THE TITLE THERETO, OR FOR THE ENFORCEMENT OF THE MANUFACTURERS', SUPPLIERS' OR VENDORS' REPRESENTATIONS, WARRANTIES OR GUARANTIES, OR ANY OTHER REPRESENTATION OR WARRANTY WITH RESPECT TO THE PROPERTY. IN NO EVENT SHALL THE STATE OR THE CORPORATION BE LIABLE OR RESPONSIBLE FOR ANY INCIDENTAL, INDIRECT, SPECIAL OR CONSEQUENTIAL DAMAGES IN CONNECTION WITH OR ARISING OUT OF THE LOCAL AGENCY FINANCING CONTRACT OR THE EXISTENCE, FURNISHING, FUNCTIONING OR USE BY THE LOCAL AGENCY OF THE PROPERTY.

The State Agency acknowledges and agrees that the Property is of a nature, size, design and capacity selected by the State Agency pursuant to its own specifications, and not by the Treasurer or the Corporation, and that neither the Treasurer nor the Corporation is a manufacturer, supplier or a vendor of such Property. THE TREASURER AND THE CORPORATION MAKE NO WARRANTY OR REPRESENTATION, EITHER EXPRESS OR IMPLIED, AND ASSUME NO RESPONSIBILITY, LIABILITY OR OBLIGATION, AS TO THE VALUE, DESIGN, CONDITION, MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR FITNESS FOR USE OF THE PROPERTY, OR AS TO THE TITLE THERETO, OR FOR THE ENFORCEMENT OF THE MANUFACTURERS', SUPPLIERS' OR VENDORS' REPRESENTATIONS, WARRANTIES OR GUARANTIES, OR ANY OTHER REPRESENTATION OR WARRANTY WITH RESPECT TO THE PROPERTY. IN NO EVENT SHALL THE TREASURER OR THE CORPORATION BE LIABLE OR RESPONSIBLE FOR ANY INCIDENTAL, INDIRECT, SPECIAL OR CONSEQUENTIAL DAMAGES IN CONNECTION WITH OR ARISING OUT OF THE STATE AGENCY FINANCING ADDENDUM OR THE EXISTENCE, FURNISHING, FUNCTIONING OR USE BY THE STATE AGENCY OF THE PROPERTY.

**Agency Installment Payments**

Each Agency Installment Payment shall consist of a Principal Component and/or an Interest Component as set forth in an exhibit to the Agency Financing Contract. Interest shall accrue and be calculated as determined by the Treasurer, which determination shall be binding and conclusive against the Agency absent manifest error. Each Agency Installment Payment payable under the Agency Financing Contract shall be paid to or upon the order of the Treasurer at such place as the Treasurer shall direct in writing not less than 10 Business Days prior to the Agency Installment Payment Date by electronic funds transfer in

lawful money of the United States of America. Payments of Additional Costs shall be made to or upon the order of the Treasurer. Each Agency Installment Payment shall be applied first to the Interest Component due under the Agency Financing Contract, and then to the Principal Component due under the Agency Financing Contract.

**Sources of Payment of Agency Installment Payments**

***Local Agency Financing Contract.*** The Local Agency acknowledges and agrees that the State is acquiring the Property from the Corporation for and on behalf of the Local Agency. Concurrently with the execution of the Local Agency Financing Contract, the State shall execute and deliver the Master Financing Contract pursuant to which the State shall agree to make Installment Payments for the acquisition of the Property for and on behalf of the respective Agencies, at such times and in such amounts as provided in the Local Agency Financing Contract, which will be sufficient in the aggregate to pay the Purchase Price of the Property to be acquired by the State for and on behalf of the Local Agency, together with all other personal property to be acquired for and on behalf of the other Local Agencies and the State Agencies, and interest thereon.

That portion of the Installment Payments that is allocable to the Purchase Price of the Local Agency Property and interest thereon shall be payable by the State solely from Agency Installment Payments to be made by the respective Local Agencies, including the Local Agency, except as otherwise provided in the Master Financing Contract. The obligation of the Local Agency to make its Agency Installment Payments shall be a direct and general obligation of the Local Agency to which the full faith and credit of such Local Agency is pledged. The State shall not be obligated to pay that portion of the Installment Payments that is allocable to the Purchase Price of the Local Agency Property and interest thereon other than from Agency Installment Payments paid by the respective Local Agencies, except as otherwise provided in the Master Financing Contract.

***Intercept of Local Agency Share of State Revenues.*** In the event that the Local Agency fails to make any payment due under the Local Agency Financing Contract, the Treasurer shall withhold an amount sufficient to make such payment from the Local Agency's share of State revenues or other amounts authorized or required by law to be distributed by the State to the Local Agency, including but not limited to leasehold excise taxes, sales and use taxes, excise taxes, property taxes, and liquor control board receipts; *provided*, that the use of any such revenues or amounts to make such payments is otherwise authorized or permitted by State law. Such withholding shall continue until all such delinquent payments have been made. Amounts withheld by the Treasurer shall be applied to make any such payment due under the Local Agency Financing Contract on behalf of the Local Agency, or to reimburse the Treasurer for any such payment made pursuant to the Local Agency Financing Contract. The Local Agency authorizes, approves and consents to any such withholding.

***Conditional Payment of Local Agency Installment Payments.*** Upon the failure of the Local Agency to make any Agency Installment Payment at such time and in such amount as required pursuant to the Local Agency Financing Contract, the Treasurer shall, to the extent of legally available appropriated funds and subject to any Executive Order reduction, make such payment into the Agency Installment Payment Fund, described below, on behalf of such Local Agency within 10 Business Days after such Agency Installment Payment Date. The Local Agency shall reimburse the State for such payments made on its behalf immediately thereafter and in any case not later than 10 Business Days after such Agency Installment Payment Date, together with interest thereon at a rate equal to the State Reimbursement Rate. Anything in the Local Agency Financing Contract to the contrary notwithstanding, failure of the Local Agency to reimburse the State for any such payment shall not constitute an Agency Event of Default under the Local Agency Financing Contract, but the State may institute such legal action and pursue such other remedies

against the Local Agency as the State deems necessary or desirable, including, but not limited to, actions for specific performance, injunction and/or the recovery of damages.

***Payments by Local Agency Treasurer.*** The treasurer of the Local Agency is authorized and directed to establish and/or maintain a special fund in the "bonds payable" category of accounts of the Local Agency for the purposes of paying the Local Agency's Agency Installment Payments and Additional Costs. The treasurer of the Local Agency is further authorized and directed to remit each payment of Agency Installment Payments to the Treasurer or its assignee on each Agency Installment Payment Date and any Additional Costs when due under the Local Agency Financing Contract. Such payment shall be made from any legally available funds of the Local Agency.

***State Agency Financing Contract.*** The State Agency acknowledges and agrees that the State is acquiring the Property from the Corporation for and on behalf of the State Agency. Concurrently with the execution of the Agency Financing Contract, the State shall execute and deliver the Master Financing Contract pursuant to which the State shall agree to make Installment Payments for the acquisition of the Property for and on behalf of the respective Agencies, at such times and in such amounts as provided therein, which will be sufficient in the aggregate to pay the Purchase Price of the Property to be acquired by the State for and on behalf of the State Agency together with all other personal property to be acquired for and on behalf of the other State Agencies, and interest thereon.

***Obligation of State Agency Subject to Appropriation.*** That portion of the Installment Payments that is allocable to the Purchase Price of the State Agency Property shall be payable by the State solely from Agency Installment Payments to be made by the respective State Agencies, including the State Agency. The obligation of the State Agency to make its Agency Installment Payments shall be subject to appropriation by the State Legislature and to Executive Order reduction. The State shall not be obligated to pay that portion of the Installment Payments that is allocable to the Purchase Price of the State Agency Property and interest thereon other than from appropriated funds of the respective State Agencies.

**Deposit and Investment of Agency Installment Payments**

The Agency acknowledges and agrees that the Agency Installment Payments shall be deposited in a special fund or funds maintained by the Treasurer (the "Agency Installment Payment Fund"). Payments of Agency Installment Payments from State Agencies shall be separately accounted for from payments from Local Agencies. The Agency Installment Payments due on each Agency Installment Payment Date shall be at least sufficient, in the aggregate, to make the Installment Payment next coming due under the Master Financing Contract. Amounts in the Agency Installment Payment Fund, including investment earnings thereon, shall be used and applied, *first*, to make the Installment Payment next coming due, *and thereafter*, but prior to the next Agency Installment Payment Date, to the extent that amounts remain in such Fund after such Installment Payment is made, to pay Additional Costs or for any other lawful purpose of the Treasurer. Amounts in the Agency Installment Payment Fund shall be invested in Qualified Investments, and shall be separately accounted for, but may be commingled with other moneys on deposit with the Treasurer solely for investment purposes. The Agency shall have no right, title or interest in or to the amounts on deposit from time to time in the Agency Installment Payment Fund.

**No Set Off**

The obligation of the Local Agency to make Agency Installment Payments from the sources set forth in the Local Agency Financing Contract and to perform its other obligations under the Local Agency Financing Contract shall be absolute and unconditional. The Local Agency shall make Agency Installment Payments as and when the same shall become due without diminution, reduction, postponement, abatement, counterclaim, defense or set-off as a result of any dispute, claim or right of

action by, against or among the State, the Corporation, the Fiscal Agent, any Agency, and/or any other Person, or for any other reason; provided, that nothing in the Local Agency Financing Contract shall be construed to release or excuse the State from the observance or performance of its obligations under the Local Agency Financing Contract. If the State shall fail to observe or perform any such obligation, the Local Agency may institute such legal action and pursue such other remedies against the State as the Local Agency deems necessary or desirable, including, but not limited to, actions for specific performance, injunction and/or the recovery of damages.

The obligation of the State Agency to make Agency Installment Payments from the sources set forth in the State Agency Financing Addendum and to perform its other obligations under the State Agency Financing Addendum shall be absolute and unconditional. The State Agency shall make Agency Installment Payments as and when the same shall become due without diminution, reduction, postponement, abatement, counterclaim, defense or set-off as a result of any dispute, claim or right of action by, against or among the State, the Corporation, the Fiscal Agent, any Agency, and/or any other Person, or for any other reason; *provided*, that nothing in the State Agency Financing Addendum shall be construed to release or excuse the Treasurer or the Corporation from the observance or performance of its obligations under the State Agency Financing Addendum or under the Master Financing Contract. If the Treasurer or the Corporation shall fail to observe or perform any such obligation, the State Agency may institute such legal action and pursue such other remedies against the Treasurer or the Corporation as the State Agency deems necessary or desirable, including, but not limited to, actions for specific performance, injunction and/or the recovery of damages.

**Assignments by the Corporation**

The Local Agency acknowledges and agrees that, concurrently with the execution and delivery of the Local Agency Financing Contract, the Corporation will unconditionally grant, sell, assign, transfer and convey to the Fiscal Agent without recourse:

(1) all of its rights to receive the Installment Payments under and pursuant to the Master Financing Contract; and

(2) all of its remaining right, title and interest in, to and under the Master Financing Contract and the Local Agency Financing Contract, and in and to the Property (including any security interest tin the Local Agency Financing Contract), including but not limited to its right to take all actions and exercise all remedies under and pursuant to the Master Financing Contract, pursuant to the Master Assignment in consideration for the payment by the Fiscal Agent to the Treasurer, as agent of the Corporation, of the proceeds of the sale of the Certificates.

The State and the Corporation have acknowledged and agreed that such grant, sale, assignment, transfer and conveyance by the Corporation is intended to be a true sale of the Corporation's right, title and interest, and that upon such grant, sale, assignment, transfer and conveyance, the Corporation shall cease to have any rights, duties or obligations under the Master Financing Contract or with respect to the Property, and the Fiscal Agent shall thereafter have all the rights, duties and obligations of the Corporation under the Local Agency Financing Contract as if the Fiscal Agent had been the original party thereto, and, except where the context otherwise requires, every reference in the Local Agency Financing Contract to the Corporation shall be deemed and construed to refer to the Fiscal Agent. Anything in the Agency Financing Contract to the contrary notwithstanding, such grant, sale, assignment, transfer and conveyance shall not confer any rights or impose any duties or obligations on the Fiscal Agent other than as expressly set forth in the Trust Agreement and the Master Assignment.

The State Agency acknowledges and agrees that, concurrently with the execution and delivery hereof, the Corporation will unconditionally grant, sell, assign, transfer and convey to the Fiscal Agent without recourse:

(1) all of its rights to receive the Installment Payments under and pursuant to the Master Financing Contract; and

(2) all of its remaining right, title and interest in, to and under the Master Financing Contract and the Agency Financing Contracts, and in and to the Property (including any security interest therein), including but not limited to its right to take all actions and exercise all remedies under and pursuant to the Master Financing Contract, pursuant to the Master Assignment in consideration for the payment by the Fiscal Agent to the Treasurer, as agent of the Corporation, of the proceeds of the sale of the Certificates.

The State and the Corporation have acknowledged and agreed that such grant, sale, assignment, transfer and conveyance by the Corporation is intended to be a true sale of the Corporation's right, title and interest, and that upon such grant, sale, assignment, transfer and conveyance, the Corporation shall cease to have any rights, duties or obligations under the Master Financing Contract or the State Agency Financing Addendum or with respect to the Property, and the Fiscal Agent shall thereafter have all the rights, duties and obligations of the Corporation thereunder and under the State Agency Financing Addendum as if the Fiscal Agent had been the original party thereto and hereto, and every reference therein and in the State Agency Financing Addendum to the Corporation shall be deemed and construed to refer to the Fiscal Agent, except where the context otherwise requires. Anything in the State Agency Financing Addendum or therein to the contrary notwithstanding, such grant, sale, assignment, transfer and conveyance shall not confer any rights or impose any duties or obligations on the Fiscal Agent other than as expressly set forth in the Trust Agreement and the Master Assignment.

**Optional Prepayment**

The Agency may, at its option, prepay all or any portion of its Agency Installment Payments then unpaid, in whole or in part on any date, by causing to be deposited with the Treasurer money and/or Government Obligations in an amount sufficient for the Treasurer to prepay or defease the portion of its Installment Payments corresponding thereto in accordance with the Master Financing Contract, and to pay any Additional Costs in connection therewith.

The Agency shall provide the Treasurer with not less than 60 days' prior written notice of its intention to prepay any of its Agency Installment Payments, which notice shall specify the date of such prepayment, and the amount and the Agency Installment Payment Dates of the Agency Installment Payments to be prepaid. The Treasurer shall notify the Agency within 15 Business Days after receipt of such notice from the Agency as to the amount required to be paid in connection with such prepayment or defeasance of the corresponding Installment Payments, including any Additional Costs in connection therewith. The determination by the Treasurer of the amount to be paid by the Agency shall be binding and conclusive against such Agency, absent manifest error.

**Revision of Agency Installment Payments upon Optional Prepayment**

The Principal Components and Interest Components of the Agency Installment Payments due on each Agency Installment Payment Date on and after the date of any prepayment pursuant to the Agency Financing Contract, as set forth in Exhibit D to the Agency Financing Contract, shall be reduced by the Treasurer to reflect such prepayment, in such amounts and on such Agency Installment Payment Dates as the Agency shall elect in its written notice to the Treasurer, pursuant to the Agency Financing Contract.

**Discharge of Agency Financing Contract**

All right, title and interest of the State in the Agency Financing Contract and all obligations of the Agency under the Agency Financing Contract shall cease, terminate, become void and be completely discharged and satisfied (except for the right of the Treasurer and the Fiscal Agent, as assignee of the Corporation, and the obligation of the Agency to have the moneys and Government Obligations so set aside applied to make the remaining Agency Installment Payments) when either:

(1) all Agency Installment Payments and all Additional Costs and other amounts due under the Agency Financing Contract have been paid in accordance therewith; or

(2) (a) the Agency shall have delivered a written notice to the Treasurer of its intention to prepay all of the Agency Installment Payments remaining unpaid;

(b) the Agency shall have caused to be deposited with the Treasurer (i) moneys and/or Government Obligations in accordance with the Agency Financing Contract; and (ii) an Opinion of Counsel to the effect that such actions are permitted under the Agency Financing Contract, under the Master Financing Contract and under the Trust Agreement and will not cause interest evidenced and represented by the Certificates to be includable in gross income for federal income tax purposes under the Code; and

(c) for so long as any Agency Installment Payments remain unpaid, provision shall have been made satisfactory to the Corporation and the Fiscal Agent for payment of all Additional Costs.

**Permitted Termination Events for State Agency Financing Addendum**

The following shall constitute a "Permitted Termination Event" under the State Agency Financing Addendum:

(1) The State Legislature elects not to appropriate sufficient funds within any biennial budget for the purpose of paying the Agent Installment Payments due under the State Agency Financing Addendum during the next occurring biennium; or

(2) The Governor of the State issues an Executive Order mandating an emergency reduction in State funding;

*provided*, that the State Agency delivers written notice thereof to the Treasurer as provided in the following paragraph.

***Written Notice Describing a Permitted Termination Event.*** If, as of five Business Days following (1) the enactment of each biennial budget by the State Legislature or (2) an Executive Order reduction in funding, the State Agency determines as a result of such legislation or Executive Order that sufficient funds will not be available to make its scheduled Agency Installment Payments for the Property in the next occurring Biennium or upon a reduction in funding in the manner as set forth above, the State Agency shall deliver written notice to the Treasurer not less than 45 days prior to the Permitted Termination Date, which notice shall describe the Permitted Termination Event, and state that the State Agency has determined that such Permitted Termination Event will result in the cancellation of the applicable Financing Contract and the related obligation of the Treasurer under the Master Financing Contract.

***Remedies of the Corporation Upon a Permitted Termination Event.*** Upon the occurrence of a Permitted Termination Event and upon the Written Request of the State Treasurer, the director or other chief administrator of the State Agency shall, at the beginning of the period for which funds have not been appropriated or for which funding has been reduced, return the Property to the Corporation and thereupon be released of its obligations to make all further Agency Installment Payments under its Agency Financing Contract and under the Master Financing Contract with respect to the Property; *provided*, that the State Agency delivers the Property in good repair, working order and condition, ordinary wear and tear excepted, and its unencumbered title to the Corporation at a location in the United States designated by the Corporation as of the end of the last month for which funding has been provided, or the end of the last month for which funding is available in the event of an Executive Order reduction in funding, and written notice is provided by the State Agency directly to the Treasurer as set forth in its Financing Contract. If the State Agency returns the Property pursuant to the terms of this paragraph, the Treasurer and the Corporation shall be entitled to retain all sums theretofore transmitted to the Treasurer or the Corporation (or to the Fiscal Agent as assignee of the Corporation) by or on behalf of the State Agency for the benefit of the Owners of the Certificates.

The occurrence of a Permitted Termination Event shall not constitute an Agency Event of Default, a Master Contract Event of Default or an Event of Default, and the remedies relating to the return of the Property are the sole remedies available to the Treasurer and the Corporation upon such occurrence. If the State Legislature provides a supplemental appropriation or the Executive Order is withdrawn prior to the expiration of the specified notice period and the Treasurer or the Corporation has not yet sold, relet or otherwise disposed of the Property, the State Agency may, by written notice to the Treasurer and the Corporation, revoke the notice of termination and continue its obligations under the Financing Contract.

**Covenants and Agreements of the Agency**

The Agency covenants and agrees as follows:

***Budget.*** The Local Agency shall take such action as may be necessary to include all the Agency Installment Payments and Additional Costs due under the Local Agency Financing Contract in its annual budget and to make the necessary annual appropriations for all such Agency Installment Payments and Additional Costs.

The State Agency shall (1) include in its biennial budget all payments required to be made by the State Agency under the State Agency Financing Addendum; (2) submit such budget to OFM at such times and in such manner as required by law; (3) use its best efforts to obtain appropriations by the State Legislature in amounts sufficient to make any such payments; (4) include all such payments in its statements of proposed expenditures for each fiscal period required by law to be submitted to OFM; and (5) use its best efforts to obtain allotments by OFM of appropriated funds sufficient to make all such payments.

***Application of Appropriations.*** To the extent permitted by law, each State Agency agrees that, to the extent that any amounts are included in its budget for purposes or facilities served, or functions or operations supported or provided, by the Property, the State Agency will allocate a sufficient portion of such amounts to the payment of the Agency Installment payments and Additional Costs due under its State Agency Financing Addendum.

***Tax-Exemption.*** The Agency shall not make any use of the proceeds of the Agency Financing Contract or the Certificates or of any other amounts, regardless of the source, or of any property, and shall not take or refrain from taking any action, that would cause the Master Financing Contract or the Certificates to be "arbitrage bonds" within the meaning of Section 148 of the Code. The Agency shall not use or permit the use of the Property or any part thereof by any Person other than a "governmental unit" as that term is

defined in Section 141 of the Code, in such manner or to such extent as would result in the loss of the exclusion from gross income for federal income tax purposes of the Interest Component of the Installment Payments under Section 103 of the Code. The Agency shall not make any use of the proceeds of the Agency Financing Contract or the Certificates or of any other amounts, and shall not take or refrain from taking any action, that would cause the Master Financing Contract or the Certificates to be "federally guaranteed" within the meaning of Section 149(b) of the Code, or "private activity bonds" within the meaning of Section 141 of the Code, or "hedge bonds" within the meaning of Section 149 of the Code. To that end, for so long as any Agency Installment Payments remain unpaid, the Agency, with respect to such proceeds and other amounts, will comply with all requirements under such Sections and all applicable regulations of the United States Department of the Treasury promulgated under the Agency Financing Contract. The Agency will at all times do and perform all acts and things permitted by law which are necessary or desirable in order to assure that the Interest Components of the Installment Payments will not be included in gross income of the Owners of the Certificates for federal income tax purposes under the Code, and will take no action that would result in such interest being so included. The Agency shall comply with the applicable provisions of the Tax Certificate and Agreement.

***Liens; Sale or Disposal.*** The Agency shall not create, incur, assume or suffer to exist any mortgage, pledge, lien, charge, encumbrance or claim on or with respect to the Property, except the rights of the Corporation as provided in the Agency Financing Contract and in the Master Financing Contract. The Agency shall promptly, at its own expense, take such action as may be necessary to duly discharge any such mortgage, pledge, lien, charge, encumbrance or claim if the same shall arise at any time. The Agency shall not grant, sell, transfer, assign, pledge, convey or otherwise dispose of any of the Property or any interest tin the Agency Financing Contract during the term of the Agency Financing Contract, and any such attempted grant, sale, transfer, assignment, pledge, conveyance or disposal shall be void.

***Pledge of Funds and Credit of Local Agency.*** The obligations of the Local Agency under the Local Agency Financing Contract constitute a debt and a general obligation of the Local Agency, and a contracting of an indebtedness by the Local Agency, to which the full faith and credit of the Local Agency are pledged. If and to the extent authorized by law, the Local Agency covenants and agrees that it will levy taxes in such amounts and at such times as shall be necessary, within and as a part of the tax levy, if any, permitted to the Local Agency without a vote of its electors, to provide funds, together with other legally available moneys, sufficient to make the Agency Installment Payments and the other payments required under the Local Agency Financing Contract.

***Use of Property.*** During the term of the Agency Financing Contract, the Agency will use the Property for the purposes of performing one or more of its essential governmental functions or responsibilities. The Agency will not permit the Property to be used or operated other than by authorized employees, agents and contractors of the Agency.

***Use; Repairs.*** For so long as the Agency is in possession of the Property, the Agency shall be solely responsible for the maintenance and repair, both ordinary and extraordinary, thereof. The Agency will: (1) keep and maintain the Property in good repair, working order and condition, and protect the same from deterioration other than normal wear and tear; (2) cause the Property to be used within its normal capacity, in the manner contemplated by the manufacturer's specification, and in compliance with the requirements of applicable laws, ordinances and regulations, the requirements of any warranties applicable thereto, and the requirements of any insurance or self-insurance program required under the Agency Financing Contract; (3) cause the Property to be used and operated by or under the direction of competent persons only, and obtain all registrations, permits and licenses, if any, required by law for the operation of the Property; and (4) will pay all costs, claims, damages, fees and charges arising out of its possession, use or maintenance of the Property. The Agency, at its expense, will furnish all parts, mechanisms and devices required to operate and maintain the Property.

***Insurance.*** The Agency shall maintain, or cause to be maintained, in full force and effect, comprehensive general liability insurance with respect to the Property in such amounts as may be reasonably determined by the Agency from time to time but in any event not less than $1,000,000 per occurrence, or such greater amount as the Treasurer may reasonably require from time to time. Such insurance may be carried under a blanket policy with umbrella coverage. Such insurance shall cover any and all liability of the Agency and its officials, officers, employees and volunteers. Such insurance shall include (1) coverage for any accident resulting in personal injury to or death of any person and consequential damages arising therefrom; and (2) comprehensive property damage insurance.

The Agency shall maintain or cause to be maintained in full force and effect fire and extended coverage insurance covering the Property in such amounts and covering such risks as the Agency may reasonably determine from time to time but in any event not less than the aggregate amount of Agency Installment Payments due under the Agency Financing Contract which remain unpaid. Such insurance may be carried under a policy or policies covering other property of the Agency. In the alternative, the Agency may assume financial responsibility for any physical damage to and/or loss of the Property; *provided, however*, that if the Agency elects this option, the Agency covenants and agrees that it will promptly repair or replace the Property promptly upon any loss or damage thereto.

The insurance required under the Agency Financing Contracts summarized above:

(1) shall be provided by a financially responsible insurance company authorized to do business in the State;

(2) shall name the State, the Corporation and the Fiscal Agent, as assignee of the Corporation, as additional insureds under the Agency Financing Contract;

(3) shall provide that the same may not be canceled or given notice of non-renewal, nor shall the terms of conditions thereof be altered, amended or modified, without at least 45 days' prior written notice being given by the insurer to the Treasurer, the Corporation and the Fiscal Agent as assignee of the Corporation; and

(4) may be provided in whole or in part through a funded program of self-insurance reviewed at least annually by an insurance actuary.

A certificate of insurance with respect to the required coverages shall be provided by the Agency to the Treasurer on or prior to the date of delivery of the Personal Property Certificate to the Treasurer.

The Agency will pay or cause to be paid when due the premiums for all insurance policies required by the Agency Financing Contract.

**Agency Event of Default**

Each of the following shall constitute an "Agency Event of Default" under the Agency Financing Contract:

(1) Failure by the Agency to pay or cause to be paid any Agency Installment Payment required to be paid under the Agency Financing Contract within 10 Business Days of the respective Agency Installment Payment Date, other than (in the case of a State Agency) as a result of a Permitted Termination Event;

(2) Failure by the Agency to observe or perform any covenant, agreement, term or condition on its part to be observed or performed under the Agency Financing Contract, other than as set forth in paragraph (1) above, for a period of 30 days after written notice from the Treasurer or the Fiscal Agent to the Agency specifying such failure and requesting that it be remedied, other than (in the case of a State Agency) as a result of a Permitted Termination Event; *provided, however*, that such period shall be extended for not more than 60 days if such failure cannot be corrected within such period, and the corrective action is commenced by the Agency within such period and diligently pursued until the failure is corrected;

(3) If any statement, representation, or warranty made by the Agency in the Agency Financing Contract or in any writing delivered by the Agency pursuant hereto or in connection therewith is false, misleading, or erroneous in any material respect; and

(4) Inability of the Agency to generally pay its debts as such debts become due, or admission by the Agency in writing of its inability to pay its debts generally or the making by the Agency of a general assignment for the benefit of creditors, or the institution of any proceeding by or against the Agency seeking to adjudicate it as bankrupt or insolvent, or seeking liquidation, winding-up, reorganization, reimbursement, adjustment, protection, relief or composition of it or its debts under any law relating to bankruptcy, insolvency or reorganization or relief of debtors, or seeking the entry of an order for relief or for appointment of a receiver, trustee, or other similar officer of it or any substantial part of its property, or the taking of any action by the Agency to authorize any of the actions set forth above in the Agency Financing Contract.

Notwithstanding the foregoing provisions, if by reason of *force majeure* the Agency is unable in whole or in part to carry out the covenants, agreements, terms and conditions on its part contained in the Agency Financing Contract, the Agency shall not be deemed in default during the continuance of such inability. The term "*force majeure*" means the following: acts of God; strikes; lockouts or other industrial disturbances or disputes; acts of public enemies; orders or restraints of any kind of the government of the United States of America or any of its departments, agencies or officials, or of its civil or military authorities; orders or restraints of the State or of any of its departments, agencies or officials or civil or military authorities of the State; wars, rebellions, insurrections; riots; civil disorders; blockade or embargo; landslides; earthquakes; fires; storms; droughts; floods; explosions; or any other cause or event not within the control of the Agency.

The Treasurer, with the prior written consent of the Fiscal Agent, may, at its election, waive any default or Agency Event of Default and its consequences under the Agency Financing Contract and annul any notice thereof by written notice to the Agency to such effect, and thereupon the respective rights of the Parties under the Agency Financing Contract shall be as they would have been if such default or Agency Event of Default had not occurred.

**Rights of Treasurer Following Agency Event of Default**

Whenever an Agency Event of Default shall have occurred and be continuing, the Treasurer shall have the following rights and remedies:

(1) By written notice to the Agency, require that the Agency promptly return possession and use of the Property to the Treasurer at any location specified in the United States (at the cost and expense of the Agency) in good repair, working order and condition, ordinary wear and tear excepted;

(2) By written notice to the Agency and the Fiscal Agent, declare an amount equal to all Agency Installment Payments to become due and payable under the Agency Financing Contract, including but not limited to the Agency Interest Components thereof accrued and unpaid, to be immediately due and payable, without further demand;

(3) Take whatever action at law or in equity may appear necessary or desirable to collect the Agency Installment Payments then due and thereafter becoming due, or to enforce the observance or performance of any covenant, agreement or obligation of the Agency under the Agency Financing Contract; and

(4) Exercise any other rights or remedies it may have under the Agency Financing Contract or under applicable law.

**No Remedy Exclusive; Non-Waiver**

No remedy conferred upon or reserved to the Treasurer under the Agency Financing Contract or under applicable law is intended to or shall be exclusive, and every such remedy shall be cumulative and shall be in addition to every other remedy given under the Agency Financing Contract or now or existing at law or in equity. No delay or omission to exercise any right or remedy accruing upon a default or an Agency Event of Default under the Agency Financing Contract shall impair any such right or remedy or shall be construed to be a waiver of such default or Agency Event of Default, but any such right or remedy may be exercised from time to time and as often as may be deemed necessary or expedient. In order to exercise any remedy reserved to the Treasurer under the Agency Financing Contract, it shall not be necessary to give any notice, other than such notice as may be required under the Agency Financing Contract. A waiver by the Treasurer of any default or Agency Event of Default under the Agency Financing Contract shall not constitute a waiver of any subsequent default or Agency Event of Default under the Agency Financing Contract, and shall not affect or impair the rights or remedies of the Treasurer in connection with any such subsequent default or Agency Event of Default.

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# APPENDIX C

## PROPOSED FORM OF CERTIFICATE COUNSEL OPINION

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[FORM OF APPROVING LEGAL OPINION]

State of Washington
c/o State Finance Committee
Olympia, Washington

Re: State of Washington Certificates of Participation, Series 2011D
(State and Local Agency Real and Personal Property)

We have acted as special counsel to the state of Washington (the "State") in connection with the execution and delivery by The Bank of New York Mellon in the capacity of fiscal agent of the State (the "Fiscal Agent") of Certificates of Participation, Series 2011D (State and Local Agency Real and Personal Property), in the Initial Principal Amount of $_____ (the "Certificates") pursuant to a Trust Agreement, Series 2011D (the "Trust Agreement"), dated as of November 16, 2011 (the "Dated Date"), by and among the State, acting by and through the State Treasurer of the State (the "State Treasurer"), the Fiscal Agent and the Washington Finance Officers Association (the "Corporation"), a Washington nonprofit corporation. Capitalized terms used in this opinion that are not otherwise defined have the meanings given such terms in Appendix I to the Trust Agreement.

The Certificates evidence and represent undivided proportionate ownership interests in the Principal Components and Interest Components of Installment Payments and Base Rent Payments to be made by the State ("State Payments") pursuant to a Master Financing Contract, Series 2011D (the "Master Financing Contract"), and a Master Financing Lease, Series 2011D (the "Master Financing Lease" and together with the Master Financing Contract, the "Master Financing Agreements"), each dated as of the Dated Date, entered into by and between the Corporation and the State, acting by and through the State Treasurer, to finance or refinance the acquisition and/or improvement of certain personal property and real property (the "Property") for State Agencies and Local Agencies (the "Agencies").

The Master Financing Contract constitutes a special, limited obligation of the State payable solely from the sources set forth therein, including Agency Installment Payments required to be paid by the State Agencies pursuant to State Agency Financing Addenda, Series 2011D (the "State Agency Financing Addenda"), to the Master Financing Contract, and by Local Agencies pursuant to Local Agency Financing Contracts, Series 2011D (the "Local Agency Financing Contracts," and, together with the State Agency Financing Addenda, the "Agency Financing Contracts"). The Master Financing Lease also constitutes a special, limited obligation of the State payable solely from the sources set forth therein, including Agency Rent Payments required to be paid by the State Agencies pursuant to State Agency Financing Lease Addenda, Series 2011D (the "State Agency Financing Lease Addenda"), to the Master Financing Lease, and by Local Agencies pursuant to Local Agency Financing Leases, Series 2011D (the "Local Agency Financing Leases," and, together with the State Agency Financing Lease Addenda, the "Financing Leases"). The Agency Financing Contracts and Financing Leases together are the "Agency Financing Agreements." Pursuant to the Master Financing Agreements, the State Treasurer is conditionally obligated, to the extent of legally available appropriated funds, to pay Agency Installment

Payments and Agency Rent Payments when due under Local Agency Financing Contracts and Local Agency Financing Leases upon the default of any Local Agency.

Pursuant to a Master Assignment, Series 2011D (Equipment), and a Master Assignment, Series 2011D (Real Property) (together, the "Master Assignments"), each dated as of the Dated Date, the Corporation has unconditionally granted, sold, assigned, transferred and conveyed to the Fiscal Agent without recourse (i) all of its rights to receive the State Payments under and pursuant to the Master Financing Agreements, and (ii) all of its remaining right, title and interest in, to and under the Master Financing Agreements and the Agency Financing Agreements, and in and to the Property (including any security interest therein), including but not limited to its right to take all actions and exercise all remedies under and pursuant to the Master Financing Agreements.

As to matters of fact material to this opinion, we have relied upon representations contained in the certified proceedings and other certifications of public officials furnished to us, without undertaking to verify the same by independent investigation.

Under the Internal Revenue Code of 1986, as amended (the "Code"), the State and the Agencies are required to comply with certain requirements after the date of execution and delivery of the Certificates in order to maintain the exclusion of the interest evidenced and represented by the Certificates from gross income for federal income tax purposes, including, without limitation, requirements concerning the qualified use of Certificate proceeds and the Property financed or refinanced with Certificate proceeds, limitations on investing gross proceeds of the Certificates in higher yielding investments in certain circumstances, and the arbitrage rebate requirement to the extent applicable to gross proceeds of the Certificates. The State and the Agencies have covenanted to comply with those requirements, but if the State or the Agencies fail to comply with those requirements, interest evidenced and represented by the Certificates could become taxable retroactive to the date of execution and delivery of the Certificates. We have not undertaken and do not undertake to monitor compliance with such requirements.

Under the statutes, regulations, published rulings and court decisions existing on the date of this opinion and based on our review of such other documents, proceedings and certifications as we have deemed necessary, it is our opinion that:

1. The Master Financing Agreements have been duly authorized, executed and delivered by the State, acting by and through the State Treasurer and the respective State Agencies, and, assuming the due authorization, execution and delivery thereof by the Corporation, constitute valid, binding and enforceable obligations of the State payable solely from the sources set forth therein. The Master Financing Agreements do not constitute general obligations of the State, and neither the full faith and credit nor the taxing power of the State is pledged to the payment thereof.

2. The obligation of each State Agency to pay Agency Installment Payments or Agency Rent Payments during the term of its State Agency Financing Addenda or State Agency Financing Lease Addenda, constitutes a valid and binding obligation of such State Agency, subject to appropriation by the State Legislature and to Executive Order reduction by the Governor of the State. Such obligation does not constitute a general obligation of the State, and neither the full faith and credit nor taxing power of the State is pledged to the payment thereof.

3. The conditional obligation of the State Treasurer pursuant to the Master Financing Agreements to pay Agency Installment Payments and Agency Rent Payments under each Local Agency

Financing Contract and Local Agency Financing Lease upon the default of any Local Agency is subject to appropriation by the State Legislature and to Executive Order reduction by the Governor of the State. Such conditional obligation does not constitute a general obligation of the State, and neither the full faith and credit nor taxing power of the State is pledged to the payment thereof.

4. Assuming (a) the due authorization, execution and delivery of the Master Assignments by the Corporation and the Fiscal Agent, (b) the due authorization, execution and delivery of the Trust Agreement by the Corporation and the Fiscal Agent, and (c) the due authorization, execution and delivery of the Certificates by the Fiscal Agent, the Certificates are entitled to the benefits of the Master Assignments and the Trust Agreement.

5. Assuming compliance by the State and the Agencies after the date of execution and delivery of the Certificates with applicable requirements of the Code, the Interest Component of each State Payment ("Interest") under the Master Financing Agreements and received by the Owners of Certificates is excluded from gross income for federal income tax purposes and is not subject to the federal alternative minimum tax applicable to individuals; however, while Interest also is not an item of tax preference for purposes of the alternative minimum tax applicable to corporations, Interest received by corporations is to be taken into account in the computation of adjusted current earnings for purposes of the alternative minimum tax applicable to corporations, Interest received by certain S corporations may be subject to tax, and Interest received by foreign corporations with United States branches may be subject to a foreign branch profits tax.

We express no opinion regarding any other federal tax consequences arising with respect to the ownership of the Certificates. Owners of the Certificates should be aware that the ownership of tax-exempt obligations may result in collateral federal income tax consequences.

Our opinions with respect to the enforceability of various documents are subject to limitations imposed by bankruptcy, insolvency or other laws affecting creditors' rights and by the application of equitable principles and the exercise of judicial discretion in appropriate cases.

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

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

Respectfully submitted,

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# APPENDIX D

# THE STATE'S 2010 AUDITED BASIC FINANCIAL STATEMENTS

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# Washington State Auditor
# Brian Sonntag

## INDEPENDENT AUDITOR'S REPORT ON FINANCIAL STATEMENTS

November 30, 2010

The Honorable Christine Gregoire
Governor, State of Washington

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund and the aggregate discretely presented component units and remaining fund information of the State of Washington, as of and for the year ended June 30, 2010, which collectively comprise the State's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the State's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the Department of Retirement Systems, Washington's Lottery, Local Government Investment Pool, University of Washington, Western Washington University, and the funds managed by the State Investment Board. Those financial statements represent part or all of the total assets, net assets, and revenues or additions of the governmental activities, the business-type activities, each major fund, and the aggregate discretely presented component units and remaining fund information as follows:

| Opinion Unit | Percent of Total Assets | Percent of Net Assets | Percent of Total Revenues/ Additions |
|---|---|---|---|
| Governmental Activities | 11.8% | 21.2% | 12.8% |
| Business-Type Activities | 78.3% | 100% | 17.4% |
| Higher Education Special Revenue Fund | 39.2% | 30.7% | 48.9% |
| Higher Education Endowment Fund | 91.2% | 96.7% | 90.4% |
| Higher Education Student Services Fund | 73.3% | 82.5% | 80.2% |
| Workers' Compensation Fund | 99.0% | 100% | 44.8% |
| Aggregate Discretely Presented Component Units and Remaining Fund Information | 90.2% | 95.5% | 83.7% |

Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinion, insofar as it relates to the amounts included for the above mentioned entities and funds are based solely on the reports of other auditors.

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

Insurance Building, P.O. Box 40021 • Olympia, Washington 98504-0021 • (360) 902-0370 • TDD Relay (800) 833-6388
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In our opinion, based on our audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund and the aggregate discretely presented component units and remaining fund information of the State of Washington, as of June 30, 2010, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

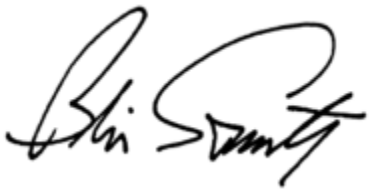
As explained in Note 1.D.1, the financial statements include pension trust fund investments valued at $21.7 billion which comprise 25.4% of total assets and 30.5% of net assets of the aggregate discretely presented component units and remaining fund information. The fair values of these investments have been estimated by management in the absence of readily determinable fair values. Management's estimates are based on information provided by the fund managers or, in the case of investments in partnerships, the general partners.

As described in Note 2, during the year ended June 30, 2010, the State implemented Governmental Accounting Standards Board Statement No. 51 - Accounting and Financial Reporting for Intangible Assets and Statement No. 53 - Accounting and Financial Reporting for Derivative Instruments.

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

Our audit was performed for the purpose of forming opinions on the financial statements that collectively comprise the State of Washington's basic financial statements. The information listed in the table of contents as combining and individual fund financial statements and schedules is presented for purposes of additional analysis and is not a required part of the basic financial statements. This information has been subjected to the auditing procedures applied by us and the other auditors in the audit of the basic financial statements and, in our opinion, based on our audit and the reports of other auditors, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

The information identified in the table of contents as the introductory and statistical sections is not a required part of the basic financial statements but is supplementary information presented for purposes of additional analysis. Such information has not been subjected to the auditing procedures applied by us and the other auditors in the audit of the basic financial statements and, accordingly, we express no opinion on it.



**BRIAN SONNTAG, CGFM**
STATE AUDITOR

# MD&A
# Management's Discussion and Analysis

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# MD&A
# Management's Discussion & Analysis

As managers of the state of Washington, we offer this narrative overview and analysis of the financial activities for the fiscal year ended June 30, 2010. We present this information in conjunction with the information included in our letter of transmittal, which can be found preceding this narrative, and with the state's financial statements, which follow. All amounts, unless otherwise indicated, are expressed in thousands of dollars.

## Financial Highlights

- Total assets of the state of Washington exceeded its liabilities by $16.2 billion (reported as net assets). Of this amount, $(11.1) billion was reported as "unrestricted (deficit) net assets." A negative balance indicates that no funds were available for discretionary purposes.

- The state of Washington's governmental funds reported a combined ending fund balance of $10.5 billion, an increase of 10 percent compared with the prior year.

- The General Fund reported an unreserved fund balance (deficit) of $(561) million, at the end of Fiscal Year 2010, or 2.4 percent of total General Fund expenditures.

- The state's capital assets increased by $1.8 billion while total bond debt increased by $2.7 billion during the current fiscal year. Of the total bond debt issued, $1.1 billion was unspent at year end largely related to a June 2010 bond issuance.

## Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the state of Washington's basic financial statements, which include three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. The focus is on both the state as a whole (government-wide) and the major individual funds. The dual perspectives allow the reader to address relevant questions, broaden a basis for comparison (year-to-year or government-to-government), and enhance the state's accountability.

### GOVERNMENT-WIDE FINANCIAL STATEMENTS

The government-wide financial statements are designed to provide readers with a broad overview of the state of Washington's finances, in a manner similar to a private sector business.

**Statement of Net Assets.** The *Statement of Net Assets* presents information on all of the state of Washington's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the state of Washington is improving or deteriorating.

**Statement of Activities.** The *Statement of Activities* presents information showing how the state's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave). The Statement of Activities is focused on both the gross and net cost of various activities (including governmental, business-type, and component unit). This is intended to summarize and simplify the reader's analysis of the revenues and costs of various state activities and the degree to which activities are subsidized by general revenues.

Both of these government-wide financial statements distinguish functions of the state of Washington that are principally supported by taxes and intergovernmental revenues (governmental activities) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (business-type activities).

The governmental activities of the state of Washington include education, human services, transportation, natural resources, adult corrections, and general government.

The business-type activities of the state of Washington include the workers' compensation and unemployment compensation programs, as well as Washington's lottery, liquor control, and various higher education student services such as housing and dining.

The government-wide financial statements can be found on pages 37-39 of this report.

## FUND FINANCIAL STATEMENTS

A fund is a group of related accounts used to maintain control over resources that are segregated for specific activities or objectives. The state of Washington, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the state can be divided into three categories: governmental funds, proprietary funds, and fiduciary funds.

**Governmental Funds.** Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for four major funds and an aggregate total for all nonmajor funds. The state's major governmental funds are the General Fund, Higher Education Special Revenue Fund, the Motor Vehicle Fund, and the Higher Education Endowment Fund. Individual fund data for the state's nonmajor governmental funds are provided in the form of combining statements elsewhere in this report. The governmental fund financial statements can be found on pages 42-45 of this report.

**Proprietary Funds.** The state of Washington maintains two different types of proprietary funds. Enterprise funds are used to report the same functions presented as business-type activities in the government-wide financial statements. Internal service funds represent an accounting device used to accumulate and allocate costs internally among the state of Washington's various functions. The state of Washington uses internal service funds to account for general services such as motor pool, central stores, data processing services, risk management, employee health insurance, and printing services. Because internal service funds predominately benefit governmental rather than business-type functions, they have been included within governmental activities in the government-wide financial statements.

Proprietary fund financial statements provide the same type of information as the government-wide financial statements, but in greater detail. The proprietary fund financial statements provide separate information for the Workers' Compensation Fund, Unemployment Compensation Fund, and the Higher Education Student Services Fund, which are considered to be major funds, as well as an aggregated total for all nonmajor enterprise funds.

The internal service funds are combined for presentation purposes. Individual fund data for the state's nonmajor proprietary funds are provided in the form of combining statements elsewhere in this report. The proprietary fund financial statements can be found on pages 46-51 of this report.

**Fiduciary Funds.** Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are not available to support the state of Washington's own programs. Washington's fiduciary funds include state administered pension plans. The accounting used for fiduciary funds is much like that used for proprietary funds. Individual fund data for the state's fiduciary funds are provided in the form of combining statements elsewhere in this report.

The fiduciary fund financial statements can be found on pages 52-53 of this report.

**Component Units.** Component units that are legally separate from the state and primarily serve or benefit those outside the state are discretely presented. They are either financially accountable to the state, or have relationships with the state such that exclusion would cause the state's financial statements to be misleading or incomplete. The state discretely reports one major component unit, the Washington State Public Stadium Authority, and four nonmajor component units.

Refer to Note 1 on pages 59-60 for more detailed information. Individual fund data for the state's nonmajor component units are provided in the form of combining statements elsewhere in this report. The component unit financial statements can be found on pages 54-55 of this report.

## NOTES TO THE FINANCIAL STATEMENTS

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 57-152 of this report.

## OTHER REQUIRED INFORMATION

In addition to this discussion and analysis, this report also presents required supplementary information on budgetary comparisons, pension plans and other post-employment benefits, funding progress, and infrastructure assets reported using the modified approach.

Required supplementary information can be found on pages 153-179 of this report.

The combining statements referred to earlier are presented immediately following the required supplementary information. Combining and individual fund statements and schedules can be found on pages 181-231 of this report.

STATE OF WASHINGTON
**Statement of Net Assets**
*(in millions of dollars)*

| | Governmental Activities | | Business-Type Activities | | Total | |
|---|---|---|---|---|---|---|
| | 2010 | 2009 | 2010 | 2009 | 2010 | 2009 |
| **ASSETS** | | | | | | |
| Current and other assets | $ 16,915 | $ 15,611 | $ 22,080 | $ 21,027 | $ 38,995 | $ 36,638 |
| Capital assets | 31,247 | 29,558 | 2,254 | 2,099 | 33,501 | 31,657 |
| Total assets | 48,162 | 45,169 | 24,334 | 23,126 | 72,496 | 68,295 |
| **LIABILITIES** | | | | | | |
| Current and other liabilities | 3,730 | 3,593 | 3,421 | 2,653 | 7,151 | 6,246 |
| Long-term liabilities outstanding | 21,234 | 17,721 | 27,934 | 25,689 | 49,168 | 43,410 |
| Total liabilities | 24,964 | 21,314 | 31,355 | 28,342 | 56,319 | 49,656 |
| **NET ASSETS** | | | | | | |
| Invested in capital assets, net of related debt | 18,201 | 17,551 | 913 | 721 | 19,114 | 18,272 |
| Restricted | 5,214 | 4,887 | 2,930 | 3,800 | 8,144 | 8,687 |
| Unrestricted (deficit) | (217) | 1,417 | (10,864) | (9,737) | (11,081) | (8,320) |
| Total net assets | $ 23,198 | $ 23,855 | $ (7,021) | $ (5,216) | $ 16,177 | $ 18,639 |

# Government-wide Financial Analysis

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. For the state of Washington, total assets exceed liabilities by $16.2 billion at June 30, 2010 as compared to $18.6 billion as reported at June 30, 2009.

The largest portion of the state's net assets (118.2 percent for Fiscal Year 2010 as compared to 98.0 percent for Fiscal Year 2009) reflects its investment in capital assets (e.g., land, buildings, equipment and intangible assets), less any related debt used to acquire those assets that is still outstanding. The state of Washington uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending.

Although the state of Washington's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

A portion of the state of Washington's net assets (50.3 percent for Fiscal Year 2010 as compared to 46.6 percent for Fiscal Year 2009) represents resources that are subject to external restrictions on how they may be used. The remaining balance of $(11.1) billion represents unrestricted (deficit) net assets. The state's overall negative balance is caused by deficits in both governmental and business-type activities.

In governmental activities, the deficit is largely related to decreased tax revenues in Fiscal Year 2010. The decline in tax revenues reflects the continued weak economy and the lack of consumer confidence.

In business-type activities, the majority of the deficit is caused by the workers' compensation program that provides time-loss, medical, disability and pension payments to qualifying individuals who sustain work-related injuries or develop occupational diseases as a result of their required work activities.

The main benefit plans of the workers' compensation program are funded on rates that will keep the plans solvent in accordance with recognized actuarial principles.

The supplemental pension cost-of-living adjustments (COLAs) granted for time-loss and disability payments, however, are funded on a pay-as-you-go basis. By statute, the state is only allowed to collect enough revenue to fund the current COLA payments.

As previously mentioned, the state's activities are divided between governmental and business-type. The majority of support for governmental activities comes from taxes and intergovernmental grants, while business-type activities are supported primarily through user charges.

STATE OF WASHINGTON

**Changes in Net Assets**

*(in millions of dollars)*

| | Governmental Activities | | Business-Type Activities | | Total | |
|---|---|---|---|---|---|---|
| | **2010** | **2009** | **2010** | **2009** | **2010** | **2009** |
| **REVENUES** | | | | | | |
| Program revenues: | | | | | | |
| Charges for services | $ 4,584 | $ 4,398 | $ 5,987 | $ 5,640 | $ 10,571 | $ 10,038 |
| Operating grants and contributions | 12,193 | 10,565 | 2,468 | 572 | 14,661 | 11,137 |
| Capital grants and contributions | 939 | 706 | - | - | 939 | 706 |
| General revenues: | | | | | | |
| Taxes | 14,982 | 16,001 | 160 | 113 | 15,142 | 16,114 |
| Interest and investment earnings (loss) | 449 | (212) | 1,743 | 291 | 2,192 | 79 |
| **Total Revenues** | 33,147 | 31,458 | 10,358 | 6,616 | 43,505 | 38,074 |
| **EXPENSES** | | | | | | |
| General government | (1,738) | (1,815) | - | - | (1,738) | (1,815) |
| Education - K-12 | (8,468) | (8,549) | - | - | (8,468) | (8,549) |
| Education - Higher education | (6,051) | (6,044) | - | - | (6,051) | (6,044) |
| Human services | (12,946) | (12,436) | - | - | (12,946) | (12,436) |
| Adult corrections | (938) | (1,044) | - | - | (938) | (1,044) |
| Natural resources and recreation | (1,084) | (1,062) | - | - | (1,084) | (1,062) |
| Transportation | (2,073) | (1,883) | - | - | (2,073) | (1,883) |
| Interest on long-term debt | (810) | (728) | - | - | (810) | (728) |
| Workers' compensation | - | - | (4,268) | (2,544) | (4,268) | (2,544) |
| Unemployment compensation | - | - | (4,729) | (2,360) | (4,729) | (2,360) |
| Higher education student services | - | - | (1,628) | (1,502) | (1,628) | (1,502) |
| Liquor control | - | - | (552) | (540) | (552) | (540) |
| Washington's lottery | - | - | (389) | (401) | (389) | (401) |
| Other business-type activities | - | - | (345) | (391) | (345) | (391) |
| **Total Expenses** | (34,108) | (33,561) | (11,911) | (7,738) | (46,019) | (41,299) |
| Excess (deficiency) of revenues over expenses before contributions to endowments and transfers | (961) | (2,103) | (1,553) | (1,122) | (2,514) | (3,225) |
| Contributions to endowments | 52 | 57 | - | - | 52 | 57 |
| Transfers | 252 | (190) | (252) | 190 | - | - |
| Increase (decrease) in net assets | (657) | (2,236) | (1,805) | (932) | (2,462) | (3,168) |
| Net assets - July 1 | 23,855 | 26,091 | (5,216) | (4,284) | 18,639 | 21,807 |
| Net assets - June 30 | $ 23,198 | $ 23,855 | $ (7,021) | $ (5,216) | $ 16,177 | $ 18,639 |

**Governmental Activities.** Governmental activities resulted in a decrease in the state of Washington's net assets of $657 million. A number of factors contributed to the decrease:

- Tax revenues decreased $1.0 billion in Fiscal Year 2010 as compared to Fiscal Year 2009 reflecting the negative impact of the slowing economy and slumping housing markets. While certain tax sources showed moderate increases, sales and use taxes reported a decrease of $435 million. Sales and use taxes are the main tax revenue for governmental activities. Taxable sales have declined due to reductions in consumer spending power as a result of job losses as well as weak consumer confidence. Real estate excise taxes also declined by $20 million reflecting the continued decline in real estate throughout Fiscal Year 2010 in spite of record low mortgage rates, declining home prices and the federal government's home-buyers tax credit program.

- Operating and capital grants and contributions increased $1.9 billion in Fiscal Year 2010 as compared to Fiscal Year 2009. American Recovery and Reinvestment Act grants made up $1.3 billion of the increase funding expenses in the areas of education, transportation, public health and the environment.

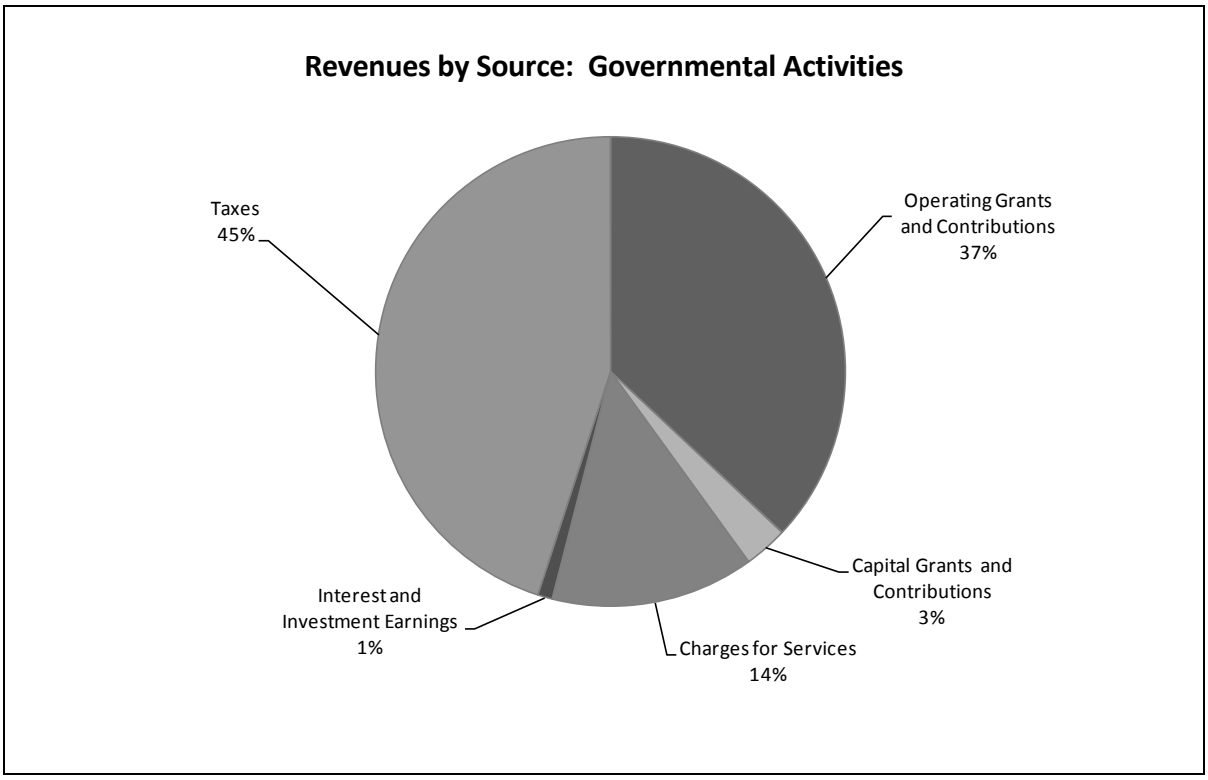
- Expenses grew slightly in spite of the drop in revenues. The expenses for human services and education comprised 80.5 percent of the total expenses for governmental activities which is consistent with the 80.5 percent in Fiscal Year 2009. Human services accounted for the majority of the growth in expenses increasing by $510 million or 4.1 percent in Fiscal Year 2010 over Fiscal Year 2009 reflecting the increased number of citizens seeking assistance from state programs and services due to the economic recession.

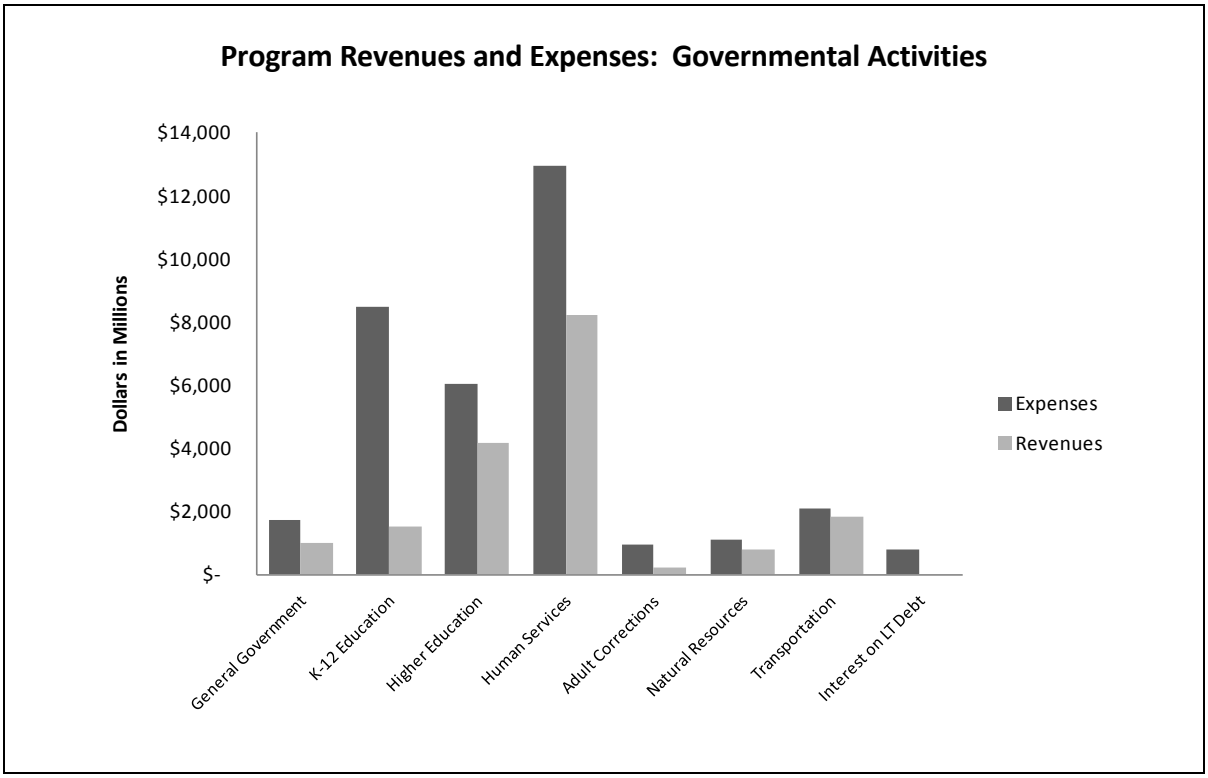
**Business-Type Activities.** Business-type activities decreased the state of Washington's net assets by $1.8 billion which included losses in both the workers' compensation and unemployment compensation activities. Key factors contributing to the operating results of business-type activities are:

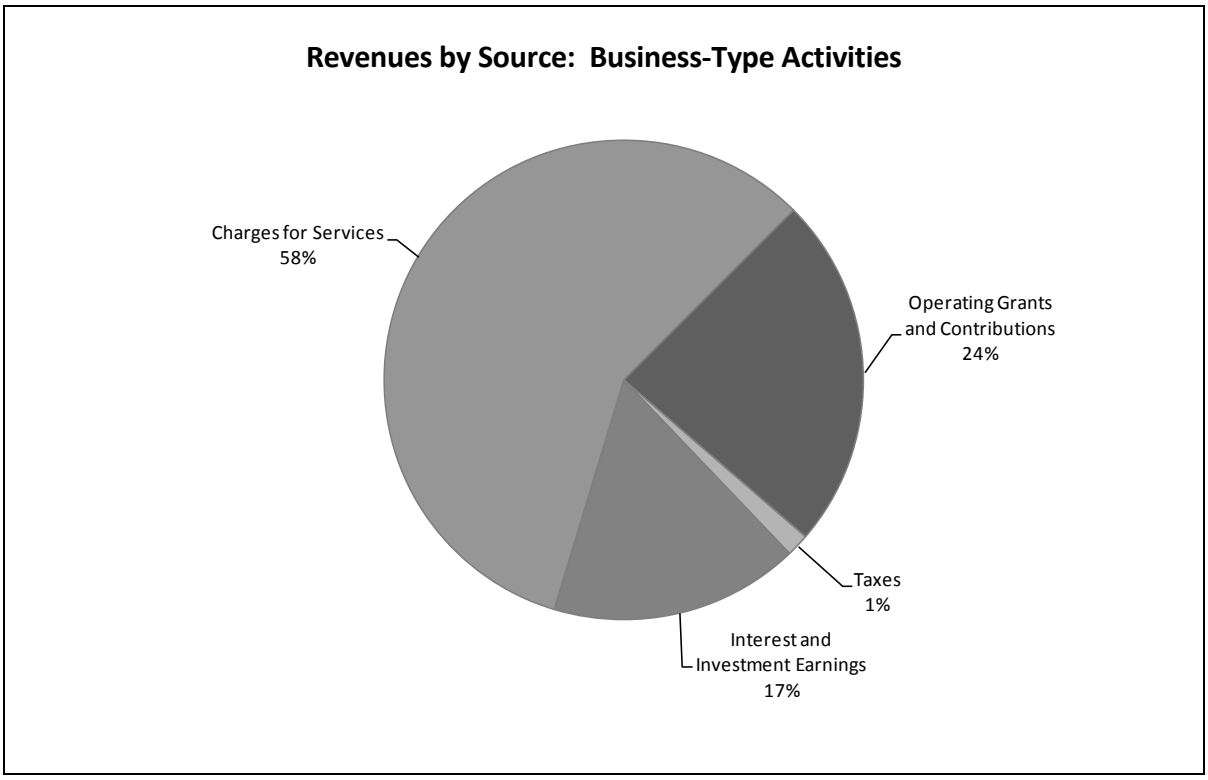
- The decrease in net assets in the workers' compensation activity in Fiscal Year 2010 was $598 million more than the decrease in Fiscal Year 2009. A number of factors contributed to the increased loss including a decrease in premium revenue of $97 million which resulted from a 5.2 percent decline in the number of reported hours worked reflecting the current recessionary stress on the job market. Claims costs increased by $1.8 billion or 82.1 percent in Fiscal Year 2010 compared with Fiscal Year 2009. The increase in claims costs is attributable to increases in forecasted future wage inflation, an increase in the number of pensions granted for permanent disability, and increases in the duration of time-loss claims affecting both current and prior year claims. Nonoperating investment income increased by $1.2 billion due to improvements in the financial markets.

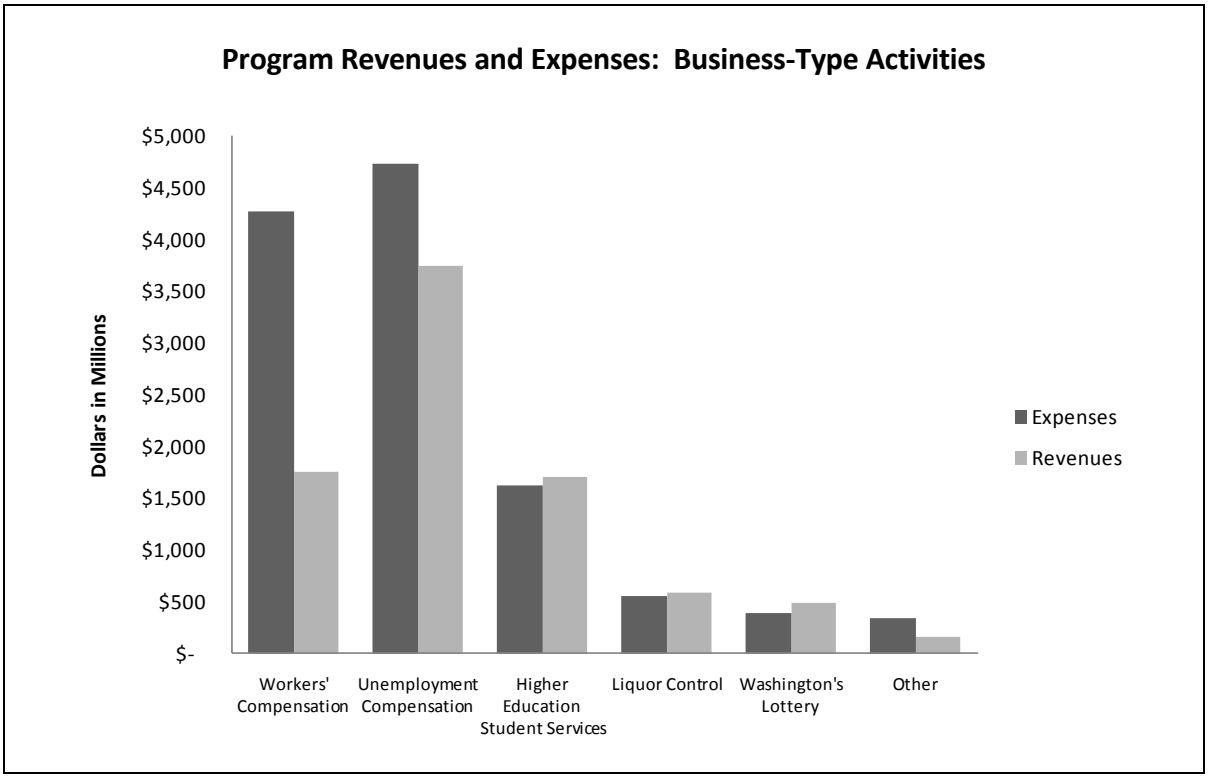
- The unemployment compensation activity reported a Fiscal Year 2010 operating loss of $985 million, compared to a $789 million operating loss in Fiscal Year 2009. Washington's unemployment insurance program is an experience-based system. Since Washington had relatively low unemployment until Fiscal Year 2009, unemployment premium revenue had been declining. Fiscal Year 2010 premium revenues reflected the first increase since Fiscal Year 2005. This increase combined with an increase in federal aid of $1.9 billion, which included American Recovery and Reinvestment Act funding, fell short of covering the increase in unemployment insurance benefits which rose by $2.4 billion over Fiscal Year 2009. The increase in benefit costs was the result of increases in the number of claims and the duration of claims. The annualized unemployment rate for the state was 9.2 percent in Fiscal Year 2010, up from 7.3 percent in Fiscal Year 2009, a 26 percent increase.

- The higher education student services activity reported relatively proportional increases in both expenses and charges for services when compared to the prior year. Additionally, both liquor control and Washington's lottery activities reported operating revenues and expenses consistent with the prior year.


Revenues by Source: Governmental Activities
Taxes
45%
Operating Grants
and Contributions
37%
Capital Grants and
Contributions
3%
Charges for Services
14%
Interest and
Investment Earnings
1%


Program Revenues and Expenses: Governmental Activities
Dollars in Millions
$14,000
$12,000
$10,000
$8,000
$6,000
$4,000
$2,000
$-
General Government
K-12 Education
Higher Education
Human Services
Adult Corrections
Natural Resources
Transportation
Interest on LT Debt
Expenses
Revenues


Revenues by Source: Business-Type Activities
Charges for Services 58%
Operating Grants and Contributions 24%
Taxes 1%
Interest and Investment Earnings 17%


Program Revenues and Expenses: Business-Type Activities
Dollars in Millions
$5,000
$4,500
$4,000
$3,500
$3,000
$2,500
$2,000
$1,500
$1,000
$500
$-
Workers' Compensation
Unemployment Compensation
Higher Education Student Services
Liquor Control
Washington's Lottery
Other
Expenses
Revenues

## Financial Analysis of the Government's Funds

As noted earlier, the state of Washington uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

**Governmental Funds.** As previously discussed, the focus of the state of Washington's governmental funds is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the state of Washington's financing requirements. In particular, unreserved fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

The General Fund is the chief operating fund of the state of Washington. Due to statutory changes, several related accounts were added to the General Fund during Fiscal Year 2010 to improve budget transparency.

At the end of Fiscal Year 2010, total fund balance for the General Fund equaled $379 million, a decrease of $783 million from Fiscal Year 2009. Unreserved fund balance included $864 million designated for working capital purposes. This amount relates to certain accrued revenues and is not considered by management to be available to spend.

The remaining unreserved fund balance deficit of $(561) million indicates that the state has overspent funds available for discretionary purposes. The deficit fund balance reflects the Fiscal Year 2010 decrease of $783 million which followed the $757 million decrease in Fiscal Year 2009. The back to back decreases are due to the recessionary economic conditions.

The increase in General Fund revenues and expenditures is largely attributable to the consolidation of the related accounts. Consistent with Fiscal Year 2009, revenues did not keep pace with the demand for services.

STATE OF WASHINGTON
**General Fund**
*(in millions of dollars)*

| | Fiscal Year 2010 | Fiscal Year 2009 | Difference Increase (Decrease) |
|---|---|---|---|
| **REVENUES** | | | |
| Taxes | $13,169 | $12,791 | $ 378 |
| Federal grants | 9,648 | 8,311 | 1,337 |
| Investment revenue (loss) | (9) | 64 | (73) |
| Other | 567 | 421 | 146 |
| **Total** | 23,375 | 21,587 | 1,788 |
| **EXPENDITURES** | | | |
| Human services | 13,209 | 11,912 | 1,297 |
| Education | 9,243 | 9,044 | 199 |
| Other | 1,331 | 1,223 | 108 |
| **Total** | 23,783 | 22,179 | 1,604 |
| Net transfers in (out) | (379) | (192) | (187) |
| Other financing sources | 4 | 27 | (23) |
| Net increase (decrease) in fund balance | $ (783) | $ (757) | $ (26) |

Expenditures continue to be concentrated in services and programs most vital to citizens – primarily human services and public education. In Fiscal Year 2010, the General Fund received $1.7 billion in American Recovery and Reinvestment Act funding predominately for human services and public education programs up from $927 million in Fiscal Year 2009.

In addition to the General Fund, the state reports the Higher Education Special Revenue, the Motor Vehicle Special Revenue and the Higher Education Endowment Funds as major governmental funds.

The fund balance of the Higher Education Special Revenue Fund increased by $114 million in Fiscal Year 2010. Increases in tuition and federal grant revenues offset the increased costs of higher education activities.

The fund balance of the Motor Vehicle Special Revenue Fund increased by $1.2 billion. The majority of this

increase is due to June bond sale proceeds intended for expenditure on construction projects during the summer months. The state issued $1.7 billion in federal Build America Bond bonds in Fiscal Year 2010 accelerating a portion of the planned Fiscal Year 2011 borrowings to take advantage of exceptionally low interest rates.

The fund balance for the Higher Education Endowment Fund increased by $251 million. While support from donors was consistent with the prior year, investment earnings of $270 million in Fiscal Year 2010 compared with investment losses of $474 million in Fiscal Year 2009 reflected improvement in the financial markets. The increase in investment earnings supported the increased use of funds to support donor specified activities.

The fund balance for nonmajor governmental funds increased by $186 million. The largest factor contributing to the increase is bond sale proceeds on hand at year end to cover construction projects in progress.

**Proprietary Funds.** The state of Washington's proprietary funds provide the same type of information found in the government-wide financial statements, but in more detail.

- The Workers' Compensation Fund reported a loss of $1.0 billion in Fiscal Year 2010. Operating revenues decreased by $101 million and operating expenses increased by $1.7 billion as compared to Fiscal Year 2009. As noted previously, operating revenues were down due to a reduction in reported worker hours reflecting the sluggish job market and claims were up due to increases in forecasted future wage inflation, an increase in the number of pensions granted for permanent disability, and increases in the duration of time-loss claims affecting both current and prior year claims. The negative changes were partially offset by an increase in investment income of $1.2 billion.

- Washington's average unemployment rate increased markedly in Fiscal Year 2010, as the continued slow national economy and weak housing markets took their toll on the labor markets. Despite an increase in federal aid of $1.9 billion, which included American Recovery and Reinvestment Act funding, the Unemployment Compensation Fund incurred a loss of $870 million.

- Activity for the various nonmajor proprietary funds resulted in a net increase to net assets of $18 million. The overall increase was reduced by the $20 million loss reported by the state's guaranteed college tuition (GET) program which is included in the Other Activities Fund. This GET loss was smaller than the $340 million loss reported in Fiscal Year 2009. The losses are primarily due to lower than projected investment earnings combined with higher than projected tuition increases. The GET program is continuing to proceed cautiously.

## General Fund Budgetary Highlights

Differences between the original budget of the General Fund and the final amended budget reflect adjustments related to changes in the state's economy during the year ended June 30, 2010. While there were no significant increases or decreases, changes to estimates are summarized as follows:

- Estimated resources increased by $950 million over the course of the first fiscal year. A decrease of $911 million was reported for taxes in recognition of the continued sluggish economy. The decrease in estimated tax revenue was offset by increases to federal grants-in-aid of $1.3 billion.

- Appropriated expenditure authority increased by $1.2 billion over the course of the Fiscal Year ended June 30, 2010. Increases were recorded in human services, natural resources and recreation, education and capital outlays of $1.2 billion, $90 million, $57 million, and $29 million, respectively. The largest decrease was in transfers to other funds of $171 million.

The state did not overspend its legal spending authority for the Fiscal Year 2010, the first year of the 2009-2011 Biennium. Actual General Fund revenues and expenditures were 48 and 49 percent of final budgeted revenues and appropriations, respectively, for the 2009-2011 Biennium.

## Capital Assets, Infrastructure, Bond Debt Administration, and Economic Factors

**Capital Assets.** The state of Washington's investment in capital assets for its governmental and business-type activities as of June 30, 2010 amounted to $33.5 billion (net of accumulated depreciation). This investment in capital assets includes land, infrastructure, museum and historical collections, buildings and other improvements, furnishings, equipment, and intangibles, as well as construction in progress.

Washington's Fiscal Year 2010 investment in capital assets, net of current year depreciation, was $1.8 billion, including increases to the state's transportation infrastructure of $1.4 billion and buildings of $558 million. The state's construction in progress includes both new construction and major improvements to state and common school capital facilities, transportation projects and assistance to local governments for public works capital projects.

Remaining commitments on these construction projects total $5.3 billion.

Additional information on the state of Washington's capital assets can be found in Note 6 beginning on page 96 of this report.

**Infrastructure.** The state of Washington first reported infrastructure under the requirements of the Governmental Accounting Standards Board (GASB) Statement No. 34 in Fiscal Year 2002. Transportation infrastructure reported includes the state highway system, emergency airports, and two short rail lines. While the rail lines are reported net of depreciation, the state highway system and emergency airports are reported using the modified approach. Under the modified approach, rather than recording depreciation, asset condition is reported.

STATE OF WASHINGTON

**Capital Assets - Net of Depreciation**

*(in millions of dollars)*

| | Governmental Activities | | Business-Type Activities | | Total | |
|---|---|---|---|---|---|---|
| | 2010 | 2009 | 2010 | 2009 | 2010 | 2009 |
| Land | $ 1,179 | $ 1,130 | $ 143 | $ 142 | $ 1,322 | $ 1,272 |
| Transportation infrastructure and other assets not depreciated | 19,758 | 18,328 | - | - | 19,758 | 18,328 |
| Buildings | 6,926 | 6,473 | 1,671 | 1,566 | 8,597 | 8,039 |
| Furnishings, equipment and intangible assets | 1,362 | 1,377 | 142 | 150 | 1,504 | 1,527 |
| Other improvements and infrastructure | 1,157 | 1,065 | 87 | 88 | 1,244 | 1,153 |
| Construction in progress | 865 | 1,185 | 211 | 153 | 1,076 | 1,338 |
| Total | $ 31,247 | $ 29,558 | $ 2,254 | $ 2,099 | $ 33,501 | $ 31,657 |

The condition of these assets, along with the rating scales for pavement, bridges, rest areas, and airports, and additional detail comparing planned-to-actual preservation and maintenance spending are available in the required supplementary information beginning on page 171.

The state highway system capital investment in Fiscal Year 2010 was a net of $1.4 billion to add additional lane miles, replace and build new bridges and highway structures, improve highway safety, increase mobility and preservation activities that extend the life of the system. Of this investment, $150.5 million was funded by the federal American Recovery and Reinvestment Act. The Washington State Department of Transportation (WSDOT) accomplished a net addition of 106 lane miles and 23 bridges and other highway structures in Fiscal Year 2010. Amounts spent during Fiscal Year 2010 to maintain and preserve these infrastructure assets were not significantly different from estimated spending plans according to the biennial budget.

The state highway system and emergency airports continue to meet established condition levels. No significant changes in condition levels were noted for pavements or bridges. Detailed information about targeted and actual condition levels for roads, bridges, rest areas, and airports can be found in the required supplementary information section of this report.

The safety of bridge structures is ensured through meticulous inspections and rating of the primary components of bridges by the WSDOT Bridge Preservation Office or local agency staff. The condition of all bridge decks, superstructures and substructures are rated based on these inspections.

The WSDOT's planned highway infrastructure projects for the next four years, Fiscal Years 2011 through 2014, would commit approximately $3.7 billion for 448 projects. These projects are either already in progress or are expected to commence within the next four years.

**Bond Debt.** At the end of Fiscal Year 2010, the state of Washington had general obligation bond debt outstanding of $16.6 billion, an increase of 18 percent over Fiscal Year 2009. This debt is secured by a pledge of the full faith and credit of the state. Additionally, the state had authorized $9.5 billion general obligation debt that remains unissued.

During Fiscal Year 2010, the state issued general obligation debt, totaling $3.9 billion, for various capital and transportation projects. The state took advantage of historically low interest rates and the federal Build America Bonds program to lock in long-term borrowing costs at unprecedented lows. Two Build America Bonds sales during Fiscal Year 2010 provided $1.6 billion to finance transportation projects at the lowest net effective true

interest cost in state history. Washington also capitalized on strong demand for Washington debt to refund outstanding bonds for a savings of $70.4 million in debt service costs.

General obligation debt is subject to the constitutional limitation as prescribed by the State Constitution. The aggregate debt contracted by the state as of June 30, 2010, does not exceed that amount for which payments of principal and interest in any fiscal year would require the state to expend more than 9 percent of the arithmetic mean of its general state revenues for the three immediately preceding fiscal years. The arithmetic mean of its general state revenues for Fiscal Years 2007, 2008, and 2009 is $12.5 billion. The debt service limitation, 9 percent of this mean, is $1.1 billion. The state's maximum annual debt service as of June 30, 2010 subject to the constitutional debt limitation is $971.3 million, or $155.4 million less than the debt service limitation.

For further information on the debt limit, refer to the Certification of the Debt Limitation of the State of Washington, available from the Office of the State Treasurer or at: http://www.tre.wa.gov/documents/debt_cdl2010.pdf.

STATE OF WASHINGTON
**Bond Debt**
*(in millions of dollars)*

| | Governmental Activities | | Business-Type Activities | | Total | |
|---|---|---|---|---|---|---|
| | 2010 | 2009 | 2010 | 2009 | 2010 | 2009 |
| General obligation (GO) bonds | $ 16,540 | $ 14,049 | $ 60 | $ 69 | $ 16,600 | $ 14,118 |
| Accreted interest on zero interest rate GO bonds | 367 | 328 | 42 | 38 | 409 | 366 |
| Revenue bonds | 743 | 616 | 1,084 | 1,074 | 1,827 | 1,690 |
| Total | $ 17,650 | $ 14,993 | $ 1,186 | $ 1,181 | $ 18,836 | $ 16,174 |

By statutory provision, the State Finance Committee (SFC) is authorized to supervise and control the issuance of all state bonds, notes, or other evidences of indebtedness.

The SFC is composed of the Governor, Lieutenant Governor, and State Treasurer, the latter serving as chairman.

As of June 30, 2010, the state of Washington's general obligation debt was rated Aa1 by Moody's Investor Service, AA+ by Standard & Poor's Rating Group (S & P), and AA+ by Fitch Ratings.

The state had revenue debt outstanding at June 30, 2010, of $1.8 billion, an increase of $137 million over Fiscal Year 2009. This increase is primarily related to revenue bonds issued by state colleges and universities. This debt is not supported or intended to be supported by the full faith and credit of the state. Revenue bond debt is generally secured by specific sources of revenue. The exception is the University of Washington who issues general revenue bonds that are payable from general revenues of the university.

Additional information on the state's bond debt obligations is presented in Note 7 beginning on page 100 of this report.

Additional information on the state's legal debt limit is presented in the statistical section on page 266 of this report.

## Conditions with Expected Future Impact

**Economic Factors.** The forecast for Washington for Fiscal Year 2011 is for a slow to moderate recovery from the recession. That said, in the coming year, legislative leaders and management will be facing a number of challenges.

- Employment is projected to begin rebounding in Fiscal Year 2011, although construction employment is not expected to show signs of recovery until the second half of Fiscal Year 2011.
- The economic recovery is expected to be slow by historical standards.
- Following September 2011 forecast projections of reduced state revenues, Governor Gregoire called for across the board cuts in the General Fund of 6.3 percent effective October 1, 2011.

**Rainy Day Account.** In November 2007, Washington State voters ratified Engrossed Substitute Senate Joint Resolution 8206, amending the state's Constitution and establishing the Budget Stabilization Account (BSA). The Constitution details a limited number of circumstances under which funds can be appropriated from the BSA, one of which is a favorable vote of at least three-fifths of the members of each house of the Legislature.

On June 30, 2010, $119 million was transferred to the BSA from the General Fund in accordance with the provisions of the Constitution. Also during Fiscal Year 2010, Engrossed Substitute House Bill 6444 authorized the transfer of $45 million from the BSA to the General Fund.

The BSA has a fund balance of $95 million as of June 30, 2010.

**November 2, 2010 General Election.** There were measures on the state's November 2, 2010 general election ballot that addressed state laws related to state operations, state imposed taxes and fees, and the calculation of the state debt limitation. These measures, if passed, could fiscally impact the state. Election results are not final or official until certified. By law, December 2, 2010 is the last day for the Office of the Secretary of State to certify General Election returns. Information is posted as available on the Secretary of State's website at http://www.sos.wa.gov.

## Requests for Information

This financial report is designed to provide a general overview of the state of Washington's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Office of Financial Management, Accounting Division, P.O. Box 43113, Olympia, WA 98504-3113.

**Basic Financial Statements**

# Governmental-wide Financial Statements

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## Statement of Net Assets

June 30, 2010

*(expressed in thousands)*

| | Primary Government | | | |
|---|---|---|---|---|
| | Governmental Activities | Business-Type Activities | Total | Component Units |
| **ASSETS** | | | | |
| Cash and pooled investments | $ 3,341,544 | $ 6,509,507 | $ 9,851,051 | $ 65,266 |
| Taxes receivable (net of allowance) | 2,837,375 | 9,790 | 2,847,165 | - |
| Other receivables (net of allowance) | 1,299,050 | 1,297,022 | 2,596,072 | 2,154 |
| Internal balances (net) | 192,382 | (192,382) | - | - |
| Due from other governments | 4,007,386 | 200,093 | 4,207,479 | - |
| Inventories | 90,610 | 98,132 | 188,742 | - |
| Investments, noncurrent | 3,863,824 | 13,749,971 | 17,613,795 | 18,469 |
| Other assets | 96,330 | 311,325 | 407,655 | 76,116 |
| Restricted assets: | | | | |
| Cash and cash equivalents | 1,105,586 | 76,398 | 1,181,984 | - |
| Investments | 8,678 | - | 8,678 | - |
| Receivables | 72,127 | 20,315 | 92,442 | - |
| Capital assets (Note 6): | | | | |
| Non-depreciable assets | 21,801,797 | 353,768 | 22,155,565 | 34,677 |
| Depreciable assets, net of depreciation | 9,445,126 | 1,900,472 | 11,345,598 | 338,377 |
| Total capital assets, net of depreciation | 31,246,923 | 2,254,240 | 33,501,163 | 373,054 |
| **Total Assets** | $ 48,161,815 | $ 24,334,411 | $ 72,496,226 | $ 535,059 |
| **LIABILITIES** | | | | |
| Accounts payable | $ 1,676,691 | $ 95,144 | $ 1,771,835 | $ 37,450 |
| Contracts and retainage payable | 177,774 | 22,038 | 199,812 | 2,566 |
| Accrued liabilities | 610,115 | 263,251 | 873,366 | 3,930 |
| Obligations under security lending agreements | 203,150 | 2,867,466 | 3,070,616 | - |
| Due to other governments | 781,463 | 130,902 | 912,365 | - |
| Unearned revenue | 279,835 | 42,334 | 322,169 | 5,429 |
| Long-term liabilities (Note 7): | | | | |
| Due within one year | 1,435,286 | 2,537,739 | 3,973,025 | - |
| Due in more than one year | 19,799,142 | 25,397,061 | 45,196,203 | 25,587 |
| **Total Liabilities** | 24,963,456 | 31,355,935 | 56,319,391 | 74,962 |
| **NET ASSETS** | | | | |
| Invested in capital assets, net of related debt | 18,200,533 | 913,094 | 19,113,627 | 343,524 |
| Restricted for: | | | | |
| Unemployment compensation | - | 2,929,842 | 2,929,842 | - |
| Other purposes | 2,298,123 | - | 2,298,123 | 20,990 |
| Expendable permanent fund principal | 1,413,326 | - | 1,413,326 | - |
| Nonexpendable permanent endowments | 1,503,472 | - | 1,503,472 | - |
| Unrestricted (deficit) | (217,095) | (10,864,460) | (11,081,555) | 95,583 |
| **Total Net Assets (Deficit)** | $ 23,198,359 | $ (7,021,524) | $ 16,176,835 | $ 460,097 |

The notes to the financial statements are an integral part of this statement.

## Statement of Activities

For the Fiscal Year Ended June 30, 2010

*(expressed in thousands)*

| Functions/Programs | Expenses | Program Revenues: Charges for Services | Program Revenues: Operating Grants and Contributions | Program Revenues: Capital Grants and Contributions |
|---|---|---|---|---|
| **PRIMARY GOVERNMENT** | | | | |
| Governmental Activities: | | | | |
| General government | $ 1,738,451 | $ 534,461 | $ 433,204 | $ 1,124 |
| Education - elementary and secondary (K-12) | 8,467,649 | 11,725 | 1,510,920 | - |
| Education - higher education | 6,051,421 | 2,210,357 | 1,945,904 | 16,009 |
| Human services | 12,946,115 | 345,415 | 7,885,895 | 6,922 |
| Adult corrections | 937,473 | 17,815 | 184,738 | - |
| Natural resources and recreation | 1,083,430 | 564,345 | 168,456 | 55,253 |
| Transportation | 2,073,086 | 899,445 | 64,002 | 859,519 |
| Interest on long-term debt | 810,156 | - | - | - |
| Total Governmental Activities | 34,107,781 | 4,583,563 | 12,193,119 | 938,827 |
| Business-Type Activities: | | | | |
| Workers' compensation | 4,267,927 | 1,755,015 | 7,805 | - |
| Unemployment compensation | 4,728,805 | 1,287,803 | 2,455,706 | - |
| Higher education student services | 1,627,819 | 1,698,098 | 4,474 | - |
| Liquor control | 552,363 | 592,638 | 10 | - |
| Washington's lottery | 388,715 | 491,076 | - | - |
| Other | 345,704 | 162,393 | 8 | 15 |
| Total Business-Type Activities | 11,911,333 | 5,987,023 | 2,468,003 | 15 |
| Total Primary Government | $ 46,019,114 | $ 10,570,586 | $ 14,661,122 | $ 938,842 |
| **COMPONENT UNITS** | $ 68,184 | $ 16,446 | $ 43,771 | $ 903 |
| Total Component Units | $ 68,184 | $ 16,446 | $ 43,771 | $ 903 |

General Revenues:
- Taxes, net of related credits:
  - Sales and use
  - Business and occupation
  - Property
  - Motor vehicle and fuel
  - Excise
  - Cigarette and tobacco
  - Public utilities
  - Insurance premium
  - Other
- Interest and investment earnings

Total general revenues

Excess (deficiency) of revenues over expenses before contributions to endowments and transfers

Contributions to endowments

Transfers

Change in Net Assets

Net assets - Beginning

Net assets - Ending

The notes to the financial statements are an integral part of this statement.

| Net (Expense) Revenue and Changes in Net Assets | | | |
|---|---|---|---|
| Primary Government | | | |
| Governmental Activities | Business-Type Activities | Total | Component Units |
| $ (769,662) | $ - | $ (769,662) | |
| (6,945,004) | - | (6,945,004) | |
| (1,879,151) | - | (1,879,151) | |
| (4,707,883) | - | (4,707,883) | |
| (734,920) | - | (734,920) | |
| (295,376) | - | (295,376) | |
| (250,120) | - | (250,120) | |
| (810,156) | - | (810,156) | |
| (16,392,272) | - | (16,392,272) | |
| - | (2,505,107) | (2,505,107) | |
| - | (985,296) | (985,296) | |
| - | 74,753 | 74,753 | |
| - | 40,285 | 40,285 | |
| - | 102,361 | 102,361 | |
| - | (183,288) | (183,288) | |
| - | (3,456,292) | (3,456,292) | |
| (16,392,272) | (3,456,292) | (19,848,564) | |
| | | | $ (7,064) |
| | | | (7,064) |
| 6,870,776 | - | 6,870,776 | - |
| 2,596,668 | - | 2,596,668 | - |
| 1,822,278 | - | 1,822,278 | - |
| 1,218,877 | - | 1,218,877 | - |
| 466,557 | 50,766 | 517,323 | - |
| 426,265 | - | 426,265 | - |
| 411,584 | - | 411,584 | - |
| 405,922 | - | 405,922 | - |
| 763,337 | 109,462 | 872,799 | - |
| 449,090 | 1,742,003 | 2,191,093 | 2,708 |
| 15,431,354 | 1,902,231 | 17,333,585 | 2,708 |
| (960,918) | (1,554,061) | (2,514,979) | (4,356) |
| 52,230 | - | 52,230 | - |
| 251,914 | (251,914) | - | - |
| (656,774) | (1,805,975) | (2,462,749) | (4,356) |
| 23,855,133 | (5,215,549) | 18,639,584 | 464,453 |
| $ 23,198,359 | $ (7,021,524) | $ 16,176,835 | $ 460,097 |

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## Basic Financial Statements

# Fund Financial Statements

## Balance Sheet
## GOVERNMENTAL FUNDS
June 30, 2010
*(expressed in thousands)*

| | General | Special Revenue: Higher Education | Special Revenue: Motor Vehicle | Higher Education Endowment | Nonmajor Governmental Funds | Total |
|---|---|---|---|---|---|---|
| **ASSETS** | | | | | | |
| Cash and pooled investments | $ - | $ 144,803 | $ 695,659 | $ 316,393 | $ 1,631,669 | $ 2,788,524 |
| Investments | 44,080 | 1,066,639 | 31,739 | 2,592,731 | 272,336 | 4,007,525 |
| Taxes receivable (net of allowance) | 2,703,247 | 21,169 | 110,536 | - | 2,423 | 2,837,375 |
| Other receivables (net of allowance) | 288,191 | 338,675 | 63,560 | 23,083 | 653,570 | 1,367,079 |
| Due from other funds | 76,085 | 155,172 | 11,432 | 28 | 1,012,920 | 1,255,637 |
| Due from other governments | 1,435,081 | 139,661 | 74,134 | 1 | 2,268,626 | 3,917,503 |
| Inventories and prepaids | 14,507 | 14,985 | 40,682 | - | 4,830 | 75,004 |
| Restricted assets: | | | | | | |
| Cash and pooled investments | - | - | 960,036 | - | 145,550 | 1,105,586 |
| Investments | - | - | - | - | 8,678 | 8,678 |
| Receivables | 885 | 65,628 | - | - | 4 | 66,517 |
| **Total Assets** | $ 4,562,076 | $ 1,946,732 | $ 1,987,778 | $ 2,932,236 | $ 6,000,606 | $ 17,429,428 |
| **LIABILITIES AND FUND BALANCES** | | | | | | |
| **Liabilities:** | | | | | | |
| Accounts payable | $ 1,186,220 | $ 69,216 | $ 155,251 | $ 2,501 | $ 203,276 | $ 1,616,464 |
| Contracts and retainages payable | 38,688 | 3,477 | 54,668 | 1,994 | 42,140 | 140,967 |
| Accrued liabilities | 206,723 | 243,891 | 87,974 | 29,634 | 78,216 | 646,438 |
| Obligations under security lending agreements | - | - | - | 158,231 | 44,919 | 203,150 |
| Due to other funds | 877,992 | 92,968 | 15,860 | 2,151 | 165,585 | 1,154,556 |
| Due to other governments | 490,557 | 604 | 68,137 | - | 118,851 | 678,149 |
| Deferred revenue | 1,361,542 | 216,874 | 24,974 | 8,999 | 808,872 | 2,421,261 |
| Claims and judgments payable | 21,605 | - | - | - | 5,626 | 27,231 |
| **Total Liabilities** | 4,183,327 | 627,030 | 406,864 | 203,510 | 1,467,485 | 6,888,216 |
| **Fund Balances:** | | | | | | |
| Reserved for: | | | | | | |
| Encumbrances | - | 226,759 | 3,946 | - | 782,222 | 1,012,927 |
| Inventories | 13,871 | 12,629 | 40,682 | - | 612 | 67,794 |
| Debt service | - | - | - | - | 93,149 | 93,149 |
| Permanent funds | - | - | - | 2,728,726 | 188,072 | 2,916,798 |
| Other specific purposes | 62,293 | 210,978 | 853 | - | 2,009,812 | 2,283,936 |
| Unreserved, designated for, reported in: | | | | | | |
| Working capital | 863,652 | - | - | - | - | 863,652 |
| Higher education | - | 107,624 | - | - | - | 107,624 |
| Special revenue funds | - | - | - | - | 157 | 157 |
| Debt service funds | - | - | - | - | 170,200 | 170,200 |
| Unreserved, undesignated | (561,067) | 761,712 | 1,535,433 | - | - | 1,736,078 |
| Unreserved, undesignated reported in: | | | | | | |
| Special revenue funds | - | - | - | - | 1,219,705 | 1,219,705 |
| Capital project funds | - | - | - | - | 69,192 | 69,192 |
| **Total Fund Balances** | 378,749 | 1,319,702 | 1,580,914 | 2,728,726 | 4,533,121 | 10,541,212 |
| **Total Liabilities and Fund Balances** | $ 4,562,076 | $ 1,946,732 | $ 1,987,778 | $ 2,932,236 | $ 6,000,606 | $ 17,429,428 |

The notes to the financial statements are an integral part of this statement.

## Reconciliation of the Balance Sheet to the Statement of Net Assets GOVERNMENTAL FUNDS

June 30, 2010

*(expressed in thousands)*

| | | |
|---|---|---|
| **Total Fund Balances for Governmental Funds** | | $ 10,541,212 |
| Amounts reported for governmental activities in the Statement of Net Assets are different because: | | |
| Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds. These assets consist of: | | |
| Non-depreciable assets | $ 21,785,333 | |
| Depreciable assets | 15,390,036 | |
| Less: Accumulated depreciation | (6,372,746) | |
| Total capital assets | | 30,802,623 |
| Some of the state's revenues will be collected after year-end, but are not available soon enough to pay for the current period's expenditures, and therefore are deferred in the funds. | | 2,142,153 |
| Certain pension trust funds have been funded in excess of the annual required contributions, creating a year-end asset. This asset is not a financial resource and therefore is not reported in the funds. | | 12,500 |
| Unmatured interest on general obligation bonds is not recognized in the funds until due. | | (337,791) |
| Internal service funds are used by management to charge the costs of certain activities to individual funds. The assets and liabilities of the internal service funds are included in governmental activities in the Statement of Net Assets. | | (257,912) |
| Some liabilities are not due and payable in the current period and therefore are not reported in the funds. Those liabilities consist of: | | |
| Bonds and other financing contracts payable | $ (17,553,730) | |
| Accreted interest on bonds | (366,515) | |
| Compensated absences | (512,553) | |
| Other postemployment benefits obligations | (697,213) | |
| Unfunded pension obligations | (191,389) | |
| Pollution remediation obligations | (174,353) | |
| Claims and judgments | (33,661) | |
| Other obligations | (175,012) | |
| Total long-term liabilities | | (19,704,426) |
| **Net Assets of Governmental Activities** | | $ 23,198,359 |

The notes to the financial statements are an integral part of this statement.

## Statement of Revenues, Expenditures, and Changes in Fund Balances
## GOVERNMENTAL FUNDS

For the Fiscal Year Ended June 30, 2010

*(expressed in thousands)*

| | General | Special Revenue: Higher Education | Special Revenue: Motor Vehicle | Higher Education Endowment | Nonmajor Governmental Funds | Total |
|---|---|---|---|---|---|---|
| **REVENUES** | | | | | | |
| Retail sales and use taxes | $ 6,801,220 | $ - | $ - | $ - | $ 69,556 | $ 6,870,776 |
| Business and occupation taxes | 2,592,710 | - | - | - | 3,958 | 2,596,668 |
| Property taxes | 1,822,278 | - | - | - | - | 1,822,278 |
| Excise taxes | 417,845 | - | - | - | 53,642 | 471,487 |
| Motor vehicle and fuel taxes | - | - | 1,203,870 | - | 15,007 | 1,218,877 |
| Other taxes | 1,535,293 | 158,736 | 26 | - | 276,634 | 1,970,689 |
| Licenses, permits, and fees | 85,637 | 617 | 375,492 | - | 525,164 | 986,910 |
| Timber sales | 4,855 | - | 27 | 20,321 | 122,448 | 147,651 |
| Other contracts and grants | 177,250 | 686,292 | 1,710 | - | 12,119 | 877,371 |
| Federal grants-in-aid | 9,647,711 | 1,389,004 | 546,918 | - | 804,202 | 12,387,835 |
| Charges for services | 55,660 | 1,787,298 | 242,283 | 1,107 | 316,972 | 2,403,320 |
| Investment income (loss) | (9,485) | 82,152 | 18,843 | 269,839 | 87,741 | 449,090 |
| Miscellaneous revenue | 182,827 | 207,821 | 27,803 | 1,852 | 498,482 | 918,785 |
| Unclaimed property | 60,853 | - | - | - | - | 60,853 |
| Contributions and donations | - | - | - | 52,230 | - | 52,230 |
| **Total Revenues** | 23,374,654 | 4,311,920 | 2,416,972 | 345,349 | 2,785,925 | 33,234,820 |
| **EXPENDITURES** | | | | | | |
| Current: | | | | | | |
| General government | 821,978 | - | 14,240 | 102 | 637,501 | 1,473,821 |
| Human services | 13,209,253 | 362 | - | - | 526,309 | 13,735,924 |
| Natural resources and recreation | 359,862 | - | 1,032 | 2 | 527,773 | 888,669 |
| Transportation | 43,930 | 1,991 | 1,246,463 | - | 583,563 | 1,875,947 |
| Education | 9,242,798 | 4,210,304 | - | 482 | 535,469 | 13,989,053 |
| Intergovernmental | 30,316 | - | 237,201 | - | 114,566 | 382,083 |
| Capital outlays | 53,796 | 187,844 | 1,468,215 | 129 | 550,111 | 2,260,095 |
| Debt service: | | | | | | |
| Principal | 20,268 | 21,545 | 469 | - | 629,035 | 671,317 |
| Interest | 570 | 6,537 | 302 | - | 732,102 | 739,511 |
| **Total Expenditures** | 23,782,771 | 4,428,583 | 2,967,922 | 715 | 4,836,429 | 36,016,420 |
| **Excess of Revenues Over (Under) Expenditures** | (408,117) | (116,663) | (550,950) | 344,634 | (2,050,504) | (2,781,600) |
| **OTHER FINANCING SOURCES (USES)** | | | | | | |
| Bonds issued | - | 41,466 | 2,060,820 | - | 1,193,290 | 3,295,576 |
| Refunding bonds issued | - | - | - | - | 723,115 | 723,115 |
| Payments to escrow agents for refunded bond debt | - | - | - | - | (792,468) | (792,468) |
| Bond issue premiums | - | 690 | 32,569 | - | 156,463 | 189,722 |
| Bond issue discounts | - | - | - | - | (69) | (69) |
| Other debt issued | 4,186 | 107,991 | - | - | 203 | 112,380 |
| Refunding other debt issued | - | 11,960 | 1,710 | - | 2,150 | 15,820 |
| Payments to escrow agents for refunded other debt | - | (12,517) | (1,800) | - | (2,262) | (16,579) |
| Transfers in | 1,187,128 | 217,859 | 24,228 | 6,734 | 2,262,876 | 3,698,825 |
| Transfers out | (1,566,398) | (136,535) | (341,733) | (100,848) | (1,306,378) | (3,451,892) |
| **Total Other Financing Sources (Uses)** | (375,084) | 230,914 | 1,775,794 | (94,114) | 2,236,920 | 3,774,430 |
| **Net Change in Fund Balances** | (783,201) | 114,251 | 1,224,844 | 250,520 | 186,416 | 992,830 |
| **Fund Balances - Beginning, as restated** | 1,161,950 | 1,205,451 | 356,070 | 2,478,206 | 4,346,705 | 9,548,382 |
| **Fund Balances - Ending** | $ 378,749 | $ 1,319,702 | $ 1,580,914 | $ 2,728,726 | $ 4,533,121 | $ 10,541,212 |

The notes to the financial statements are an integral part of this statement.

## Reconciliation of the Statement of Revenues, Expenditures and Changes in Fund Balances to the Statement of Activities
## GOVERNMENTAL FUNDS

For the Fiscal Year Ended June 30, 2010
*(expressed in thousands)*

| | | |
|---|---|---|
| **Net Change in Fund Balances - Total Governmental Funds** | | $ 992,830 |
| Amounts reported for governmental activities in the Statement of Activities are different because: | | |
| Capital outlays are reported as expenditures in governmental funds. However, in the Statement of Activities, the cost of capital assets is allocated over their estimated useful lives as depreciation expense. In the current period, these amounts are: | | |
| Capital outlays | $ 2,206,643 | |
| Less: Depreciation expense | (508,267) | 1,698,376 |
| Some revenues in the Statement of Activities do not provide current financial resources, and therefore, are deferred in governmental funds. Also, revenues related to prior periods that became available during the current period are reported in governmental funds but are eliminated in the Statement of Activities. This amount is the net adjustment. | | 62,746 |
| Pension trust funding in excess of annual required contributions uses current financial resources, but does not qualify as an expense. | | (2,300) |
| Internal service funds are used by management to charge the costs of certain activities to individual funds. The change in net assets of the internal service funds is reported with governmental activities. | | (70,715) |
| Bond proceeds and other financing contracts provide current financial resources to governmental funds, while the repayment of the related debt principal consumes those financial resources. These transactions, however, have no effect on net assets. In the current period, these amounts consist of: | | |
| Bonds and other financing contracts issued | $ (4,800,227) | |
| Principal payments on bonds and other financing contracts | 2,109,660 | |
| Accreted interest on bonds | (38,898) | (2,729,465) |
| Some expenses/revenue reductions reported in the Statement of Activities do not require the use of current financial resources and, therefore, are not recognized in governmental funds. Also payments of certain obligations related to prior periods are recognized in governmental funds but are eliminated in the Statement of Activities. In the current period, the net adjustments consist of: | | |
| Compensated absences | $ 6,414 | |
| Other postemployment benefits obligations | (253,559) | |
| Unfunded pension obligations | (37,259) | |
| Pollution remediation obligations | (139,348) | |
| Claims and judgments | (56) | |
| Accrued interest | (31,838) | |
| Unclaimed property | (93,158) | |
| Other obligations | (59,442) | (608,246) |
| **Change in Net Assets of Governmental Activities** | | $ (656,774) |

The notes to the financial statements are an integral part of this statement.

## Statement of Fund Net Assets
## PROPRIETARY FUNDS
June 30, 2010
*(expressed in thousands)*

| | Business-Type Activities Enterprise Funds | | | | | Governmental Activities |
|---|---|---|---|---|---|---|
| | Workers' Compensation | Unemployment Compensation | Higher Education Student Services | Nonmajor Enterprise Funds | Total | Internal Service Funds |
| **ASSETS** | | | | | | |
| **Current Assets:** | | | | | | |
| Cash and pooled investments | $ 47,007 | $ 2,321,418 | $ 871,501 | $ 347,259 | $ 3,587,185 | $ 335,349 |
| Investments | 2,377,679 | - | 4,353 | 540,290 | 2,922,322 | 2,702 |
| Taxes receivable (net of allowance) | - | - | - | 9,790 | 9,790 | - |
| Other receivables (net of allowance) | 588,631 | 521,125 | 159,153 | 28,113 | 1,297,022 | 6,973 |
| Due from other funds | 528 | 6,339 | 26,438 | 8,816 | 42,121 | 171,376 |
| Due from other governments | 1,207 | 104,828 | 53,325 | 3,767 | 163,127 | 8,396 |
| Inventories | 120 | - | 42,102 | 55,910 | 98,132 | 17,962 |
| Prepaid expenses | - | - | 19,397 | 1,343 | 20,740 | 5,102 |
| Restricted assets: | | | | | | |
| Cash and pooled investments | - | - | 76,398 | - | 76,398 | - |
| Receivables | - | - | - | 20,315 | 20,315 | 5,610 |
| **Total Current Assets** | 3,015,172 | 2,953,710 | 1,252,667 | 1,015,603 | 8,237,152 | 553,470 |
| **Noncurrent Assets:** | | | | | | |
| Investments, noncurrent | 11,894,481 | - | 223,455 | 1,632,035 | 13,749,971 | 71,268 |
| Other noncurrent assets | - | - | 67,806 | 222,778 | 290,584 | 29 |
| Capital assets: | | | | | | |
| Land and other non-depreciable assets | 3,240 | - | 60,439 | 79,072 | 142,751 | 3,836 |
| Buildings | 62,705 | - | 1,920,425 | 420,691 | 2,403,821 | 168,506 |
| Other improvements | 1,661 | - | 74,401 | 21,751 | 97,813 | 18,796 |
| Furnishings, equipment and intangible assets | 69,688 | - | 394,769 | 70,169 | 534,626 | 766,227 |
| Infrastructure | - | - | 30,110 | - | 30,110 | 1,818 |
| Accumulated depreciation | (81,377) | - | (914,115) | (170,406) | (1,165,898) | (527,511) |
| Construction in progress | 7,443 | - | 153,540 | 50,034 | 211,017 | 12,628 |
| **Total Noncurrent Assets** | 11,957,841 | - | 2,010,830 | 2,326,124 | 16,294,795 | 515,597 |
| **Total Assets** | 14,973,013 | 2,953,710 | 3,263,497 | 3,341,727 | 24,531,947 | 1,069,067 |
| **LIABILITIES** | | | | | | |
| **Current Liabilities:** | | | | | | |
| Accounts payable | 2,882 | - | 61,591 | 30,671 | 95,144 | 60,226 |
| Contracts and retainages payable | 7,306 | - | 11,937 | 93,094 | 112,337 | 36,779 |
| Accrued liabilities | 161,014 | 2,613 | 156,726 | 128,644 | 448,997 | 32,524 |
| Obligations under security lending agreements | 2,377,679 | - | - | 489,787 | 2,867,466 | - |
| Bonds and notes payable | 4,030 | - | 47,017 | 74,062 | 125,109 | 23,775 |
| Due to other funds | 5,334 | 1,120 | 175,640 | 28,490 | 210,584 | 102,469 |
| Due to other governments | - | 20,135 | 6 | 97,716 | 117,857 | 41 |
| Unearned revenue | 7,996 | - | 34,286 | 52 | 42,334 | 726 |
| Claims and judgments payable | 2,132,081 | - | - | 4,501 | 2,136,582 | 237,626 |
| **Total Current Liabilities** | 4,698,322 | 23,868 | 487,203 | 947,017 | 6,156,410 | 494,166 |
| **Noncurrent Liabilities:** | | | | | | |
| Claims and judgments payable | 21,893,751 | - | - | 7,989 | 21,901,740 | 635,530 |
| Bonds and notes payable | 18,080 | - | 1,092,441 | 251,481 | 1,362,002 | 171,843 |
| Other long-term liabilities | 29,914 | - | 90,983 | 2,012,422 | 2,133,319 | 25,440 |
| **Total Noncurrent Liabilities** | 21,941,745 | - | 1,183,424 | 2,271,892 | 25,397,061 | 832,813 |
| **Total Liabilities** | 26,640,067 | 23,868 | 1,670,627 | 3,218,909 | 31,553,471 | 1,326,979 |
| **NET ASSETS** | | | | | | |
| Invested in capital assets, net of related debt | 41,251 | - | 656,509 | 215,334 | 913,094 | 254,293 |
| Restricted for: | | | | | | |
| Unemployment compensation | - | 2,929,842 | - | - | 2,929,842 | - |
| Unrestricted | (11,708,305) | - | 936,361 | (92,516) | (10,864,460) | (512,205) |
| **Total Net Assets (Deficit)** | $ (11,667,054) | $ 2,929,842 | $ 1,592,870 | $ 122,818 | $ (7,021,524) | $ (257,912) |

The notes to the financial statements are an integral part of this statement.

## Statement of Revenues, Expenses, and Changes in Fund Net Assets
## PROPRIETARY FUNDS
For the Fiscal Year Ended June 30, 2010
*(expressed in thousands)*

| | Business-Type Activities Enterprise Funds | | | | | Governmental Activities |
|---|---|---|---|---|---|---|
| | Workers' Compensation | Unemployment Compensation | Higher Education Student Services | Nonmajor Enterprise Funds | Total | Internal Service Funds |
| **OPERATING REVENUES** | | | | | | |
| Sales | $ - | $ - | $ 145,636 | $ 637,350 | $ 782,986 | $ 101,884 |
| Less: Cost of goods sold | - | - | 91,390 | 424,824 | 516,214 | 87,524 |
| Gross profit | - | - | 54,246 | 212,526 | 266,772 | 14,360 |
| Charges for services | 25 | - | 1,339,785 | 80,082 | 1,419,892 | 606,664 |
| Premiums and assessments | 1,727,722 | 1,241,121 | - | - | 2,968,843 | 1,300,093 |
| Federal aid for unemployment insurance benefits | - | 2,455,706 | - | - | 2,455,706 | - |
| Lottery ticket proceeds | - | - | - | 491,021 | 491,021 | - |
| Miscellaneous revenue | 27,195 | 46,682 | 209,960 | 7,090 | 290,927 | 111,189 |
| **Total Operating Revenues** | 1,754,942 | 3,743,509 | 1,603,991 | 790,719 | 7,893,161 | 2,032,306 |
| **OPERATING EXPENSES** | | | | | | |
| Salaries and wages | 137,086 | - | 577,094 | 99,495 | 813,675 | 296,368 |
| Employee benefits | 48,557 | - | 154,896 | 41,630 | 245,083 | 83,609 |
| Personal services | 4,521 | - | 15,196 | 22,052 | 41,769 | 19,541 |
| Goods and services | 67,817 | - | 594,709 | 125,952 | 788,478 | 294,955 |
| Travel | 3,339 | - | 18,086 | 2,463 | 23,888 | 3,531 |
| Premiums and claims | 3,971,059 | 4,728,804 | - | - | 8,699,863 | 1,333,761 |
| Lottery prize payments | - | - | - | 291,828 | 291,828 | - |
| Depreciation and amortization | 7,991 | - | 101,021 | 16,325 | 125,337 | 69,208 |
| Guaranteed education tuition expense | - | - | - | 181,664 | 181,664 | - |
| Miscellaneous expenses | 26,287 | - | 16,113 | 578 | 42,978 | 2,223 |
| **Total Operating Expenses** | 4,266,657 | 4,728,804 | 1,477,115 | 781,987 | 11,254,563 | 2,103,196 |
| **Operating Income (Loss)** | (2,511,715) | (985,295) | 126,876 | 8,732 | (3,361,402) | (70,890) |
| **NONOPERATING REVENUES (EXPENSES)** | | | | | | |
| Earnings (loss) on investments | 1,454,440 | 115,416 | 24,802 | 147,345 | 1,742,003 | 5,195 |
| Interest expense | (1,271) | - | (59,313) | (34,917) | (95,501) | (8,207) |
| Distributions to other governments | - | - | - | (45,053) | (45,053) | - |
| Tax revenue | - | - | - | 160,228 | 160,228 | - |
| Other revenues (expenses) | 7,878 | - | 7,191 | 30,581 | 45,650 | (626) |
| **Total Nonoperating Revenues (Expenses)** | 1,461,047 | 115,416 | (27,320) | 258,184 | 1,807,327 | (3,638) |
| **Income (Loss) Before Contributions and Transfers** | (1,050,668) | (869,879) | 99,556 | 266,916 | (1,554,075) | (74,528) |
| Capital contributions | - | - | - | 15 | 15 | 1,809 |
| Transfers in | 840 | - | 19,869 | 27,136 | 47,845 | 25,310 |
| Transfers out | - | - | (23,570) | (276,190) | (299,760) | (23,306) |
| **Net Contributions and Transfers** | 840 | - | (3,701) | (249,039) | (251,900) | 3,813 |
| **Change in Net Assets** | (1,049,828) | (869,879) | 95,855 | 17,877 | (1,805,975) | (70,715) |
| **Net Assets (Deficit) - Beginning, as restated** | (10,617,226) | 3,799,721 | 1,497,015 | 104,941 | (5,215,549) | (187,197) |
| **Net Assets (Deficit) - Ending** | $ (11,667,054) | $ 2,929,842 | $ 1,592,870 | $ 122,818 | $ (7,021,524) | $ (257,912) |

The notes to the financial statements are an integral part of this statement.

## Statement of Cash Flows
## PROPRIETARY FUNDS
For the Fiscal Year Ended June 30, 2010
*(expressed in thousands)*

| | Business-Type Activities Enterprise Funds | | | |
|---|---|---|---|---|
| | Workers' Compensation | Unemployment Compensation | Higher Education Student Services | Nonmajor Enterprise Funds |
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | | | |
| Receipts from customers | $ 1,952,915 | $ 1,074,166 | $ 1,477,391 | $ 1,436,342 |
| Payments to suppliers | (2,282,720) | (4,721,068) | (602,589) | (970,861) |
| Payments to employees | (178,887) | - | (708,190) | (135,136) |
| Other receipts (payments) | 27,196 | 2,453,363 | 209,960 | 7,090 |
| Net Cash Provided (Used) by Operating Activities | (481,496) | (1,193,539) | 376,572 | 337,435 |
| **CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES** | | | | |
| Transfers in | 840 | - | 19,869 | 27,136 |
| Transfers out | - | - | (23,570) | (276,190) |
| Operating grants and donations received | 7,604 | - | 4,755 | 18 |
| Taxes and license fees collected | 113 | - | - | 186,208 |
| Distributions to other governments | - | - | - | (45,053) |
| Other noncapital financing sources (uses) | - | - | - | 4,384 |
| Net Cash Provided (Used) by Noncapital Financing Activities | 8,557 | - | 1,054 | (103,497) |
| **CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES** | | | | |
| Interest paid | (1,346) | - | (60,307) | (13,602) |
| Capital contributions | - | - | - | 15 |
| Principal payments on long-term capital financing | (3,820) | - | (54,364) | (24,185) |
| Proceeds from long-term capital financing | - | - | 143,779 | - |
| Proceeds from sale of capital assets | 39 | - | 14,094 | 989 |
| Acquisitions of capital assets | (8,086) | - | (351,400) | (25,057) |
| Net Cash Provided (Used) by Capital and Related Financing Activities | (13,213) | - | (308,198) | (61,840) |
| **CASH FLOWS FROM INVESTING ACTIVITIES** | | | | |
| Receipt of interest | 523,356 | 115,416 | 18,350 | 18,929 |
| Proceeds from sale of investment securities | 5,021,292 | - | 30,688 | 433,527 |
| Purchases of investment securities | (5,082,205) | - | (27,254) | (584,049) |
| Net Cash Provided (Used) by Investing Activities | 462,443 | 115,416 | 21,784 | (131,593) |
| Net Increase (Decrease) in Cash and Pooled Investments | (23,709) | (1,078,123) | 91,212 | 40,505 |
| Cash and Pooled Investments, July 1, as restated | 70,716 | 3,399,541 | 856,687 | 306,754 |
| Cash and Pooled Investments, June 30 | $ 47,007 | $ 2,321,418 | $ 947,899 | $ 347,259 |
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | | | |
| Operating Income (Loss) | $ (2,511,715) | $ (985,295) | $ 126,876 | $ 8,732 |
| **Adjustments to Reconcile Operating Income (Loss) to Net Cash Provided by Operations:** | | | | |
| Depreciation | 7,991 | - | 101,021 | 16,325 |
| **Change in Assets: Decrease (Increase)** | | | | |
| Receivables (net of allowance) | 251,649 | (215,981) | (5,103) | (16,047) |
| Inventories | 22 | - | (1,838) | (6,124) |
| Prepaid expenses | 38 | - | 13,616 | (979) |
| **Change in Liabilities: Increase (Decrease)** | | | | |
| Payables | 1,770,519 | 7,737 | 142,000 | 335,528 |
| **Net Cash or Cash Equivalents Provided by (Used in) Operating Activities** | $ (481,496) | $ (1,193,539) | $ 376,572 | $ 337,435 |

The notes to the financial statements are an integral part of this statement.

Continued

| Total | Governmental Activities<br>Internal Service Funds |
|---|---|
| $ 5,940,814 | $ 2,036,236 |
| (8,577,238) | (1,692,577) |
| (1,022,213) | (379,904) |
| 2,697,609 | 111,188 |
| (961,028) | 74,943 |
| | |
| 47,845 | 25,310 |
| (299,760) | (23,306) |
| 12,377 | 520 |
| 186,321 | - |
| (45,053) | - |
| 4,384 | (1) |
| (93,886) | 2,523 |
| | |
| (75,255) | (8,299) |
| 15 | - |
| (82,369) | (46,987) |
| 143,779 | 33,148 |
| 15,122 | 6,967 |
| (384,543) | (66,109) |
| (383,251) | (81,280) |
| | |
| 676,051 | 5,737 |
| 5,485,507 | 35,573 |
| (5,693,508) | (39,501) |
| 468,050 | 1,809 |
| | |
| (970,115) | (2,005) |
| 4,633,698 | 337,354 |
| $ 3,663,583 | $ 335,349 |
| | |
| $ (3,361,402) | $ (70,890) |
| | |
| 125,337 | 69,208 |
| | |
| 14,518 | 28,226 |
| (7,940) | 211 |
| 12,675 | 478 |
| | |
| 2,255,784 | 47,710 |
| $ (961,028) | $ 74,943 |

## Statement of Cash Flows
## PROPRIETARY FUNDS
For the Fiscal Year Ended June 30, 2010
*(expressed in thousands)*

| | Business-Type Activities Enterprise Funds | | | |
|---|---|---|---|---|
| | Workers' Compensation | Unemployment Compensation | Higher Education Student Services | Nonmajor Enterprise Funds |
| **NONCASH INVESTING, CAPITAL AND FINANCING ACTIVITIES** | | | | |
| Contributions of capital assets | $ - | $ - | $ - | $ - |
| Acquisition of capital assets through capital leases | - | - | 71 | - |
| Refunding Certificates of Participation issued | - | - | 6,725 | - |
| Refunding Certificates of Participation redeemed | - | - | 7,005 | - |
| Amortization of annuity prize liability | - | - | - | 17,352 |
| Increase (decrease) in fair value of investments | 928,502 | - | 39 | 127,586 |
| Refunding bonds issued | - | - | 53,470 | - |
| Refunding bonds redeemed | - | - | 56,295 | - |
| Amortization of debt premium (issue costs/discount) | - | - | (383) | (110) |
| Accretion of interest on zero coupon bonds | - | - | - | (3,709) |
| Increase in ownership of joint venture | - | - | 6,963 | - |

The notes to the financial statements are an integral part of this statement.

Concluded

| Total | Governmental Activities<br>Internal Service Funds |
|---|---|
| $ - | $ 1,809 |
| 71 | 15 |
| 6,725 | 15,075 |
| 7,005 | 15,490 |
| 17,352 | - |
| 1,056,127 | (528) |
| 53,470 | - |
| 56,295 | - |
| (493) | - |
| (3,709) | - |
| 6,963 | - |

## Statement of Fiduciary Net Assets
## FIDUCIARY FUNDS
June 30, 2010
*(expressed in thousands)*

| | Private-Purpose Trust | Local Government Investment Pool | Pension and Other Employee Benefit Plans | Agency Funds |
|---|---|---|---|---|
| **ASSETS** | | | | |
| **Current Assets:** | | | | |
| Cash and pooled investments | $ 8,155 | $ 3,535,387 | $ 317,199 | $ 262,259 |
| Investments | - | 3,852,658 | - | - |
| Receivables, pension and other employee benefit plans: | | | | |
| Employers | - | - | 111,752 | - |
| Members (net of allowance) | - | - | 2,560 | - |
| Interest and dividends | - | - | 168,917 | - |
| Investment trades pending | - | - | 3,599,468 | - |
| Due from other pension and other employee benefit funds | - | - | 1,626 | - |
| Other receivables, all other funds | - | 1,542 | - | 10,613 |
| Due from other funds | - | - | 79 | 215 |
| Due from other governments | - | - | - | 18,135 |
| **Total Current Assets** | 8,155 | 7,389,587 | 4,201,601 | 291,222 |
| **Noncurrent Assets:** | | | | |
| Investments, noncurrent, pension and other employee benefit plans: | | | | |
| Public equity | - | - | 22,686,332 | - |
| Fixed income | - | - | 11,758,745 | - |
| Private equity | - | - | 13,560,126 | - |
| Real estate | - | - | 7,483,584 | - |
| Security lending | - | - | 3,667,614 | - |
| Liquidity | - | - | 1,645,221 | - |
| Tangible asset | - | - | 610,388 | - |
| Investments, noncurrent, all other funds | 18,128 | 939,909 | - | 17,858 |
| Other noncurrent assets | - | - | - | 32,175 |
| Capital assets: | | | | |
| Furnishings, equipment and intangible assets | 32 | - | - | - |
| Accumulated depreciation | (15) | - | - | - |
| **Total Noncurrent Assets** | 18,145 | 939,909 | 61,412,010 | 50,033 |
| **Total Assets** | 26,300 | 8,329,496 | 65,613,611 | $ 341,255 |
| **LIABILITIES** | | | | |
| Accounts payable | 286 | - | - | $ 9,048 |
| Contracts and retainages payable | - | - | - | 37,133 |
| Accrued liabilities | 111 | 57 | 4,177,204 | 53,616 |
| Obligations under security lending agreements | - | - | 3,667,614 | - |
| Due to other funds | - | - | 1,763 | 56 |
| Due to other pension and other employee benefit funds | - | - | 1,626 | - |
| Due to other governments | - | - | - | 209,228 |
| Unearned revenue | - | - | 1,087 | - |
| Other long-term liabilities | - | - | - | 32,174 |
| **Total Liabilities** | 397 | 57 | 7,849,294 | $ 341,255 |
| **NET ASSETS** | | | | |
| Net assets held in trust for: | | | | |
| Pension benefits | - | - | 55,315,440 | |
| Deferred compensation participants | - | - | 2,448,877 | |
| Local government pool participants | - | 8,329,439 | - | |
| Individuals, organizations & other governments | 25,903 | - | - | |
| **Total Net Assets** | $ 25,903 | $ 8,329,439 | $ 57,764,317 | |

The notes to the financial statements are an integral part of this statement.

## Statement of Changes in Fiduciary Net Assets
## FIDUCIARY FUNDS
For the Fiscal Year Ended June 30, 2010
*(expressed in thousands)*

| | Private-Purpose Trust | Local Government Investment Pool | Pension and Other Employee Benefit Plans |
|---|---|---|---|
| **ADDITIONS** | | | |
| Contributions: | | | |
| Employers | $ - | $ - | $ 920,043 |
| Members | - | - | 941,664 |
| State | - | - | 68,631 |
| Participants | - | 17,193,607 | 185,120 |
| Total Contributions | - | 17,193,607 | 2,115,458 |
| Investment Income: | | | |
| Net appreciation (depreciation) in fair value | - | - | 5,306,164 |
| Interest and dividends | - | 32,586 | 1,586,364 |
| Less: Investment expenses | - | - | (226,686) |
| Net Investment Income (Loss) | - | 32,586 | 6,665,842 |
| Other Additions: | | | |
| Unclaimed property | 48,422 | - | - |
| Transfers from other pension plans | - | - | 19,905 |
| Other contracts, grants and miscellaneous | 1 | - | 1,148 |
| Total Other Additions | 48,423 | - | 21,053 |
| **Total Additions** | 48,423 | 17,226,193 | 8,802,353 |
| **DEDUCTIONS** | | | |
| Pension benefits | - | - | 2,754,169 |
| Pension refunds | - | - | 202,207 |
| Transfers to other pension plans | - | - | 19,905 |
| Administrative expenses | 3,482 | 657 | 2,666 |
| Distributions to participants | - | 16,922,279 | 108,578 |
| Payments to or on behalf of individuals, organizations and other governments in accordance with state unclaimed property laws | 40,739 | - | - |
| **Total Deductions** | 44,221 | 16,922,936 | 3,087,525 |
| **Net Increase (Decrease)** | 4,202 | 303,257 | 5,714,828 |
| **Net Assets - Beginning** | 21,701 | 8,026,182 | 52,049,489 |
| **Net Assets - Ending** | $ 25,903 | $ 8,329,439 | $ 57,764,317 |

The notes to the financial statements are an integral part of this statement.

# Statement of Fund Net Assets
## COMPONENT UNITS
June 30, 2010
*(expressed in thousands)*

| | Public Stadium | Nonmajor Component Units | Total |
|---|---|---|---|
| **ASSETS** | | | |
| **Current Assets:** | | | |
| Cash and pooled investments | $ 6,738 | $ 14,925 | $ 21,663 |
| Investments | 3,784 | 39,819 | 43,603 |
| Other receivables (net of allowance) | 442 | 1,712 | 2,154 |
| Prepaid expenses | 24 | 175 | 199 |
| **Total Current Assets** | 10,988 | 56,631 | 67,619 |
| **Noncurrent Assets:** | | | |
| Investments, noncurrent | 18,469 | - | 18,469 |
| Other noncurrent assets | - | 75,917 | 75,917 |
| Capital assets: | | | |
| Land | 34,677 | - | 34,677 |
| Buildings | 460,025 | - | 460,025 |
| Furnishings, equipment and intangible assets | 23,129 | 1,655 | 24,784 |
| Accumulated depreciation | (145,112) | (1,320) | (146,432) |
| **Total Noncurrent Assets** | 391,188 | 76,252 | 467,440 |
| **Total Assets** | 402,176 | 132,883 | 535,059 |
| **LIABILITIES** | | | |
| **Current Liabilities:** | | | |
| Accounts payable | 18 | 37,432 | 37,450 |
| Contracts and retainages payable | 2,566 | - | 2,566 |
| Accrued liabilities | 3,860 | 70 | 3,930 |
| Unearned revenue | 86 | 5,343 | 5,429 |
| **Total Current Liabilities** | 6,530 | 42,845 | 49,375 |
| **Noncurrent Liabilities:** | | | |
| Other long-term liabilities | 25,587 | - | 25,587 |
| **Total Noncurrent Liabilities** | 25,587 | - | 25,587 |
| **Total Liabilities** | 32,117 | 42,845 | 74,962 |
| **NET ASSETS** | | | |
| Invested in capital assets, net of related debt | 343,189 | 335 | 343,524 |
| Restricted for deferred sales tax | 20,490 | - | 20,490 |
| Restricted for other purposes | - | 500 | 500 |
| Unrestricted | 6,380 | 89,203 | 95,583 |
| **Total Net Assets (Deficit)** | $ 370,059 | $ 90,038 | $ 460,097 |

The notes to the financial statements are an integral part of this statement.

## Statement of Revenues, Expenses, and Changes in Fund Net Assets
## COMPONENT UNITS
For the Fiscal Year Ended June 30, 2010
*(expressed in thousands)*

| | Public Stadium | Nonmajor Component Units | Total |
|---|---|---|---|
| **OPERATING REVENUES** | | | |
| Charges for services | $ 1,031 | $ 15,415 | $ 16,446 |
| **Total Operating Revenues** | 1,031 | 15,415 | 16,446 |
| **OPERATING EXPENSES** | | | |
| Salaries and wages | 404 | 4,573 | 4,977 |
| Employee benefits | 74 | 1,247 | 1,321 |
| Personal services | 183 | 1,576 | 1,759 |
| Goods and services | 827 | 2,132 | 2,959 |
| Travel | 2 | 33 | 35 |
| Depreciation and amortization | 15,558 | 161 | 15,719 |
| Miscellaneous expenses | - | 173 | 173 |
| **Total Operating Expenses** | 17,048 | 9,895 | 26,943 |
| **Operating Income (Loss)** | (16,017) | 5,520 | (10,497) |
| **NONOPERATING REVENUES (EXPENSES)** | | | |
| Earnings (loss) on investments | 1,130 | 1,578 | 2,708 |
| Operating grants and contributions | - | 41,810 | 41,810 |
| Distributions of operating grants | - | (41,256) | (41,256) |
| Naming rights | 1,961 | - | 1,961 |
| Other | 15 | - | 15 |
| **Total Nonoperating Revenues (Expenses)** | 3,106 | 2,132 | 5,238 |
| **Income (Loss)** | (12,911) | 7,652 | (5,259) |
| Capital grants and contributions | 903 | - | 903 |
| **Total Contributions and Transfers** | 903 | - | 903 |
| **Change in Net Assets** | (12,008) | 7,652 | (4,356) |
| **Net Assets - Beginning** | 382,067 | 82,386 | 464,453 |
| **Net Assets - Ending** | $ 370,059 | $ 90,038 | $ 460,097 |

The notes to the financial statements are an integral part of this statement.

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# Index

## Notes to the Financial Statements

For the Fiscal Year Ended June 30, 2010


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# Note 1
## Summary of Significant Accounting Policies

The accompanying financial statements of the state of Washington have been prepared in conformity with generally accepted accounting principles (GAAP). The Office of Financial Management (OFM) is the primary authority for the state's accounting and reporting requirements. OFM has adopted the pronouncements of the Governmental Accounting Standards Board (GASB), which is the accepted standard-setting body for establishing governmental accounting and financial reporting principles nationally. For government-wide and enterprise fund reporting, the state follows only those private-sector standards issued on or before November 30, 1989, unless those pronouncements conflict with or contradict the pronouncements of the GASB. Following is a summary of the significant accounting policies:

### A. REPORTING ENTITY

In defining the state of Washington for financial reporting purposes, management considers: all funds, organizations, institutions, agencies, departments, and offices that are legally part of the state (the primary government); organizations for which the state is financially accountable; and other organizations for which the nature and significance of their relationship with the state are such that exclusion would cause the state's financial statements to be misleading or incomplete.

Financial accountability exists when the primary government appoints a voting majority of an organization's governing body and is either able to impose its will on that organization or there is a potential for the organization to provide specific financial benefits to, or impose specific financial burdens on, the primary government. The primary government may be financially accountable if an organization is fiscally dependent on the primary government regardless of whether the organization has a separately elected governing board, a governing board appointed by a higher level of government, or a jointly appointed board. An organization is fiscally dependent if it is unable to determine its budget without another government having the substantive authority to approve or modify that budget, to levy taxes or set rates or charges without substantive approval by another government, or to issue bonded debt without substantive approval by another government.

Based on these criteria, the following are included in the financial statements of the primary government:

**State Agencies.** Except as otherwise described herein, all state elected offices, departments, agencies, commissions, boards, committees, authorities, and councils (agencies) and all funds and subsidiary accounts of the state are included in the primary government. Executives of these agencies are either elected, directly appointed by the Governor, appointed by a board which is appointed by the Governor, or appointed by a board which is in part appointed by the Governor.

Additionally, a small number of board positions are established by statute or independently elected. The state Legislature creates these agencies, assigns their programs, approves operational funding, and requires financial accountability. The Legislature also authorizes all bond issuances for capital construction projects for the benefit of state agencies. The legal liability for these bonds and the ownership of agency assets resides with the state.

**Colleges and Universities.** The governing boards of the five state universities, the state college, and the 34 state community and technical colleges are appointed by the Governor. Each college's governing board appoints a president to function as chief administrator. The state Legislature approves budgets and budget amendments for the colleges' appropriated funds, which include the state's General Fund as well as certain capital projects funds. The state Treasurer issues general obligation debt for major campus construction projects. However, the colleges are authorized to issue revenue bonds. The University of Washington issues general revenue bonds that are payable from general revenues, including student tuition and fees, grant indirect cost recovery, sales and services revenue, and investment income. The remainder of the college revenue bonds pledge the income derived from acquired or constructed assets such as housing, dining, and parking facilities. These revenue bonds are payable solely from, and secured by, fees and revenues derived from the operation of constructed facilities; the legal liability for the bonds and the ownership of the college assets reside with the state. Colleges do not have separate corporate powers and sue and are sued as part of the state with legal representation provided through the state Attorney General's Office. Since the colleges are legally part of the state, their financial operations, including their blended component units, are reported in the primary government financial statements using the fund structure prescribed by GASB.

**Retirement Systems.** The state of Washington, through the Department of Retirement Systems, administers eight retirement systems for public employees of the state and political subdivisions: the Public Employees' Retirement System, the Teachers' Retirement System, the School Employees' Retirement System, the Law Enforcement Officers' and Fire Fighters' Retirement System, the Washington State Patrol Retirement System, the Public Safety Employees' Retirement System, the Judicial Retirement System, and the Judges' Retirement Fund. The

director of the Department of Retirement Systems is appointed by the Governor.

There are two additional retirement systems administered outside of the Department of Retirement Systems. The Volunteer Fire Fighters' and Reserve Officers' Relief and Pension Fund is administered through the Board for Volunteer Fire Fighters, which is appointed by the Governor. The Judicial Retirement Account is administered through the Administrative Office of the Courts under the direction of the Board for Judicial Administration.

The state Legislature establishes laws pertaining to the creation and administration of all public retirement systems. The participants of the public retirement systems, together with the state, provide funding for all costs of the systems based upon actuarial valuations. The state establishes benefit levels and approves the actuarial assumptions used in determining contribution levels.

All ten of the aforementioned retirement systems are included in the primary government's financial statements.

**Blended Component Units.** Blended component units, although legally separate entities, are part of the state's operations in substance. Accordingly, they are reported as part of the state and blended into the appropriate funds. The following entities are blended in the state's financial statements:

**Tobacco Settlement Authority (TSA).** The TSA was created by the Washington State Legislature in March 2002 as a public instrumentality separate and distinct from the state. It is governed by a five-member board appointed by the Governor. It was created solely for the purpose of issuing bonds to securitize a portion of the state's future tobacco settlement revenue. Proceeds of the debt instrument were transferred to the state to help fund health care, long-term care, and other programs of the state. Refer to Note 7 for additional information.

Financial reports for the TSA may be obtained from the authority at the following address:

Tobacco Settlement Authority
1000 Second Avenue, Suite 2700
Seattle, WA 98104-1046

**Other Blended Component Units.** Tumwater Office Properties, the University of Washington (UW) Alumni Association, UW Physicians, UW Physicians Network, Community Development Properties C-D, Educational Research Properties, Radford Court Properties, Twenty-Fifth Avenue Properties, TSB Properties, Washington Biomedical Research Properties I and II, and Washington Biomedical Research Facilities 3 are blended component units in the state's financial statements. All the aforementioned blended component units provide services entirely or almost entirely to the state. Financial information for these blended component units may be obtained from their respective administrative offices.

**Discrete Component Units.** Discretely presented component units are reported in a separate column in the government-wide financial statements. Discretely presented component units are legally separate from the state and primarily serve or benefit those outside of the state. They are financially accountable to the state, or have relationships with the state such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete. These entities are reported as discrete component units because state officials either serve on or appoint the members of the governing bodies of the authorities. The state also has the ability to influence the operations of the authorities through legislation. The following entities are discretely presented in the financial statements of the state in the component unit's column:

The Washington State Housing Finance Commission, the Washington Higher Education Facilities Authority, the Washington Health Care Facilities Authority, and the Washington Economic Development Finance Authority (financing authorities) were created by the state Legislature in a way that specifically prevents them from causing the state to be liable or responsible for their acts and obligations, including, but not limited to, any obligation to pay principal and interest on financing authority bonds. The financing authorities cannot obligate the state, either legally or morally, and the state has not assumed any obligation of, or with respect to, the financing authorities.

Financial reports of these financing authorities may be obtained from each authority at the following addresses:

Washington Health Care Facilities Authority
410 - 11th Avenue SE, Suite 201
PO Box 40935
Olympia, WA 98504-0935

Washington State Housing Finance Commission
Washington Higher Education Facilities Authority
Washington Economic Development Finance Authority
1000 Second Avenue, Suite 2700
Seattle, WA 98104-1046

The Washington State Public Stadium Authority (PSA) was created by the state Legislature to acquire, construct, own, and operate a football/soccer stadium, exhibition center, and parking garage. Construction was completed in 2002. PSA capital assets, net of accumulated depreciation, total $373 million. The state issued general obligation bonds for a portion of the cost of the stadium construction. The total public share of the stadium and exhibition center cost did not exceed $300 million from all state and local government funding sources, as defined in statute.

Project costs in excess of $300 million were the responsibility of the project's private partner, First & Goal, Inc. The bonds are being repaid through new state lottery games, a state sales tax credit, extension of the local hotel/motel tax, and parking and admissions taxes at the new facility. Financial reports of the PSA may be obtained at the following address:

Washington State Public Stadium Authority
Qwest Field & Event Center
800 Occidental Avenue South, #700
Seattle, WA 98134

The state's component units each have a year-end of June 30 with the exception of the Washington Economic Development Finance Authority which has a December 31 year-end.

**Joint Venture**. In 1998, the University of Washington Medical Center (Medical Center) entered into an agreement with Seattle Children's Hospital and Fred Hutchinson Cancer Research Center to establish the Seattle Cancer Care Alliance (SCCA). Each member of the SCCA has a one-third interest. The mission of the SCCA is to eliminate cancer as a cause of human suffering and death and to become recognized as the premier cancer research and treatment center in the Pacific Northwest. The SCCA integrates the cancer research, teaching, and clinical cancer programs of all three institutions to provide state-of-the-art cancer care. Under the agreement, the Medical Center provides the patient care to all adult inpatients of the SCCA.

Inpatient Services – The SCCA operates a 20-bed unit located within the Medical Center in which its adult inpatients receive care. The fiscal intermediary has determined that the 20-bed unit qualifies as a hospital within a hospital for Medicare reimbursement purposes. The SCCA provides medical oversight and management of the inpatient unit. Under agreements, the Medical Center provides inpatient care services to the SCCA including necessary personnel, equipment, and ancillary services.

Outpatient Services – The SCCA operates an ambulatory cancer care service facility in Seattle. The Medical Center provides various services to the SCCA's outpatient facility including certain pharmacy, laboratory, and pathology services as well as billing, purchasing, and other administrative services.

The state accounts for the Medical Center's interest in SCCA under the equity method of accounting. Income of $7.4 million was recorded in Fiscal Year 2010, bringing the total equity investment to $63 million which is recognized in the state's financial statements in the Higher Education Student Services Fund.

Separate financial statements for SCCA may be obtained from:

Seattle Cancer Care Alliance
825 Eastlake Avenue East
PO Box 19023
Seattle, WA 98109-1023

## B. GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS

### Government-wide Financial Statements

The state presents two basic government-wide financial statements: the Statement of Net Assets and the Statement of Activities. These government-wide financial statements report information on all non-fiduciary activities of the primary government and its component units. The financial information for the primary government is distinguished between governmental and business-type activities. Governmental activities generally are financed through taxes, intergovernmental revenues, and other non-exchange revenues. Business-type activities are financed in whole or in part by fees charged to external parties for goods and services.

**Statement of Net Assets.** The Statement of Net Assets presents the state's non-fiduciary assets and liabilities. As a general rule, balances between governmental and business-type activities are eliminated.

Assets and liabilities are presented in a net assets format in order of liquidity. Net assets are classified into three categories:

- Invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation and reduced by outstanding balances of bonds, notes and other debt that are attributed to the acquisition, construction, or improvement of those assets.

- Restricted net assets result when constraints are placed on net asset use either by external parties or by law through constitutional provision or enabling legislation.

- Unrestricted net assets consist of net assets that do not meet the definition of the two preceding categories.

**Statement of Activities.** The Statement of Activities reports the extent to which each major state program is supported by general state revenues or is self-financed through fees and intergovernmental aid. For governmental activities, a major program is defined as a function. For business-type activities, a major program is an identifiable activity.

Program revenues offset the direct expenses of major programs. Direct expenses are those that are clearly identifiable within a specific function or activity. Program revenues are identified using the following criteria:

- Charges to customers for goods and services of the program. A customer is one who directly benefits from the goods or services or is otherwise directly affected by the program, such as a state citizen or taxpayer, or other governments or nongovernmental entities.

- Amounts received from outside entities that are restricted to one or more specific programs. These amounts can be operating or capital in nature.

- Earnings on investments that are restricted to a specific program are also considered program revenues.

General revenues consist of taxes and other items not meeting the definition of program revenues.

Generally the effect of internal activities is eliminated. Exceptions to this rule include charges between the workers' compensation insurance programs and various other state programs and functions. Elimination of these charges would distort the direct costs and revenues reported for the various activities involved.

## Fund Financial Statements

The state uses 663 accounts that are combined into 54 rollup funds. The state presents separate financial statements for governmental funds, proprietary funds, and fiduciary funds. Major individual governmental funds and major individual proprietary funds are reported in separate columns in the fund financial statements, with nonmajor funds being combined into a single column regardless of fund type. Internal service and fiduciary funds are reported by fund type. Major funds include:

**Major Governmental Funds:**

- **General Fund** is the state's primary operating fund. This fund accounts for all financial resources and transactions not accounted for in other funds.

- **Higher Education Special Revenue Fund** primarily accounts for grants and contracts received for research and other educational purposes. This fund also accounts for charges for services by state institutions of higher education.

- **Motor Vehicle Special Revenue Fund** accounts for highway activities of the Washington State Patrol, operations of the state ferry system, maintenance of non-interstate highways and bridges, completion and preservation of the interstate system, and other transportation improvements. Motor Vehicle Fund revenues are generated from vehicle fuel taxes, vehicle licenses, tolling, and federal transportation agencies.

- **Higher Education Endowment Permanent Fund** accounts for gifts and bequests that the donors have specified must remain intact. Each gift is governed by various restrictions on the investment and use of the funds.

**Major Enterprise Funds:**

- **Workers' Compensation Fund** accounts for the workers' compensation program that provides medical, time-loss, and disability benefit payments to qualifying individuals sustaining work-related injuries.

- **Unemployment Compensation Fund** accounts for the unemployment compensation program. It accounts for the deposit of funds, requisitioned from the Federal Unemployment Trust Fund, to provide services to eligible participants within the state and to pay unemployment benefits.

- **Higher Education Student Services Fund** is used by colleges and universities principally for bookstore, cafeteria, parking, student housing, food service, and hospital business enterprise activities.

The state includes the following governmental and proprietary fund types within nonmajor funds:

**Nonmajor Governmental Funds:**

- **Special Revenue Funds** account for the proceeds of specific revenue sources (other than trusts for individuals, private organizations, or other governments, or for major capital projects) that are legally restricted to expenditures for specific purposes. These include a variety of state programs including public safety and health assistance programs; natural resource and wildlife protection and management programs; driver licensing and non-highway transportation improvements; K-12 school construction; and construction and loan programs for local public works projects.

- **Debt Service Funds** account for the accumulation of resources for, and the payment of, principal and interest on the state's bonds issued in support of governmental activities.

- **Capital Projects Funds** account for the acquisition, construction, or improvement of major capital facilities including higher education facilities.

- **Common School Permanent Fund** accounts for the principal derived from the sale of timber. Interest earned is used for the benefit of common schools.

**Nonmajor Proprietary Funds:**

- **Enterprise Funds** account for the state's business type operations for which a fee is charged to external users for goods or services including: the state lottery; state liquor stores; the guaranteed college tuition program; and the convention and trade center.

- **Internal Service Funds** account for the provision of legal, motor pool, data processing, risk management, health insurance, and other services by one department or agency to other departments or agencies of the state on a cost-reimbursement basis.

The state reports the following fiduciary funds:

- **Pension (and other employee benefit) Trust Funds** are used to report resources that are required to be held in trust by the state for the members and beneficiaries of defined benefit and defined contribution pension plans, and other employee benefit plans.

- **Investment Trust Fund** accounts for the external portion of the Local Government Investment Pool (LGIP), which is reported by the state as the sponsoring government.

- **Private-Purpose Trust Fund** is used to report trust arrangements, other than pension and investment trusts, under which principal and income benefit individuals, private organizations, or other governments such as the administration of unclaimed property.

- **Agency Funds** account for resources held by the state in a custodial capacity for other governments, private organizations, or individuals.

**Operating and Nonoperating Revenues and Expenses.** The state's proprietary funds make a distinction between operating and nonoperating revenues and expenses. Operating revenues and expenses generally result from providing goods and services directly related to the principal operations of the funds. For example, operating revenues for the state's workers' compensation and health insurance funds consist of premiums and assessments collected. Operating expenses consist of claims paid to covered individuals, claims adjustment expenses, costs of commercial insurance coverage and administrative expenses. All revenues and expenses not meeting this definition are reported as nonoperating, including interest expense and investment gains and losses.

**Application of Restricted/Unrestricted Resources.** When both restricted and unrestricted resources are available for use, it is the state's policy to use restricted resources first and then use unrestricted resources as they are needed.

## C. MEASUREMENT FOCUS AND BASIS OF ACCOUNTING

For government-wide reporting purposes, the state uses the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of the related cash flows. Property taxes are recognized as revenue in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

For fund statement reporting purposes, the state uses the current financial resources measurement focus and modified accrual basis of accounting for governmental funds. With the current financial resources measurement focus, generally only current assets and current liabilities are included on the governmental funds balance sheet. Operating statements for these funds present inflows (i.e., revenues and other financing sources) and outflows (i.e., expenditures and other financing uses) of expendable financial resources.

Under the modified accrual basis of accounting, revenues are recognized when susceptible to accrual (i.e., when they become both measurable and available). "Measurable" means the amount of the transaction can be reasonably estimated. "Available" means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. Primary revenues that are determined to be susceptible to accrual include sales taxes, business and occupation taxes, motor fuel taxes, federal grants-in-aid, and charges for services.

Revenues from property taxes are determined to be available if collectible within 60 days. Taxes imposed on exchange transactions are accrued when the underlying exchange transaction occurs if collectible within one year. Revenue for timber cutting contracts is accrued when the timber is harvested. Revenues from licenses, permits, and fees are recognized when received in cash. Revenues related to expenditure-driven grant agreements are recognized when the qualifying expenditures are made, provided that the availability criteria is met. Expenditure-driven grant revenue is considered available if it can be collected by the state at the same time cash is disbursed to cover the associated grant expenditure. Pledges are accrued when the eligibility requirements are met and resources are available. All other accrued revenue sources are determined to be available if collectible within 12 months.

Property taxes are levied in December for the following calendar year. The first half-year collections are due by April 30, and the second half-year collections are due by October 31. Since the state is on a fiscal year ending June 30, the first half-year collections are recognized as revenue,

if collectible within 60 days of the fiscal year end. The second half-year collections are recognized as receivables offset by deferred revenue. The lien date on property taxes is January 1 of the tax levy year.

Under modified accrual accounting, expenditures are generally recognized when the related liability is incurred.

However, unmatured interest on general long-term debt is recognized when due, and certain compensated absences, other postemployment benefits, and claims and judgments are recognized when the obligations are expected to be liquidated with available expendable financial resources.

The state reports deferred revenues on its governmental fund balance sheet under certain conditions. Deferred revenues arise when a potential revenue does not meet both the "measurable" and the "available" criteria for revenue recognition in the current period. Deferred revenues also arise when resources are received by the state before it has a legal claim to them, such as when grant monies are received prior to incurring qualifying expenditures/expenses.

All proprietary and trust funds are accounted for using the economic resources measurement focus. With this measurement focus, all assets and liabilities associated with the operations of these funds are included on their respective statements of net assets. Operating statements present increases (i.e., revenues) and decreases (i.e., expenses) in total net assets. Net assets in proprietary funds are segregated into three components: invested in capital assets, net of related debt; restricted; and unrestricted.

Net assets for trust funds are held in trust for external individuals and organizations.

All proprietary and trust funds are reported using the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recognized when incurred.

## D. ASSETS, LIABILITIES, AND NET ASSETS OR EQUITY

### 1. Cash and Investments

Investments of surplus or pooled cash balances are reported on the accompanying Statements of Net Assets, Balance Sheets and Statements of Cash Flows as "Cash and Pooled Investments." The Office of the State Treasurer invests state treasury cash surpluses where funds can be disbursed at any time without prior notice or penalty. For reporting purposes, pooled investments are stated at fair value or amortized cost, which approximates fair value. For purposes of reporting cash flows, the state considers cash and pooled investments to be cash equivalents. Pooled investments include short-term, highly-liquid investments that are both readily convertible to cash and are so near their maturity dates that they present insignificant risk of changes in value because of changes in interest rates.

The method of accounting for noncurrent investments varies depending upon the fund classification. Investments in the state's Local Government Investment Pool (LGIP), an external investment pool operated in a manner consistent with the Securities and Exchange Commission's (SEC) Rule 2a-7 of the Investment Company Act of 1940, are reported at amortized cost. The Office of the State Treasurer prepares a stand-alone LGIP financial report. A copy of the report is available from the Office of the State Treasurer, PO Box 40200, Olympia, Washington 98504-0200, phone number (360) 902-9000 or TTY (360) 902-8963.

Certain pension trust fund investments, including real estate and private equity, are reported at fair values based on appraisals or estimates in the absence of readily ascertainable fair values. At June 30, 2010, these investments are valued at $21.7 billion. Because of the inherent uncertainties in the estimation of fair value, it is possible that the estimates will change.

All other noncurrent investments are reported at fair value. Fair values are based on published market prices, quotations from national security exchanges and security pricing services, or by the respective fund managers for securities that are not actively traded. Privately held mortgages are valued at cost, which approximates fair value. Additional disclosure describing investments is provided in Note 3.

### 2. Receivables and Payables

Receivables in the state's governmental fund type accounts consist primarily of taxes and federal revenues. Receivables in all other funds have arisen in the ordinary course of business. Receivables are recorded when either the asset or revenue recognition criteria (refer to Note 1.C) have been met. All receivables are reported net of an allowance for accounts estimated to be uncollectible.

For government-wide reporting purposes, amounts recorded as interfund/interagency receivables and payables are eliminated in the governmental and business-type activities columns on the Statement of Net Assets, except for the net residual balances due between the governmental and business-type activities, which are reported as internal balances. Amounts recorded in governmental and business-type activities as due to or from fiduciary funds have been reported as due to or from other governments.

Noncurrent receivables are recorded in the Workers' Compensation Fund representing estimated recoveries from third parties for a certain portion of claims expenses that are recorded as noncurrent claims payable. The accrued recoveries are computed using a variety of actuarial and statistical techniques and are discounted at assumed interest rates to arrive at the recorded value.

Disclosures related to the Workers' Compensation Fund activities and claims payable are provided in Notes 1.E.1 and 7.E.

## 3. Inventories and Prepaids

Consumable inventories, consisting of expendable materials and supplies held for consumption, are valued and reported in the state's financial statements if the fiscal year-end balance on hand within an agency is estimated to be $25,000 or more. Consumable inventories are generally valued at cost using the first-in, first-out method. Donated consumable inventories are recorded at fair market value.

All merchandise inventories are considered reportable for financial statement purposes. Merchandise inventories are generally valued at cost using the first-in, first-out method.

Inventories of governmental funds are valued at cost and recorded using the consumption method. Proprietary funds expense inventories when used or sold.

For governmental fund financial reporting, inventory balances are also recorded as a reservation of fund balance indicating that they do not constitute "available spendable resources" except for $4.9 million in federally donated consumable inventories, which are offset by deferred revenues because they do not constitute an "available" resource until consumed.

Prepaid items are those certain types of supplies and/or services (not inventory) that are acquired or purchased during an accounting period but not used or consumed during that accounting period.

In governmental fund type accounts, prepaid items are generally accounted for using the purchases method. Under the purchases method, prepaid items are treated as expenditures when purchased and residual balances, if any, at year end are not accounted for as assets.

In proprietary and trust fund type accounts, prepaid items are accounted for using the consumption method. The portion of supplies or services consumed or used during a period is recorded as an expense. The balance that remains is reported as an asset until consumed or used.

## 4. Restricted Assets

Unspent proceeds of state bond issues and other debt financing programs are classified as restricted assets because their use is limited by applicable bond and other debt covenants. These are reflected on the balance sheets and statements of net assets.

## 5. Capital Assets

Except as noted below, it is the state's policy to capitalize:

- All land;
- All additions and improvements to the state highway system;
- Infrastructure, other than the state highway system, with a cost of $100,000 or more;
- Buildings, building improvements, and leasehold improvements with a cost of $100,000 or more;
- Intangible assets, either purchased or internally developed, with a cost of $1,000,000 or more that are identifiable by meeting one of the following conditions:
    - The asset is capable of being separate or divided and sold, transferred, licensed, rented, exchanged; or
    - The asset arises from contractual or other legal rights, regardless of whether those rights are transferable or separable;
- All other capital assets with a unit cost of $5,000 or greater, or collections with a total cost of $5,000 or greater, unless otherwise noted; and
- All capital assets acquired with Certificates of Participation, a debt financing program administered by the Office of the State Treasurer.

Assets acquired by capital leases are capitalized if the asset's fair market value meets the state's capitalization threshold described above.

Purchased capital assets are valued at cost where historical records are available and at estimated historical cost where no historical records exist. Capital asset costs include the purchase price plus those costs necessary to place the asset in its intended location and condition for use (ancillary costs). Normal maintenance and repair costs that do not materially add to the value or extend the life of the state's capital assets are not capitalized.

Donated capital assets are valued at their estimated fair market value on the date of donation, plus all appropriate ancillary costs. When the fair market value is not practically determinable due to lack of sufficient records, estimated cost is used. Where necessary, estimates of original cost and fair market value are derived by factoring price levels from the current period to the time of acquisition.

The value of assets constructed by agencies for their own use includes all direct construction costs and indirect costs that are related to the construction. In enterprise and trust funds, net interest costs (if material) incurred during the period of construction are capitalized.

State agencies have the option to capitalize art collections, library reserve collections, and museum and historical collections that are considered inexhaustible, in that their value does not diminish over time, if all of the following conditions are met:

- The collection is held for public exhibition, education, or research in furtherance of public service, rather than financial gain.
- The collection is protected, kept unencumbered, cared for, and preserved.
- The collection is subject to policy requirements that the proceeds from sales of collection items be used to acquire other items for the collection.

Depreciation/amortization is calculated using the straight-line method over the estimated useful lives of the assets. Generally, estimated useful lives are as follows:

| | |
|---|---|
| Buildings & building components | 5-50 years |
| Furnishings, equipment & collections | 3-50 years |
| Other improvements | 3-50 years |
| Intangibles | 3-50 years |
| Infrastructure | 20-50 years |

The cost and related accumulated depreciation/ amortization of disposed capital assets are removed from the accounting records.

The state capitalizes the state highway system as a network but does not depreciate it since the system is being preserved approximately at or above a condition level established by the state. That condition level is documented and disclosed. Additionally, the highway system is managed using an asset management system that includes:

- Maintenance of an up-to-date inventory of system assets,
- Performance of condition assessments of the assets at least every three years with summarization of the results using a measurement scale, and
- Annual estimation of the amount to maintain and preserve the assets at the condition level established and disclosed.

All state highway system expenditures that preserve the useful life of the system are expensed in the period incurred. Additions and improvements that increase the capacity or efficiency of the system are capitalized. This approach of reporting condition instead of depreciating the highway system is called the modified approach.

For government-wide financial reporting purposes, capital assets of the state are reported as assets in the applicable governmental or business-type activities column on the Statement of Net Assets. Depreciation/amortization expense related to capital assets is reported in the Statement of Activities.

Capital assets and the related depreciation/amortization expense are also reported in the proprietary fund financial statements.

In governmental funds, capital assets are not capitalized in the accounts that acquire or construct them. Instead, capital acquisitions and construction are reflected as expenditures in the year assets are acquired or construction costs are incurred. No depreciation/amortization is reported.

## 6. Compensated Absences

State employees accrue vested vacation leave at a variable rate based on years of service. In general, accrued vacation leave cannot exceed 240 hours at the employee's anniversary date.

Employees accrue sick leave at the rate of one day per month without limitation on the amount that can be accumulated. Sick leave is not vested; i.e., the state does not pay employees for unused sick leave upon termination except upon employee death or retirement. At death or retirement, the state is liable for 25 percent of the employee's accumulated sick leave. In addition, the state has a sick leave buyout option in which, each January, employees who accumulate sick leave in excess of 480 hours may redeem sick leave earned but not taken during the previous year at the rate of one day's pay in exchange for each four days of sick leave.

It is the state's policy to liquidate unpaid compensated absences outstanding at June 30 with future resources rather than advance funding it with currently available expendable financial resources.

For government-wide reporting purposes, the state reports compensated absences obligations as liabilities in the applicable governmental or business-type activities columns on the Statement of Net Assets.

For fund statement reporting purposes, governmental funds recognize an expenditure for annual and sick leave when it is payable, i.e., upon employee's use, resignation, or retirement. Proprietary and trust funds recognize the expense and accrue a liability for annual leave and estimated sick leave buyout, including related payroll taxes and benefits as applicable, as the leave is earned.

### 7. Long-Term Liabilities

In the government-wide and proprietary fund financial statements, long-term obligations of the state are reported as liabilities on the Statement of Net Assets. Bonds payable are reported net of applicable original issuance premium or discount. When material, bond premiums, discounts, and issue costs are deferred and amortized over the life of the bonds.

For governmental fund financial reporting, the face (par) amount of debt issued is reported as other financing sources. Premiums and discounts on original debt issuance are also reported as other financing sources and uses, respectively. Issue costs are reported as debt service expenditures.

### 8. Fund Equity

In the fund financial statements, governmental funds report the difference between fund assets and fund liabilities as "fund balance." Reserved fund balance represents that portion of fund balance that is (1) not available for appropriation or expenditure, and/or (2) legally segregated for a specific future use. Unreserved, designated fund balance indicates tentative plans for future use of financial resources. Unreserved, undesignated fund balance represents the amount available for appropriation.

In proprietary funds, fund equity is called net assets. Net assets are comprised of three components: invested in capital assets, net of related debt; restricted; and unrestricted.

## E. OTHER INFORMATION

### 1. Insurance Activities

**Workers' Compensation.** Title 51 RCW establishes the state of Washington's workers' compensation program. The statute requires all applicable employers to secure coverage for job-related injuries and diseases through the Workers' Compensation Fund or through self-insurance.

Direct private insurance is not authorized, although self-insurers are permitted to reinsure up to 80 percent of their obligations through private insurers.

The Workers' Compensation Fund, an enterprise fund, is used to account for the workers' compensation program which provides time-loss, medical, vocational, disability, and pension benefits to qualifying individuals sustaining work-related injuries or illnesses. The main benefit plans of the workers' compensation program are funded based on rates that will keep these plans solvent in accordance with recognized actuarial principles. The supplemental pension plan supports cost-of-living adjustments (COLA) granted for time-loss and disability payments; however, these are funded on a pay-as-you-go basis. By statute, the state is only allowed to collect enough revenue to fund the current COLA payments.

Premiums are based on individual employers' reported payroll hours and insurance rates based on each employer's risk classification(s) and past experience, except the Supplemental Pension Fund premiums are based on a flat rate per hours worked independent of risk class or past experience. In addition to its regular premium plan which is required for all employers, the Workers' Compensation Fund offers a voluntary retrospective premium rating plan under which premiums are subject to three annual adjustments based on group and individual employers' loss experience. Initial adjustments to the standard premiums are paid to or collected from the groups and individual employers approximately ten months after the end of each plan year.

The Department of Labor and Industries, as administrator of the workers' compensation program, establishes claims liabilities based on estimates of the ultimate cost of claims (including future claims adjustment expenses) that have already occurred. The length of time for which such costs must be estimated varies depending on the benefit involved. Because actual claims costs depend on such complex factors as inflation, changes in doctrines of legal liabilities, claims adjudication, and judgments, the process used in computing claims liabilities does not necessarily result in an exact amount.

Claims liabilities are recomputed periodically using a variety of actuarial and statistical techniques to produce current estimates that reflect recent paid losses, claim frequency, and other economic, legal, and social factors. A provision for inflation in the calculation of estimated future claim costs is implicit in the calculation because reliance is placed both on actual historical data that reflect past inflation and on other factors that are considered to be appropriate modifiers of past experience. Changes to claims liabilities from prior periods are charged or credited to expense in the periods in which they are made.

**Risk Management.** The state of Washington operates a self-insurance liability program pursuant to RCW 4.92.130. The state manages its tort claims as an insurance business activity rather than a general governmental activity. The state's policy is generally not to purchase commercial insurance for the risk of losses to which it is exposed. Instead, the state's management believes it is more economical to manage its risks internally and set aside assets for claims settlement in the Risk Management Fund, an internal service fund. A limited amount of commercial insurance is purchased for liabilities arising from the operations of the Washington State ferries, employee bonds, and to limit the exposure to catastrophic losses. Settled claims resulting from these risks have not exceeded

commercial insurance coverage in any of the past eight fiscal years. Otherwise, the self-insurance liability program services all claims against the state for injuries and property damage to third parties. The majority of state funds and agencies participate in the self-insurance liability program in proportion to their anticipated exposure to liability losses.

**Health Insurance.** The state of Washington administers and provides medical, dental, basic life, and basic long-term disability insurance coverage for eligible state employees. In addition, the state offers coverage to K-12 school districts, educational service districts, tribal governments, political subdivisions, and employee organizations representing state civil service workers. The state establishes eligibility requirements and approves plan benefits of all participating health care organizations. Because the state and its employees are the predominant participants in the employee health insurance program, it is accounted for in the Employee Insurance Fund, an internal service fund.

The state's share of the cost of coverage for state employees is based on a per capita amount determined annually by the Legislature and allocated to state agencies.

The Health Care Authority, as administrator of the health care benefits program, collects this monthly "premium" from agencies for each active employee enrolled in the program. State employees self-pay for coverage beyond the state's contribution. Cost of coverage for non-state employees is paid by their respective employers. Most coverage is available on a self-paid basis to former employees and employees who are temporarily not in pay status.

Most coverage is also available on a self-paid basis to eligible retirees. In accordance with the provisions of GASB Statement No. 43, an agency fund, the Retiree Health Insurance Fund, is used to account for the retiree health insurance program. For additional information, refer to Note 12.

The state secures commercial insurance for certain coverage offered, but self-insures the risk of loss for the Uniform Medical Plan and the Aetna Public Health Plan.

The Uniform Medical and Aetna Public Health Plans enrolled 63.1 percent of the eligible subscribers in Fiscal Year 2010. Claims are paid from premiums collected, and claims adjudication is contracted through a third-party administrator.

Considerations in calculating liabilities include frequency of claims, administrative costs, industry inflation trends, advances in medical technology, and other social and economic factors. Liabilities include an amount for claims incurred but not reported.

## 2. Postemployment Benefits

**COBRA.** In compliance with federal law, the Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA), the state offers health and dental benefits on a temporary basis to qualified beneficiaries whose benefit coverage would otherwise end because of a qualifying event such as loss of employment. COBRA coverage is available on a self-paid basis and is the same medical and dental coverage available to state employees.

**Medical Expense Plan.** As disclosed in Note 1.D, at the time of separation from state service due to retirement or death, the state offers a 25 percent buyout of an employee's accumulated sick leave. Individual state agencies may offer eligible employees a medical expense plan (MEP) that meets the requirements of the Internal Revenue Code. Agencies offering an MEP deposit the retiring employee's sick leave buyout in the MEP for reimbursement of medical expenses.

**Retirement Benefits.** Refer to Note 11 Retirement Plans and Note 12 Other Postemployment Benefits.

## 3. Interfund/Interagency Activities

The state engages in two major categories of interfund/interagency activity: reciprocal and nonreciprocal. Reciprocal interfund/interagency activity is the internal counterpart to exchange and exchange-like transactions and includes both interfund loans and services provided and used. Nonreciprocal activity is nonexchange in nature and includes both transfers and reimbursements.

## 4. Donor-restricted Endowments

The state of Washington reports endowments in higher education endowment permanent accounts. These accounts are established outside of the state treasury for use by the higher education institutions. There is no state law that governs endowment spending; rather, the policies of individual university and college boards govern the spending of net appreciation on investments.

Prior to Fiscal Year 2009, the institutions generally used a 5 percent spending rate policy for authorizing and spending investment income. However, in light of the 2008-2009 financial crisis and subsequent drop in endowment values, the institutions adopted interim spending policies that decreased distributions to campus programs during Fiscal Years 2009 and 2010. Thereafter, distributions will remain at reduced levels until market conditions warrant a return to normal spending.

The net appreciation available for authorization for expenditure by governing boards totaled $151 million. This amount is reported as Restricted for Permanent Funds – Expendable on the government-wide Statement of Net Assets.

# Note 2
## Accounting and Reporting Changes

**Reporting Changes.** Effective for Fiscal Year 2010 reporting, the state implemented the following new standards issued by the Governmental Accounting Standards Board (GASB):

Statement No. 51, *Accounting and Financial Reporting for Intangible Assets.* Statement No. 51 requires that all intangible assets not specifically excluded by its scope provisions be classified as capital assets. This statement also requires that an intangible asset be recognized in the Statement of Net Assets only if it is considered identifiable.

Retroactive reporting of the provisions of the statement is generally required with the exception of intangible assets considered to have indefinite useful lives and those considered to be internally generated. The state did not have any intangibles assets at June 30, 2010 that were subject to retroactive reporting.

Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments.* Statement No. 53 requires the state to report derivative instruments at fair value as assets or liabilities in the financial statements and to disclose a summary of derivative instrument activity as well as the objectives, significant terms, and risks associated with derivative instruments.

**Fund Reclassification.** During Fiscal Year 2010, it was determined that an activity being reported in the Central Administrative and Regulatory Fund, a Nonmajor Governmental Fund, would be more appropriately reported in the Health Insurance Internal Service Fund. To correct this situation, beginning fund balances were restated to effect the proper fund classification of the activity.

Fund equity at July 1, 2009, has been restated as follows (expressed in thousands):

| | Fund equity at June 30, 2009, as previously reported | Fund Reclassification | Prior Period Adjustment | Fund equity as restated, July 1, 2009 |
|---|---|---|---|---|
| **Governmental Funds:** | | | | |
| General | $ 1,161,950 | $ - | $ - | $ 1,161,950 |
| Higher Education Special Revenue | 1,205,451 | - | - | 1,205,451 |
| Motor Vehicle Special Revenue * | 356,070 | - | - | 356,070 |
| Higher Education Endowment | 2,478,206 | - | - | 2,478,206 |
| Nonmajor Governmental * | 4,347,186 | (481) | - | 4,346,705 |
| **Proprietary Funds:** | | | | |
| Enterprise Funds: | | | | |
| Workers' Compensation | (10,617,226) | - | - | (10,617,226) |
| Unemployment Compensation | 3,799,721 | - | - | 3,799,721 |
| Higher Education Student Services | 1,497,015 | - | - | 1,497,015 |
| Nonmajor Enterprise | 104,941 | - | - | 104,941 |
| Internal Service Funds | (187,678) | 481 | - | (187,197) |
| **Fiduciary Funds:** | | | | |
| Private Purpose Trust | 21,701 | - | - | 21,701 |
| Local Government Investment Pool | 8,026,182 | - | - | 8,026,182 |
| Pension and Other Employee Benefit Plans | 52,049,489 | - | - | 52,049,489 |
| **Component Units:** | | | | |
| Public Stadium | 382,067 | - | - | 382,067 |
| Nonmajor Component Units | 82,386 | - | - | 82,386 |

* The Motor Vehicle Special Revenue was reported as a nonmajor governmental fund in Fiscal Year 2009, but became a major fund for reporting purposes in Fiscal Year 2010.

# Note 3
## Deposits and Investments

### A. DEPOSITS

**Custodial Credit Risk**. Custodial credit risk is the risk associated with the failure of a depository financial institution. In the event of a depository financial institution's failure, it is the risk that the state would not be able to recover its deposits or collateralized securities that are in the possession of the outside parties.

The state minimizes custodial credit risk by restrictions set forth in state law. Statutes restrict the State Treasurer to deposit funds in financial institutions that are physically located in Washington unless otherwise expressly permitted by statute and authorized by the Washington Public Deposit Protection Commission (PDPC). The PDPC, established under chapter 39.58 of the Revised Code of Washington (RCW), makes and enforces regulations and administers a collateral pool program to ensure public funds are protected if a financial institution becomes insolvent. Securities pledged are held by a trustee agent for the benefit of the collateral pool.

At June 30, 2010, $829.8 million of the state's deposits with financial institutions were either insured or collateralized, with the remaining $23.9 million uninsured/ uncollateralized. The Federal Deposit Insurance Corporation (FDIC) covers the state's insured deposits and the PDPC provides collateral protection.

### B. INVESTMENTS – PENSION AND OTHER EMPLOYEE BENEFIT TRUST FUNDS (PENSION TRUST FUNDS)

#### 1. Summary of Investment Policies

Under RCW 43.33A.030, trusteeship of the pension trust funds is vested within the voting members of the Washington State Investment Board (WSIB). The Legislature has established a standard of care for investment of these funds in RCW 43.33A.140. Additionally, the WSIB and its staff must comply with other state laws, such as the Ethics in Public Service Act, chapter 42.52 RCW, as it makes its investment decisions and seeks to meet its investment objectives.

The WSIB manages the self-directed investments of the Public Employees' Retirement System (PERS) Plan 3, Teachers' Retirement System (TRS) Plan 3, School Employees' Retirement System (SERS) Plan 3 or Deferred Compensation. Administration of these plans and program rests with the Department of Retirement Systems (DRS). Members of the plans and program select and manage their asset allocation among the various investment options offered.

The WSIB is authorized to invest as provided by statute (chapter 43.33A RCW) and WSIB policy. The WSIB is authorized to invest in the following: U.S. Treasury bills; discount notes; repurchase agreements; reverse repurchase agreements; banker's acceptances; commercial paper; guaranteed investment contracts; U.S. Government and Agency (government sponsored corporations eligible for collateral purposes at the Federal Reserve) securities; non-U.S. dollar bonds; investment grade corporate bonds; non-investment grade corporate bonds; publicly traded mortgage-backed securities; privately placed mortgages; private placements of corporate debt; U.S. and foreign common stock; U.S. preferred stock; convertible securities; private equity including but not limited to investment corporations, partnerships, and limited liability companies for venture capital, leveraged buy-outs, real estate and other tangible assets, or other forms of private equity; asset backed securities; and derivative securities including futures, options, options on futures, forward contracts, and swap transactions. There were no violations of these investment restrictions during Fiscal Year 2010.

The WSIB manages pension fund assets to maximize return at a prudent level of risk (RCW 43.33A.110). The WSIB establishes asset allocation targets that must be considered at all times when making investment decisions. The asset mix may deviate from the target. Deviations greater than predetermined acceptable levels require rebalancing back to the target. When an asset class exceeds its range, the goal of rebalancing is to meet the target allocation within consideration of the other remaining asset classes.

**Eligible Investments.** Pension trust funds are invested in the Commingled Trust Fund (CTF). The CTF is comprised of public market equities, fixed income securities, private equity investments, real estate and tangible assets. The CTF's performance benchmark objective is to exceed the return of a policy benchmark consisting of public market indices weighted according to asset allocation targets. The asset allocation for the CTF is formally reviewed at least every four years. The allocation policy will be reviewed more frequently if the WSIB believes there has been a fundamental change in the structure of the capital markets or in the underlying cash flow or liability structure of the pension trust funds.

In October 2007, the public equity program adopted a global benchmark, the Dow Jones Global Total Stock Markets Index, reflecting the globalization of capital markets. The CTF also reduced its asset allocation to public equity from 46 percent to 37 percent to facilitate increased allocations to alternative investments (private equity, real estate, and tangible assets).

Even though the fund moved to a global benchmark, the program was not substantially restructured and, thus, the public equity portfolio remains a combination of separate U.S. and international components. Because U.S. equity markets are generally efficient, all of the WSIB's investments in this segment are in a low-cost, broad-based passive index fund. In keeping with the belief that international equity markets are less efficient while acknowledging that international efficiency is increasing, the WSIB's developed markets international equity program has increased its use of passive strategies to 35 percent, but kept the majority of the program in active mandates. The entire emerging markets equity program is actively managed.

The portfolio is constrained by policy from investing more than 1 percent of the portfolio's par holdings in any single issuer with a quality rating below investment grade (as defined by Barclays Capital Global Family of Fixed Income Indices). Total holdings of below investment grade credit bonds shall not exceed 15 percent of total bond holdings. The duration of the portfolio (the sensitivity of the portfolio's fair value to changes in the level of interest rates) is targeted to be within 20 percent of the duration of the Barclays Capital Universal Index.

In addition, the major sector allocations are limited to the following ranges: U.S treasuries and government agencies – 10 percent to 45 percent, credit bonds – 10 percent to 60 percent, asset backed securities – 0 percent to 10 percent, commercial mortgage-backed securities – 0 percent to 10 percent, and mortgage-backed securities – 5 percent to 45 percent.

Pension trust funds can be invested in any appropriate private equity investment opportunity that has the potential for returns superior to traditional investment opportunities and which is not prohibited by the WSIB's policies or by law. These investment types include venture capital investments, corporate finance, distressed, international and mezzanine investments. Private equity investments are made through limited partnership vehicles.

The portfolio is managed to meet or exceed the returns of the Russell 3000 (lagged by one quarter) plus 300 basis points. To meet the return and plan objectives, the private equity portfolio has diversified investments in companies in a variety of growth stages. The portfolio also includes a broad cross-section of opportunities in different industries and geographic regions.

The primary goal of the tangible asset portfolio is to generate a long-term, high quality, stable income stream. The secondary goal is to generate appreciation approximately commensurate with inflation. The structure of the investments are primarily targeted to be tangible asset operating companies providing the WSIB with governance provisions related to acquisition, dispositions, and ongoing operational decisions for annual capital expenditures. The tangible asset portfolio invests in a number of sectors, but the primary focus is infrastructure, timber, and natural resource rights (oil and natural gas).

The WSIB's current return objective for tangible assets calls for a target benchmark of 4 percent above the U.S. Consumer Price Index over a long-term investment horizon defined as at least five years.

The WSIB's real estate program is an externally managed pool of selected partnership investments, intended to provide alternative portfolio characteristics when compared to traditional stock and bond investments. The majority of the WSIB's partnerships invest in institutional-quality real estate assets that are leased to third parties. The combination of income generated from bond-like lease payments, coupled with the hard asset qualities of commercial real estate, combine to generate returns that are expected to fall between the return expectations for fixed income and equities over the long term. The real estate portfolio is managed to deliver risk-adjusted returns that are consistent with the WSIB's long-term return expectations for the asset class.

The WSIB's real estate partnerships typically invest in private real estate assets that are held for long-term income and appreciation. Many of the WSIB's investment partnerships do not involve co-investment with other financial entities, thereby providing the WSIB with control provisions related to transactions and ongoing operational decisions for annual capital expenditures.

Volatility in the real estate portfolio is minimized through a combination of factors. First, the majority of the WSIB's partners own real estate assets in a private investment form which are not subject to public market volatility. Secondly, real estate capital is diversified among a host of partners with varying investment styles. Thirdly, partnership assets are invested in numerous economic regions, including foreign markets, and in various property types. Finally, the WSIB's partners invest at different points within the properties' capital structure and life cycle.

The WSIB's current benchmark seeks to earn an 8 percent annual investment return over a rolling 10-year period.

The innovation portfolio investment strategy is to provide WSIB with the ability to invest in assets that fall outside of traditional asset classes and to provide the WSIB with comfort and demonstrated success before committing large dollar amounts to the strategy. The overall benchmark for the innovation portfolio is the weighted average of the underlying benchmark for each asset in the portfolio.

Currently, all innovation portfolio investment managers are investing in publicly traded common stock.

## 2. Unfunded Commitments

The WSIB has entered into a number of agreements that commit the pension trust funds, upon request, to make additional investment purchases up to predetermined amounts. As of June 30, 2010, the retirement funds had unfunded commitments of $7.6 billion, $7.4 billion and $482 million in private equity, real estate and tangible assets, respectively.

## 3. Securities Lending

State law and Board policy permit the pension trust funds to participate in securities lending programs to augment investment income. The WSIB has entered into an agreement with JPMorgan to act as agent for the WSIB in securities lending transactions. As JPMorgan is the custodian bank for the WSIB, it is counterparty to securities lending transactions.

The pension trust funds report securities lent (the underlying securities) as assets in the Statement of Net Assets. Cash received as collateral on securities lending transactions and investments made with that cash are reported as assets.

Securities received as collateral are reported as assets if the pension trust funds have the ability to pledge or sell them without a borrower default. Liabilities resulting from these transactions are also reported in the Statement of Net Assets. Securities lending transactions collateralized by securities that the pension trust funds do not have the ability to pledge or sell unless the borrower defaults are not reported as assets and liabilities.

Securities were loaned (consisting of fixed income and equities) and collateralized by the pension trust funds' agent with cash and U.S. government securities (exclusive of mortgage backed securities and letters of credit), and irrevocable letters of credit. When the loaned securities had collateral denominated in the same currency, the collateral requirement was 102 percent of the fair value, including accrued interest, of the securities loaned. All other securities were required to be collateralized at 105 percent of the fair value, including accrued interest, of the loaned securities.

The collateral held and fair value of securities on loan at June 30, 2010, were $4.0 billion and $3.9 billion respectively. At year-end, the amounts the pension trust funds owed the borrowers exceeded the amounts the borrowers owed pension trust funds, resulting in no credit risk exposure.

During Fiscal Year 2010, securities lending transactions could be terminated on demand by either the WSIB or the borrower. The weighted average maturity of loans for 2010 was 2.2 days.

Cash collateral was invested by the WSIB's agents in securities in the WSIB's separately managed short-term investment pool (average final maturity of 30 days). Because the securities lending agreements were terminable at will, their duration did not generally match the duration of the investments made with the cash collateral.

Non-cash collateral could not be pledged or sold absent borrower default. Accordingly, non-cash collateral held under securities lending contracts with a value of $304 million has not been included in the Statement of Net Assets. There are no restrictions on the amount of securities that can be lent.

Securities were lent with the agreement that they would be returned in the future for exchange of the collateral. JPMorgan indemnified the WSIB by agreeing to purchase replacement securities or return the cash collateral in the event a borrower failed to return the loaned securities or pay distributions thereon. JPMorgan's responsibilities included performing appropriate borrower and collateral investment credit analyses, demanding adequate types and levels of collateral, and complying with applicable federal regulations concerning securities lending.

During Fiscal Year 2010, there were no significant violations of legal or contractual provisions, or failures by any borrowers to return loaned securities or to pay distributions thereon. Further, the pension trust funds incurred no losses during Fiscal Year 2010 resulting from a default by either the borrowers or the securities lending agents.

## 4. Interest Rate Risk

Interest rate risk is the risk that changes in interest rates over time will adversely affect the fair value of an investment. Effective duration is the measure of a debt investment's exposure to fair value changes arising from changes in interest rates. Effective duration uses the present value of future cash flows, weighted for those flows as a percentage of the investment's full price.

Increases in prevailing interest rates generally translate into decreases in fair values of those investments, and decreases in interest rates result in increases in valuations.

The WSIB does not have a formal policy specifically for interest rate risk. The pension trust funds' fixed income investments are actively managed to exceed the return of the Barclays Capital Universal Index, with a duration that is not 20 percent higher or lower than the duration of the index.

As of June 30, 2010, the pension trust funds' duration was within the duration target of this index.

The following schedule provides information about the interest rate risks associated with the pension trust funds' investments as of June 30, 2010. The schedule displays various asset classes held by maturity in years and credit ratings. Residential mortgage backed, commercial mortgage backed, and asset backed securities are reported using the average life within the portfolio. The average life is a calculated estimate of the average time (in years) until maturity for these securities taking into account possible prepayments of principal. All other securities on this schedule are reported using the stated maturity date. Foreign corporate bonds and corporate equities are reported in U.S. dollar (USD) and non U.S. dollar (Non USD) denominations.

**Pension Trust Funds**
**June 30, 2010**
(expressed in thousands)

| | | Maturity | | | | |
|---|---|---|---|---|---|---|
| **Investment Type** | **Fair Value** | **Less than 1 Year** | **1-5 Years** | **6-10 Years** | **More than 10 Years** | **Credit Rating** |
| Asset backed securities | $ 188,397 | $ 19,141 | $ 155,122 | $ 7,499 | $ 6,635 | Multiple |
| Residential mortgage backed securities | 2,875,074 | 360,808 | 2,502,015 | 12,251 | - | Multiple |
| Commercial mortgage backed securities | 478,293 | 60,363 | 416,905 | 1,025 | - | Multiple |
| Corporate bonds - domestic | 1,624,171 | 15,092 | 450,788 | 982,961 | 175,330 | Multiple |
| Corporate bonds - foreign (USD) | 4,405,322 | 103,819 | 979,626 | 2,639,195 | 682,682 | Multiple |
| Corporate bonds - foreign (Non USD) | 666,549 | - | 242,745 | 307,068 | 116,736 | Multiple |
| U.S. government treasuries | 673,678 | - | 673,678 | - | - | Aaa |
| Treasury inflation protected securities | 847,259 | - | 847,259 | - | - | Aaa |
| | 11,758,743 | $ 559,223 | $ 6,268,138 | $ 3,949,999 | $ 981,383 | |
| Corporate stock (USD) | 659,330 | | | | | |
| Corporate stock (Non USD) | 7,504,394 | | | | | |
| Commingled equity index funds | 10,204,806 | | | | | |
| Alternative investments | 21,654,099 | | | | | |
| Liquidity | 1,061,657 | | | | | |
| Securities lending collateral | 3,667,615 | | | | | |
| **Total** | $ 56,510,644 | | | | | |

Investments with multiple credit ratings are presented using the Moody's rating scale as follows:

**Pension Trust Funds**
**Investments with Multiple Credit Ratings**
**June 30, 2010**
(expressed in thousands)

| | Investment Type | | | | | | |
|---|---|---|---|---|---|---|---|
| **Moody's Equivalent Credit Rating** | **Asset-Backed Securities** | **Residential Mortgage Backed Securities** | **Commercial Mortgage Backed Securities** | **Corporate Bonds - Domestic** | **Corporate Bonds -Foreign (USD)** | **Corporate Bonds - Foreign (Non USD)** | **Total** |
| Aaa | $ 146,601 | $ 2,816,711 | $ 385,755 | $ 102,049 | $ 27,344 | $ 511,086 | $ 3,989,546 |
| Aa1 | - | 3,997 | - | - | - | - | 3,997 |
| Aa2 | 531 | 8,077 | 52,032 | - | 186,560 | - | 247,200 |
| Aa3 | 6,978 | 3,535 | 40,506 | 143,150 | 252,738 | - | 446,907 |
| A1 | - | 2,864 | - | 112,531 | 492,134 | - | 607,529 |
| A2 | - | - | - | 226,212 | 163,997 | 788 | 390,997 |
| A3 | - | - | - | 71,017 | 364,398 | 29,214 | 464,629 |
| Baa1 | 3,116 | 4,582 | - | 389,580 | 419,845 | - | 817,123 |
| Baa2 | - | 2,733 | - | 367,526 | 851,575 | 26,834 | 1,248,668 |
| Baa3 and lower | 31,171 | 32,575 | - | 212,106 | 1,646,731 | 98,627 | 2,021,210 |
| **Total** | $ 188,397 | $ 2,875,074 | $ 478,293 | $ 1,624,171 | $ 4,405,322 | $ 666,549 | $ 10,237,806 |

## 5. Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Rated debt investments of the pension trust funds as of June 30, 2010, were rated by Moody's and/or an equivalent national rating organization.

**Concentration of Credit Risk.** Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer. The WSIB policy states no corporate fixed income issue shall exceed 3 percent of cost at the time of purchase or 6 percent of fair value thereafter of the fund, and no high yield issues shall exceed 1 percent of cost or 2 percent of fair value of the fund. There was no concentration of credit risk exceeding these policy guidelines as of June 30, 2010.

**Custodial Credit Risk.** Custodial credit risk is the risk that, in the event of a failure of the counterparty to a transaction, the pension trust funds would not be able to recover the value of investments that are in the possession of an outside party. The WSIB does not have a policy specifically for custodial credit risk. The WSIB mitigates custodial risk by having its investment securities held by its custodian. Also, investment securities are registered in the name of the WSIB for the benefit of the pension trust funds, excluding cash and cash equivalents and repurchase agreements held as securities lending collateral.

## 6. Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. The WSIB does not have a formal policy to limit foreign currency risk. The WSIB manages their exposure to fair value loss by requiring their international securities investment managers to maintain diversified portfolios by sector and by issuer to limit foreign currency and security risk.

The following schedule presents the exposure of pension fund investments to foreign currency risk. The schedule provides information on deposits and investments held in various foreign currencies, which are stated in U.S. dollars.

**Pension Trust Funds**
**Foreign Currency Risk**
**June 30, 2010**
(expressed in thousands)

| | Investment Type | | | | | |
|---|---|---|---|---|---|---|
| **Foreign Currency Denomination** | **Currency** | **Fixed Income** | **Equity** | **Private Equity** | **Real Estate** | **Total** |
| Australia-Dollar | $ 4,378 | $ 373,361 | $ 365,690 | $ - | $ 18,282 | $ 761,711 |
| Brazil-Real | 399 | 134,079 | 100,424 | - | - | 234,902 |
| Canada-Dollar | 1,858 | - | 453,623 | - | - | 455,481 |
| Denmark-Krone | 348 | - | 81,982 | - | - | 82,330 |
| E.M.U.-Euro | 41,010 | - | 2,006,480 | 1,575,005 | 120,529 | 3,743,024 |
| Hong Kong-Dollar | 1,165 | - | 332,591 | - | - | 333,756 |
| India-Rupee | 1,148 | - | 81,184 | - | - | 82,332 |
| Indonesia-Rupiah | 4 | 26,068 | 36,854 | - | - | 62,926 |
| Japan-Yen | 11,054 | - | 1,302,333 | - | - | 1,313,387 |
| Mexico-Peso | 338 | 29,214 | 36,480 | - | - | 66,032 |
| Norway-Krone | 1,169 | 43,247 | 72,110 | - | - | 116,526 |
| Poland-Zloty | 504 | - | 18,298 | - | - | 18,802 |
| Singapore-Dollar | 413 | - | 111,556 | - | - | 111,969 |
| South Africa-Rand | 113 | - | 97,343 | - | - | 97,456 |
| South Korea-Won | 392 | - | 116,472 | - | - | 116,864 |
| Sweden-Krona | 849 | - | 184,503 | 694 | - | 186,046 |
| Switzerland-Franc | 3,182 | - | 505,957 | - | - | 509,139 |
| Taiwan-Dollar | 11,533 | - | 106,170 | - | - | 117,703 |
| Turkey-Lira | 265 | 49,028 | 94,903 | - | - | 144,196 |
| United Kingdom-Pound | 3,556 | 788 | 1,274,108 | 9,486 | - | 1,287,938 |
| Other-Miscellaneous | 1,422 | 10,764 | 125,333 | - | - | 137,519 |
| **Total** | $ 85,100 | $ 666,549 | $ 7,504,394 | $ 1,585,185 | $ 138,811 | $ 9,980,039 |

## 7. Derivatives

Pension trust funds are authorized to utilize various derivative financial instruments, including mortgage-backed securities, financial futures, forward contracts, interest rate swaps, credit default swaps, equity swaps, and options. Derivative transactions involve, to varying degrees, market and credit risk. In connection with the international and domestic active equity strategy, at June 30, 2010, the pension trust funds held investments in financial futures, forward currency contracts and other derivative securities that are recorded at fair value with changes in value recognized in investment income in the Statement of Changes in Net Assets in the period of change.

Derivatives are generally used to achieve the desired market exposure of a security, index or currency, adjust portfolio duration, or rebalance the total portfolio to the target asset allocation. Derivative contracts are instruments that derive their value from underlying assets, indices, reference interest rates, or a combination of these factors. A derivative instrument could be a contract negotiated on behalf of the pension trust funds and a specific counterparty. This would typically be referred to as an "over the counter (OTC) contract" such as forward contracts and to be announced (TBA) securities. Alternatively, a derivative instrument, such as futures, could be listed and traded on an exchange and referred to as "exchange traded".

Inherent in the use of OTC derivatives, the pension trust funds are exposed to counterparty credit risk on all open OTC positions. Counterparty credit risk is the risk that a derivative counterparty may fail to meet its payment obligation under the derivative contract. As of June 30, 2010, the pension trust funds counterparty risk was not deemed to be significant, whether evaluating counterparty exposure outright or netting collateral against net asset positions on contracts with each counterparty.

Mortgage TBA's are used to achieve the desired market exposure of a security or asset class or adjust portfolio duration. A TBA is a contract for the purchase or sale of agency mortgage-backed securities to be delivered at a future agreed-upon date. TBA's carry future settlement risk due to the possibility of not receiving the asset or associated gains specified in the contract and such loss upon failure by counterparties to deliver under the contracts is not material at June 30, 2010.

Futures contracts are standardized, exchange-traded contracts to purchase or sell a specific financial instrument at a predetermined price. Gains and losses on futures contracts are settled daily based on a notional (underlying) principal value and do not involve an actual transfer of the specific instrument. The exchange assumes the risk that the counterparty will not pay and generally requires margin payments to minimize such risk. Futures are generally used to achieve the desired market exposure of a security or index or rebalance the total portfolio.

Forward currency contracts are agreements to exchange the currency of one country for the currency of another country at an agreed-upon price and settlement date. These forward commitments are not standardized and carry credit risk due to the possible nonperformance by one of the counterparties. The maximum potential loss is the aggregate face value in U.S. dollars at the time the contract was opened; however, the likelihood of such loss is remote. At June 30, 2010, the pension trust funds had outstanding forward currency contracts to purchase foreign currencies with a fair value of $1.6 billion and outstanding contracts to sell foreign currencies with a fair value of $1.6 billion. The net unrealized loss of $1.8 million is included in the Statement of Changes in Net Assets. The contracts have varying maturity dates ranging from July 1, 2010, to November 10, 2010.

At June 30, 2010, the pension trust funds' fixed income portfolio held derivative securities consisting of collateralized mortgage obligations with a fair value of $1.1 billion. Domestic and foreign passive equity index fund managers may also utilize various derivative securities to manage exposure to risk and increase portfolio returns. Information on the extent of use and holdings of derivative securities by passive equity index fund managers is unavailable.

Derivatives which are exchange traded are not subject to credit risk. The maximum loss that would be recognized at June 30, 2010, if all counterparties fail to perform as contracted is $1.8 million of unrealized gain on TBA securities. This maximum exposure is reduced by $1.8 million of unrealized losses on forward currency contracts, resulting in de minimus exposure to credit risk.

At June 30, 2010, the counterparties' credit ratings for forward currency contracts that are subject to credit risk had a credit rating of no less than A2 using the Moody's rating scale.

The following schedule presents the significant terms for derivatives held as investments by the WSIB.

**Pension Trust Funds**
**Derivative Investments**
**June 30, 2010**
(expressed in thousands)

| | Changes in Fair Value - Included in Investment Income (Loss) Amount | Fair Value - Investment Derivative Amount | Notional |
|---|---|---|---|
| **Futures Contracts:** | | | |
| Bond index futures | $ 4,952 | $ 4,952 | 4 |
| Equity index futures | 19,262 | (1,990) | 3 |
| **Total** | $ 24,214 | $ 2,962 | 7 |
| | | | |
| **To Be Announced (TBA) Securities:** | | | |
| **Total** | $ 1,810 | $ 257,135 | 242,000 |
| | | | |
| **Forward Currency Contracts:** | | | |
| Australia-Dollar | $ 2,177 | $ 1,791 | 61,633 |
| Canada-Dollar | 5,355 | (1,027) | 133,531 |
| Czech Republic-Koruna | 361 | (29) | (179,503) |
| Denmark-Krone | (56) | (44) | (35,714) |
| E.M.U.-Euro | (2,612) | (2,304) | (70,243) |
| Hong Kong-Dollar | (53) | (54) | (294,796) |
| Hungary-Forint | 675 | 409 | (920,416) |
| Israel-Shekel | - | - | 1,281 |
| Japan-Yen | (478) | 2,813 | 6,747,048 |
| Mexico-Peso | - | - | (2,323) |
| New Zealand-Dollar | 117 | (1) | (2) |
| Norway-Krone | 21 | 20 | (87,285) |
| Poland-Zloty | 2,242 | 479 | (17,930) |
| Singapore-Dollar | 4 | 1 | (2,189) |
| South Africa-Rand | (94) | (89) | (16,362) |
| Sweden-Krona | (3,090) | (2,606) | (442,845) |
| Switzerland-Franc | 34 | (150) | (3,234) |
| United Kingdom-Pound | (555) | (1,003) | 19,899 |
| United States-Dollar | - | - | (60,699) |
| **Total** | $ 4,048 | $ (1,794) | 4,829,851 |

## 8. Reverse Repurchase Agreements

State law permits the WSIB to enter into reverse repurchase agreements, that is, a sale of securities with a simultaneous agreement to repurchase them in the future at the same price plus a contract rate of interest. The fair value of the securities underlying reverse repurchase agreements normally exceeds the cash received, providing the dealers margin against a decline in fair value of the securities. If the dealers default on their obligations to resell these securities to the state or provide securities or cash of equal value, the WSIB would suffer an economic loss equal to the difference between the fair value plus accrued interest of the underlying securities and the agreement obligation, including accrued interest. There were no reverse repurchase agreements during the year and there were no liabilities outstanding as of June 30, 2010.

## C. INVESTMENTS – WORKERS' COMPENSATION FUND

### 1. Summary of Investment Policies

Under RCW 43.33A.030, trusteeship over the investment of the workers' compensation fund investments is vested in the voting members of the WSIB. The Legislature established a standard of care for investment of these funds in RCW 43.33A.140. Additionally, the WSIB must comply with other state laws, such as the Ethics in Public Service Act, chapter 42.52 RCW, as it makes investment decisions and seeks to meet its investment objectives.

In accordance with state laws, the workers' compensation fund investments are managed to limit fluctuations in the industrial insurance premiums, and subject to this purpose, achieve a maximum return at a prudent level of risk. Based on this requirement, the order of the objectives is:

- Maintain the solvency of the funds.
- Maintain premium rate stability.
- Ensure sufficient assets are available to fund the expected liability payments.
- Subject to those above, achieve a maximum return at a prudent level of risk.

**Eligible Investments.** Eligible investments are securities and deposits that are in accordance with the WSIB's investment policy and RCW 43.33A.110. Eligible investments include:

- U.S. Equities.
- International Equities.
- U.S. Treasuries and Government Agencies.
- Credit Bonds.
- Mortgage-Backed Securities rated investment grade, as defined by Barclays Capital Global Family of Fixed Income Indices.
- Asset-Backed Securities rated investment grade, as defined by Barclays Capital Global Family of Fixed Income Indices.
- Commercial Mortgage-Backed Securities rated investment grade, as defined by Barclays Capital Global Family of Fixed Income Indices.
- Investment Grade Non-U.S. Dollar Bonds.

**Investment Restrictions.** To meet stated objectives, investments of workers' compensation funds are subject to the following constraints:

- All assets under the management of the WSIB are to be invested to maximize return at a prudent level of risk in accordance with RCW 43.33A.110 and RCW 43.33A.140.
- Asset allocations are to be reviewed every three to four years or sooner if there are significant changes in funding levels or the liability durations.
- Assets are to be rebalanced across asset classes when the fair value of the assets falls outside the policy ranges. The timing of any rebalancing will be based on market opportunities, cash flows, and the consideration of transaction costs; therefore, they need not occur immediately.
- No corporate fixed income issue cost shall exceed 3 percent of the fund's fair value at the time of purchase, nor shall its fair value exceed 6 percent of the fund's fair value at any time.
- The benchmark and structure for U.S. equities will be the broad U.S. stock market as defined by the Dow Jones U.S. Total Stock Market Index. The benchmark and structure for international equities will be the Morgan Stanley Capital International All Country World Ex U.S. Investable Market Index (MSCI ACW Ex U.S. IMI). Both portfolios will be 100 percent passively managed in commingled index funds. The commingled funds may use futures for hedging or establishing a long-term position.
- Sector allocation for U.S. equities should be within a range of 55 percent to 65 percent. Allocation for international equities should be within a range of 35 percent to 45 percent.
- The fixed income portfolios' structure varies depending upon the required duration target. The duration targets are reviewed every three years, or sooner, if there are significant changes in the funding levels or the liability durations.
- Sector allocation of fixed income investments must be managed within the following prescribed ranges: U.S. Treasuries and government agencies – 5 percent to 25 percent, credit bonds – 20 percent to 70 percent, asset backed securities – 0 percent to 10 percent, commercial mortgage backed securities – 0 percent to 10 percent and mortgage backed securities – 0 percent to 25 percent. These targets are long-term in nature. Deviations may occur in the short-term as a result of interim market conditions. However, if a range is

exceeded the portfolios must be rebalanced as soon as it is practical to the target allocations.

- Total holdings of below investment grade credit bonds (as defined by Barclays Capital Global Family of Fixed Income Indices) should not exceed 5 percent of total fixed income holdings.

## 2. Securities Lending

State law and Board policy permit the workers' compensation fund to participate in securities lending programs to augment investment income. The WSIB has entered into an agreement with JPMorgan to act as agent for the workers' compensation fund in securities lending transactions. As JPMorgan is the custodian bank for the workers' compensation fund, it is counterparty to securities lending transactions.

The workers' compensation fund reports securities lent (the underlying securities) as assets in the Statement of Net Assets. Cash received as collateral on securities lending transactions and investments made with that cash are reported as assets. Securities received as collateral are reported as assets if the workers' compensation fund has the ability to pledge or sell them without a borrower default. Liabilities resulting from these transactions are also reported in the Statement of Net Assets. Securities lending transactions collateralized by securities that the workers' compensation fund does not have the ability to pledge or sell unless the borrower defaults are not reported as assets and liabilities.

Fixed income securities were loaned and collateralized by the WSIB's agent with cash and U.S. government securities (exclusive of mortgage backed securities and letters of credit), and irrevocable letters of credit. When the loaned securities had collateral denominated in the same currency, the collateral requirement was 102 percent of the fair value, including accrued interest, of the securities loaned. All other securities were required to be collateralized at 105 percent of the fair value, including accrued interest, of the loaned securities. The collateral held and fair value of securities on loan at June 30, 2010 was $2.6 billion and $2.5 billion, respectively. As of June 30, 2010, the amounts the workers' compensation fund owed the borrowers exceeded the amounts the borrowers owed the workers' compensation fund resulting in no credit risk exposure to borrowers.

During Fiscal Year 2010, securities lending transactions could be terminated on demand by either the workers' compensation fund or the borrower. The weighted average maturity of loans was 2.2 days.

Cash collateral was invested by the workers' compensation fund in the WSIB's short-term investment pool (average final maturity of 30 days). Because the securities lending agreements were terminable at will, their duration did not generally match the duration of the investments made with the cash collateral. Non-cash collateral could not be pledged or sold absent borrower default. Accordingly, non-cash collateral held under securities lending contracts with a value of $197 million have not been included in the Statement of Net Assets. There are no restrictions on the amount of securities that can be lent.

Securities were lent with the agreement that they would be returned in the future for exchange of the collateral. JPMorgan indemnified the workers' compensation fund by agreeing to purchase replacement securities or return the cash collateral in the event a borrower failed to return the loaned securities or pay distributions thereon. JPMorgan's responsibilities included performing appropriate borrower and collateral investment credit analyses, demanding adequate types and levels of collateral, and complying with applicable federal regulations concerning securities lending.

During Fiscal Year 2010, there were no significant violations of legal or contractual provisions, no failures by any borrowers to return loaned securities or to pay distributions thereon. Further, the workers' compensation fund incurred no losses during Fiscal Year 2010 resulting from a default by either the borrowers or the securities lending agents.

## 3. Interest Rate Risk

Interest rate risk is the risk that changes in interest rates over time will adversely affect the fair value of an investment. Effective duration is the measure of a debt investment's exposure to fair value changes arising from changes in interest rates. Effective duration uses the present value of cash flows, weighted for those flows as a percentage of the investment's full price. Increases in prevailing interest rates generally translate into decreases in fair values of those investments. The WSIB does not have a formal policy specifically for interest rate risk.

The workers' compensation fixed income investments are actively managed to exceed the return of the Comparable Market Index, with volatility as measured by duration to be similar to or less than the index. As of June 30, 2010, the durations of the various fixed income classes were within the duration targets of the Comparable Market Index.

The workers' compensation fund investments include both U.S. agencies and corporate debt variable-rate securities, most of which reset periodically to the market interest rate. Because these securities frequently re-price to prevailing market rates, interest rate risk is substantially reduced at each periodic reset date.

The following schedule provides information about the interest rate risks associated with the workers' compensation fund investments as of June 30, 2010. The schedule displays various asset classes held by maturity in years, effective durations, and credit ratings. Residential mortgage backed, commercial mortgage backed, and asset backed securities are reported using the average life within the portfolio. The average life is a calculated estimate of the average time (in years) until maturity for these securities taking into account possible prepayments of principal. All other securities on the schedule are reported using the stated maturity date.

**Workers' Compensation Fund**
**June 30, 2010**
(expressed in thousands)

| | | Maturity | | | | |
|---|---|---|---|---|---|---|
| **Investment Type** | **Fair Value** | **Less than 1 Year** | **1-5 Years** | **6-10 Years** | **More than 10 Years** | **Credit Rating** |
| Residential mortgage backed securities | $ 1,747,601 | $ 23,935 | $ 889,862 | $ 732,074 | $ 101,730 | Aaa |
| Commercial mortgage backed securities | 554,452 | 56,490 | 351,054 | 146,125 | 783 | Multiple |
| Corporate bonds-domestic | 3,081,812 | 125,039 | 680,589 | 1,016,490 | 1,259,694 | Multiple |
| Corporate bonds-foreign (USD) | 2,753,892 | 118,326 | 824,662 | 1,029,889 | 781,015 | Multiple |
| Government securities-domestic: | | | | | | |
| U.S. government treasuries | 605,292 | - | 605,292 | - | - | Aaa |
| U.S. treasury inflation protected securities | 1,606,498 | 89,365 | 246,323 | 704,527 | 566,283 | Aaa |
| | 10,349,547 | $ 413,155 | $ 3,597,782 | $ 3,629,105 | $ 2,709,505 | |
| Commingled index funds-domestic | 775,728 | | | | | |
| Commingled index funds-foreign | 548,241 | | | | | |
| Money market funds | 220,860 | | | | | |
| Securities lending collateral | 2,377,679 | | | | | |
| **Total** | $ 14,272,055 | | | | | |

Investments with multiple credit ratings are presented using the Moody's rating scale as follows:

**Workers' Compensation Fund**
**Investments with Multiple Credit Ratings**
**June 30, 2010**
(expressed in thousands)

| | Investment Type | | | |
|---|---|---|---|---|
| **Moody's Equivalent Credit Rating** | **Commercial Mortgage Backed Securities** | **Corporate Bonds - Domestic** | **Corporate Bonds-Foreign (USD)** | **Total** |
| Aaa | $ 485,785 | $ 116,121 | $ 375,071 | $ 976,977 |
| Aa2 | 28,161 | - | 245,091 | 273,252 |
| Aa3 | 40,506 | 364,886 | 316,124 | 721,516 |
| A1 | - | 307,416 | 329,248 | 636,664 |
| A2 | - | 786,111 | 84,836 | 870,947 |
| A3 | - | 290,627 | 240,360 | 530,987 |
| Baa1 | - | 510,699 | 288,580 | 799,279 |
| Baa2 | - | 513,004 | 522,373 | 1,035,377 |
| Baa3 and lower | - | 169,785 | 300,244 | 470,029 |
| Other | - | 23,163 | 51,965 | 75,128 |
| **Total** | $ 554,452 | $ 3,081,812 | $ 2,753,892 | $ 6,390,156 |

### 4. Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The rated debt investments of the workers' compensation fund as of June 30, 2010, were rated by Moody's and/or an equivalent national rating organization.

**Concentration of Credit Risk.** Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer. The workers' compensation fund policy states no corporate fixed income issue's cost shall exceed 3 percent of the fund's fair value at the time of purchase, nor shall its fair value exceed 6 percent of the fund's fair value at any time. There was no concentration of credit risk as of June 30, 2010.

**Custodial Credit Risk.** Custodial credit risk is the risk that, in the event of a failure of the counterparty to a transaction, the workers' compensation fund would not be able to recover the value of investments that are in the possession of an outside party. The workers' compensation fund does not have a policy specifically for custodial credit risk. The WSIB mitigates custodial credit risk by having its investment securities held by its custodian. Also, investment securities are registered in the name of the WSIB for the benefit of the workers' compensation fund, excluding cash and cash equivalents and repurchase agreements held as securities lending collateral.

### 5. Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. The workers' compensation fund does not have a formal policy to limit foreign currency risk. The workers' compensation funds had $548 million invested in an international commingled equity index fund. As such, no currency denomination risk is presented.

### 6. Derivatives

The workers' compensation fund is authorized to utilize various derivative financial instruments, including mortgage-backed securities, financial futures, forward contracts, interest rate and equity swaps, and options to manage its exposure to fluctuations in interest and currency rates while increasing portfolio returns. Derivative transactions involve, to varying degrees, market and credit risk. The workers' compensation fund mitigates market risks arising from derivative transactions by requiring collateral in cash and investments to be maintained equal to the securities positions outstanding, and thereby prohibiting the use of leverage or speculation. Credit risks arising from derivative transactions are mitigated by selecting and monitoring creditworthy counterparties and collateral issuers.

Consistent with the workers' compensation fund's authority to invest in derivatives, international active equity managers may make limited investments in financial futures, forward contracts or other derivative securities to manage exposure to currency rate risk and equitize excess cash holdings. No such derivative securities were held as of June 30, 2010.

Domestic and foreign passive equity index fund managers may also utilize various derivative securities to manage exposure to risk and increase portfolio returns. Information on the extent of use and holdings of derivative securities by passive equity index fund managers is unavailable. At June 30, 2010, the only derivative securities held directly by the workers' compensation fund were collateralized mortgage obligations (CMOs) of $1.7 billion.

### 7. Reverse Repurchase Agreements

State law permits the WSIB to enter into reverse repurchase agreements, that is, a sale of securities with a simultaneous agreement to repurchase them in the future at the same price plus a contract rate of interest. The fair value of the securities underlying reverse repurchase agreements normally exceeds the cash received, providing the dealers margin against a decline in fair value of the securities. If the dealers default on their obligations to resell these securities to the state or provide securities or cash of equal value, the WSIB would suffer an economic loss equal to the difference between the fair value plus accrued interest of the underlying securities and the agreement obligation, including accrued interest. There were no reverse repurchase agreements during Fiscal Year 2010 and there were no liabilities outstanding as of June 30, 2010.

## D. INVESTMENTS – LOCAL GOVERNMENT INVESTMENT POOL (LGIP)

### 1. Summary of Investment Policies

The LGIP is managed and operated by the Office of the State Treasurer (OST). The State Finance Committee is the administrator of the statute that created the pool and adopts appropriate rules. The OST is responsible for establishing the investment policy for the pool and reviews it annually. Any proposed changes are reviewed by the LGIP Advisory Committee. The terms of the policy are designed to ensure the safety and liquidity of the funds deposited in the LGIP.

The LGIP is comparable to a Rule 2a-7 money market fund recognized by the Securities and Exchange Commission (17CFR.270.2a-7). Rule 2a-7 funds are limited to high quality obligations with limited maximum and average maturities, the effect of which is to minimize

both market and credit risk. As such, investments are reported at amortized cost (which approximates fair value).

**Investment Objectives.** The objectives of the LGIP investment policy, in priority order, are safety, liquidity, and return on investment. To provide for the safety and liquidity of funds deposited in the LGIP, the state treasurer and designated investment officers shall:

- Adhere to all restrictions on the investment of funds established by law and by the policy.
- Limit the purchase of investments in securities so that the weighted average maturity of the portfolio, as defined in Section VI of the policy, does not exceed 90 days.
- Limit the purchase of investments to securities that have a maximum final maturity of 397 days, with the exceptions listed in section VI of the policy.
- Limit the purchase of investments in securities other than those issued by the U.S. government or its agencies.
- Prepare regular reports of portfolio activity.

The primary objective of safety will be measured in cash, as opposed to accounting terms, where different, and in terms of the portfolio, as a whole, as opposed to the terms of any individual transaction. This means, for example, that a single transaction that generated an accounting loss but actually increased the amount of cash received in the portfolio would be considered to have increased capital, and not decreased it. Within the restrictions necessary to ensure the safety and liquidity of funds, the investment portfolio of the LGIP will be structured to attain a market rate of return throughout an economic cycle.

**Eligible Investments.** Eligible investments are only those securities and deposits authorized by statute (Chapters 39.58, 39.59, 43.84.080 and 43.250 RCW). Eligible investments include:

- Obligations of the U.S. government.
- Obligations of U.S. government agencies, or of corporations wholly owned by the U.S. government.
- Obligations of government sponsored corporations that are, or may become eligible as collateral for advances to member banks as determined by the board of governors of the Federal Reserve.
- Banker's acceptances purchased on the secondary market rated with the highest short-term credit rating of any two Nationally Recognized Statistical Rating Organizations (NRSROs), at the time of purchase. If the banker's acceptance is rated by more than two NRSROs, it must have the highest rating from all of the organizations.
- Commercial paper provided that the OST adheres with policies and procedures of the WSIB regarding commercial paper (RCW 43.84.080(7)).
- Certificates of deposit with financial institutions qualified by the Washington Public Deposit Protection Commission.
- Obligations of the state of Washington or its political sub-divisions.

**Investment Restrictions.** To provide for the safety and liquidity of LGIP Funds, the investment portfolio will be subject to the following restrictions:

- All money market securities are required to be rated A-1 by Standard and Poor's Corporation and P-1 by Moody's Investors Services, Inc.
- Investments are restricted to fixed rate securities that mature in 397 days or less, and floating and variable rate securities that mature in 762 days or less.
- The weighted average maturity of the portfolio may not exceed 90 days.
- Cash generated through securities lending or reverse repurchase agreement transactions will not increase the dollar amount of specified investment types beyond stated limits.

## 2. Securities Lending

The LGIP investment policy requires that any securities on loan be made available by the lending agent for next day liquidity at the option of the LGIP. During Fiscal Year 2010, the LGIP had no credit risk exposure to borrowers because the amounts owed to the borrowers exceeded the amounts the borrowers owed the LGIP. Furthermore, the contract requires the lending agent to indemnify the LGIP if the borrowers fail to return the securities (and if collateral is inadequate to replace the securities lent) or if the borrower fails to pay the LGIP for income distribution by the securities' issuers while the securities are on loan.

The LGIP cannot pledge or sell collateral securities received unless the borrower defaults. The LGIP investment policy limits the amount of reverse repurchase agreements and securities lending to 30 percent of the total portfolio. There were neither violations of legal or contractual provisions nor any losses resulting from a default of a borrower or lending agent during the year.

State statutes permit the LGIP to lend its securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. The LGIP, which has contracted with a lending agent to lend securities in the LGIP, earns a fee for this activity. The lending agent lends securities and receives collateral, which can be in the form of cash or other securities. The collateral, which must be valued at 102 percent of the fair value of the loaned securities, is priced daily and, if necessary, action is taken to maintain the collateralization level at 102 percent.

The cash is invested by the lending agent in repurchase agreements or money market instruments, in accordance with investment guidelines approved by the LGIP. The securities held as collateral and the securities underlying the cash collateral are held by the LGIP's custodian. There were no securities on loan as of June 30, 2010.

## 3. Interest Rate Risk

Interest rate risk is the risk that changes in interest rates of debt instruments will adversely affect the fair value of an investment.

The portfolio is managed in a manner consistent with the Securities and Exchange Commission's Rule 2a-7 of the Investment Company Act of 1940, i.e., money market funds. Much of the Rule 2a-7 investment guidelines are directed towards limiting interest rate risk, in order to maintain a stable net asset value.

The LGIP policy places a 90-day maximum on the weighted average maturity. Further, the maximum maturity of any security will not exceed 397 days, except securities utilized in repurchase agreements and U.S.

Agency floating or variable rate notes may have a maximum maturity of 762 days, provided that they have reset dates within one year and which on any reset date can reasonably be expected to have a market value that approximates its amortized cost.

As of June 30, 2010, the LGIP had a weighted average maturity of 49 days.

The following schedule presents the LGIP investments by type and provides information about the interest rate risks associated with the LGIP investments as of June 30, 2010.

**Local Government Investment Pool (LGIP)**
**June 30, 2010**
(expressed in thousands)

| | | Maturity | |
|---|---|---|---|
| **Investment Type** | **Fair Value** | **Less than 1 Year** | **1-5 Years** |
| U.S. government obligations | $ 449,640 | $ 449,640 | $ - |
| U.S. agency obligations | 5,082,699 | 4,142,790 | 939,909 |
| Repurchase agreements | 2,600,000 | 2,600,000 | - |
| Certificates of deposit | 38,000 | 38,000 | - |
| Interest bearing bank accounts | 826,328 | 826,328 | - |
| **Total** | $ 8,996,667 | $ 8,056,758 | $ 939,909 |

## 4. Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The LGIP investment policy limits the types of securities available for investment to obligations of the U.S. government or its agencies, obligations of government-sponsored corporations, banker's acceptances, commercial paper, deposits with qualified public depositaries, or obligations of the state of Washington or its political subdivisions.

Banker's acceptances and commercial paper must be rated with the highest short-term credit rating of any two Nationally Recognized Statistical Rating Organizations (NRSROs) at the time of purchase. The LGIP currently does not have any banker's acceptances, commercial paper, or municipal bonds in its portfolio.

**Custodial Credit Risk.** Custodial credit risk is the risk that, in the event of a failure of the counter party, the LGIP will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party. The LGIP investment policy requires that securities purchased by the office be held by the master custodian, acting as an independent third party, in its safekeeping or trust department. Securities utilized in repurchase agreements are subject to additional restrictions. These restrictions are designed to limit the LGIP's exposure to risk and insure the safety of the investment. All securities utilized in repurchase agreements were rated AAA. The market value of securities utilized in repurchase agreements must be at least 102 percent of the value of the repurchase agreement.

**Concentration of Credit Risk.** Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. The LGIP mitigates concentration of credit risk by limiting the percentage of the portfolio invested with any one issuer.

With the exception of U.S. Treasury and U.S. Agency securities, the OST mitigates concentration of credit risk by limiting the purchase of securities of any one issuer to no more than 5 percent of the portfolio. As of June 30, 2010, U.S. Treasury securities comprised 5.0 percent of the total portfolio. U.S. Agency securities comprised 56.5 percent of the total portfolio, including Federal Home Loan Mortgage Corporation (11.7 percent), Federal Home Loan Bank (8.3 percent), Federal National Mortgage Association (20.2 percent), and Federal Farm Credit Bank (16.3 percent).

### 5. Foreign Currency Risk. None.

### 6. Derivatives

A derivative is a futures, forward, swap, or option contract, or other financial instrument with similar characteristics. The LGIP did not own, buy, or sell derivatives during the fiscal year.

### 7. Reverse Repurchase Agreements

State law also permits the LGIP to enter into reverse repurchase agreements, which are, by contract, sales of securities with a simultaneous agreement to repurchase them in the future at the same price plus a contract rate of interest.

The fair value of the securities pledged as collateral by the LGIP underlying the reverse repurchase agreements normally exceeds the cash received, providing the dealers a margin against a decline in the fair value of the securities.

If the dealers default on their obligations to resell these securities to the LGIP or to provide equal value in securities or cash, the LGIP would suffer an economic loss equal to the difference between the fair value plus accrued interest of the underlying securities and the agreement obligation, including accrued interest. During the fiscal year there was no credit risk for the LGIP due to the fair value plus accrued interest of the underlying securities being less than the fair value plus accrued interest of the reinvested cash. On June 30, 2010, there were no obligations under reverse repurchase agreements.

The market value, plus accrued income, of mortgage-backed securities utilized in repurchase agreements with more than seven days remaining until maturity will be 105 percent of the value of the repurchase agreement. The market value, plus accrued income, of securities utilized in all other repurchase agreements will be 102 percent of the value of the repurchase agreement.

The securities utilized in repurchase agreements are priced daily and held by the LGIP's custodian in the state's name. Collateralized Mortgage Obligations (CMO) utilized in repurchase agreements must pass the Federal Financial Institutions Examination Council (FFIEC) test, or not exceed a volatility rating of V-5 by Fitch Investor Services, or a similar rating of a nationally recognized rating agency. As of June 30, 2010, repurchase agreements totaled $2.6 billion.

## E. INVESTMENTS – HIGHER EDUCATION SPECIAL REVENUE AND ENDOWMENT FUNDS

### 1. Summary of Investment Policies

The investments of the University of Washington represent 74 percent of the total investments in Higher Education Special Revenue and Endowment Funds.

The Board of Regents of the University of Washington is responsible for the management of the University's investments. The Board establishes investment policy, which is carried out by the Chief Investment Officer.

The University of Washington Investment Committee (UWINCO) comprised of Board members and investment professionals advises on matters relating to the management of the University's investment portfolios.

The majority of the University's investments are insured, registered, and held by the University's custodial bank as an agent for the University. Investments not held by the custodian include lent securities, mutual funds, venture capital, private equity, distressed, marketable alternatives, mortgages, real estate, and miscellaneous investments.

The University combines most short-term cash balances in the Invested Funds Pool. At June 30, 2010, the Invested Funds Pool totaled $1.1 billion. The fund also owns units in the Consolidated Endowment Fund valued at $354.9 million on June 30, 2010.

By University policy, departments with qualifying funds in the Invested Funds Pool receive distributions based on their average balances and on the type of balance. Campus depositors received 2 percent in Fiscal Year 2010. Endowment operating and gift accounts received 3 percent in Fiscal Year 2010. The difference between the actual earnings of the Invested Funds Pool and the calculated distributions is used to support activities benefiting all University departments.

The majority of the endowed funds are invested in a pooled fund called the Consolidated Endowment Fund (CEF). Individual endowments purchase units in the pool on the basis of a per unit valuation of the CEF at fair value on the last business day of the calendar quarter. Income is distributed based on the number of units held.

During Fiscal Year 2009, in light of the 2008-2009 financial crises and the decline in the CEF market value, the Board of Regents implemented an interim spending policy. Under the interim policy, year-over-year CEF distributions decreased from the Fiscal Year 2008 level by 25 percent in Fiscal Years 2009 and 2010.

At their October 21, 2010 meeting, the Board of Regents adopted a new spending policy for the CEF replacing the interim spending policy. Under the new policy, quarterly distributions to programs will equal 4 percent of a five-year rolling average. The new policy is effective with the December 2010 quarterly distributions with the five year averaging period implemented incrementally. The administrative fee of 1 percent supporting campus-wide fundraising and stewardship activities and offsetting the internal cost of managing endowment assets continues but will now be based on a five year average value consistent with the basis for program distributions.

The University records its permanent endowments at the lower of original gift value or current market value in the Restricted Nonexpendable Net Assets category. Of the total $1.1 billion permanent endowment funds (at fair value) as of June 30, 2010, the aggregate amount of the deficiencies where the fair value of the assets is less than the original gifts is $53.3 million at June 30, 2010.

Funds in irrevocable trusts managed by trustees other than the University are not reported in the financial statements. The fair value of these funds was $45.6 million at June 30, 2010. Income received from these trusts which is included in investment income, was $2.2 million for the year ended June 30, 2010.

Net appreciation (depreciation) in the fair value of investments includes both realized and unrealized gains and losses on investments. The University realized net gains of $138 million in 2010 from the sale of investments. The calculation of realized gains and losses is independent of the net appreciation of the fair value of investments. Realized gains and losses on investments that have been held in more than one fiscal year and are sold in the current year, include the net appreciation of these investments reported in the prior year(s).

The net (depreciation) appreciation in the fair value of investments during the year ended June 30, 2010 was $223.8 million.

The following schedule presents the fair value of the University of Washington's investments by type at June 30, 2010:

**University of Washington**
**June 30, 2010**
(expressed in thousands)

| Investment Type | Fair Value |
|---|---|
| Cash equivalents | $ 337,842 |
| Domestic fixed income | 1,105,961 |
| Foreign fixed income | 18,909 |
| Domestic equity | 421,489 |
| Foreign equity | 479,014 |
| Non-marketable alternatives | 407,847 |
| Absolute return | 376,730 |
| Real estate | 9,737 |
| Miscellaneous | 4,471 |
| **Total** | $ 3,162,000 |

## 2. Funding Commitments

The University enters into contracts with investment managers to fund alternate investments. As of June 30, 2010, the University had outstanding commitments to fund alternative investments in the amount of $215.3 million.

## 3. Securities Lending

The University's investment policies permit it to lend its securities to broker dealers and other entities. Due to market conditions, the University terminated this program in September 2008, and as of June 30, 2010 the University has no securities on loan.

## 4. Interest Rate Risk

The University manages interest rate risk through its investment policies and the investment guidelines established with each manager. Each fixed income manager is assigned a maximum boundary for duration as compared to the manager's relevant benchmark index. The goal is to allow ample freedom for the manager to perform, while controlling the interest rate risk in the portfolio. Modified duration, which estimates the sensitivity of a bond's price to interest rate changes, is based on a calculation entitled Macaulay duration.

Macaulay is an accepted calculation developed for a portfolio of bonds assembled to fund a fixed liability. Macaulay duration is calculated as follows: sum of discounted time-weighted cash flows divided by the bond price. Modified duration is calculated using the following formula: Macaulay duration divided by (one plus yield-to-maturity divided by the number of coupon payments per year).

The Interest Rate Risk Schedule presents the modified duration of the University's investments for which duration is measured. Duration figures at June 30, 2010, exclude $60.4 million of fixed-income securities held outside the CEF and the Invested Funds Pool. These amounts, which in total makeup 1.9 percent of the University's investments, are not included in the duration figures below.

**University of Washington**
**Interest Rate Risk**
**Duration as of June 30, 2010**
(expressed in thousands, modified duration in years)

| | Consolidated Endowment Fund | | Invested Funds Pool | |
|---|---|---|---|---|
| | Asset Value | Duration | Asset Value | Duration |
| **Domestic Fixed Income** | | | | |
| Asset backed securities | $ 28,716 | 2.11 | $ 33,336 | 1.87 |
| Cash equivalents | 54,932 | 1.59 | 252,486 | 0.02 |
| Corporate bonds | 84,748 | 2.84 | 37,797 | 1.55 |
| Government and agencies | 143,467 | 1.99 | 692,698 | 3.26 |
| Mortgage related | 16,052 | 2.53 | 45,230 | 2.91 |
| Subtotal Domestic Fixed Income | 327,915 | 2.18 | 1,061,547 | 2.37 |
| **International Fixed Income** | | | | |
| Cash equivalents | 3 | - | - | - |
| International fixed | 5,620 | 3.89 | 7,215 | 2.21 |
| Subtotal International Fixed Income | 5,623 | 3.89 | 7,215 | 2.21 |
| **Total** | $ 333,538 | 2.14 | $ 1,068,762 | 2.36 |

## 5. Credit Risk

Credit risk is the risk that the issuer or other counterparty to a financial instrument will not fulfill its obligations, or negative perceptions of the issuer's ability to make these payments will cause prices to decline.

The University investment policies limit fixed income exposure to investment grade assets. The investment policy for the University's invested funds cash pool requires each manager to maintain an average quality rating of "AA" as issued by a nationally recognized rating organization. The invested funds liquidity pool requires each manager to maintain an average quality rating of "A" and to hold 50 percent of their portfolios in government and government agency issues.

The investment policy for the CEF reflects its long-term nature by specifying average quality rating levels by individual manager, but still restricting investments to investment grade credits.

**Custodial Credit Risk.** Custodial credit risk is the risk that, in the event of a failure of the counterparty to a transaction, the University will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party. The University does not have a formal policy regarding custodial credit risk. However, all University assets are held in the name of the University of Washington and are not subject to custodial credit risk.

**Concentration of Credit Risk.** Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer. The University mitigates concentration of credit risk by maintaining a portfolio of investment grade assets and by the due diligence of each manager.

The following schedule provides information on investments subject to credit risk.

**University of Washington**
**Investments Credit Rating**
**As of June 30, 2010**
(expressed in thousands)

| Credit Rating | Consolidated Endowment Fund Asset Value | Invested Funds Asset Value |
|---|---|---|
| AAA | $ 81,363 | $ 179,212 |
| AA | 38,473 | 20,504 |
| A | 30,979 | 5,062 |
| BBB | 8,384 | 2,930 |
| BB | 188 | 1,514 |
| B | 449 | 1,564 |
| CCC | 485 | 7,936 |
| CC | 203 | 1,612 |
| Not rated | 13,254 | 9,419 |
| **Total** | $ 173,778 | $ 229,753 |

## 6. Foreign Currency Risk

The University's investment policies permit investments in international equity and other asset classes that can include foreign currency exposure. The University also enters into foreign currency forward contracts, futures contracts, and options to manage the foreign currency exposure.

At June 30, 2010, the University had net outstanding forward commitments to sell foreign currency with a total fair value of $4.7 million, which equals 0.15 percent of the total portfolio.

The following schedule details the market value of foreign denominated securities by currency type in the CEF.

**University of Washington**
**Consolidated Endowment Fund**
**Foreign Currency Risk**
**June 30, 2010**
(expressed in thousands)

| Foreign Currency | Foreign Fixed Income | Foreign Equity | Alternatives and Other Investments |
|---|---|---|---|
| Australia-Dollar | $ - | $ 7,159 | $ 4,436 |
| Brazil-Real | - | 43,553 | 306 |
| Britain-Pound | 4,134 | 34,199 | 16,970 |
| Canada-Dollar | 1,224 | 9,023 | 15,353 |
| China-Renminbi | - | 43,613 | 7,511 |
| E.M.U.-Euro | 1,681 | 52,258 | 59,432 |
| India-Rupee | - | 30,865 | 22,170 |
| Hong Kong-Dollar | - | 31,300 | 4,804 |
| Japan-Yen | - | 40,845 | 13,273 |
| Russia-Ruble | - | 27,717 | 2,070 |
| Singapore-Dollar | - | 10,641 | 1,946 |
| South Korea-Won | - | 18,897 | 867 |
| Switzerland-Franc | 1,600 | 18,971 | 3,431 |
| Taiwan-Dollar | 3 | 19,845 | 2,648 |
| Other (less than 2% total exposure) | - | 77,545 | 20,999 |
| **Total** | $ 8,642 | $ 466,431 | $ 176,216 |

### 7. Derivatives

The University's investments include certain derivative instruments and structured notes that derive their value from a security, asset, or index. Under the University's investment policies and guidelines derivatives may be used to manage the aggregate portfolio risk/return profile. This includes the use of swaps, options, futures and other derivative products to adjust exposures, to equitize cash, or to rebalance across asset classes.

The University's participation in investment derivative activity in total return swaps during Fiscal Year 2010 is summarized in the following schedule. The values are based on quoted market prices.

Credit exposure represents exposure to counterparties relating to financial instruments where gains exceed collateral held by the University or losses are less than the collateral posted by the University. There was no credit exposure as of June 30, 2010.

The University did not invest in derivatives for hedging purposes during Fiscal Year 2010. Details on foreign currency derivatives are disclosed under Foreign Currency Risk.

**University of Washington**
**Derivative Investments**
**June 30, 2010**
(expressed in thousands)

| | Change in Fair Value | | Fair Value | | | |
|---|---|---|---|---|---|---|
| **Derivative Instrument** | **Classification** | **Amount** | **Classification** | **Amount** | **Notional** | **Counterparty Credit Rating** |
| Equity swap | Investment revenue (loss) | $ (5,110) | Investment | $ (5,110) | $ 92,940 | A-1 |

### 8. Reverse Repurchase Agreements – None.

## F. INVESTMENTS - OFFICE OF THE STATE TREASURER CASH MANAGEMENT ACCOUNT

### 1. Summary of Investment Policies

The Office of the State Treasurer (OST) operates the state's Cash Management Account for investing Treasury/Trust Funds in excess of daily requirements.

The overall objective of the OST investment policy is to construct, from eligible investments noted below, an investment portfolio that is optimal or efficient. An optimal or efficient portfolio is one that provides the greatest expected return for a given expected level of risk, or the lowest expected risk for a given expected return.

The emphasis on "expected" is to recognize that investment decisions are made under conditions of risk and uncertainty. Neither the actual risk nor return of any investment decision is known with certainty at the time the decision is made.

**Eligible Investments.** Eligible investments are only those securities and deposits authorized by statute (Chapters 39.58, 39.59, 43.84.080 and 43.250 RCW). Eligible investments include:

- Obligations of the U.S. government.
- Obligations of U.S. government agencies, or of corporations wholly owned by the U.S. government.
- Obligations of government sponsored corporations that are or may become eligible as collateral for advances to member banks as determined by the board of governors of the Federal Reserve.
- Banker's acceptances purchased on the secondary market rated with the highest short-term credit rating of any two Nationally Recognized Statistical Rating Organizations (NRSROs), at the time of purchase. If the banker's acceptance is rated by more than two NRSROs, it must have the highest rating from all of the organizations.
- Commercial paper, provided that the OST adheres with policies and procedures of the State Investment Board regarding commercial paper (RCW 43.84.080(7).
- Deposits with financial institutions qualified by the Washington Public Deposit Protection Commission.
- Local Government Investment Pool, for proceeds of bonds or other debt obligations, when the investments are made in order to comply with the Internal Revenue Code of 1986, as amended.
- Obligations of the state of Washington or its political sub-divisions.

**Investment Restrictions.** To provide for the safety and liquidity of Treasury/Trust Funds, the Cash Management Account investment portfolio is subject to the following restrictions:

- The final maturity of any security will not exceed ten years.
- Purchase of collateralized mortgage obligations (CMO) requires prior approval from the treasurer or assistant treasurer; CMO securities must pass the Federal Institutions Examination Council (FFIEC) test, or not exceed a volatility rating of V-5 by Fitch Investor Services, or a similar rating of a nationally recognized rating agency.
- The allocation to investments subject to high sensitivity or reduced marketability will not exceed 15 percent of the daily balance of the portfolio.

Additionally, investments in non-government securities, excluding collateral of repurchase agreements, must fall within prescribed limits.

## 2. Securities Lending

State statutes permit the OST to lend its securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. The OST, which has contracted with a lending agent to lend securities, earns a fee for this activity.

The OST lending agent lends U.S. government and U.S. agency securities and receives collateral, which can be in the form of cash or other securities. The collateral, which must be valued at 102 percent of the fair value of the loaned securities, is priced daily and, if necessary, action is taken to maintain the collateralization level at 102 percent.

The cash is invested by the lending agent in repurchase agreements or money market instruments, in accordance with investment guidelines approved by the OST.

The securities held as collateral and the securities underlying the cash collateral are held by the custodian.

The contract with the lending agent requires them to indemnify the OST if the borrowers fail to return the securities (and if the collateral is inadequate to replace the securities lent) or if the borrower fails to pay the OST for income distribution by the securities' issuers while the securities are on loan. The OST cannot pledge or sell collateral securities received unless the borrower defaults. At June 30, 2010, there were no securities on loan.

The OST investment policy requires that any securities on loan be made available by the lending agent for next day liquidity at the option of the OST. During Fiscal Year 2010, the OST had no credit risk exposure to borrowers because the amounts owed to the borrowers exceeded the amounts the borrowers owed the OST.

There were no violations of legal or contractual provisions or any losses resulting from a default of a borrower or lending agent during the fiscal year.

## 3. Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the value of the investment. The Treasury/Trust investments are separated into portfolios with objectives based primarily on liquidity needs.

The OST's investment policy limits the weighted average maturity of its investments based on cash flow expectations. Policy also directs due diligence to be exercised with timely reporting of material deviation from expectations and actions taken to control adverse developments as may be possible.

The following schedule presents the fair value of the OST's investments by type at June 30, 2010.

**Office of the State Treasurer (OST)**
**Cash Management Account**
**June 30, 2010**
(expressed in thousands)

| | | Maturity | |
|---|---|---|---|
| **Investment Type** | **Fair Value** | **Less than 1 Year** | **1-5 Years** |
| U.S. agency obligations | $ 1,047,761 | $ 141,034 | $ 906,727 |
| U.S. government obligations | 248,657 | - | 248,657 |
| Repurchase agreements | 2,400,000 | 2,400,000 | - |
| Certificates of deposit | 187,177 | 187,177 | - |
| Interest bearing bank accounts | 231,296 | 231,296 | - |
| **Total** | $ 4,114,891 | $ 2,959,507 | $ 1,155,384 |

### 4. Credit Risk

The OST limits credit risk by adhering to the OST investment policy which restricts the types of investments the OST can participate in, such as: U.S. government and agency securities, banker's acceptances, commercial paper, and deposits with qualified public depositaries.

**Custodial Credit Risk.** The custodial credit risk for investments is the risk that, in the event of a failure of the counterparty, a government will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party. The OST investment policy requires that securities purchased by the office to be held by the master custodian, acting as an independent third party, in its safekeeping or trust department. Securities utilized in repurchase agreements are subject to additional restrictions. These restrictions are designed to limit the OST's exposure to risk and insure the safety of the investment.

**Concentration of Credit Risk.** Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. For non-governmental securities, the OST limits its exposure to concentration of credit risk by restricting the amount of investments to no more than 5 percent of the portfolio to any single issuer. During Fiscal Year 2010, the non-governmental securities of a single issuer held by the Cash Management Account did not exceed 5 percent of the total portfolio.

### 5. Foreign Currency Risk - None.

### 6. Derivatives - None.

### 7. Reverse Repurchase Agreements

State law also permits the OST to enter into reverse repurchase agreements, which are, by contract, sales of securities with a simultaneous agreement to repurchase them in the future at the same price plus a contract rate of interest. The fair value of the securities pledged as collateral by the OST underlying the reverse repurchase agreements normally exceeds the cash received, providing the dealers a margin against a decline in the fair value of the securities. If the dealers default on their obligations to resell these securities to the OST or to provide equal value in securities or cash, the OST would suffer an economic loss equal to the differences between the fair value plus accrued interest of the underlying securities and the agreement obligation, including accrued interest. The OST investment policy limits the amount of reverse repurchase agreements to 30 percent of the total portfolio.

The market value, plus accrued income, of mortgage-backed securities utilized in repurchase agreements with more than seven days remaining until maturity will be 105 percent of the value of the repurchase agreement.

The market value, plus accrued income, of securities utilized in all other repurchase agreements will be 102 percent of the value of the repurchase agreement. The securities utilized in repurchase agreements are priced daily and held by the Treasury/Trust custodian in the state's name. Collateralized Mortgage Obligations (CMOs) utilized in repurchase agreements must pass the Federal Financial Institutions Examination Council (FFIEC) test, or not exceed a volatility rating of V-5 by Fitch Investor Services, or a similar rating of a nationally recognized rating agency. There were no reverse repurchase agreements as of June 30, 2010.

# Note 4
## Receivables and Deferred/Unearned Revenues

### A. GOVERNMENTAL FUNDS

#### Taxes Receivable

Taxes receivable at June 30, 2010, consisted of the following (expressed in thousands):

| Taxes Receivable | General | Higher Education Special Revenue | Motor Vehicle Special Revenue | Higher Education Endowment | Nonmajor Governmental Funds | Total |
|---|---|---|---|---|---|---|
| Property | $ 965,191 | $ - | $ - | $ - | $ 221 | $ 965,412 |
| Sales | 1,293,167 | 3,534 | - | - | 2,090 | 1,298,791 |
| Business and occupation | 490,627 | - | - | - | - | 490,627 |
| Estate | 4,574 | 17,635 | - | - | - | 22,209 |
| Fuel | - | - | 111,238 | - | 2 | 111,240 |
| Other | 2,925 | - | - | - | 132 | 3,057 |
| Subtotals | 2,756,484 | 21,169 | 111,238 | - | 2,445 | 2,891,336 |
| Less: Allowance for uncollectible receivables | 53,237 | - | 702 | - | 22 | 53,961 |
| **Total Taxes Receivable** | $ 2,703,247 | $ 21,169 | $ 110,536 | $ - | $ 2,423 | $ 2,837,375 |

#### Other Receivables

Other receivables at June 30, 2010, consisted of the following (expressed in thousands):

| Other Receivables | General | Higher Education Special Revenue | Motor Vehicle Special Revenue | Higher Education Endowment | Nonmajor Governmental Funds | Total |
|---|---|---|---|---|---|---|
| Public assistance (1) | $ 1,132,069 | $ - | $ - | $ - | $ - | $ 1,132,069 |
| Accounts receivable | 63,603 | 175,815 | 25,119 | 860 | 43,053 | 308,450 |
| Interest | - | 6,744 | - | 4,160 | 3,956 | 14,860 |
| Loans (2) | 2,887 | 132,964 | - | - | 374,497 | 510,348 |
| Long-term contracts (3) | 1,449 | - | - | 8,639 | 53,633 | 63,721 |
| Miscellaneous | 30,045 | 44,368 | 46,858 | 9,437 | 192,631 | 323,339 |
| Subtotals | 1,230,053 | 359,891 | 71,977 | 23,096 | 667,770 | 2,352,787 |
| Less: Allowance for uncollectible receivables | 941,862 | 21,216 | 8,417 | 13 | 14,200 | 985,708 |
| **Total Other Receivables** | $ 288,191 | $ 338,675 | $ 63,560 | $ 23,083 | $ 653,570 | $ 1,367,079 |

Notes:

(1) Public assistance receivables mainly represent amounts owed the state as a part of the Support Enforcement Program at the Department of Social and Health Services for the amounts due from persons required to pay support for individuals currently on state assistance, and have a low realization expectation. Accordingly, the receivable is offset by a large allowance for uncollectible receivables.

(2) Significant long-term portions of loans receivable include $108 million in the Higher Education Special Revenue Fund for student loans and $364 million in Nonmajor Governmental Funds for low income housing, public works, and economic development/revitalization loans.

(3) Long-term contracts in Nonmajor Governmental Funds are for timber sales contracts.

### Deferred Revenue

Deferred revenues at June 30, 2010, consisted of the following (expressed in thousands):

| Deferred Revenue | General | Higher Education Special Revenue | Motor Vehicle Special Revenue | Higher Education Endowment | Nonmajor Governmental Funds | Total |
|---|---|---|---|---|---|---|
| Property taxes | $ 946,756 | $ - | $ - | $ - | $ 78 | $ 946,834 |
| Other taxes | 334,959 | 14,638 | - | - | 106 | 349,703 |
| Timber sales | 1,448 | - | - | 8,640 | 53,633 | 63,721 |
| Charges for services | 17,457 | 196,087 | 13,629 | 359 | 35,593 | 263,125 |
| Donable goods | 636 | - | - | - | 4,218 | 4,854 |
| Grants and donations | 27,927 | 759 | 137 | - | 16,963 | 45,786 |
| Loan program | 1,694 | - | - | - | 677,336 | 679,030 |
| Miscellaneous | 30,665 | 5,390 | 11,208 | - | 20,945 | 68,208 |
| **Total Deferred Revenue** | $ 1,361,542 | $ 216,874 | $ 24,974 | $ 8,999 | $ 808,872 | $ 2,421,261 |

## B. PROPRIETARY FUNDS

### Taxes Receivable

Taxes receivable at June 30, 2010, consisted of $9.8 million in liquor taxes reported in Nonmajor Enterprise Funds.

### Other Receivables

Other receivables at June 30, 2010, consisted of the following (expressed in thousands):

| | Business-Type Activities Enterprise Funds | | | | | Governmental Activities |
|---|---|---|---|---|---|---|
| Other Receivables | Workers' Compensation | Unemployment Compensation | Higher Education Student Services | Nonmajor Enterprise Funds | Total | Internal Service Funds |
| Accounts receivable | $ 110,950 | $ - | $ 228,926 | $ 22,420 | $ 362,296 | $ 4,167 |
| Interest | 102,318 | - | 530 | 4,434 | 107,282 | 14 |
| Loans | - | - | 5 | - | 5 | - |
| Miscellaneous | 484,946 | 651,415 | 17,273 | 1,423 | 1,155,057 | 3,021 |
| Subtotals | 698,214 | 651,415 | 246,734 | 28,277 | 1,624,640 | 7,202 |
| Less: Allowance for uncollectible receivables | 109,583 | 130,290 | 87,581 | 164 | 327,618 | 229 |
| **Total Other Receivables** | $ 588,631 | $ 521,125 | $ 159,153 | $ 28,113 | $ 1,297,022 | $ 6,973 |

### Unearned Revenue

Unearned revenue at June 30, 2010, consisted of the following (expressed in thousands):

| | Business-Type Activities Enterprise Funds | | | | | Governmental Activities |
|---|---|---|---|---|---|---|
| Unearned Revenue | Workers' Compensation | Unemployment Compensation | Higher Education Student Services | Nonmajor Enterprise Funds | Total | Internal Service Funds |
| Charges for services | $ 3 | $ - | $ 33,563 | $ 9 | $ 33,575 | $ 726 |
| Other taxes | 87 | - | - | 43 | 130 | - |
| Miscellaneous | 7,906 | - | 723 | - | 8,629 | - |
| **Total Unearned Revenue** | $ 7,996 | $ - | $ 34,286 | $ 52 | $ 42,334 | $ 726 |

## C. FIDUCIARY FUNDS

### Other Receivables

Other receivables at June 30, 2010, consisted of the following (expressed in thousands):

| Other Receivables | Local Government Investment Pool | Agency Funds |
|---|---|---|
| Interest | $ 1,542 | $ 10,423 |
| Other | - | 2,109 |
| Subtotals | 1,542 | 12,532 |
| Less: Allowance for uncollectible receivables | - | 1,919 |
| **Total Other Receivables** | $ 1,542 | $ 10,613 |

### Unearned Revenue

Unearned revenue at June 30, 2010, consisted of $1.1 million for service credit restorations reported in Pension and Other Employee Benefit Funds.

# Note 5
## Interfund Balances and Transfers

### A. INTERFUND BALANCES

Interfund balances as reported in the financial statements at June 30, 2010, consisted of the following (expressed in thousands):

| | Due From | | | | |
|---|---|---|---|---|---|
| Due To | General | Higher Education Special Revenue | Motor Vehicle Special Revenue | Higher Education Endowment | Nonmajor Governmental Funds |
| General | $ - | $ 25,495 | $ 2,462 | $ - | $ 31,402 |
| Higher Educ. Special Revenue | 45,313 | - | 608 | 12 | 15,335 |
| Motor Vehicle Special Revenue | 947 | 5 | - | - | 8,742 |
| Higher Education Endowment | - | - | - | - | - |
| Nonmajor Governmental Funds | 792,139 | 1,192 | 2,790 | 2,139 | 91,085 |
| Workers' Compensation | 72 | 41 | - | - | 1 |
| Unemployment Compensation | 2,421 | 1,861 | 359 | - | 572 |
| Higher Educ. Student Services | 10,407 | 8,718 | 52 | - | 6,704 |
| Nonmajor Enterprise Funds | 5,383 | 86 | 706 | - | 533 |
| Internal Service Funds | 21,301 | 55,570 | 8,883 | - | 11,211 |
| Fiduciary Funds | 9 | - | - | - | - |
| **Totals** | $ 877,992 | $ 92,968 | $ 15,860 | $ 2,151 | $ 165,585 |

Interfund balances are expected to be paid within one year from the date of the financial statements. These balances resulted from the time lag between the dates that (1) interfund goods and services were provided and when the payments occurred, and (2) interfund transfers were accrued and when the liquidations occurred.

In addition to the interfund balances noted in the schedule above, there are interfund balances of $1.6 million within the state's Pension Trust Funds.

| Workers' Compensation | Unemployment Compensation | Higher Education Student Services | Nonmajor Enterprise Funds | Internal Service Funds | Fiduciary Funds | Totals |
|---|---|---|---|---|---|---|
| $ 196 | $ - | $ 1 | $ 14,967 | $ 1,562 | $ - | $ 76,085 |
| 318 | - | 65,054 | 2 | 28,530 | - | 155,172 |
| 2 | - | - | 3 | 1,733 | - | 11,432 |
| - | - | - | - | - | 28 | 28 |
| 106 | 1,120 | 110,352 | 10,791 | 1,185 | 21 | 1,012,920 |
| - | - | - | - | 400 | 14 | 528 |
| 607 | - | 64 | 182 | 273 | - | 6,339 |
| 226 | - | - | - | 3 | 328 | 26,438 |
| 31 | - | 116 | 1,090 | 868 | 3 | 8,816 |
| 3,828 | - | 53 | 1,202 | 67,903 | 1,425 | 171,376 |
| 20 | - | - | 253 | 12 | - | 294 |
| $ 5,334 | $ 1,120 | $ 175,640 | $ 28,490 | $ 102,469 | $ 1,819 | $ 1,469,428 |

## B. INTERFUND TRANSFERS

Interfund transfers as reported in the financial statements for the year ended June 30, 2010, consisted of the following (expressed in thousands):

| | Transferred To | | | | |
|---|---|---|---|---|---|
| **Transferred From** | **General** | **Higher Education Special Revenue** | **Motor Vehicle Special Revenue** | **Higher Education Endowment** | **Nonmajor Governmental Funds** |
| General | $ - | $ 203,231 | $ - | $ 499 | $ 1,344,063 |
| Higher Educ. Special Revenue | 55,936 | - | - | 3,511 | 60,717 |
| Motor Vehicle Special Revenue | - | - | - | - | 341,733 |
| Higher Education Endowment | - | 103 | - | - | 100,718 |
| Nonmajor Governmental Funds | 1,000,061 | - | 24,228 | 2,177 | 278,568 |
| Workers' Compensation | - | - | - | - | - |
| Higher Educ. Student Services | - | 1,423 | - | - | 18,731 |
| Nonmajor Enterprise Funds | 125,499 | 13,100 | - | - | 118,346 |
| Internal Service Funds | 5,632 | 2 | - | 547 | - |
| **Totals** | $ 1,187,128 | $ 217,859 | $ 24,228 | $ 6,734 | $ 2,262,876 |

* Transfers of $3 million of capital assets were made from Proprietary Funds to Governmental Funds.

Except as noted below, transfers are used to 1) move revenues from the fund that statute requires to collect them to the fund that statute requires to expend them, 2) move receipts designated for debt service from the funds collecting the receipts to the debt service fund as debt service payments become due, 3) move unrestricted revenues collected in the General Fund to finance various programs accounted for in other funds in accordance with budgetary authorizations, 4) move profits from the Liquor Fund and the Lottery Fund as required by law, and 5) transfer amounts to and from the General Fund as required by law.

Pursuant to Engrossed Substitute Senate Bill 5073, effective July 1, 2009, six accounts, previously reported within Nonmajor Governmental funds were consolidated into the General Fund. Because of the close relationship between these accounts and the General Fund, they were consolidated to improve budget transparency. The consolidation resulted in an $89 million transfer into the General Fund.

On June 30, 2010, $119 million was transferred to the Budget Stabilization Account (BSA) in accordance with the provisions of the Constitution. The BSA is reported within Nonmajor Governmental Funds. The Constitution details a limited number of circumstances under which funds can be appropriated from the BSA, one of which is a favorable vote of at least three-fifths of the members of each house of the Legislature. During Fiscal Year 2010, Engrossed Substitute House Bill 6444 authorized the transfer of $45 million from the BSA to the General Fund.

Engrossed Substitute House Bill 6444 also required transfer of $829 million from other funds to the General Fund to address revenue shortfalls.

In addition to the transfers noted in the schedule above, there were transfers of $20 million within the state's Pension Trust Funds.

| Workers' Compensation | Higher Education Student Services | Nonmajor Enterprise Funds | Internal Service Funds | Capital Asset Transfers * | Totals |
|---|---|---|---|---|---|
| $ - | $ - | $ 7,750 | $ 10,855 | $ - | $ 1,566,398 |
| - | 11,561 | - | 4,810 | - | 136,535 |
| - | - | - | - | - | 341,733 |
| - | 27 | - | - | - | 100,848 |
| - | 1,329 | 15 | - | - | 1,306,378 |
| - | - | - | - | - | - |
| - | - | - | 459 | 2,957 | 23,570 |
| - | - | 19,224 | - | 21 | 276,190 |
| 840 | 6,952 | 147 | 9,186 | - | 23,306 |
| $ 840 | $ 19,869 | $ 27,136 | $ 25,310 | $ 2,978 | $ 3,774,958 |

# Note 6
## Capital Assets

Capital assets at June 30, 2010, are reported by the state of Washington within Governmental Activities and Business-Type Activities, as applicable.

### A. GOVERNMENTAL CAPITAL ASSETS

The following is a summary of governmental capital asset activity for the year ended June 30, 2010 (expressed in thousands):

| Capital Assets | Balances July 1, 2009 | Additions | Deletions | Balances June 30, 2010 |
|---|---|---|---|---|
| **Capital assets, not being depreciated:** | | | | |
| Land | $ 1,130,220 | $ 125,548 | $ (77,004) | $ 1,178,764 |
| Transportation infrastructure | 18,214,619 | 1,430,009 | (18) | 19,644,610 |
| Intangible assets- indefinite lives | - | 2,552 | - | 2,552 |
| Art collections, library reserves, and museum and historical collections | 113,899 | 2,107 | (5,523) | 110,483 |
| Construction in progress | 1,184,622 | 537,752 | (856,986) | 865,388 |
| **Total capital assets, not being depreciated** | 20,643,360 | | | 21,801,797 |
| **Capital assets, being depreciated:** | | | | |
| Buildings | 9,704,545 | 709,337 | (12,559) | 10,401,323 |
| Accumulated depreciation | (3,231,393) | (251,880) | 7,825 | (3,475,448) |
| Net buildings | 6,473,152 | | | 6,925,875 |
| Other improvements | 1,141,720 | 97,236 | (4,027) | 1,234,929 |
| Accumulated depreciation | (472,828) | (43,370) | 2,011 | (514,187) |
| Net other improvements | 668,892 | | | 720,742 |
| Furnishings, equipment and intangible assets | 3,790,589 | 242,377 | (130,301) | 3,902,665 |
| Accumulated depreciation | (2,413,843) | (251,292) | 124,730 | (2,540,405) |
| Net furnishings, equipment and intangible assets | 1,376,746 | | | 1,362,260 |
| Infrastructure | 735,070 | 71,395 | - | 806,465 |
| Accumulated depreciation | (339,283) | (30,933) | - | (370,216) |
| Net infrastructure | 395,787 | | | 436,249 |
| **Total capital assets, being depreciated, net** | 8,914,577 | | | 9,445,126 |
| **Governmental Activities Capital Assets, Net** | $ 29,557,937 | | | $ 31,246,923 |

## B. BUSINESS-TYPE CAPITAL ASSETS

The following is a summary of business-type capital asset activity for the year ended June 30, 2010 (expressed in thousands):

| Capital Assets | Balances July 1, 2009 | Additions | Deletions | Balances June 30, 2010 |
|---|---|---|---|---|
| **Capital assets, not being depreciated:** | | | | |
| Land | $ 142,347 | $ 369 | $ - | $ 142,716 |
| Art collections | 35 | - | - | 35 |
| Construction in progress | 153,466 | 184,484 | (126,933) | 211,017 |
| **Total capital assets, not being depreciated** | 295,848 | | | 353,768 |
| **Capital assets, being depreciated:** | | | | |
| Buildings | 2,226,911 | 185,160 | (8,250) | 2,403,821 |
| Accumulated depreciation | (660,759) | (73,539) | 1,863 | (732,435) |
| Net buildings | 1,566,152 | | | 1,671,386 |
| Other improvements | 91,290 | 6,523 | - | 97,813 |
| Accumulated depreciation | (23,747) | (3,419) | - | (27,166) |
| Net other improvements | 67,543 | | | 70,647 |
| Furnishings, equipment and intangible assets | 507,256 | 40,393 | (13,023) | 534,626 |
| Accumulated depreciation | (357,499) | (47,115) | 12,150 | (392,464) |
| Net furnishings, equipment and intangible assets | 149,757 | | | 142,162 |
| Infrastructure | 34,995 | 1,234 | (6,119) | 30,110 |
| Accumulated depreciation | (15,364) | (1,264) | 2,795 | (13,833) |
| Net infrastructure | 19,631 | | | 16,277 |
| **Total capital assets, being depreciated, net** | 1,803,083 | | | 1,900,472 |
| **Business-Type Activities Capital Assets, Net** | $ 2,098,931 | | | $ 2,254,240 |

## C. DEPRECIATION

Depreciation expense for the year ended June 30, 2010, was charged by the primary government as follows (expressed in thousands):

| | Amount |
|---|---|
| **Governmental Activities:** | |
| General government | $ 61,189 |
| Education - elementary and secondary (K-12) | 3,335 |
| Education - higher education | 319,554 |
| Human services | 22,875 |
| Adult corrections | 39,616 |
| Natural resources and recreation | 39,734 |
| Transportation | 91,172 |
| **Total Depreciation Expense - Governmental Activities*** | $ 577,475 |
| **Business-Type Activities:** | |
| Workers' compensation | $ 7,991 |
| Unemployment compensation | - |
| Higher education student services | 101,021 |
| Other | 16,325 |
| **Total Depreciation Expense - Business-Type Activities** | $ 125,337 |

*Includes $69 million internal service fund depreciation that was allocated to functions as a part of the net internal service fund activity.

## D. CONSTRUCTION IN PROGRESS

Major construction commitments of the state at June 30, 2010, are as follows (expressed in thousands):

| Agency / Project Commitments | Construction In Progress June 30, 2010 | Remaining Project Commitments |
|---|---|---|
| **Department of General Administration:** | | |
| O'Brien building improvement, Transportation building improvements and other projects | $ 33,510 | $ 44,179 |
| **Department of Labor and Industries:** | | |
| Early Claims Solution software and Detecting Unregistered Employers software | 7,443 | 13,405 |
| **Department of Social and Health Services:** | | |
| State hospital and juvenile rehab construction and renovations, and other projects | 48,755 | 4,641 |
| **Department of Veterans Affairs:** | | |
| Veterans Cemetery and other facility rehabilitation projects | 8,519 | 1,438 |
| **Department of Corrections:** | | |
| Correctional centers construction, improvements, and other projects | 68,846 | 380,464 |
| **Department of Transportation:** | | |
| State highway office and maintenance facilities, and ferry vessels and terminals | 216,480 | 189,213 |
| Transportation infrastructure | - | 3,654,122 |
| **Parks and Recreation Commission:** | | |
| Cama Beach dining hall and Rasar Group camp development | 3,722 | 1,946 |
| **Department of Fish and Wildlife:** | | |
| Skookumchuck Hatchery renovation, Deschutes Watershed center, and other projects | 12,340 | 13,151 |
| **Employment Security Department:** | | |
| Next Generation Taxis Systemp project | 14,848 | 43,610 |
| **State Convention and Trade Center:** | | |
| MOHAI property | 50,034 | 7,966 |
| **Higher Education Facilities:** | | |
| University of Washington | 280,521 | 263,779 |
| Washington State University | 29,585 | 277,147 |
| Eastern Washington University | 7,417 | 2,694 |
| Central Washington University | 11,773 | 58,410 |
| The Evergreen State College | 17,051 | 4,880 |
| Western Washington University | 42,880 | 43,886 |
| Community and Technical Colleges | 218,504 | 333,859 |
| **Other agencies miscellaneous projects** | 4,177 | 7,497 |
| **Total Construction in Progress** | $ 1,076,405 | $ 5,346,287 |

# Note 7
## Long-Term Liabilities

### A. BONDS PAYABLE

Bonds payable at June 30, 2010, are reported by the state of Washington within governmental activities and business-type activities, as applicable.

The State Constitution and enabling statutes authorize the incurrence of state general obligation debt, to which the state's full faith, credit, and taxing power are pledged, either by the State Legislature or by a body designated by statute (presently the State Finance Committee).

Legislative authorization arises from:

- An affirmative vote of 60 percent of the members of each house of the Legislature, without voter approval, in which case the amount of such debt is generally subject to the constitutional debt limitation described below;

- When authorized by law for a distinct work or object and approved by a majority of the voters voting thereon at a general election, or a special election called for that purpose, in which case the amount of the debt so approved is not subject to the constitutional debt limitations described below;

- By the State Finance Committee without limitation as to amount, and without approval of the Legislature or approval of the voters.

The State Finance Committee debt authorization does not require voter approval; however, it is limited to providing for: (1) meeting temporary deficiencies of the state treasury if such debt is discharged within 12 months of the date of incurrence and is incurred only to provide for appropriations already made by the Legislature; or (2) refunding of outstanding obligations of the state.

#### Legal Debt Limitation

The State Constitution limits the amount of state debt that may be incurred by restricting the amount of general state revenues which may be allocated to pay principal and interest on debt subject to these limitations. More specifically, the constitutional debt limitation prohibits the issuance of new debt if it would cause the maximum annual debt service on all thereafter outstanding debt to exceed 9 percent of the arithmetic mean of general state revenues for the preceding three fiscal years. This limitation restricts the incurrence of new debt and not the amount of debt service that may be paid by the state in future years.

The State Constitution and current statues require the State Treasurer to certify the debt service limitation for each fiscal year. In accordance with these provisions, the debt service limitation for Fiscal Year 2010 is $1.1 billion.

This computation excludes specific bond issues and types, which are not secured by general state revenues. Of the $16.6 billion general obligation bond debt outstanding at June 30, 2010, $10.2 billion is subject to the limitation.

Based on the debt limitation calculation, the debt service requirements as of June 30, 2010, did not exceed the authorized debt service limitation.

For further information on the debt limit refer to the Certification of the Debt Limitation of the State of Washington available from the Office of the State Treasurer at: http://www.tre.wa.gov/documents/debt_cdl2010.pdf, or to the Statistical Section of this report.

#### Authorized But Unissued

The state had a total of $9.5 billion in general obligation bonds authorized but unissued as of June 30, 2010, for the purpose of capital construction and transportation projects throughout the state.

#### Interest Rates

Interest rates on fixed rate general obligation bonds ranged from 1.15 to 7.25 percent. Variable rate demand obligations (VRDO) of $131.4 million as of June 30, 2010, are remarketed on a weekly basis. Interest rates on revenue bonds range from 2.50 to 7.40 percent.

### Debt Service Requirements to Maturity

#### General Obligations Bonds

General obligation bonds have been authorized and issued primarily to provide funds for:

- Acquisition and construction of state and common school capital facilities;
- Transportation construction and improvement projects;
- Assistance to local governments for public works capital projects; and
- Refunding of general obligation bonds outstanding.

Outstanding general obligations bonds are presented in the Washington State Treasurer's Annual Report for 2010. A copy of the report is available from the Office of the State Treasurer, PO Box 40200, Olympia, Washington, 98504-0200, phone number (360) 902-9000 or TTY (360) 902-8963, or by visiting their website at: http://www.tre.wa.gov/aboutUs/publications/annualReports.shtml.

Total debt service requirements to maturity for general obligation bonds as of June 30, 2010, are as follows (expressed in thousands):

| | Governmental Activities | | Business-Type Activities | | Totals | |
|---|---|---|---|---|---|---|
| **General Obligation Bonds** | **Principal** | **Interest** | **Principal** | **Interest** | **Principal** | **Interest** |
| **By Fiscal Year:** | | | | | | |
| 2011 | $ 622,283 | $ 786,377 | $ 8,196 | $ 4,140 | $ 630,479 | $ 790,517 |
| 2012 | 619,785 | 780,244 | 7,484 | 3,767 | 627,269 | 784,011 |
| 2013 | 648,907 | 748,645 | 7,081 | 3,480 | 655,988 | 752,125 |
| 2014 | 683,842 | 719,232 | 3,805 | 553 | 687,647 | 719,785 |
| 2015 | 715,165 | 696,972 | 4,030 | 341 | 719,195 | 697,313 |
| 2016-2020 | 3,895,221 | 3,087,521 | 29,297 | 56,404 | 3,924,518 | 3,143,925 |
| 2021-2025 | 3,664,484 | 2,126,573 | - | - | 3,664,484 | 2,126,573 |
| 2026-2030 | 3,287,523 | 1,307,698 | - | - | 3,287,523 | 1,307,698 |
| 2031-2035 | 1,907,150 | 341,308 | - | - | 1,907,150 | 341,308 |
| 2036-2045 | 495,698 | 76,581 | - | - | 495,698 | 76,581 |
| **Total Debt Service Requirements** | $ 16,540,058 | $ 10,671,151 | $ 59,893 | $ 68,685 | $ 16,599,951 | $ 10,739,836 |

## Revenue Bonds

Revenue bonds are authorized under current state statutes, which provide for the issuance of bonds that are not supported, or not intended to be supported, by the full faith and credit of the state.

The University of Washington issues general revenue bonds that are payable from general revenues, including student tuition and fees, grant indirect cost recovery, sales and services revenue, and investment income. General revenue bonds outstanding as of June 30, 2010, include $141.7 million in governmental activities and $631.6 million in business-type activities.

The remainder of the state's revenue bonds pledge income derived from acquired or constructed assets for retirement of the debt and payment of the related interest.

Total debt service requirements for revenue bonds to maturity as of June 30, 2010, are as follows (expressed in thousands):

| | Governmental Activities | | Business-Type Activities | | Totals | |
|---|---|---|---|---|---|---|
| **Revenue Bonds** | **Principal** | **Interest** | **Principal** | **Interest** | **Principal** | **Interest** |
| **By Fiscal Year:** | | | | | | |
| 2011 | $ 24,132 | $ 40,519 | $ 40,106 | $ 49,672 | $ 64,238 | $ 90,191 |
| 2012 | 22,145 | 39,417 | 30,221 | 48,517 | 52,366 | 87,934 |
| 2013 | 8,210 | 38,321 | 31,960 | 47,183 | 40,170 | 85,504 |
| 2014 | 20,961 | 37,949 | 33,023 | 45,689 | 53,984 | 83,638 |
| 2015 | 17,330 | 36,757 | 35,535 | 44,585 | 52,865 | 81,342 |
| 2016-2020 | 131,688 | 164,030 | 188,102 | 196,490 | 319,790 | 360,520 |
| 2021-2025 | 154,204 | 124,779 | 189,131 | 152,451 | 343,335 | 277,230 |
| 2026-2030 | 190,138 | 77,508 | 161,029 | 107,885 | 351,167 | 185,393 |
| 2031-2035 | 87,274 | 23,545 | 125,397 | 65,869 | 212,671 | 89,414 |
| 2036-2040 | 86,916 | 8,410 | 249,441 | 24,664 | 336,357 | 33,074 |
| **Total Debt Service Requirements** | $ 742,998 | $ 591,235 | $ 1,083,945 | $ 783,005 | $ 1,826,943 | $ 1,374,240 |

Governmental activities include revenue bonds outstanding at June 30, 2010, of $422.9 million issued by the Tobacco Settlement Authority (TSA), which is a blended component unit of the state. In November 2002, the TSA issued $517 million in bonds and transferred $450 million to the state to be used for increased health care, long-term care, and other programs.

These bonds do not constitute either a legal or moral obligation of the state, nor does the state pledge its full faith, credit, or taxing power for payment of these bonds. The bonds are obligations of the TSA and are secured solely by the TSA's right to receive 29.2 percent of the state's tobacco settlement revenues, restricted investments of the TSA, undistributed TSA bond proceeds, and the earnings thereon held under the indenture authorizing the bonds. Total principal and interest remaining on the bonds is $800.6 million, payable through 2032. For the current year, pledged revenue and debt service were $44.1 million and $46.6 million, respectively.

Governmental activities include revenue bonds outstanding at June 30, 2010, of $111.7 million issued by Washington State University. The bonds were issued to fund various capital construction projects.

These bonds do not constitute either a legal or moral obligation of the state, nor does the state pledge its full faith, credit, or taxing power for payment of these bonds. Total principal and interest remaining on the bonds is $176.5 million, payable through 2034. For the current year, pledged revenue and debt service were $24.6 million and $1.5 million, respectively.

Governmental activities also include revenue bonds outstanding at June 30, 2010, of $54.9 million issued by the Tumwater Office Properties (TOP), which is a blended component unit of the state. The bonds, issued in 2004, are payable solely from the trust estate pledged under the indenture, including rental payments. The bonds were used to construct an office building in Tumwater, Washington which the state occupied beginning in Fiscal Year 2006.

The bonds are not a general obligation of the state, nor does the state pledge its full faith, credit, or taxing power for payment of these bonds. Total principal and interest remaining on the bonds is $90.4 million, payable through 2028. For the current year, pledged revenue and debt service were $3.6 million and $3.6 million, respectively.

Additionally, governmental activities include revenue bonds outstanding at June 30, 2010, of $11.8 million issued by the City of Aberdeen. The bonds were used to extend utilities to the state Department of Corrections Stafford Creek Corrections Center (SCCC). The Department of Corrections entered into an agreement with the City of Aberdeen to pay a system development fee sufficient to pay the debt service on the bonds. The bonds were issued in 1998 and 2002, and refunded by the City in 2010, and are payable solely from current operating appropriations.

The bonds are not a general obligation of the state, nor does the state pledge its full faith, credit, or taxing power for payment of these bonds. Total principal and interest remaining on these bonds is $14.5 million, payable through 2022. For the current year, pledged revenue and debt service were $1.6 million and $1.6 million, respectively.

The state's colleges and universities issue bonds for the purpose of housing, dining, parking, and student facilities construction. These bonds are reported within business-type activities and are secured by a pledge of specific revenues. These bonds are not a general obligation of the state, nor does the state pledge its full faith, credit, or taxing power for payment of these bonds.

Total pledged specific revenues for the state's colleges and universities to repay the principal and interest of revenue bonds as of June 30, 2010, are as follows (expressed in thousands):

| Source of Revenue Pledged | Housing and Dining Revenues (Net of Operating Expenses) | Student Facilities Fees and Earnings on Invested Fees | Parking Revenues (Net of Operating Expenses) | Bookstore Revenues |
|---|---|---|---|---|
| Current revenue pledged | $ 47,289 | $ 47,153 | $ 10,889 | $ 543 |
| Current year debt service | 17,367 | 24,887 | 1,318 | 228 |
| Total future revenues pledged * | 366,253 | 647,742 | 37,631 | 5,481 |
| Description of debt | Housing and dining bonds, issued in 1998-2010 | Student facilities bonds, issued in 1996-2009 and refunding revenue bonds, issued in 2002-2006 | Parking system and refunding revenue bonds, issued in 2004-2005 | Student union and recreation center bonds issued in 2004 |
| Purpose of debt | Construction and renovation of student housing and dining projects | Construction, renovation and improvements to student activity facilities and sports stadium | Construction of parking garage and improvements | Construct new bookstore as part of new student union and recreation center building |
| Term of commitment | 2013-2038 | 2019-2038 | 2024-2030 | 2034 |
| Percentage of debt service to pledged revenues (current year) | 36.7% | 52.8% | 12.1% | 42.1% |

* Total future principal and interest payments.

## B. CERTIFICATES OF PARTICIPATION

Certificates of participation at June 30, 2010, are reported by the state of Washington within governmental activities and business-type activities, as applicable.

Current state law authorizes the state to enter into long-term financing contracts for the acquisition of real or personal property and for the issuance of certificates of participation in the contracts. These certificates of participation do not fall under the general obligation debt limitations and are generally payable only from annual appropriations by the Legislature.

Other specific provisions could also affect the state's obligation under certain agreements. The certificates of participation are recorded for financial reporting purposes if the possibility of the state not meeting the terms of the agreements is considered remote.

Total debt service requirements for certificates of participation to maturity as of June 30, 2010, are as follows (expressed in thousands):

| | Governmental Activities | | Business-Type Activities | | Totals | |
|---|---|---|---|---|---|---|
| **Certificates of Participation** | **Principal** | **Interest** | **Principal** | **Interest** | **Principal** | **Interest** |
| **By Fiscal Year:** | | | | | | |
| 2011 | $ 54,711 | $ 25,990 | $ 74,503 | $ 16,940 | $ 129,214 | $ 42,930 |
| 2012 | 46,097 | 15,794 | 30,046 | 10,294 | 76,143 | 26,088 |
| 2013 | 43,688 | 14,006 | 28,476 | 9,129 | 72,164 | 23,135 |
| 2014 | 44,179 | 12,327 | 28,796 | 8,035 | 72,975 | 20,362 |
| 2015 | 40,838 | 10,493 | 26,618 | 6,840 | 67,456 | 17,333 |
| 2016-2020 | 125,033 | 32,643 | 42,666 | 21,276 | 167,699 | 53,919 |
| 2021-2025 | 61,333 | 15,643 | 39,977 | 10,196 | 101,310 | 25,839 |
| 2026-2030 | 33,457 | 3,927 | 21,808 | 2,560 | 55,265 | 6,487 |
| **Total Debt Service Requirements** | $ 449,336 | $ 130,823 | $ 292,890 | $ 85,270 | $ 742,226 | $ 216,093 |

## C. DEBT REFUNDINGS

When advantageous and permitted by statute and bond covenants, the State Finance Committee authorizes the refunding of outstanding bonds and certificates of participation. Colleges and universities may also refund revenue bonds.

When the state refunds outstanding bonds, the net proceeds of each refunding issue are used to purchase U.S. government securities that are placed in irrevocable trusts with escrow agents to provide for all future debt service payments on the refunded bonds.

As a result, the refunded bonds are considered defeased and the liability is removed from the government-wide statement of net assets.

### Current Year Defeasances

#### Bonds

**Governmental Activities**.
On July 8, 2009, the state issued $386.4 million of various purpose general obligation refunding bonds with an average interest rate of 4.89 percent to refund $419.9 million of various purpose general obligation bonds with an average interest rate of 4.99 percent. The refunding resulted in a $40.9 million gross debt service savings over the next 14 years and a net present value savings of $34.1 million.

On October 14, 2009, the state issued $215.5 million of various purpose general obligation refunding bonds with an average interest rate of 5.24 percent to refund $222 million of various purpose general obligation bonds with an average interest rate of 5 percent. The refunding resulted in a $19.2 million gross debt service savings over the next 16 years and a net present value savings of $15.3 million.

On October 14, 2009, the state issued $121.2 million of motor vehicle fuel tax refunding bonds with an average interest rate of 5.24 percent to refund $124.5 million of motor vehicle fuel tax bonds with an average interest rate of 5 percent. The refunding resulted in a $10.4 million gross debt service savings over the next 16 years and a net present value savings of $8.3 million.

**Business-Type Activities**.
On October 28, 2009, Washington State University issued $38.4 million of student recreation center refunding revenue bonds with an average interest rate of 4.42 percent to refund $40.5 million of student recreation center revenue bonds with an average interest rate of 5 percent. The refunding resulted in a $5.8 million gross debt service savings over the next 22 years and an economic gain of $3.9 million.

On June 29, 2010, Washington State University issued $15 million of housing and dining refunding revenue bonds with an average interest rate of 3.83 percent to refund $15.8 million of housing and dining revenue bonds with an average interest rate of 4.95 percent. The refunding resulted in a $2.1 million gross debt service savings over the next 14 years and an economic gain of $1.7 million.

### Certificates of Participation (COPs)

On October 8, 2009, the state issued $33.1 million in refunding certificates of participation with an average interest rate of 3.97 percent to refund $34.1 million of certificates of participation with an average interest rate of 5.18 percent. The refunding resulted in a $3.6 million gross debt service savings over the next 12 years and a net present value savings of $3.6 million.

On June 15, 2010, the state issued $4.5 million in refunding certificates of participation with an average interest rate of 3.09 percent to refund $4.5 million of certificates of participation with an average interest rate of 5.27 percent. The refunding resulted in a $0.8 million gross debt service savings over the next 11 years and a net present value savings of $0.6 million.

## Prior Year Defeasances

In prior years, the state defeased certain general obligation bonds, revenue bonds, and certificates of participation by placing the proceeds of new bonds and certificates in an irrevocable trust to provide for all future debt service payments on the prior bonds and certificates.

Accordingly, the trust account assets and the liability for the defeased bonds and certificates are not included in the state's financial statements.

### General Obligation Bond Debt

On June 30, 2010, $615.9 million of general obligation bonded debt outstanding is considered defeased.

### Revenue Bond Debt

On June 30, 2010, $68.8 million of revenue bonded debt outstanding is considered defeased.

### Certificates of Participation Debt

On June 30, 2010, $138.5 million of certificates of participation debt outstanding is considered defeased.

## D. LEASES

Leases at June 30, 2010, are reported by the state of Washington within governmental activities and business-type activities, as applicable.

The state leases land, office facilities, office and computer equipment, and other assets under a variety of agreements. Although lease terms vary, most leases are subject to appropriation from the State Legislature to continue the obligation. If the possibility of receiving no funding from the Legislature is remote, leases are considered noncancelable for financial reporting purposes. Leases that represent acquisitions are classified as capital leases, and the related assets and liabilities are recorded in the financial records at the inception of the lease.

Other leases are classified as operating leases with the lease payments recorded as expenditures or expenses during the life of the lease. Certain operating leases are renewable for specified periods. In most cases, management expects that the leases will be renewed or replaced by other leases.

Land, buildings and equipment under capital leases as of June 30, 2010, include the following (expressed in thousands):

| | Governmental Activities | Business-Type Activities |
|---|---|---|
| Land (non-depreciable) | $ 52 | $ - |
| Buildings | 14,435 | 6,271 |
| Equipment | 17,198 | 17,499 |
| Less: Accumulated depreciation | (22,183) | (20,161) |
| **Totals** | $ 9,502 | $ 3,609 |

The following schedule presents future minimum payments for capital and operating leases as of June 30, 2010 (expressed in thousands):

| Capital and Operating Leases | Capital Leases | | Operating Leases | |
|---|---|---|---|---|
| | Governmental Activities | Business-Type Activities | Governmental Activities | Business-Type Activities |
| **By Fiscal Year:** | | | | |
| 2011 | $ 4,705 | $ 2,559 | $ 98,477 | $ 29,830 |
| 2012 | 3,075 | 1,002 | 83,187 | 28,758 |
| 2013 | 2,143 | 404 | 71,739 | 29,113 |
| 2014 | 744 | 400 | 62,454 | 28,704 |
| 2015-2019 | 338 | 392 | 51,539 | 27,737 |
| 2020-2024 | 1,667 | 1,925 | 133,770 | 50,928 |
| 2025-2029 | 1,275 | 818 | 70,388 | - |
| 2030-2034 | 1,143 | - | 57,918 | - |
| 2035-2039 | 1,143 | - | 57,720 | - |
| 2040-2044 | 1,257 | - | 57,288 | - |
| **Total Future Minimum Payments** | 17,490 | 7,500 | 744,480 | 195,070 |
| Less: Executory Costs and Interest Costs | (3,204) | (1,409) | - | - |
| **Net Present Value of Future Minimum Lease Payments** | $ 14,286 | $ 6,091 | $ 744,480 | $ 195,070 |

The total operating lease rental expense for Fiscal Year 2010 for governmental activities was $178.1 million, of which $365 thousand was for contingent rentals. The total operating lease rental expense for Fiscal Year 2010 for business-type activities was $45.1 million.

## E. CLAIMS AND JUDGMENTS

Claims and judgments are materially related to three activities: workers' compensation, risk management, and health insurance. Workers' compensation is a business-type activity, and risk management and health insurance are governmental activities. A description of the risks to which the state is exposed by these activities, and the ways in which the state handles the risks, is presented in Note 1.E.

### Workers' Compensation

At June 30, 2010, $40.0 billion of unpaid claims and claim adjustment expenses are presented at their net present and settlement value of $24.0 billion. These claims are discounted at assumed interest rates of 2.5 percent (time loss and medical) to 6.5 percent (pensions) to arrive at a settlement value.

The claims and claim adjustment liabilities of $24.0 billion as of June 30, 2010, include $12.8 billion for supplemental pension cost of living adjustments (COLAs) that by statute are not to be fully funded.

These COLA payments are funded on a pay-as-you-go basis, and the workers' compensation actuaries have indicated that future premium payments will be sufficient to pay these claims as they come due.

The remaining claims liabilities of $11.2 billion are fully funded by long-term investments, net of obligations under securities lending agreements.

Changes in the balances of workers' compensation claims liabilities during Fiscal Years 2009 and 2010 were as follows (expressed in thousands):

| Workers' Compensation Fund | Balances Beginning of Fiscal Year | Incurred Claims and Changes in Estimates | Claim Payments | Balances End of Fiscal Year |
|---|---|---|---|---|
| 2009 | $ 21,887,148 | 2,334,749 | (2,057,829) | $ 22,164,068 |
| 2010 | $ 22,164,068 | 3,943,217 | (2,081,453) | $ 24,025,832 |

## Risk Management

Risk management reports tort liabilities when it becomes probable that a loss has occurred and the amount of that loss can be reasonably estimated. Liabilities include an actuarially determined amount for tort claims that have been incurred but not reported. It also includes an actuarial estimate of loss adjustment expenses for tort defense.

Because actual liabilities depend on such complex factors as inflation, changes in legal doctrines, and damage awards, it should be recognized that future loss emergence will likely deviate, perhaps materially, from the actuarial estimates. Liabilities are re-evaluated annually to take into consideration recently settled claims, the frequency of claims, and other economic or social factors.

The state is a defendant in a significant number of lawsuits pertaining to general and automobile liability matters.

As of June 30, 2010, outstanding and actuarially determined claims against the state and its agencies including actuarially projected defense costs were $727.1 million for which the state has recorded a liability. The state is restricted by law from accumulating funds in the Self Insurance Liability Program in excess of 50 percent of total outstanding and actuarially determined liabilities.

At June 30, 2010, the Risk Management Fund held $115.8 million in cash and pooled investments designated for payment of these claims under the state's Self Insurance Liability Program.

Changes in the balances of risk management claims liabilities during Fiscal Years 2009 and 2010 were as follows (expressed in thousands):

| Risk Management Fund | Balances Beginning of Fiscal Year | Incurred Claims and Changes in Estimates | Claim Payments | Tort Defense Payments | Balances End of Fiscal Year |
|---|---|---|---|---|---|
| 2009 | $ 649,761 | 142,517 | (52,963) | (19,118) | $ 720,197 |
| 2010 | $ 720,197 | 82,387 | (47,425) | (28,023) | $ 727,136 |

## Health Insurance

The Health Insurance Fund establishes a liability when it becomes probable that a loss has occurred and the amount of that loss can be reasonably estimated. Liabilities include an actuarially determined amount for claims that have been incurred but not reported. Because actual claims liabilities depend on various complex factors, the process used in computing claims liabilities does not always result in an exact amount.

Claims liabilities are re-evaluated periodically to take into consideration recently settled claims, the frequency of claims, and other economic and social factors.

At June 30, 2010, health insurance claims liabilities totaling $88.4 million are fully funded with cash and investments, net of obligations under securities lending agreements.

Changes in the balances of health insurance claim liabilities during Fiscal Years 2009 and 2010 were as follows (expressed in thousands):

| Health Insurance Fund | Balances Beginning of Fiscal Year | Incurred Claims and Changes in Estimates | Claim Payments | Balances End of Fiscal Year |
|---|---|---|---|---|
| 2009 | $ 69,934 | 779,143 | (765,636) | $ 83,441 |
| 2010 | $ 83,441 | 879,324 | (874,370) | $ 88,395 |

## F. POLLUTION REMEDIATION

The state reports pollution remediation obligations in accordance with GASB Statement No. 49. The liability reported involves estimates of financial responsibility and amounts recoverable as well as remediation costs.

The liability could change over time as new information becomes available and as a result of changes in remediation costs, technology and regulations governing remediation efforts. Additionally, the responsibilities and liabilities discussed in this disclosure are intended to refer to obligations solely in the accounting context. This disclosure does not constitute an admission of any legal responsibility or liability. Further, it does not establish or affect the rights or obligations of any person under the law, nor does this disclosure impose upon the state any new mandatory duties or obligations.

The state and its agencies are participating as potentially responsible parties in numerous pollution remediation projects under the provisions of the federal Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA, generally referred to as Superfund) and the state Model Toxics Control Act.

There are 19 projects in progress for which the state has recorded a liability of $28.8 million which includes an estimated recovery amount of $283 thousand that is not yet realized or realizable.

The state has also voluntarily agreed to conduct certain remediation activities to the extent of funding paid to the state by third parties for such purposes. In Fiscal Year 2010, the state received funding of $148 million from third parties for these remediation activities. At June 30, 2010, the state has recorded a liability of $145.5 million for remaining project commitments.

Overall, the state has recorded a pollution remediation liability of $174.3 million, measured at its estimated amount, using the expected cash flow technique. The overall estimate is based on professional judgment, experience, and historical cost data. For some projects, the state can reasonably estimate the range of expected outlays early in the process because the site situation is common or similar to other sites with which the state has experience. In other cases, the estimates are limited to an amount specified in a settlement agreement, consent decree, or contract for remediation services.

The pollution remediation activity at some sites for which the state would otherwise have a reportable obligation is at a point where certain costs are not reasonably estimable. For example, a site assessment, remedial investigation, or feasibility study is in progress and the cleanup methodology has not yet been determined: and, consequently, associated future costs cannot be estimated.

The state's reported liability does not include remediation costs for future activities where costs are not yet reasonably estimable.

## G. LONG-TERM LIABILITY ACTIVITY

Long-term liability activity at June 30, 2010, is reported by the state of Washington within governmental activities and business-type activities, as applicable. Long-term liability activity for governmental activities for the Fiscal Year 2010 is as follows (expressed in thousands):

| Governmental Activities: | Beginning Balance July 1, 2009 | Additions | Reductions | Ending Balance June 30, 2010 | Amounts Due Within One Year |
|---|---|---|---|---|---|
| **Long-Term Debt:** | | | | | |
| GO Bonds Payable: | | | | | |
| General obligation (GO) bonds | $ 13,310,430 | $ 3,865,560 | $ 1,339,770 | $ 15,836,220 | $ 584,640 |
| GO - zero coupon bonds (principal) | 738,719 | - | 34,881 | 703,838 | 37,643 |
| Subtotal - GO bonds payable | 14,049,149 | 3,865,560 | 1,374,651 | 16,540,058 | 622,283 |
| Accreted interest - GO - zero coupon bonds | 327,617 | 38,898 | - | 366,515 | - |
| Revenue bonds payable | 616,071 | 164,221 | 37,294 | 742,998 | 24,132 |
| Less: Deferred amounts for issuance discounts | (8,729) | - | (779) | (7,950) | - |
| **Total Bonds Payable** | 14,984,108 | 4,068,679 | 1,411,166 | 17,641,621 | 646,415 |
| **Other Liabilities:** | | | | | |
| Certificates of participation | 395,092 | 146,395 | 92,151 | 449,336 | 54,711 |
| Claims and judgments | 924,541 | 54,025 | 44,518 | 934,048 | 272,189 |
| Installment contracts | 2,775 | - | 105 | 2,670 | - |
| Leases | 9,631 | 9,923 | 5,268 | 14,286 | 4,276 |
| Compensated absences | 552,974 | 333,410 | 338,632 | 547,752 | 59,944 |
| Unfunded pension obligations | 154,130 | 41,976 | 4,717 | 191,389 | - |
| Other postemployment benefits obligations | 443,655 | 253,558 | - | 697,213 | - |
| Pollution remediation obligations | 35,005 | 144,255 | 4,907 | 174,353 | - |
| Unclaimed property refunds | 2 | 93,197 | - | 93,199 | 41 |
| Other | 218,982 | 1,180,324 | 910,745 | 488,561 | 397,710 |
| **Total Other Liabilities** | 2,736,787 | 2,257,063 | 1,401,043 | 3,592,807 | 788,871 |
| **Total Long-Term Debt** | $ 17,720,895 | $ 6,325,742 | $ 2,812,209 | $ 21,234,428 | $ 1,435,286 |

For governmental activities, payments on the certificates of participation are being repaid directly from various governmental funds. The compensated absences liability will be liquidated approximately 50 percent by the General Fund, 27 percent by the Higher Education Special Revenue Fund, 10 percent by the Motor Vehicle Fund, and the balance by various other governmental funds. The claims and judgments liability will be liquidated approximately 78 percent by the Risk Management Fund (an internal service fund), 9 percent by the Health Insurance Fund (an internal service fund), and the balance by various other governmental funds. The pollution remediation liability will be liquidated approximately 85 percent by the Central Administrative and Regulatory Fund, a nonmajor governmental fund, and the balance by various other governmental funds. Leases, installment contract obligations, and other liabilities will be repaid from various other governmental funds.

Long-term liability activity for business-type activities for the Fiscal Year 2010 (expressed in thousands) is as follows:

| Business-Type Activities | Beginning Balance July 1, 2009 | Additions | Reductions | Ending Balance June 30, 2010 | Amounts Due Within One Year |
|---|---|---|---|---|---|
| **Long-Term Debt:** | | | | | |
| GO Bonds Payable: | | | | | |
| General obligation (GO) bonds | $ 40,520 | $ - | $ 8,010 | $ 32,510 | $ 7,355 |
| GO - zero coupon bonds (principal) | 28,284 | - | 901 | 27,383 | 841 |
| Subtotal - GO bonds payable | 68,804 | - | 8,911 | 59,893 | 8,196 |
| Accreted interest - GO - zero coupon bonds | 38,051 | 3,709 | - | 41,760 | - |
| Revenue bonds payable | 1,073,807 | 89,714 | 79,576 | 1,083,945 | 40,106 |
| Plus: Unamortized amounts issuance premiums | 11,296 | 2,786 | 1,140 | 12,942 | - |
| Less: Deferred amounts for issuance discounts | (1,601) | - | (1,118) | (483) | - |
| Less: Deferred gain/loss on bond refunding | (7,747) | (2,693) | (1,532) | (8,908) | - |
| **Total Bonds Payable** | 1,182,610 | 93,516 | 86,977 | 1,189,149 | 48,302 |
| **Other Liabilities:** | | | | | |
| Certificates of participation | 310,040 | 58,067 | 75,217 | 292,890 | 74,503 |
| Less: Deferred amounts for issuance discounts | (1,167) | - | (148) | (1,019) | - |
| Claims and judgments | 22,175,347 | 2,044,518 | 181,543 | 24,038,322 | 2,136,582 |
| Lottery prize annuities payable | 309,964 | 73,354 | 107,407 | 275,911 | 50,127 |
| Tuition benefits payable | 1,492,100 | 447,832 | 86,528 | 1,853,404 | 90,300 |
| Leases | 9,670 | 71 | 3,650 | 6,091 | 2,304 |
| Compensated absences | 55,684 | 27,339 | 23,823 | 59,200 | 26,040 |
| Other postemployment benefits obligation | 49,896 | 30,763 | - | 80,659 | - |
| Other | 105,049 | 575,435 | 540,291 | 140,193 | 109,581 |
| **Total Other Liabilities** | 24,506,583 | 3,257,379 | 1,018,311 | 26,745,651 | 2,489,437 |
| **Total Long-Term Debt** | $ 25,689,193 | $ 3,350,895 | $ 1,105,288 | $ 27,934,800 | $ 2,537,739 |

# Note 8
## No Commitment Debt

The Washington State Housing Finance Commission, Washington Higher Education Facilities Authority, Washington Health Care Facilities Authority, and Washington Economic Development Finance Authority (financing authorities) were created by the state Legislature. For financial reporting purposes, they are discretely presented as component units. These financing authorities issue bonds for the purpose of making loans to qualified borrowers for capital acquisitions, construction, and related improvements.

These bonds do not constitute either a legal or moral obligation of the state or these financing authorities, nor does the state or these financing authorities pledge their faith and credit for the payment of such bonds.

Debt service on the bonds is payable solely from payments made by the borrowers pursuant to loan agreements. Due to their no commitment nature, the bonds issued by these financing authorities are excluded from the state's financial statements.

The schedule below presents the June 30, 2010, balances for the "No Commitment" debt of the state's financing authorities (expressed in thousands):

| Financing Authorities | Principal Balance |
|---|---|
| Washington State Housing Finance Commission | $ 3,910,818 |
| Washington Higher Education Facilities Authority | 689,283 |
| Washington Health Care Facilities Authority | 4,800,000 |
| Washington Economic Development Finance Authority | 715,678 |
| **Total No Commitment Debt** | $ 10,115,779 |

# Note 9
## Fund Balances Reserved for Other Specific Purposes

The nature and purposes of fund balances reserved for other specific purposes as of June 30, 2010, are listed below (expressed in thousands):

| Fund Balances | General | Higher Education Special Revenue | Motor Vehicle Special Revenue | Higer Education Endowment | Nonmajor Governmental Funds | Totals |
|---|---|---|---|---|---|---|
| **Reserved for Other Specific Purposes:** | | | | | | |
| Long-term receivables | $ 61,011 | $ 2,921 | $ 284 | $ - | $ 1,759,682 | $ 1,823,898 |
| Long-term investments | - | 105,135 | - | - | 946 | 106,081 |
| Long-term student loans | - | 99,880 | - | - | - | 99,880 |
| Budget stabilization (Rainy Day) | - | - | - | - | 95,050 | 95,050 |
| Petty cash | 599 | 3,042 | 569 | - | 228 | 4,438 |
| Pollution remediation | - | - | - | - | 153,391 | 153,391 |
| Investments with trustees | 683 | - | - | - | 515 | 1,198 |
| **Total Reserved for Other Specific Purposes** | $ 62,293 | $ 210,978 | $ 853 | $ - | $ 2,009,812 | $ 2,283,936 |

# Note 10
## Deficit Net Assets

### Guaranteed Education Tuition

The Guaranteed Education Tuition (GET) program within the Other Activities Fund, an enterprise fund, had deficit net assets of $254.6 million at June 30, 2010.

The Higher Education Coordinating Board administers the GET program which is Washington's Internal Revenue Service Code 529 prepaid college tuition plan. It was established to help make higher education more affordable and accessible to all citizens of the state by offering a savings incentive to protect purchasers and beneficiaries from rising tuition costs.

The Committee on Advance Tuition Payment establishes the policies of the program and sets the price of a tuition unit. Since GET began in 1998, families have opened more than 119,000 accounts.

In recent years, the GET program has experienced losses primarily due to reduced investment earnings and higher than projected tuition increases.

The following schedule details the changes in net assets for the GET program during the fiscal year ended June 30, 2010 (expressed in thousands):

| Guaranteed Education Tuition Program | Net Assets (Deficit) |
|---|---|
| **Balance, July 1, 2009** | $ (234,322) |
| Fiscal Year 2010 activity | (20,297) |
| **Balance, June 30, 2010** | $ (254,619) |

### Risk Management Fund

The Risk Management Fund, an internal service fund, had deficit net assets of $616.1 million at June 30, 2010. The Risk Management Fund is used to administer the Self-Insurance Liability Program. This program investigates, processes, and adjudicates all tort and sundry claims filed against Washington state agencies. The Self Insurance Liability Program, initiated in 1990, is intended to provide funds for the payment of all tort claims and defense expenses.

The Risk Management Fund is supported by premium assessments to state agencies. The state is restricted by law from accumulating funds in the Self Insurance Liability Program in excess of 50 percent of total outstanding and actuarially determined claims. As a consequence, when outstanding and incurred but not reported claims are actuarially determined and accrued, the result is deficit net assets.

The following schedule details the changes in net assets for the Risk Management Fund during the fiscal year ended June 30, 2010 (expressed in thousands):

| Risk Management Fund | Net Assets (Deficit) |
|---|---|
| **Balance, July 1, 2009** | $ (617,748) |
| Fiscal Year 2010 activity | 1,633 |
| **Balance, June 30, 2010** | $ (616,115) |

## Health Insurance Fund

The Health Insurance Fund, an internal service fund, had deficit net assets of $41 million at June 30, 2010. The Health Insurance Fund is used to account for premiums and costs associated with employees' insurance benefits.

The state of Washington, through the Public Employees Benefits Board (PEBB) program, provides medical, dental, life, and long-term disability coverage to eligible state employees as a benefit of employment. Coverage is provided through private health insurance plans and self-insured products.

The deficit net assets at June 30, 2010 resulted from higher than expected costs to provide health care benefits.

The following schedule details the changes in net assets for the Health Insurance Fund during the fiscal year ended June 30, 2010 (expressed in thousands):

| Health Insurance Fund | Net Assets (Deficit) |
|---|---|
| **Balance, July 1, 2009, as restated** | $ 28,830 |
| Fiscal Year 2010 activity | (69,851) |
| **Balance, June 30, 2010** | $ (41,021) |

# Note 11
## Retirement Plans

### A. GENERAL

The state of Washington, through the Department of Retirement Systems, the Board for Volunteer Fire Fighters, and the Administrative Office of the Courts, administers 13 defined benefit retirement plans, three combination defined benefit/defined contribution retirement plans, and one defined contribution retirement plan covering eligible employees of the state and local governments.

#### Basis of Accounting

Pension plans administered by the state are accounted for using the accrual basis of accounting. Under the accrual basis of accounting, employee and employer contributions are recognized in the period in which employee services are performed; investment gains and losses are recognized as incurred; and benefits and refunds are recognized when due and payable in accordance with the terms of the applicable plan.

#### Investments

Pension plan investments are presented at fair value. Fair values are based on published market prices, quotations from national security exchanges and security pricing services, or by the respective fund managers for securities that are not actively traded. Privately held mortgages are valued at cost, which approximates fair value. Certain pension trust fund investments, including real estate and private equity, are valued based on appraisals or independent advisors. The pension funds have no investments of any commercial or industrial organization whose market value exceeds 5 percent of each plan's net assets. Additional disclosure describing investments is provided in Note 3.

**Department of Retirement Systems.** As established in chapter 41.50 of the Revised Code of Washington (RCW), the Department of Retirement Systems (DRS) administers eight retirement systems comprising 12 defined benefit pension plans and three combination defined benefit/defined contribution plans as follows:

- Public Employees' Retirement System (PERS)
  - Plan 1 - defined benefit
  - Plan 2 - defined benefit
  - Plan 3 - defined benefit/defined contribution
- Teachers' Retirement System (TRS)
  - Plan 1 - defined benefit
  - Plan 2 - defined benefit
  - Plan 3 – defined benefit/defined contribution
- School Employees' Retirement System (SERS)
  - Plan 2 - defined benefit
  - Plan 3 - defined benefit/defined contribution
- Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF)
  - Plan 1 - defined benefit
  - Plan 2 - defined benefit
- Washington State Patrol Retirement System (WSPRS)
  - Plan 1 - defined benefit
  - Plan 2 - defined benefit
- Public Safety Employees' Retirement System (PSERS)
  - Plan 2 - defined benefit
- Judicial Retirement System (JRS)
  - Defined benefit plan
- Judges' Retirement Fund (Judges)
  - Defined benefit plan

Although some assets of the plans are commingled for investment purposes, each plan's assets may be used only for the payment of benefits to the members of that plan in accordance with the terms of the plan.

Administration of the PERS, TRS, SERS, LEOFF, WSPRS, and PSERS systems and plans was funded by an employer rate of 0.16 percent of employee salaries. Administration of the JRS and Judges plans is funded by means of legislative appropriations.

The Department of Retirement Systems prepares a stand-alone financial report. Copies of the report that include financial statements and required supplementary information may be obtained by writing to Washington State Department of Retirement Systems, PO Box 48380, Olympia, Washington 98504-8380 or by visiting their website at: http:\\www.drs.wa.gov.

**Board for Volunteer Fire Fighters.** As established in chapter 41.24 RCW, the Washington Board for Volunteer Fire Fighters' administers the Volunteer Fire Fighters' and Reserve Officers' Relief and Pension Fund (VFFRPF), a defined benefit plan. Administration of VFFRPF is funded through legislative appropriation.

**Administrative Office of the Courts.** As established in chapter 2.14 RCW, the Administrative Office of the Courts administers the Judicial Retirement Account (JRA), a defined contribution plan. Administration of JRA is funded through member fees.

**Higher Education.** In addition to the retirement plans administered by the state of Washington, eligible higher education state employees may participate in privately administered Higher Education Retirement defined contribution plans.

Plan descriptions, funding policies, a table of employer contributions required and paid for defined benefit plans, schedules of funded status and funding progress, defined benefit pension plans valuations, annual pension cost, and three year trend information follow in Note 11.B through G, respectively. Information related to changes in actuarial assumptions and methods, and changes in benefit provisions are provided in Note 11.H and I. For information related to defined contribution plans, refer to Note 11.J. Details on plan net assets and changes in plan net assets of pension plans and other employee benefit funds administered by the state are presented in Note 11.K.

Membership of each state administered plan consisted of the following at June 30, 2009, the date of the latest actuarial valuation for all plans:

**Number of Participating Members**

| Plans Administered by the State | Retirees and Beneficiaries Receiving Benefits | Terminated Members Entitled To But Not Yet Receiving Benefits | Active Plan Members Vested | Active Plan Members Nonvested | Total Members |
|---|---|---|---|---|---|
| PERS 1 | 54,147 | 2,125 | 9,630 | 724 | 66,626 |
| PERS 2 | 19,790 | 22,824 | 85,965 | 35,835 | 164,414 |
| PERS 3 | 920 | 3,125 | 9,744 | 17,337 | 31,126 |
| TRS 1 | 36,032 | 843 | 5,129 | 75 | 42,079 |
| TRS 2 | 2,104 | 2,472 | 6,153 | 3,021 | 13,750 |
| TRS 3 | 1,791 | 5,345 | 29,585 | 23,425 | 60,146 |
| SERS 2 | 2,870 | 4,644 | 14,899 | 5,298 | 27,711 |
| SERS 3 | 1,759 | 4,549 | 16,590 | 15,687 | 38,585 |
| LEOFF 1 | 8,087 | 2 | 356 | - | 8,445 |
| LEOFF 2 | 1,367 | 672 | 13,007 | 3,944 | 18,990 |
| WSPRS 1 | 834 | 122 | 829 | 1 | 1,786 |
| WSPRS 2 | - | 4 | 101 | 163 | 268 |
| PSERS 2 | 2 | - | - | 4,340 | 4,342 |
| JRS | 124 | - | 9 | - | 133 |
| Judges | 13 | - | - | - | 13 |
| JRA | 1 | 185 | 11 | - | 197 |
| VFFRPF | 3,612 | 6,059 | 4,174 | 6,584 | 20,429 |
| **Total** | 133,453 | 52,971 | 196,182 | 116,434 | 499,040 |

Following is a summary of the number of government employers participating in state administered retirement plans as of June 30, 2010:

**Number of Participating Employers**

| Plan | State Agencies | School Districts | Counties/ Municipalities | Other Political Subdivisions |
|---|---|---|---|---|
| PERS 1 | 146 | 229 | 166 | 193 |
| PERS 2 | 178 | - | 270 | 485 |
| PERS 3 | 163 | - | 209 | 287 |
| TRS 1 | 54 | 271 | - | - |
| TRS 2 | 23 | 283 | - | - |
| TRS 3 | 31 | 302 | - | - |
| SERS 2 | - | 298 | - | - |
| SERS 3 | 1 | 300 | - | - |
| LEOFF 1 | - | - | 54 | 15 |
| LEOFF 2 | 8 | - | 215 | 149 |
| WSPRS 1 | 1 | - | - | - |
| WSPRS 2 | 1 | - | - | - |
| PSERS 2 | 10 | - | 63 | - |
| JRS | 2 | - | - | - |
| Judges | - | - | - | - |
| JRA | 3 | - | - | - |
| VFFRPF | - | - | - | 671 |

Employers can participate in multiple systems and/or plans.

## B. PLAN DESCRIPTIONS

### Public Employees' Retirement System (PERS)

The Legislature established PERS in 1947. Membership in the system includes: elected officials; state employees; employees of the Supreme, Appeals, and Superior Courts (other than judges currently in a judicial retirement system); employees of legislative committees; community and technical colleges, college and university employees not in national higher education retirement programs; judges of district and municipal courts; and employees of local governments.

The Higher Education Retirement Plans are not administered by DRS. Approximately 52 percent of PERS salaries are accounted for by state employment. PERS retirement benefit provisions are established in chapters 41.34 and 41.40 RCW and may be amended only by the state Legislature.

PERS is a cost-sharing multiple-employer retirement system comprised of three separate plans for membership purposes: Plans 1 and 2 are defined benefit plans and Plan 3 is a combination defined benefit/ defined contribution plan.

PERS participants who joined the system by September 30, 1977, are Plan 1 members. Those who joined on or after October 1, 1977, and by either, February 28, 2002, for state and higher education employees, or August 31, 2002, for local government employees, are Plan 2 members unless they exercise an option to transfer their membership to Plan 3.

PERS participants joining the system on or after March 1, 2002, for state and higher education employees, or September 1, 2002, for local government employees, have the irrevocable option of choosing membership in either PERS Plan 2 or PERS Plan 3. The option must be exercised within 90 days of employment. An employee is reported in Plan 2 until a choice is made. Employees who fail to choose within 90 days default to PERS Plan 3. Notwithstanding, PERS Plan 2 and Plan 3 members may opt out of plan membership if terminally ill with less than five years to live.

PERS is comprised of and reported as three separate plans: Plan 1, Plan 2/3, and Plan 3. Plan 1 accounts for the defined benefits of Plan 1 members. Plan 2/3 accounts for the defined benefits of Plan 2 members and the defined benefit portion of benefits for Plan 3 members. Plan 3 accounts for the defined contribution portion of benefits for Plan 3 members.

Although members can only be a member of either Plan 2 or Plan 3, the defined benefit portions of Plan 2 and Plan 3 are accounted for in the same pension trust fund. All assets of this Plan 2/3 defined benefit plan may legally be used to pay the defined benefits of any of the Plan 2 or Plan 3 members or beneficiaries, as defined by the terms of the plan.

PERS defined benefit retirement benefits are financed from a combination of investment earnings and employer and employee contributions. Employee contributions to the PERS Plan 1 and 2 defined benefit plans accrue interest at a rate specified by DRS.

During Fiscal Year 2010, the DRS-established rate on employee contributions was 5.5 percent compounded quarterly. Employees in PERS Plan 1 and 2 can elect to withdraw total employee contributions and interest thereon upon separation from PERS-covered employment.

PERS Plan 3 defined contribution benefits are financed from employee contributions and investment earnings. Employees in PERS Plan 3 can elect to withdraw total employee contributions adjusted by earnings and losses from the investment of those contributions upon separation from PERS-covered employment.

PERS Plan 1 retirement benefits are vested after an employee completes five years of eligible service. Plan 1 members are eligible for retirement after 30 years of service, or at the age of 60 with five years of service, or at the age of 55 with 25 years of service. Plan 1 members retiring from inactive status prior to the age of 65 may receive actuarially reduced benefits. Benefits are also actuarially reduced when a Plan 1 member chooses a survivor option.

The annual benefit is 2 percent of the average final compensation (AFC) per year of service (AFC is based on the greatest compensation during any 24 eligible consecutive compensation months), capped at 60 percent.

A cost-of-living allowance (COLA) is granted at age 66 based upon years of service times the COLA amount (based on the Consumer Price Index), capped at 3 percent annually. Plan 1 retirees, after being retired one year, will receive the annual COLA adjustment in July if they turn 66 years of age any time in the calendar year in which the COLA is given. Plan 1 members may also elect to receive an additional COLA amount (based on the Consumer Price Index), capped at 3 percent annually. To offset the cost of this annual adjustment, the benefit is reduced.

PERS Plan 1 provides duty and non-duty disability benefits. Duty disability retirement benefits for disablement prior to the age of 60 consist of a temporary life annuity payable to the age of 60. The allowance

amount is $350 a month, or two-thirds of the monthly AFC, whichever is less.

The benefit is reduced by any worker's compensation benefit and is payable as long as the member remains disabled or until the member attains the age of 60. A member with five years of membership service is eligible for non-duty disability retirement. Prior to the age of 55, the allowance amount is 2 percent of the AFC for each year of service reduced by 2 percent for each year that the member's age is less than 55.

The total benefit is limited to 60 percent of the AFC and is actuarially reduced to reflect the choice of a survivor option. A COLA is granted at age 66 based upon years of service times the COLA amount (indexed to the Seattle Consumer Price Index), capped at 3 percent annually. Plan 1 members may also elect to receive an additional COLA amount (indexed to the Seattle Consumer Price Index), capped at 3 percent annually. To offset the costs of this annual adjustment, the benefit is reduced.

PERS Plan 1 members can receive credit for military service while actively serving in the military, if such credit makes them eligible to retire. Members can also purchase up to 24 months of service credit lost because of an on-the-job injury.

PERS Plan 2 retirement benefits are vested after an employee completes five years of eligible service. Plan 2 members may retire at the age of 65 with five years of service, or at the age of 55 with 20 years of service, with an allowance of 2 percent of the AFC per year of service. (AFC is based on the greatest compensation during any eligible consecutive 60-month period.)

Plan 2 retirements prior to the age of 65 receive reduced benefits. If retirement is at age 55 or older with at least 30 years of service, a 3 percent per year reduction applies; otherwise an actuarial reduction will apply. The benefit is also actuarially reduced to reflect the choice of a survivor option. There is no cap on years of service credit; and a COLA is granted (based on the Consumer Price Index), capped at 3 percent annually.

Refunds provided to survivors of PERS Plan 2 members that leave eligible employment after earning ten years of service credit and are subsequently killed in uniformed service to the United States while participating in Operation Enduring Freedom or Persian Gulf, Operation Iraqi Freedom is increased from 100 to 200 percent of the accumulated contributions in the member's account.

PERS Plan 3 has a dual benefit structure. Employer contributions finance a defined benefit component, and member contributions finance a defined contribution component.

The defined benefit portion provides a benefit calculated at 1 percent of the AFC per year of service. (AFC is based on the greatest compensation during any eligible consecutive 60-month period.)

Effective June 7, 2006, PERS Plan 3 members may be vested either after ten years of service or after five years of service, as long as 12 consecutive months of service were accrued after attainment of age 44. Plan 3 members are immediately vested in the defined contribution portion of their plan. Vested Plan 3 members are eligible to retire with full benefits at age 65. Plan 3 retirements prior to the age of 65 receive reduced benefits.

If retirement is at age 55 or older with at least 30 years of service, a 3 percent per year reduction applies; otherwise an actuarial reduction will apply. The benefit is also actuarially reduced to reflect the choice of a survivor option. There is no cap on years of service credit; and Plan 3 provides the same COLA as Plan 2. Refer to section J of this note for a description of the defined contribution component of PERS Plan 3.

PERS Plan 2 and Plan 3 provide disability benefits. There is no minimum amount of service credit required for eligibility. The Plan 2 allowance amount is 2 percent of the AFC for each year of service. For Plan 3 the allowance amount is 1 percent of the AFC for each year of service.

Benefits are actuarially reduced for each year that the member's age is less than 65, and to reflect the choice of a survivor option. There is no cap on years of service credit, and a COLA is granted (indexed to the Seattle Consumer Price Index) capped at 3 percent annually. PERS members may purchase up to 24 consecutive months of service credit for each period of temporary duty disability.

Beneficiaries of a PERS Plan 2 or 3 member with 10 years of service who is killed in the course of employment receive retirement benefits without actuarial reduction, if the member was not at normal retirement age at death. This provision applies to any member killed in the course of employment, on or after June 10, 2004, if found eligible by the Director of the Department of Labor and Industries.

PERS Plan 2 and Plan 3 members can purchase service credit for military service that interrupts employment.

Additionally, PERS Plan 2 and Plan 3 members who become totally incapacitated for continued employment while serving in the uniformed services may apply for interruptive military service credit. Should any such member die during this active duty, the member's surviving spouse or eligible children may purchase credit on behalf of the deceased member.

PERS Plan 2 and Plan 3 members can purchase up to 24 months of service credit lost because of an on-the-job injury. PERS Plan 2 and Plan 3 members who apply for early retirement may, at the time of retirement, purchase up to five years of additional service credit. The cost of the additional service credit is the actuarial equivalent value of the resulting increase in the member's benefit.

A $150,000 death benefit is provided to the estate (or duly designated nominee) of a PERS member who dies in the line of service as a result of injuries sustained in the course of employment, or if the death resulted from an occupational disease or infection that arose naturally or by a duty related illness, and proximately out of their covered employment, if found eligible by the Director of the Department of Labor and Industries.

PERS members may also purchase up to five years of additional service credit once eligible for retirement. This credit can only be purchased at the time of retirement, and cannot be used to qualify for any retirement eligibility or benefit reductions based upon years of service. This credit is to be used exclusively to provide the member with a monthly annuity that is paid in addition to the member's retirement allowance.

Portability of retirement benefits allows for PERS members' compensation that is reportable in all dual members' systems, except in WSPRS, to be included in the calculation of all dual members' benefits, and removing the "maximum benefit rule" for dual members who have less than 15 years of service in one capped plan and service in one uncapped plan.

Effective after the January 2008 distribution, gain sharing for PERS Plan 1 and Plan 3 members was discontinued.

Additional COLAs were provided to PERS Plan 1 retirees in July 2009 and new alternative early retirement provisions were created for PERS Plan 2 and Plan 3 members.

Beginning January 1, 2007 through December 31, 2007, judicial members of PERS were given the choice to participate in the Judicial Benefit Multiplier (JBM) Program enacted in 2006.

Justices or judges in PERS Plans 1 and 2 were able to make a one-time irrevocable election to pay increased contributions that would fund a retirement benefit with a 3.5 percent multiplier. The benefit would be capped at 75 percent of AFC.

Judges in PERS Plan 3 could elect a 1.6 percent of pay per year of service benefit, capped at 37.5 percent of AFC.

Members who chose to participate would:

- Accrue service credit at the higher multiplier beginning with the date of their election.
- Be subject to the benefit cap of 75 percent of AFC.
- Stop contributing to the Judicial Retirement Account (JRA).
- Pay higher contributions.
- Be given the option to increase the multiplier on past judicial service.

Members who did not choose to participate would:

- Continue to accrue service credit at the regular multiplier (i.e. 1 percent, 2 percent, or 3 percent).
- Continue to participate in JRA, if applicable.
- Never be a participant in the JBM program.
- Continue to pay contributions at the regular PERS rate.

Newly elected justices and judges who chose to become PERS members on or after January 1, 2007, or who had not previously opted into PERS membership, were required to participate in the JBM program.

Members required to join the JBM program would:

- Return to prior PERS Plan if membership had previously been established.
- Be mandated into Plan 2 and not have a Plan 3 transfer choice, if a new PERS member.
- Accrue the higher multiplier for all judicial service.
- Not contribute to JRA.
- Not have the option to increase the multiplier for past judicial service.

Judges and justices who are members of PERS may purchase prior judicial service credit at a higher multiplier at retirement.

During the period of January 1, 2009 through June 30, 2009, active and inactive PERS members who were not then serving as justices or judges, but who have served as such in the past, may request an increase in their benefit multiplier for past periods of judicial service and pay a cost that is the actuarial equivalent of the increase.

Material changes in PERS benefit provisions for the fiscal year ended June 30, 2010, are listed in the table at the end of this section.

## Teachers' Retirement System (TRS)

TRS was legislatively established in 1938. Eligibility for membership requires service as a certificated public school employee in an instructional, administrative or supervisory capacity. TRS is comprised principally of non-state employees. TRS retirement benefit provisions are established in chapters 41.32 and 41.34 RCW and may be amended only by the state Legislature.

TRS is a cost-sharing multiple-employer retirement system comprised of three separate plans for membership purposes: Plans 1 and 2 are defined benefit plans and Plan 3 is a combination defined benefit/defined contribution plan.

TRS participants who joined the system by September 30, 1977, are Plan 1 members. Those who joined on or after October 1, 1977, and by June 30, 1996, are Plan 2 members unless they exercised an option to transfer their membership to Plan 3.

TRS participants joining the system on or after July 1, 1996, and those who exercised their transfer option, are members of TRS Plan 3.

TRS members hired on or after July 1, 2007 have 90 days to make an irrevocable choice to enroll in either Plan 2 or Plan 3. An employee is reported in Plan 2 until a choice is made.

Employees who fail to choose within 90 days default to TRS Plan 3. Notwithstanding, TRS Plan 2 and Plan 3 members may opt out of plan membership if terminally ill, with less than five years to live.

TRS is comprised of and reported as three separate plans: Plan 1, Plan 2/3, and Plan 3. Plan 1 accounts for the defined benefits of Plan 1 members. Plan 2/3 accounts for the defined benefits of Plan 2 members and the defined benefit portion of benefits for Plan 3 members. Plan 3 accounts for the defined contribution portion of benefits for Plan 3 members.

Although members can only be a member of either Plan 2 or Plan 3, the defined benefit portions of Plan 2 and Plan 3 are accounted for in the same pension trust fund. All assets of this Plan 2/3 defined benefit plan may legally be used to pay the defined benefits of any of the Plan 2 or Plan 3 members or beneficiaries, as defined by the terms of the plan.

TRS defined benefit retirement benefits are financed from a combination of investment earnings and employer and employee contributions. Employee contributions to the TRS Plan 1 and 2 defined benefit plans accrue interest at a rate specified by DRS.

During Fiscal Year 2010, the DRS-established rate on employee contributions was 5.5 percent compounded quarterly. Employees in TRS Plan 1 and 2 can elect to withdraw total employee contributions and interest thereon upon separation from TRS-covered employment. TRS Plan 3 defined contribution benefits are financed from employee contributions and investment earnings.

Employees in TRS Plan 3 can elect to withdraw total employee contributions adjusted by earnings and losses from the investment of those contributions upon separation from TRS-covered employment.

TRS Plan 1 retirement benefits are vested after an employee completes five years of eligible service. Plan 1 members are eligible for retirement after 30 years of service, or at the age of 60 with five years of service, or at the age of 55 with 25 years of service. The annual pension is 2 percent of the average final compensation (AFC) per year of service (AFC is based on the greatest compensation during the highest of any consecutive two compensation contract years), capped at 60 percent.

A COLA is granted at age 66 based upon years of service times the COLA amount, increased by 3 percent annually. Plan 1 retirees will receive the annual COLA adjustment in July if they turn 66 years of age any time in the calendar year in which the COLA is given. Plan 1 members may also elect to receive an additional COLA amount (based on the Consumer Price Index), capped at 3 percent annually. To offset the cost of this annual adjustment, the benefit is reduced.

TRS Plan 1 provides death and temporary disability benefits. TRS Plan 1 members receive the following additional lump sum death benefits: retired members- $400 (if retired with ten years of full-time membership), $400 (if inactive with ten years of membership), active members $600 (if employed full-time at time of death).

Members on temporary disability receive a monthly payment of $180 payable for up to two years, for the same occurrence. After five years of service, members on a disability retirement receive an allowance based on their salary and service to date of disability. Members enrolled in TRS prior to April 25, 1973, may elect a benefit based on the formula in effect at that time.

TRS Plan 2 retirement benefits are vested after an employee completes five years of eligible service. Plan 2 members may retire at the age of 65 with five years of service, or at the age of 55 with 20 years of service, with an allowance of 2 percent of the AFC per year of service. (AFC is based on the greatest compensation during any eligible consecutive 60-month period.) Plan 2 retirements prior to the age of 65 receive reduced benefits.

If retirement is at age 55 or older with at least 30 years of service, a 3 percent per year reduction applies; otherwise an actuarial reduction will apply. There is no cap on years of service credit; and a COLA is granted (indexed to the Seattle Consumer Price Index), capped at 3 percent annually.

TRS Plan 3 has a dual benefit structure. Employer contributions finance a defined benefit component, and member contributions finance a defined contribution component. The defined benefit portion provides a benefit calculated at 1 percent of the AFC per year of service. (AFC is based on the greatest compensation during any eligible consecutive 60-month period.)

Effective June 7, 2006, TRS Plan 3 members may be vested either after ten years of service or after five years of service, as long as 12 consecutive months of service were accrued after attainment of age 44. Plan 3 retirements prior to the age of 65 receive reduced benefits.

If retirement is at age 55 or older with at least 30 years of service, a 3 percent per year reduction applies; otherwise an actuarial reduction will apply. There is no cap on years of service credit; and Plan 3 provides the same COLA as Plan 2. Refer to section J of this note for a description of the defined contribution component of TRS Plan 3.

TRS Plan 2 and Plan 3 members who work for at least five months of a six-month period, from September through August, and earn 630 hours or more within that six-month period receive six months of service credit.

Plan 2 and Plan 3 members need have only two years of service credit in order to be eligible to purchase up to seven years of service credit for public education experience earned in another state or with the federal government.

TRS Plan 2 and Plan 3 provide disability benefits. There is no minimum amount of service credit required for eligibility. The Plan 2 allowance amount is 2 percent of the AFC for each year of service. For Plan 3, the allowance amount is 1 percent of the AFC for each year of service. Benefits are actuarially reduced for each year that the member's age is less than 65, and to reflect the choice of a survivor option.

Beneficiaries of a TRS Plan 2 or Plan 3 member with ten years of service who is killed in the course of employment receive retirement benefits without actuarial reduction, if the member was not at normal retirement age at death. This provision applies to any member killed in the course of employment, on or after June 10, 2004, if found eligible by the Director of the Department of Labor and Industries.

TRS members can purchase service credit for military service that interrupts employment. Additionally, TRS members who become totally incapacitated for continued employment while serving in the uniformed services may apply for interruptive military service credit. Should any such member die during this active duty, the member's surviving spouse or eligible children may purchase credit on behalf of the deceased member.

TRS members may purchase up to 24 consecutive months of service credit for each period of temporary duty disability.

TRS members may purchase up to five years of additional service credit once eligible for retirement.

This credit can only be purchased at the time of retirement, and cannot be used to qualify for any retirement eligibility or benefit reductions based upon years of service. This credit is to be used exclusively to provide the member with a monthly annuity that is paid in addition to the member's retirement allowance.

Active TRS Plan 2 and Plan 3 members may also make a one-time purchase of up to seven years of service credit for education experience earned in a state or federal public school outside the state of Washington. Completion of at least five years of service under TRS is required.

A $150,000 death benefit is provided to the estate (or duly designated nominee) of a TRS member who dies in the line of service as a result of injuries sustained in the course of employment, or if the death resulted from an occupational disease or infection that arose naturally and proximately out of their covered employment or duty related illness, if found eligible by the Director of the Department of Labor and Industries.

Portability of retirement benefits allows for TRS members' compensation that is reportable in all dual members' systems, except in WSPRS, to be included in the calculation of all dual members' benefits, and removing the "maximum benefit rule" for dual members who have less than 15 years of service in one capped plan and service in one uncapped plan.

Effective after the January 2008 distribution, gain sharing for TRS Plan 1 and Plan 3 members was discontinued. Additional COLAs were provided to TRS Plan 1 retirees in July 2009 and new alternative early retirement provisions were created for TRS Plan 2 and Plan 3 members.

Beginning January 1, 2007 through December 31, 2007, judicial members of TRS were given the choice to participate in the Judicial Benefit Multiplier (JBM) Program enacted in 2006.

Justices or judges in TRS Plan 1 were able to make a one-time irrevocable election to pay increased contributions that would fund a retirement benefit with a 3.5 percent multiplier. The benefit would be capped at 75 percent of AFC.

Members who chose to participate would:

- Accrue service credit at the higher multiplier beginning with the date of their election.
- Be subject to the benefit cap of 75 percent of AFC.
- Stop contributing to the Judicial Retirement Account (JRA).
- Pay higher contributions.
- Be given the option to increase the multiplier on past judicial service.

Members who did not choose to participate would:

- Continue to accrue service credit at the regular multiplier (i.e. 2 percent).
- Continue to participate in JRA, if applicable.
- Never be a participant in the JBM program.
- Continue to pay contributions at the regular TRS rate.

Newly elected justices and judges who chose to become TRS members on or after January 1, 2007, or who had not previously opted into TRS membership, were required to participate in the JBM program. Members required to join the JBM program would:

- Return to prior TRS Plan if membership had previously been established.
- Accrue the higher multiplier for all judicial service.
- Not contribute to JRA.
- Not have the option to increase the multiplier for past judicial service.

Material changes in TRS benefit provisions for the fiscal year ended June 30, 2010, are listed in the table at the end of this section.

### School Employees' Retirement System (SERS)

The Legislature established SERS in 2000. Membership in the system includes all classified employees of school districts or educational service districts. SERS is comprised principally of non-state employees. SERS retirement benefit provisions are established in chapters 41.34 and 41.35 RCW and may be amended only by the state Legislature.

SERS is a cost-sharing multiple-employer retirement system comprised of two separate plans for membership purposes: Plan 2 is a defined benefit plan and Plan 3 is a combination defined benefit/defined contribution plan.

As of September 1, 2000, the membership of classified school employees in PERS Plan 2 was transferred to SERS Plan 2. Those who joined on or after October 1, 1977, and by August 31, 2000, are SERS Plan 2 members unless they exercised an option to transfer their membership to Plan 3.

SERS participants joining the system on or after September 1, 2000, and those who exercised their transfer option, are members of SERS Plan 3.

SERS members hired on or after July 1, 2007 have 90 days to make an irrevocable choice to enroll in either Plan 2 or Plan 3. An employee is reported in Plan 2 until a choice is made. Employees who fail to choose within 90 days default to SERS Plan 3. Notwithstanding, SERS Plan 2 and Plan 3 members may opt out of plan membership if terminally ill, with less than five years to live.

SERS is comprised of and reported as two separate plans: Plan 2/3 and Plan 3. Plan 2/3 accounts for the defined benefits of Plan 2 members and the defined benefit portion of benefits for Plan 3 members. Plan 3 accounts for the defined contribution portion of benefits for Plan 3 members.

Although members can only be a member of either Plan 2 or Plan 3, the defined benefit portions of Plan 2 and Plan 3 are accounted for in the same pension trust fund. All assets of this Plan 2/3 defined benefit plan may legally be used to pay the defined benefits of any of the Plan 2 or Plan 3 members or beneficiaries, as defined by the terms of the plan.

SERS defined benefit retirement benefits are financed from a combination of investment earnings and employer and employee contributions. Employee contributions to the SERS Plan 2 defined benefit plan accrue interest at a rate specified by DRS. During Fiscal Year 2010, the DRS-established rate on employee contributions was 5.5 percent compounded quarterly.

Employees in SERS Plan 2 can elect to withdraw total employee contributions and interest thereon upon separation from SERS-covered employment. SERS Plan 3 defined contribution benefits are financed from employee contributions and investment earnings.

Employees in SERS Plan 3 can elect to withdraw total employee contributions adjusted by earnings and losses from the investment of those contributions upon separation from SERS-covered employment.

SERS Plan 2 retirement benefits are vested after an employee completes five years of eligible service. Plan 2 members may retire at the age of 65 with five years of service, or at the age of 55 with 20 years of service, with an allowance of 2 percent of the average final compensation (AFC) per year of service. (AFC is based on the greatest compensation during any eligible consecutive 60-month period.)

Plan 2 retirements prior to the age of 65 receive reduced benefits. If retirement is at age 55 or older with at least 30 years of service, a 3 percent per year reduction applies; otherwise an actuarial reduction will apply. The benefit is also actuarially reduced to reflect the choice of a survivor option. There is no cap on years of service credit; and a COLA is granted (indexed to the Seattle Consumer Price Index), capped at 3 percent annually.

SERS Plan 3 has a dual benefit structure. Employer contributions finance a defined benefit component, and member contributions finance a defined contribution component. The defined benefit portion provides a benefit calculated at 1 percent of the AFC per year of service. (AFC is based on the greatest compensation during any eligible consecutive 60-month period.)

Effective June 7, 2006, SERS Plan 3 members are vested in the defined benefit portion of their plan after ten years of service; or after 5 years of service if 12 months of that service are earned after age 44; or after five service credit years earned in PERS Plan 2 by September 1, 2000. Plan 3 members are immediately vested in the defined contribution portion of their plan. Vested Plan 3 members are eligible to retire with full benefits at the age of 65. SERS Plan 3 members who retire prior to the age of 65 receive reduced benefits.

If retirement is at age 55 or older with at least 30 years of service, a 3 percent per year reduction applies; otherwise an actuarial reduction will apply. The benefit is also actuarially reduced to reflect the choice of a survivor option. There is no cap on years of service credit; and Plan 3 provides the same COLA as Plan 2. Refer to section J of this note for a description of the defined contribution component of SERS Plan 3.

Effective after the January 2008 distribution, gain sharing for SERS Plan 3 members was discontinued and new alternative early retirement provisions were created for SERS Plan 2 and Plan 3 members.

SERS members can purchase service credit for military service that interrupts employment. Additionally, SERS members who become totally incapacitated for continued employment while serving in the uniformed services may apply for interruptive military service credit. Should any such member die during this active duty, the member's surviving spouse or eligible children may purchase service credit on behalf of the deceased member. SERS members may purchase up to 24 consecutive months of service credit for each period of temporary duty disability.

SERS provides disability benefits. There is no minimum amount of service credit required for eligibility. The Plan 2 allowance amount is 2 percent of the AFC for each year of service. For Plan 3 the allowance amount is 1 percent of the AFC for each year of service. Benefits are actuarially reduced for each year that the member's age is less than 65, and to reflect the choice of a survivor option.

Beneficiaries of a SERS member with ten years of service who is killed in the course of employment receive retirement benefits without actuarial reduction, if the member was not at normal retirement age at death. This provision applies to any member killed in the course of employment, on or after June 10, 2004, if found eligible by the Director of the Department of Labor and Industries.

SERS members who apply for early retirement may, at the time of retirement, purchase up to five years of additional service credit. The cost of the additional service credit is the actuarial equivalent value of the resulting increase in the member's benefit.

SERS members may also purchase up to five years of additional service credit once eligible for retirement. This credit can only be purchased at the time of retirement, and cannot be used to qualify for any retirement eligibility or benefit reductions based upon years of service. This credit is to be used exclusively to provide the member with a monthly annuity that is paid in addition to the member's retirement allowance.

SERS members who work for at least five months of a six-month period, from September through August, and earn 630 hours or more within that six-month period receive six months of service credit.

A $150,000 death benefit is provided to the estate (or duly designated nominee) of a SERS member who dies in the line of service as a result of injuries sustained in the course of employment, or if the death resulted from an occupational disease or infection that arose naturally and proximately out of their covered employment, or duty related illness if found eligible by the Director of the Department of Labor and Industries.

Portability of retirement benefits allows for SERS members' compensation that is reportable in all dual members' systems, except in WSPRS, to be included in the calculation of all dual members' benefits, and

removing the "maximum benefit rule" for dual members who have less than 15 years of service in one capped plan and service in one uncapped plan.

Material changes in SERS benefit provisions for the fiscal year ended June 30, 2010, are listed in the table at the end of this section.

### Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF)

LEOFF was established in 1970 by the Legislature. Membership includes all full-time, fully compensated, local law enforcement officers and firefighters, and as of July 24, 2005, those emergency medical technicians who were given the option and chose LEOFF Plan 2 membership.

LEOFF membership is comprised primarily of non-state employees, with Department of Fish and Wildlife enforcement officers who were first included prospectively effective July 27, 2003, being a major exception. LEOFF retirement benefit provisions are established in chapter 41.26 RCW and may be amended only by the state Legislature.

LEOFF is a cost-sharing multiple-employer retirement system comprised of two separate defined benefit plans. LEOFF participants who joined the system by September 30, 1977 are Plan 1 members. Those who joined on or after October 1, 1977, are Plan 2 members.

Effective July 1, 2003, the LEOFF Plan 2 Retirement Board was established by Initiative 790 to provide governance of LEOFF Plan 2. The Board's duties include adopting contribution rates and recommending policy changes to the Legislature for the LEOFF Plan 2 retirement plan.

LEOFF defined benefit retirement benefits are financed from a combination of investment earnings, employer and employee contributions, and a special funding situation in which the state pays through state legislative appropriations. Employee contributions to the LEOFF Plan 1 and 2 defined benefit plans accrue interest at a rate specified by DRS.

During Fiscal Year 2010, the DRS-established rate on employee contributions was 5.5 percent compounded quarterly. Employees in LEOFF Plan 1 and 2 can elect to withdraw total employee contributions and interest earnings thereon upon separation from LEOFF-covered employment.

LEOFF Plan 1 retirement benefits are vested after an employee completes five years of eligible service. Plan 1 members are eligible for retirement with five years of service at the age of 50.

The benefit per year of service calculated as a percent of final average salary (FAS) is as follows:

| Term of Service | Percent of FAS |
|---|---|
| 20+ | 2.0% |
| 10-19 | 1.5% |
| 5-9 | 1.0% |

The FAS is the basic monthly salary received at the time of retirement, provided a member has held the same position or rank for 12 months preceding the date of retirement. Otherwise, it is the average of the highest consecutive 24 months' salary within the last ten years of service. A COLA is granted (indexed to the Seattle Consumer Price Index).

LEOFF Plan 1 provides death and disability benefits. Death benefits for Plan 1 members on active duty consist of the following: (1) If eligible spouse, 50 percent of the FAS, plus 5 percent of FAS for each surviving child, with a limitation on the combined allowances of 60 percent of the FAS; or (2) If no eligible spouse, 30 percent of FAS for the first child plus 10 percent for each additional child, subject to a 60 percent limitation of FAS.

The LEOFF Plan 1 disability allowance is 50 percent of the FAS plus 5 percent for each child up to a maximum of 60 percent. Upon recovery from disability before the age of 50, a member is restored to service with full credit for service while disabled. Upon recovery after the age of 50, the benefit continues as the greater of the member's disability allowance or service retirement allowance.

LEOFF Plan 1 members may purchase up to five years of additional service credit once eligible for retirement. This credit can only be purchased at the time of retirement, and cannot be used to qualify for any retirement eligibility or benefit reductions based upon years of service. This credit is to be used exclusively to provide the member with a monthly annuity that is paid in addition to the member's retirement allowance.

LEOFF Plan 2 members are vested after the completion of five years of eligible service. Plan 2 members may retire at age 50 with 20 years of service, or at the age of 53 with five years of service, with an allowance of 2 percent of the FAS per year of service (FAS is based on the highest consecutive 60 months). Plan 2 members who retire prior to the age of 53 receive reduced benefits.

Benefits are actuarially reduced for each year that the benefit commences prior to age 53 and to reflect the choice of a survivor option. If the member has at least 20 years of service and is age 50, the reduction is 3 percent for each year prior to age 53. There is no cap on years of service credit; and a COLA is granted (based on the Consumer Price Index), capped at 3 percent annually.

LEOFF Plan 2 members may purchase up to five years of additional service credit at retirement. LEOFF Plan 2 members can also purchase service credit for military service that interrupts employment.

Additionally, LEOFF Plan 2 members who become totally incapacitated for continued employment while serving in the uniformed services may apply for interruptive military service credit. Should any such member die during this active duty, the member's surviving spouse or eligible children may purchase credit on behalf of the deceased member.

LEOFF Plan 2 provides disability benefits. There is no minimum amount of service credit required for eligibility. The Plan 2 allowance amount is 2 percent of the FAS for each year of service. Benefits are actuarially reduced for each year that the member's age is less than 53, unless the disability is duty-related, and to reflect the choice of a survivor option.

If the member has at least 20 years of service and is age 50, the reduction is 3 percent for each year prior to age 53. Plan 2 members may purchase up to 24 consecutive months of service credit for each period of temporary duty disability.

For Emergency Medical Technicians who joined LEOFF Plan 2 as a result of 2003 and 2005 legislation, the five year waiting period is waived when they retire due to disability or die.

Members of LEOFF Plan 2 who leave service because of a line of duty disability are allowed to withdraw 150 percent of accumulated member contributions. This withdrawal benefit is not subject to federal income tax.

Alternatively, members of LEOFF Plan 2 who leave service because of a line of duty disability may be eligible to receive a retirement allowance of at least 10 percent of the FAS and 2 percent per year of service beyond five years. The first 10 percent of FAS is not subject to federal income tax.

LEOFF Plan 2 members who are severely disabled in the line of duty and incapable of substantial gainful employment in any capacity in the future, can receive a catastrophic disability benefit from LEOFF Plan 2 equal to 70 percent of their FAS subject to offsets for workers' compensation and Social Security disability benefits received.

LEOFF Plan 2 retirees may return to work in an eligible position covered by another retirement system, choose membership in that system and suspend their pension benefits, or not choose membership and continue receiving pension benefits without interruption.

Beneficiaries of a LEOFF Plan 2 member with ten years of service who is killed in the course of employment receive retirement benefits without actuarial reduction, if the member was not at normal retirement age at death.

This provision applied to any member killed in the course of employment, or after June 10, 2004, if found eligible by the Director of the Department of Labor and Industries.

Beginning in 2011, when state General Fund revenues increase by at least 5 percent over the prior biennium's revenues, the State Treasurer will transfer, subject to legislative appropriation, specific amounts into a Local Public Safety Enhancement Account. Half of this transfer will be proportionately distributed to all jurisdictions with LEOFF Plan 2 members. The other half will be transferred to a LEOFF Retirement System Benefits Improvement Account to fund benefit enhancements for LEOFF Plan 2 members.

Eligible survivors of LEOFF Plan 2 members who are killed in the line of duty are reimbursed for the cost of on-going health care insurance coverage.

A $150,000 death benefit is provided to the estate (or duly designated nominee) of a LEOFF Plan 2 member who dies as a result of injuries sustained in the course of employment or dies from occupational disease or duty-related illness such as an infectious disease or cancer resulting from a job-related exposure, or duty related illness if found eligible by the Director of the Department of Labor and Industries.

Portability of retirement benefits allows for LEOFF Plan 2 members' compensation that is reportable in all dual members' systems, except in WSPRS, to be included in the calculation of all dual members' benefits, and removing the "maximum benefit rule" for dual members who have less than 15 years of service in one capped plan and service in one uncapped plan.

Active LEOFF members can choose whether or not to obtain and pay for Medicare coverage through a "divided referendum" process.

Material changes in LEOFF benefit provisions for the fiscal year ended June 30, 2010, are listed in the table at the end of this section.

### Washington State Patrol Retirement System (WSPRS)

WSPRS was established by the Legislature in 1947. Any commissioned employee of the Washington State Patrol is eligible to participate. WSPRS benefits are established in chapter 43.43 RCW and may be amended only by the state Legislature.

WSPRS is a single-employer defined benefit retirement system. WSPRS participants who joined the system by December 31, 2002, are Plan 1 members. Those who joined on or after January 1, 2003, are Plan 2 members.

For financial reporting and investment purposes, however, both plans are accounted for in the same pension fund.

WSPRS retirement benefits are financed from a combination of investment earnings and employer and employee contributions. Employee contributions to WSPRS accrue interest at a rate specified by DRS.

During Fiscal Year 2010, the DRS-established rate on employee contributions was 5.364 percent annually, compounded monthly. Employees in WSPRS can elect to withdraw total employee contributions and interest earnings thereon upon separation from WSPRS-covered employment.

WSPRS member contribution rates will be no more than 7 percent of pay plus half the cost of any future benefit improvements. Employers will pay the contribution rate required to cover all system costs that are not covered by the member contribution rate. Also a minimum total contribution rate is established for WSPRS, beginning July 1, 2010.

There is no vesting requirement for active WSPRS members. Inactive WSPRS members are vested after the completion of five years of eligible service. Members are eligible for retirement at the age of 55 with five years of service, or after 25 years of service.

The annual pension is 2 percent of the average final salary (AFS), capped at 75 percent, per year of service. A cost-of-living allowance is granted (indexed to the Seattle Consumer Price Index), capped at 3 percent annually. The WSPRS mandatory retirement age is 65, but does not apply to the member serving as chief of the Washington State Patrol.

WSPRS members may purchase up to five years of additional service credit once eligible for retirement. This credit can only be purchased at the time of retirement, and cannot be used to qualify for any retirement eligibility or benefit reductions based upon years of service. This credit is to be used exclusively to provide the member with a monthly annuity that is paid in addition to the member's retirement allowance.

WSPRS benefit provisions include death benefits; however, the system provides no disability benefits. Disability benefits may be available from the Washington State Patrol. If disability benefits are received, the member may be eligible to acquire service credit for the period of disability.

A $150,000 death benefit is provided to the estate (or duly designated nominee) of a WSPRS member who dies as a result of injuries sustained in the course of employment or dies from occupational disease or duty-related illness such as an infectious disease or cancer resulting from a job-related exposure, or duty related illness if found eligible by the Director of the Department of Labor and Industries.

The spouse and dependent children of a WSPRS member who is killed in the course of employment will be reimbursed for any payments of medical premiums to the Washington State Health Care Authority.

For WSPRS Plan 1 members, AFS is based on the average of the two highest-paid service credit years and excludes voluntary overtime.

Death benefits for Plan 1 members on active duty consist of the following: (1) If eligible spouse, 50 percent of the AFS, plus 5 percent of the AFS for each surviving child, with a limitation on the combined allowances of 60 percent of the AFS; or (2) If no eligible spouse, 30 percent of AFS for the first child plus 10 percent for each additional child, subject to a 60 percent limitation of AFS.

For WSPRS Plan 2 members, AFS is based on the average of the five consecutive highest-paid service credit years and excludes both voluntary overtime and cash-outs of annual and holiday leave. At retirement, Plan 2 members also have the option of selecting an actuarially reduced benefit in order to provide for post-retirement survivor benefits.

Death benefits for active-duty Plan 2 members consist of the following: (1) If the member is single or has less than ten years of service, the return of the member's accumulated contributions; or (2) If the member is married, has an eligible child, or has completed ten years of service, a reduced benefit allowance reflecting a joint and 100 percent survivor option or 150 percent of the member's accumulated contributions, at the survivor's option. WSPRS Plan 2 members can purchase service credit for military service that interrupts employment.

Additionally, WSPRS Plan 2 members who become totally incapacitated for continued employment while serving in the uniformed services may apply for interruptive military service credit. Should any such member die during this active duty, the member's surviving spouse or eligible children may purchase credit on behalf of the deceased member.

Beneficiaries of a WSPRS Plan 2 member with ten years of service who is killed in the course of employment receive retirement benefits without actuarial reduction, if the member was not of normal retirement age at death.

This provision applies to any member killed in the course of employment, on or after June 10, 2004, if found eligible by the Director of the Department of Labor and Industries.

Material changes in WSPRS benefit provisions for the fiscal year ended June 30, 2010, are listed in the table at the end of this section.

**Public Safety Employees' Retirement System (PSERS)**

PSERS was created by the 2004 Legislature and became effective July 1, 2006. PSERS pension benefit provisions have been established by chapter 41.37 RCW and may be only amended by the state Legislature. PSERS is a cost-sharing multiple-employer retirement system comprised of a single defined benefit plan, PSERS Plan 2.

PSERS membership includes:

- Full-time employees of a covered employer on or before July 1, 2006, who met at least one of the PSERS eligibility criteria, and elected membership during the election period of July 1, 2006 to September 30, 2006; and,
- Full-time employees hired on or after July 1, 2006 by a covered employer, that meet at least one of the PSERS eligibility criteria.

A "covered employer" is one that participates in PSERS. Covered employers include:

- State of Washington agencies: Department of Corrections, Parks and Recreation Commission, Gambling Commission, Washington State Patrol, Liquor Control Board, and Department of Natural Resources;
- Washington state counties; and,
- Washington cities except for Seattle, Tacoma and Spokane.

To be eligible for PSERS, an employee must work on a full-time basis and:

- Have completed a certified criminal justice training course with authority to arrest, conduct criminal investigations, enforce the criminal laws of Washington, and carry a firearm as part of the job; or
- Have primary responsibility to ensure the custody and security of incarcerated or probationary individuals; or
- Function as a limited authority Washington peace officer, as defined in RCW 10.93.020; or
- Have primary responsibility to supervise eligible members who meet the above criteria.

PSERS defined benefit retirement benefits are financed from a combination of investment earnings and employer and employee contributions. Employee contributions to the PSERS defined benefit plans accrue interest at a rate specified by DRS.

During Fiscal Year 2010, the DRS-established rate on employee contributions was 5.5 percent compounded quarterly. Employees in PSERS can elect to withdraw total employee contributions and interest thereon upon separation from PSERS-covered employment.

PSERS benefits are vested after an employee completes five years of eligible service. PSERS members may retire at the age 65 with five years of service, or at the age of 60 with at least ten years of PSERS service credit, with an allowance of 2 percent of the average final compensation (AFC) per year of service.

The AFC is the monthly average of the member's 60 consecutive highest-paid service credit months, excluding any severance pay such as lump-sum payments for deferred sick leave, vacation or annual leave. Plan 2 retirees prior to the age of 60 receive reduced benefits. If retirement is at age 53 or older with at least 20 years of service, a 3 percent per year reduction for each year between the age at retirement and age 60 applies. There is no cap on years of service credit; and a cost-of-living allowance is granted (indexed to the Seattle Consumer Price Index), capped at 3 percent annually.

PSERS members can purchase service credit for military service that interrupts employment. Additionally, PSERS members who become totally incapacitated for continued employment while serving in the uniformed services may apply for interruptive military service credit. Should any such member die during this active duty, the member's surviving spouse or eligible children may purchase credit on behalf of the deceased member.

PSERS members may also purchase up to five years of additional service credit once eligible for retirement. This credit can only be purchased at the time of retirement, and cannot be used to qualify for any retirement eligibility or benefit reductions based upon years of service. This credit is to be used exclusively to provide the member with a monthly annuity that is paid in addition to the member's retirement allowance.

PSERS provides disability benefits. There is no minimum amount of service credit required for eligibility. Eligibility is based on the member being totally incapacitated for

continued employment with a PSERS employer and leaving that employment as a result of the disability. The disability allowance is 2 percent of the average final compensation (AFC) for each year of service.

AFC is based on the member's 60 consecutive highest creditable months of service. Service credit is the total years and months of service credit at the time the member separates from employment. Benefits are actuarially reduced for each year that the member's age is less than 60 (with ten or more service credit years in PSERS), or less than 65 (with fewer than ten service credit years).

PSERS members may purchase up to 24 consecutive months of service credit (up from 12 months) for each period of temporary duty disability.

Beneficiaries of a PSERS member with ten years of service who is killed in the course of employment receive retirement benefits without actuarial reduction, if the member was not at normal retirement age at death. This provision applies to any member killed in the course of employment, if found eligible by the Director of the Department of Labor and Industries.

A $150,000 death benefit is provided to the estate (or duly designated nominee) of a PSERS member who dies as a result of injuries sustained in the course of employment, or if the death resulted from an occupational disease or infection that arose naturally and proximately out of their covered employment, or duty related illness if found eligible by the Director of the Department of Labor and Industries.

Portability of retirement benefits allows for PSERS members' compensation that is reportable in all dual members' systems, except in WSPRS, to be included in the calculation of all dual members' benefits, and removing the "maximum benefit rule" for dual members who have less than 15 years of service in one capped plan and service in one uncapped plan.

Material changes to PSERS benefit provisions for the fiscal year ended June 30, 2010, are listed in the table at the end of this section.

### Judicial Retirement System (JRS)

JRS was established by the Legislature in 1971. Membership includes judges elected or appointed to the Supreme Court, Court of Appeals, and Superior Courts on or after August 9, 1971. The system was closed to new entrants on July 1, 1988, with new judges joining PERS Plan 2. JRS retirement benefit provisions are established in chapter 2.10 RCW and may be amended only by the state Legislature.

JRS is an agent multiple-employer retirement system comprised of a single defined benefit plan. JRS retirement benefits are financed on a pay-as-you-go basis from a combination of investment earnings, employer contributions, employee contributions, and a special funding situation in which the state pays the remaining contributions.

During Fiscal Year 2010, the DRS established rate on employee contributions was 5.5 percent, compounded quarterly. JRS employees who are vested in the plan may not elect to withdraw their contributions upon termination.

However, any JRS member that left the system before July 1, 1988, or his/her spouse, who was ineligible to receive a benefit at that time, may apply and receive a refund of such contributions from DRS, if said contributions have not been already refunded via a sundry claims appropriation from the state Legislature.

JRS members are eligible for retirement at the age of 60 with 15 years of service, or at the age of 60 after 12 years of service (if the member left office involuntarily) with at least 15 years after beginning judicial service.

The benefit per year of service calculated as a percent of average final compensation (AFC) is the table below. This benefit is capped at 75 percent of AFC, exclusive of cost of living increases.

| Term of Service | Percent of AFC |
|---|---|
| 15+ | 3.5% |
| 10-14 | 3.0% |

Death and disability benefits are also provided. Eligibility for death benefits while on active duty requires ten or more years of service. A monthly spousal benefit is provided which is equal to 50 percent of the benefit a member would have received if retired.

If the member is retired, the surviving spouse receives the greater of 50 percent of the member's retirement benefit or 25 percent of the AFC. For members with ten or more years of service, a disability benefit of 50 percent of AFC is provided.

Material changes in JRS benefit provisions for the fiscal year ended June 30, 2010, are listed in the table at the end of this section.

### Judges' Retirement Fund (Judges)

The Judges' Retirement Fund was created by the Legislature on March 22, 1937 to provide retirement benefits to judges of the Supreme Court, Court of Appeals, or Superior Courts of the state of Washington.

Subsequent legislation required that all judges, first appointed or elected to office on or after August 1, 1971, enter the Judicial Retirement System. Judges' retirement benefit provisions are established in chapter 2.12 RCW and may be amended only by the state Legislature.

The Judges' Retirement Fund is an agent multiple-employer retirement system comprised of a single defined benefit plan. There are currently no active members in this plan.

Retirement benefits were financed on a pay-as-you-go basis from a combination of past employee contributions, past employer contributions, and a special funding situation in which the state paid the remaining contributions. Retirees did not earn interest on their contributions, nor could they elect to withdraw their contributions upon termination.

Judges' members are eligible for retirement at the age of 70 with ten years of service, or at any age with 18 years of service. Members are eligible to receive a partial retirement allowance after 12 years of credited service as a judge. With the exception of a partial retirement allowance, the member receives a benefit equal to one-half of the monthly salary being received as a judge at the time of retirement, or at the end of the term immediately prior to retirement if retirement occurs after the expiration of the member's term in office. A partial retirement allowance is based on the proportion of the member's 12 or more years of service in relation to 18 years of service.

Material changes in benefit provisions for Judges for the fiscal year ended June 30, 2010, are listed in the table at the end of this section.

### The Volunteer Fire Fighters' and Reserve Officers' Relief and Pension Fund (VFFRPF)

The Volunteer Fire Fighters' Relief Act was created by the Legislature in 1935 and the pension portion of the act was added in 1945. Membership in the system requires volunteer firefighter service with a fire department of an electing municipality of Washington State, emergency work as an emergency medical technician with an emergency medical service district, or work as a commissioned reserve law enforcement officer.

Retirement benefits are established in chapter 41.24 RCW and may be amended only by the state Legislature.

VFFRPF is a cost-sharing multiple-employer retirement system that provides death and active duty disability benefits to all members, and optional defined benefit pension plan payments. VFFRPF retirement benefits are financed from a combination of investment earnings, member contributions, municipality contributions, and a special funding situation where the state pays the remaining contributions. Since retirement benefits cover volunteer service, benefits are paid based on years of service not salary. Members are vested after ten years of service. VFFRPF members accrue no interest on contributions and may elect to withdraw their contributions upon termination.

After 25 years of active membership, members having reached the age of 65 and who have paid their annual retirement fee for 25 years are entitled to receive a monthly benefit of $50 plus $10 per year of service. The maximum monthly benefit is $300. Reduced pensions are available for members under the age of 65 or with less than 25 years of service.

Death and active duty disability benefits are provided at no cost to the member. Death benefits in the line of duty consist of a lump sum of $152,000. Funeral and burial expenses are also paid in a lump sum of $2,000 for members on active duty. Members receiving disability benefits at the time of death shall be paid $500.

Members on active duty shall receive disability payments of $2,550 per month for up to six months; thereafter, payments are reduced. Disabled members receive $1,275 per month, their spouse $255, and dependent children $110.

Effective July 22, 2007, vocational rehabilitation may be paid for disabled members who are unable to return to their previous employment. Members that qualify are subject to a $4,000 maximum limit and are required to follow certain conditions established by the board and authorized by chapter 41.24 RCW.

Effective July 1, 2001, the disability income benefits and the maximum survivor benefits under the Relief Plan are increased for increases in the Consumer Price Index.

Material changes in VFFRPF benefit provisions for the fiscal year ended June 30, 2010, are listed in the table at the end of this section.

**Material Legislative Changes to Pension Plans**
For the Fiscal Year Ended June 30, 2010

| System/Plan Affected | Effective Date | Description of the changes |
|---|---|---|
| LEOFF 1, PERS, PSERS, SERS, TRS, and WSPRS | 7/1/09 | The actuarial method of funding the unfunded liability of PERS 1 and TRS 1 is restructured. Changes are also made to the demographic assumptions for, and pension contribution rates of, the state retirement systems/plans (with the exception of LEOFF 2). Additionally, the implementation of minimum contribution rats for WSPRS and the Plans 2 and 3 (except for LEOFF 2) is delayed until the 2011-13 biennium (Chapter 561, Laws of 2009). |
| LEOFF 2 | 7/26/09 | Eligible service and disability retirements are now classified as Occupational Disability retirements for the purpose of allowing affected retirees to take advantage of favorable tax treatment on their pension befit based on the first 10 percent of the members salary (Chapter 95, Laws of 2009). |
| PERS 1 | 7/26/09 | The survivor of any PERS 1 member who qualifies for retirement but has not applied, or who has 10 years of service credit, now has the option of either a monthly survivor benefit or the lump sum of contributions plus interest, upon the member's death (Chapter 111, Laws of 2009). |
| LEOFF 2 | 7/26/09 | Department of Fish and Wildlife Enforcement Officers can transfer service credit earned as an enforcement officer in PERS 2 or 3 to LEOFF 2. Member, employer and state contributions will increase to the extent necessary to fund the difference in the value of the service credit transferred between the plans and the member contributions transferred into LEOFF 2 (Chapter 157, Laws of 2009). |
| LEOFF 2, PERS 2/3, SERS 2/3, TRS 2/3, and WSPRS | 7/26/09 | Up to five years of no-cost service credit is available for members who can provide proof to DRS that their public employment was interrupted by military service that occurred during a period of war (as defined in statute), and that they initiated the process for re-employment with the same employer no later than 90 days from the date of their honorable discharge. Members who previously purchased military service credit are eligible to receive a refund of their contributions (Chapter 205, Laws of 2009). |
| PERS 2 and SERS 2 | 7/26/09 | The automatic transfer of prior PERS 2 service to SERS 2 service when the member becomes employed in an eligible SERS position on or after August 1, 2009 is ended. Current and inactive SERS 2 members who had prior PERS service credit transferred to SERS 2 can request beginning September 1, 2009 through November 30, 2009, that their service credit be moved back to PERS 2 (Chapter 209, Laws of 2009). |
| LEOFF, PERS, PSERS, SERS, TRS and WSPRS | 7/26/09 | The eligibility for an unreduced benefit to survivors of members who leave an employer and die while honorably serving in the National Guard or military reserves during a period of war (as defined in statute) is extended (Chapter 226, Laws of 2009). |
| All Systems and Plans | 7/26/09 – 1/1/14 | Domestic partners registered with the state will be treated the same as married spouses, to the extent that treatment is not in conflict with federal laws (Chapter 521, Laws of 2009). |
| WSPRS 2 | 7/26/09 | State-registered domestic partners of WSPRS members are granted the ability to receive the survivor and death benefits available to spouses (Chapter 522, Laws of 2009). |
| LEOFF 2 | 7/26/09 | Domestic partners of LEOFF 2 members are granted the same rights and options as spouses (Chapter 523, Laws of 2009). |
| LEOFF 2 | 3/17/10 | The Director of Fire Protection, who was previously a member of LEOFF 2, now has the choice to continue membership in LEOFF 2 while employed in this role. This position is otherwise covered by PERS (Chapter 80, Laws of 2010). |
| PERS System | 6/10/10 | Eligible employees of the Higher Education Coordinating Board now have the ability to participate in the Higher Education Retirement Plan instead of the Public Employees' Retirement System (Chapter 21, Laws of 2010). |

**Material Legislative Changes to Pension Plans (concluded)**
For the Fiscal Year Ended June 30, 2010

| System/Plan Affected | Effective Date | Description of the changes |
|---|---|---|
| LEOFF 2 | 6/10/10 | Shared leave can now be treated as reportable compensation for LEOFF 2 members. Earnings can be used in the calculation of a member's benefit, and service credit will be earned according to the hours reported (Chapter 50, Laws of 2010). |
| PERS 2/3, SERS 2/3 | 6/10/10 | Half-time service credit is now granted to qualifying members who worked for an educational employer in school years prior to January 1, 1987 (Chapter 103, Laws of 2010). |
| LEOFF 2 and WSPRS | 6/10/10 | The payment of medical insurance premiums for qualifying LEOFF 2 and WSPRS members who are catastrophically disabled in the line of duty, and their spouses and dependent children will now be made by the LEOFF 2 pension fund for LEOFF 2 members and by the Washington State Patrol for WSPRS members (Chapter 259, Laws of 2010). |
| LEOFF 1 and PERS 1 | 6/10/10 | PERS 1 members who retired on or after January 1, 1998, can use any service transferred from LEOFF 1 to qualify for military service credit at no cost (Chapter 260, Laws of 2010). |
| LEOFF and WSPRS | 6/10/10 | Additional benefits are provided to survivors of police officers, fire fighters and State Patrol officers killed in the line of duty (Chapter 261, Laws of 2010). |
| PERS 3, SERS 3, and TRS 3 | 6/30/10 – 6/30/11 | The Employee Retirement Benefits Board is abolished and its former duties are transferred to the DRS Director. Said duties include providing recommendations to the WSIB on self-directed investment options for defined contribution plans, determining the payment options for plan 3 members, ratifying administrative charges assessed to members who participate in self-directed investment options and providing recommendations on investment options for the Deferred Compensation Plan (Chapter 7, Laws of 2010). |

## C. FUNDING POLICIES

With the exception of LEOFF Plan 2, the Legislature provided for minimum contribution rates for all retirement plans (Chapter 561, Laws of 2009). The LEOFF 2 Board provided for minimum contribution rates for the LEOFF Plan 2. These minimum rates will go into effect beginning with the 2011-13 biennium.

The table at the end of this section provides the required contribution rates for all plans (expressed as a percentage of current year covered payroll) at the close of Fiscal Year 2010.

### Public Employees' Retirement System (PERS)

Each biennium, the state Pension Funding Council adopts Plan 1 employer contribution rates, Plan 2 employer and employee contribution rates, and Plan 3 employer contribution rates. Employee contribution rates for Plan 1 are established by statute at 6 percent for state agencies and local government unit employees, and at 7.5 percent for state government elected officials.

The employer and employee contribution rates for Plan 2 and the employer contribution rate for Plan 3 are developed by the Office of the State Actuary to fully fund Plan 2 and the defined benefit portion of Plan 3. All employers are required to contribute at the level established by the Legislature. Under PERS Plan 3, employer contributions finance the defined benefit portion of the plan and member contributions finance the defined contribution portion.

The Director of DRS sets Plan 3 employee contribution rates. Six rate options are available ranging from 5 to 15 percent; two of the options are graduated rates dependent on the employee's age.

As a result of the implementation of the Judicial Benefit Multiplier (JBM) Program in January 2007, a second tier of employer and employee rates were developed to fund, along with investment earnings, the increased retirement benefits of those justices and judges that participate in the program.

The methods used to determine the contribution requirements are established under state statute in accordance with chapters 41.40 and 41.45 RCW.

### Teachers' Retirement System (TRS)

Each biennium the state Pension Funding Council adopts Plan 1 employer contribution rates, Plan 2 employer and employee contribution rates, and Plan 3 employer contribution rates.

Employee contribution rates for Plan 1 are established by statute at 6 percent for state agencies and local government unit employees, and at 7.5 percent for state elected officials.

The employer and employee contribution rates for Plan 2 and the employer contribution rate for Plan 3 are developed by the Office of the State Actuary to fully fund Plan 2 and the defined benefit portion of Plan 3. All employers are required to contribute at the level established by the Legislature.

Under TRS Plan 3, employer contributions finance the defined benefit portion of the plan and member contributions finance the defined contribution portion.

The Director of DRS sets Plan 3 employee contribution rates. Six rate options are available ranging from 5 to 15 percent; two of the options are graduated rates dependent on the employee's age.

The methods used to determine the contribution requirements are established under state statute in accordance with chapters 41.32 and 41.45 RCW.

As a result of the implementation of the Judicial Benefit Multiplier (JBM) Program in January 2007, a second tier of employee rates were developed to fund, along with investment earnings, the increased retirement benefits of those judges that participate in the program.

The required employer contribution rate for a TRS employer of Supreme Court Justices, Court of Appeals Judges and Superior Court Judges equals the TRS contribution rate. The required member contribution rate of TRS 1 Supreme Court Justices, Court of Appeals Judges and Superior Court Judges is the TRS 1 rate of 6 percent plus 3.76 percent of pay. These higher rates, along with investment earnings, are intended to fund the increased retirement benefits of those judges that choose to participate in the JBM program.

### School Employees' Retirement System (SERS)

Each biennium the state Pension Funding Council adopts Plan 2 employer and employee contribution rates and Plan 3 employer contribution rates. The employer and employee contribution rates for Plan 2 and the employer contribution rate for Plan 3 are developed by the Office of the State Actuary to fully fund Plan 2 and the defined benefit portion of Plan 3. All employers are required to contribute at the level established by the Legislature. Under SERS Plan 3, employer contributions finance the defined benefit portion of the plan and member contributions finance the defined contribution portion.

The Director of DRS sets Plan 3 employee contribution rates. Six rate options are available ranging from 5 to 15 percent; two of the options are graduated rates dependent on the employee's age.

The methods used to determine the contribution requirements are established under state statute in chapters 41.35 and 41.45 RCW.

### Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF)

Beginning July 1, 2000, Plan 1 employers and employees are not required to contribute as long as the plan remains fully funded. Employer and employee contribution rates are developed by the Office of the State Actuary to fully fund the plan. Plan 2 employers and employees are required to pay at the level adopted by the LEOFF 2 Board. All employers are required to contribute at the level required by state statute.

The Legislature, by means of a special funding arrangement, appropriated money from the state General Fund to supplement the current service liability and fund the prior service costs of Plan 1 and Plan 2 in accordance with the requirements of the Pension Funding Council and the LEOFF 2 Board.

However, this special funding situation is not mandated by the State Constitution and this funding requirement could be returned to the employers by a change of statute. For Fiscal Year 2010, the state contributed $51.4 million to LEOFF Plan 2.

### Washington State Patrol Retirement System (WSPRS)

Each biennium, the state Pension Funding Council adopts the employee and the state contribution rates. The employee and the state contribution rates are developed by the Office of the State Actuary to fully fund the plan.

State statute also requires employees to contribute at a rate of at least 2 percent. The methods used to determine the contribution requirements are established under state statute in accordance with chapters 43.43 and 41.45 RCW.

### Public Safety Employees' Retirement System (PSERS)

Each biennium the state Pension Funding Council adopts Plan 2 employers and employee contribution rates. The employer and employee contribution rates for Plan 2 are developed by the Office of the State Actuary to fully fund Plan 2. All employers are required to contribute at the level established by the Legislature. The methods used to determine the contribution requirements are established under state statute in chapters 41.37 and 41.45 RCW.

### Judicial Retirement System (JRS)

Contributions made are based on rates set in chapter 2.10 RCW. By statute, employees are required to contribute 7.5 percent with an equal amount contributed by the state. In addition, the state guarantees the solvency of the JRS on a pay-as-you-go basis. Each biennium, the Legislature, through biennial appropriations from the state General Fund, contributes amounts sufficient to meet benefit payment requirements. For Fiscal Year 2010, the state contributed $ 11.6 million.

### Judges' Retirement Fund (Judges)

Contributions made are based on rates set in chapter 2.12 RCW. By statute, employees are required to contribute 6.5 percent with an equal amount contributed by the state. In addition, the state guarantees the solvency of the Judges' Retirement Fund on a pay-as-you-go basis. As of June 30, 2008, there are no active members remaining in the Judges Retirement Fund and member contributions are no longer collected. Each biennium, the Legislature, through biennial appropriations from the state General Fund, contributes amounts sufficient to meet benefit payment requirements. For Fiscal Year 2010, however, no appropriations or contributions were made.

### The Volunteer Fire Fighters' and Reserve Officers' Relief and Pension Fund (VFFRPF)

The retirement provisions of VFFRPF is funded through member contributions of $30 per year, employer contributions of $30 per year, and 40 percent of the Fire Insurance Premium Tax, as per chapter 41.24 RCW.

VFFRPF members earn no interest on contributions and may elect to withdraw their contributions upon termination.

Administrative expenses are funded through fire insurance premium taxes and are maintained in a separate fund. Amounts not needed for administrative expenses are transferred to VFFRPF.

Required contribution rates (expressed as a percentage of current year covered payroll) for all retirement plans at the close of Fiscal Year 2010 were as follows:

| Actual Contribution Rates | Employer | | | Employee | | |
|---|---|---|---|---|---|---|
| | Plan 1 | Plan 2 | Plan 3 | Plan 1 | Plan 2 | Plan 3 |
| **PERS** | | | | | | |
| **Members Not Participating in JBM** | | | | | | |
| State agencies* | 5.31% | 5.31% | 5.31%** | 6.00% | 3.90% | *** |
| Local governmental units* | 5.31% | 5.31% | 5.31% | 6.00% | 3.90% | *** |
| State gov't elected officials* | 7.89% | 5.31% | 5.31%** | 7.50% | 3.90% | *** |
| **Members Participating in JBM** | | | | | | |
| State agencies* | 7.81% | 7.81% | 7.81%** | 9.76% | 7.25% | 7.50%**** |
| Local governmental units* | 5.31% | 5.31% | 5.31%** | 12.26% | 9.75% | 7.50%**** |
| **TRS** | | | | | | |
| **Members Not Participating in JBM** | | | | | | |
| State agencies* | 6.14% | 6.14% | 6.14%** | 6.00% | 3.36% | *** |
| Local governmental units* | 6.14% | 6.14% | 6.14%** | 6.00% | 3.36% | *** |
| State gov't elected officials* | 6.14% | 6.14% | 6.14%** | 7.50% | 3.36% | *** |
| **Members Participating in JBM** | | | | | | |
| State agencies* | 6.14% | n/a | n/a | 9.76% | n/a | n/a |
| **SERS** | | | | | | |
| State agencies* | n/a | 5.44% | 5.44%** | n/a | 3.14% | *** |
| Local governmental units* | n/a | 5.44% | 5.44%** | n/a | 3.14% | *** |
| **LEOFF** | | | | | | |
| Ports and universities* | n/a | 8.62% | n/a | n/a | 8.46% | n/a |
| Local governmental units* | 0.16% | 5.24% | n/a | n/a | 8.46% | n/a |
| State of Washington | n/a | 3.38% | n/a | n/a | n/a | n/a |
| **WSPRS** | | | | | | |
| State agencies* | 6.56% | 6.56% | n/a | 5.08% | 5.08% | n/a |
| **PSERS** | | | | | | |
| State agencies* | n/a | 7.85% | n/a | n/a | 6.55% | n/a |
| Local governmental units* | n/a | 7.85% | n/a | n/a | 6.55% | n/a |

* Includes and administrative expense rate of 0.16%.

** Plan 3 defined benefit portion only.

*** Variable from 5% to 15% based on rate selected by the member.

**** Minimum Rate.

## D. EMPLOYER CONTRIBUTIONS REQUIRED AND PAID

The following table presents the state of Washington's required contributions in millions of dollars to cost-sharing plans in accordance with the funding policy. All contributions required by the funding method were paid.

| | 2010 | 2009 | 2008 |
|---|---|---|---|
| PERS Plan 1 | $78.2 | $169.0 | $115.5 |
| PERS Plan 2/3 | 160.4 | 217.6 | 159.6 |
| TRS Plan 1 | 5.6 | 8.0 | 4.3 |
| TRS Plan 2/3 | 0.8 | 0.8 | 0.5 |
| SERS Plan 2/3 | 0.0 | 0.0 | 0.0 |
| PSERS Plan 2 | 7.8 | 7.7 | 5.9 |
| LEOFF Plan 1 | 0.0 | 0.0 | 0.0 |
| LEOFF Plan 2 | 52.2 | 52.0 | 45.9 |
| VFFRPF | 5.7 | 5.2 | 5.0 |

There are no long-term contracts for contributions for any of the retirement plans administered by the state.

## E. FUNDED STATUS AND FUNDING PROGRESS

The funded status of each plan as of June 30, 2009, the most recent actuarial valuation date, is as follows (dollars in millions):

| | Actuarial Value of Assets (a) | Actuarial Accrued Liability (AAL) Entry Age (b) | Unfunded AAL (UAAL) (b-a) | Funded Ratio (a/b) | Covered Payroll (c) | UAAL as a Percentage of Covered Payroll ((b-a)/c) |
|---|---|---|---|---|---|---|
| PERS Plan 1 | $ 9,775.6 | $ 13,984.5 | $ 4,208.9 | 70% | $ 580.0 | 726% |
| PERS Plan 2/3* | 18,260.4 | 18,397.9 | 137.5 | 99% | 8,132.2 | 2% |
| TRS Plan 1 | 8,146.2 | 10,820.0 | 2,673.8 | 75% | 388.8 | 688% |
| TRS Plan 2/3* | 6,160.0 | 6,048.4 | (111.6) | 102% | 3,957.3 | 0% |
| SERS Plan 2/3* | 2,503.2 | 2,493.2 | (10.0) | 100% | 1,466.5 | 0% |
| LEOFF Plan 1 | 5,612.1 | 4,491.7 | (1,120.4) | 125% | 33.3 | 0% |
| LEOFF Plan 2* | 5,564.2 | 4,629.0 | (935.2) | 120% | 1,442.5 | 0% |
| WSPRS 1/2* | 900.4 | 789.3 | (111.1) | 114% | 83.0 | 0% |
| PSERS 2* | 69.2 | 63.8 | (5.4) | 108% | 223.4 | 0% |
| JRS | 1.8 | 89.3 | 87.5 | 2% | 0.9 | 9,722% |
| Judges | 3.3 | 3.4 | 0.1 | 97% | N/A | N/A |
| VFFRPF | 165.7 | 163.0 | (2.7) | 102% | N/A | N/A |

N/A indicates data not applicable

* These plans use the aggregate actuarial cost method which does not identify or separately amortize unfunded actuarial liabilities. For this reason, the information shown above has been prepared using the entry age actuarial cost method and is intended to serve as a surrogate for the funded status and funding progress of these plans.

Source: Washington State Office of the State Actuary

The Schedules of Funding Progress, presented as Required Supplementary Information (RSI) following the notes to the financial statements, present multi-year trend information about whether the actuarial values of plan assets are increasing or decreasing over time relative to the AALs (Actuarial Accrued Liability) for benefits. Additional information for the state's defined benefit plans as of the latest valuation date is presented on the following pages.

## Defined Benefit Pension Plans Administered by the State

For the Fiscal Year Ended June 30, 2010

The information was determined as part of the actuarial valuations at the dates indicated below. Additional information as of the latest valuation follows.

| | PERS Plan 1 | PERS Plan 2/3 | TRS Plan 1 | TRS Plan 2/3 |
|---|---|---|---|---|
| **Valuation date** | 6/30/2009 | 6/30/2009 | 6/30/2009 | 6/30/2009 |
| **Actuarial cost method** | Entry Age Normal[1] | Aggregate[3] | Entry Age Normal[1] | Aggregate[3] |
| **Amortization method** | | | | |
| Funding | Level %[5] | N/A | Level %[5] | N/A |
| GASB | Level $ | N/A | Level $ | N/A |
| **Remaining amortization period (closed)** | 10-year rolling | N/A | 10-year rolling | N/A |
| **Asset valuation method** | 8-year graded smoothed fair value[9] | 8-year graded smoothed fair value[9] | 8-year graded smoothed fair value[9] | 8-year graded smoothed fair value[9] |
| **Actuarial assumptions** | | | | |
| Investment rate of return[10] | 8.00% | 8.00% | 8.00% | 8.00% |
| Projected salary increases | | | | |
| Salary inflation at 4.5%, plus the merit increases described below[6]: | | | | |
| Initial salary merit (grades down to 0%) | 6.1% | 6.1% | 5.8% | 5.8% |
| Merit period (years of service) | 17 yrs | 17 yrs | 26 yrs | 26 yrs |
| **Includes inflation at** | N/A | 3.50% | N/A | 3.50% |
| **Cost of living adjustments** | Uniform COLA[7] | CPI increase, maximum 3% | Uniform COLA[7] | CPI increase, maximum 3% |

N/A indicates data not applicable.

[1] Based on a variation of the Entry Age Normal (EAN) cost method

[2] Based on a variation of the Frozen Initial Liability (FIL) cost method.

[3] The aggregate cost method does not identify or separately amortize unfunded actuarial liabilities.

[4] Pay-As-You-Go basis for funding.

[5] Level percent of payroll, including system growth.

[6] LEOFF Plan 2 assumes 4.5% of salary inflation

[7] The Uniform COLA - Generally, all retirees over age 66 receive an increase in their monthly benefit at least once a year. The Uniform COLA amount is calculated as the last unrounded Uniform COLA amount increased by 3%, rounded to the nearest penny. These are some historical monthly COLA amounts per year of service:

| Date | Uniform COLA |
|---|---|
| 7/1/2003 | $1.18 |
| 7/1/2004 | $1.21 |
| 7/1/2005 | $1.25 |
| 7/1/2006 | $1.29 |
| 7/1/2007 | $1.33 |
| 7/1/2008 | $1.73 |
| 7/1/2009 | $1.83 |
| 7/1/2010 | $1.88 |

| SERS Plan 2/3 | LEOFF Plan 1 | LEOFF Plan 2 | PSERS Plan 2 | VFFRPF[8] |
|---|---|---|---|---|
| 6/30/2009 | 6/30/2009 | 6/30/2009 | 6/30/2009 | 6/30/2009 |
| Aggregate[3] | Frozen Initial Liability[2] | Aggregate[3] | Aggregate[3] | Entry Age[4] |
| N/A | Level %[5] | N/A | N/A | Level $ |
| N/A | Level $ | N/A | N/A | Level $ |
| N/A | 7/01/2008 - 6/30/2024 | N/A | N/A | 15-year rolling |
| 8-year graded smoothed fair value[9] | 8-year graded smoothed fair value[9] | 8-year graded smoothed fair value[9] | 8-year graded smoothed fair value[9] | 8-year smoothed fair value[9] |
| 8.00% | 8.00% | 8.00% | 8.00% | 7.00% |
| 6.9% | 11.0% | 11.0% | 6.1% | N/A |
| 20 yrs | 21 yrs | 21 yrs | 17 yrs | N/A |
| 3.50% CPI increase, maximum 3% | 3.50% CPI increase | 3.50% CPI increase maximum 3% | 3.50% CPI increase, maximum 3% | N/A None |

[8] VFFRPF uses the Entry Age Funding Method for pensions, and the Pay-As-You-Go Method for the relief costs.

[9] Asset Valuation Method (8 year smoothed fair value): The actuarial value of assets is calculated under an adjusted market value method by starting with the market value of assets. For subsequent years the actuarial value of assets is determined by adjusting the market value of assets to reflect the difference between the actual investment return and the expected investment return during each of the last 8 years or, if fewer, the completed years since adoption, at the following rates per year (annual recognition). The actuarial value of assets is subject to a 30% market value corridor, so it will lie between 70% and 130% of the market value of assets.

| Annual Gain/Loss | | | Annual Gain/Loss | | |
|---|---|---|---|---|---|
| Rate of Return | Smoothing Period | Annual Recognition | Rate of Return | Smoothing Period | Annual Recognition |
| 15% and up | 8 years | 12.50% | 6-7% | 2 years | 50.00% |
| 14-15% | 7 years | 14.29% | 5-6% | 3 years | 33.33% |
| 13-14% | 6 years | 16.67% | 4-5% | 4 years | 25.00% |
| 12-13% | 5 years | 20.00% | 3-4% | 5 years | 20.00% |
| 11-12% | 4 years | 25.00% | 2-3% | 6 years | 16.67% |
| 10-11% | 3 years | 33.33% | 1-2% | 7 years | 14.29% |
| 9-10% | 2 years | 50.00% | 1% and lower | 8 years | 12.50% |
| 7-9% | 1 year | 100.00% | | | |

[10] With the exception of the VFFRPF, the legislature prescribes the assumed rate of investment return for all plans. The VFFRPF Annual Gain/Loss is set at a 7% assumed rate of return.

## F. ANNUAL PENSION COST AND OTHER RELATED INFORMATION

Current year annual pension cost, net pension obligation (NPO) and related information for the current year for the state's single employer and agent multiple-employer defined benefit plans are as follows (dollars in millions):

| | WSPRS*** | JRS | Judges |
|---|---|---|---|
| **Annual Pension Cost and Net Pension Obligation:** | | | |
| Annual required contribution | $ 6.6 | $ 20.4 | $ - |
| Interest on NPO | (1.1) | 5.9 | (0.1) |
| Adjustment to annual required contribution | 1.6 | (17.2) | 0.3 |
| Annual pension cost | 7.1 | 9.1 | 0.2 |
| Less: Contributions made | 5.3 | 11.6 | - |
| Increase (decrease) in NPO | 1.8 | (2.5) | 0.2 |
| NPO at beginning of year | (13.2) | 74.3 | (1.3) |
| NPO at end of year | $(11.4) | $71.8 | $(1.1) |
| **Actuarial assumptions:** | | | |
| Valuation date | 6/30/09 | 6/30/09 | 6/30/09 |
| Actuarial cost method | Aggregate* | Entry age | Entry age |
| Amortization method | n/a | Level $ | Level $ |
| Remaining amortization period (closed) | n/a | 5-year rolling | 5-year rolling |
| Asset valuation method | 8 year graded smoothed fair value | Market | Market |
| Investment rate of return**** | 8% | 8% | 8% |
| Projected salary increases | 4.0%** | 4.0% | N/A |
| Includes inflation at | 3.5% | 3.5% | 3.5% |
| Cost-of-living adjustments | CPI increase, maximum 3% | CPI increase, maximum 3% | none |

* The aggregate cost method does not identify or separately amortize unfunded actuarial accrued liabilities.

** WSPRS also assumes a variable salary merit increase for a merit period of 25 years.

*** Revised NPO at beginning of year for WSPRS (reported at end of prior year at $(13.5).

****The Legislature prescribes the assumed rate of investment return.

## G. THREE YEAR HISTORICAL TREND INFORMATION

The following table presents three-year trend information in millions for the plans listed:

| | 2010 | 2009 | 2008 |
|---|---|---|---|
| **WSPRS** | | | |
| Annual pension cost | $ 7.1 | $ 5.0 | $ 7.5 |
| % of APC contributed | 74.2 | 127.4 | 89.2 |
| NPO | $(11.4) | $(13.4) | $(12.7) |
| **JRS** | | | |
| Annual pension cost | $ 9.1 | $ 9.8 | $ 12.2 |
| % of APC contributed | 127.5 | 105.1 | 79.5 |
| NPO | $ 71.8 | $ 74.3 | $ 74.8 |
| **Judges** | | | |
| Annual pension cost | $ 0.2 | $ 0.2 | $ 0.5 |
| % of APC contributed | 0.0 | 0.0 | 0.0 |
| NPO | $ (1.1) | $ (1.3) | $ (1.5) |

There are no long-term contracts for contributions for any of the retirement plans administered by the state.

## H. CHANGES IN ACTUARIAL ASSUMPTIONS AND METHODS

The assumed ratio of survivors selecting annuities was increased to reflect changes accordance with Chapters 521, 522 and 523, Laws of 2009 related to domestic partnership benefits.

New benefits for survivors of PERS Plan 1 inactive deaths were implemented in accordance with Chapter 111, Laws of 2009.

The TRS Plan 1 supplemental death benefits were included in the valuation model. In prior valuations the liability was estimated outside the valuation process.

The TRS general salary increase assumption was changed to include the bonuses received by members who attain national board certification.

The assumed ratio of survivors of WSPRS Plan 2 duty-related deaths selecting annuities was changed to 60 percent, regardless of the member's age at death.

The cost reimbursement of medical premiums for LEOFF Plan 2 and WSPRS survivors of duty-related deaths was removed from the pension plan. This cost will be valued separately and future benefits paid from a 401 (h) account.

The LEOFF Plan 2 early retirement factors and joint and survivor factors were updated based on the results of the 2001-2006 demographic experience study adopted by the LEOFF Plan 2 Retirement Board.

A disability assumption experience study was performed for LEOFF Plan 2 based on recent experience data. Both the disability rates and the percent of disabilities assumed to be catastrophic changed.

The LEOFF Plan 2 inactive death benefit was refined in the model to include the survivor's option to select 150 percent of the member's savings in lieu of a monthly benefit.

## I. CHANGES IN BENEFIT PROVISIONS

Legislation as adopted allowing employees of the Higher Education Coordinating Board to participate in the Higher Education Retirement Plan when certain conditions are met (Chapter 21, Laws of 2010).

Half time service credit is granted for members of PERS and SERS Plans 2 and 3 for educational employment prior to January 1, 1987 (Chapter 103, Laws of 2010).

The lump-sum death benefit for members of LEOFF Plan 2 and WSPRS Plan 2 is increased to $214,000 and is automatically adjusted each year by an amount equal to CPI with a 3 percent per year maximum, this applies to all members of LEOFF Plan 2 and WSPRS Plan 2 killed in the course of employment since January 1, 2003 (Chapter 261, Laws of 2010).

The optional lump sum payment payable upon remarriage is increased for LEOFF Plan 2 and PSERS Plan 2 survivors of a member killed in the course of employment from 24 times the monthly allowance that the member was receiving at the time or remarriage to an amount equal to 36 times the monthly allowance (Chapter 261, Laws of 2010).

The disability allowance of a LEOFF Plan 2 member that is totally disabled in the line of duty includes reimbursement for any payments made for employer provided medical insurance after the relevant effective date. This includes medical insurance offered under the federal Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA) and Medicare Parts A and B. For members of WSPRS, the compensation of an officer totally disabled during the line of duty includes reimbursement for any payments of premiums for employer-provided medical insurance. An officer is considered totally disabled for purposes of the reimbursement benefit is he or she is unable to perform any substantial gainful activity due to a condition expected to last at least 12 months. (Chapter 259, Laws of 2010).

LEOFF Plan 1 members who transferred service credit to PERS Plan 1 between July 1, 1997 and July 1, 1998,

are permitted to include the years of transferred service in meeting the 25 years of member service requirement to qualify for up to five years of prior, or non-interruptive, military service (Chapter 260, Laws of 2010).

Employer authorized shared leave received by LEOFF Plan 2 members from a non-state employer, must receive the same treatment in respect to service credit and FAS that a member would normally receive if using accrued annual leave or sick leave. This applies to directly and indirectly transferred leave, such as through a shared leave pool, and includes leave transferred prior to the effective date of the act providing that retirement contributions were made on the shared leave (Chapter 50, Laws of 2010).

The actuarial salary growth assumption used in the PERS, SERS, TRS, PSERS, WSPRS and LEOFF Plan 1 is reduced to 4 percent per year, and contribution rates to cover PERS Plan 1 and TRS Plan 1 UAAL were established to amortize the UAAL over a rolling 10 year period subject to minimum rates (Chapter 561, Laws of 2009).

## J. DEFINED CONTRIBUTION PLANS

### Public Employees' Retirement System Plan 3 (PERS 3)

The Public Employees' Retirement System (PERS) Plan 3 is a combination defined benefit/defined contribution plan administered by the state through the Department of Retirement Systems (DRS).

Eligible employees include: elected officials; state employees; employees of the Supreme, Appeals, and Superior Courts (other than judges currently in a judicial retirement system); employees of legislative committees; community and technical colleges, college and university employees not in national higher education retirement programs; judges of district and municipal courts; and employees of local governments.

PERS participants who joined on or after October 1, 1977, and by either, February 28, 2002, for state and higher education employees, or August 31, 2002, for local government employees, are Plan 2 members unless they exercise an option to transfer their membership to Plan 3.

PERS participants who joined the system on or after March 1, 2002, for state and higher education employees, or September 1, 2002, for local government employees have the irrevocable option of choosing membership in either PERS Plan 2 or PERS Plan 3.
The option must be exercised within 90 days of employment. An employee is reported in Plan 2 until a choice is made. Employees who fail to choose within 90 days default to PERS Plan 3. Refer to section B of this note for PERS plan descriptions.

PERS Plan 3 has a dual benefit structure. Employer contributions finance a defined benefit component, and member contributions finance the defined contribution component. As established by chapter 41.34 RCW, employee contribution rates to the defined contribution component range from 5 to 15 percent of salaries based on member choice. There are currently no requirements for employer contributions to the defined contribution component of PERS Plan 3.

PERS Plan 3 defined contribution retirement benefits are solely dependent upon the results of investment activities. Members may elect to self-direct the investment of their contributions as authorized by the Employee Retirement Benefits Board. Any expenses incurred in conjunction with self-directed investments are to be paid by members. Absent a member's self-direction, PERS Plan 3 investments are made in the same portfolio as that of the PERS 2/3 defined benefit plan.

For Fiscal Year 2010, employee contributions required and made were $92.7 million, and plan refunds paid out were $41.7 million.

### Teachers' Retirement System Plan 3 (TRS 3)

The Teachers' Retirement System (TRS) Plan 3 is a combination defined benefit/defined contribution plan administered by the state through the Department of Retirement Systems (DRS).

Eligibility for membership requires service as a certificated public school employee working in an instructional, administrative or supervisory capacity. TRS participants who joined on or after October 1, 1977, and by June 30, 1996, are Plan 2 members unless they exercised an option to transfer their membership to Plan 3. TRS participants joining the system on or after July 1, 1996, and those who exercised their transfer option, are members of TRS Plan 3. Refer to section B of this note for TRS plan descriptions.

TRS Plan 3 has a dual benefit structure. Employer contributions finance a defined benefit component, and member contributions finance the defined contribution component. As established by chapter 41.34 RCW, employee contribution rates to the defined contribution component range from 5 to 15 percent of salaries based on member choice. There are currently no requirements for employer contributions to the defined contribution component of TRS Plan 3.

TRS Plan 3 defined contribution retirement benefits are solely dependent upon the results of investment

activities. Members may elect to self-direct the investment of their contributions as authorized by the Employee Retirement Benefits Board. Any expenses incurred in conjunction with self-directed investments are to be paid by members. Absent a member's self-direction, TRS Plan 3 investments are made in the same portfolio as that of the TRS 2/3 defined benefit plan.

For Fiscal Year 2010, employee contributions required and made were $254.2 million and plan refunds paid out were $71.7 million.

### School Employees' Retirement System Plan 3 (SERS 3)

The School Employees' Retirement System (SERS) Plan 3 is a combination defined benefit/defined contribution plan administered by the state through the Department of Retirement Systems (DRS).

Eligible employees include classified employees of school districts and educational service districts who joined PERS Plan 2 on or after October 1, 1977, and by August 31, 2000, and were transferred to SERS Plan 2 on September 1, 2000.

Members transferred from PERS Plan 2 to SERS Plan 2 may exercise an option to transfer their membership to SERS Plan 3. SERS participants joining the system on or after September 1, 2000, and before July 1, 2007, are also members of SERS Plan 3. SERS members hired on or after July 1, 2007 have 90 days to choose between SERS Plan 2 and SERS Plan 3. Individuals who fail to make a choice will default to SERS Plan 3. Refer to section B of this note for SERS plan descriptions.

SERS Plan 3 has a dual benefit structure. Employer contributions finance a defined benefit component, and member contributions finance the defined contribution component. As established by chapter 41.34 RCW, employee contribution rates to the defined contribution component range from 5 to 15 percent of salaries based on member choice. There are currently no requirements for employer contributions to the defined contribution component of SERS Plan 3.

SERS Plan 3 defined contribution retirement benefits are solely dependent upon the results of investment activities. Members may elect to self-direct the investment of their contributions as authorized by the Employee Retirement Benefits Board. Any expenses incurred in conjunction with self-directed investments are to be paid by members. Absent a member's self-direction, SERS Plan 3 investments are made in the same portfolio as that of the SERS 2/3 defined benefit plan.

For Fiscal Year 2010, employee contributions required and made were $60.3 million and plan refunds paid out were $33.9 million.

### Judicial Retirement Account (JRA)

The Judicial Retirement Account Plan was established by the Legislature in 1988 to provide supplemental retirement benefits. It is a defined contribution plan administered by the state Administrative Office of the Courts, under the direction of the Board for Judicial Administration.

Membership includes judges elected or appointed to the Supreme Court, Court of Appeals, and Superior Courts, and who are members of PERS for their services as a judge. Vesting is full and immediate. There are three participating employers in JRA.

Member contributions equal 2.5 percent of covered salary and the state, as employer, matches this amount. Contributions are collected by the Administrative Office of the Courts. The employer and employee obligations to contribute are established per chapter 2.14 RCW. Plan provisions and contribution requirements are established in state statute and may be amended only by the State Legislature.

Beginning January 1, 2007 through December 31, 2007 any judicial members of the Public Employees' Retirement System (PERS) and the Teachers' Retirement System (TRS) eligible to participate in JRA were able to make a one-time irrevocable election to discontinue future contributions to JRA, in lieu of prospective contributions to the Judicial Benefit Multiplier Program (JBM).

Beginning January 1, 2007 any newly elected or appointed Supreme Court justice, Court of Appeals judge or Superior Court judge is no longer able to participate in JRA and is enrolled in the JBM (enacted in 2006). As of June 30, 2008, 189 JRA member judges have elected to enroll in JBM.

Current-year covered payroll for JRA employees was $2.5 million for the Fiscal Year ended June 30, 2010. For Fiscal Year 2010, the contribution requirement for JRA was $86 thousand. Actual employer and employee contributions were $43 and $43 thousand respectively. Plan benefits paid out for Fiscal Year 2010 totaled $0.4 million.

A JRA member who separates from judicial service for any reason is entitled to receive a lump-sum distribution of the accumulated contributions. The administrator of JRA may adopt rules establishing other payment options. If a member dies, the amount of accumulated contributions standing to the member's credit at the time of the member's death shall be paid

to the member's estate, or such person or persons, trust or organization as the member has nominated by written designation.

The Administrator of JRA has entered an agreement with DRS for accounting and reporting services, and the Washington State Investment Board (SIB) for investment services. DRS is responsible for all record keeping, accounting, and reporting of member accounts. As of April 2006, DRS also became responsible for collection of JRA contributions.

The SIB has the full power to establish investment policy, develop participant investment options, and manage the investment funds from the JRA plan, consistent with the provisions of RCW 2.14.080 and RCW 43.84.150.

### Higher Education Retirement Plans

The Higher Education Retirement Plans are privately administered defined contribution plans with a supplemental plan component. As authorized by RCW 28B.10, the plans cover higher education faculty and other positions as designated by each institution. The state and regional universities, the state college, and the state community and technical colleges each participate in a plan.

Contributions to the plans are invested in annuity contracts or mutual fund accounts offered by one or more fund sponsors. Benefits from fund sponsors are available upon separation or retirement at the member's option. Employees have, at all times, a 100 percent vested interest in their accumulations.

RCW 28.B.10.400 et. seq. assigns the authority to establish and amend benefit provisions to: the board of regents of the state universities, the boards of trustees of the regional universities and the state college, and the state board for community colleges.

Employee contribution rates, based on age, range from 5 to 10 percent of salary. The employers match the employee contributions. The employer and employee obligations to contribute are established per chapter 28B.10 RCW.

Effective July 29, 2009, domestic partners registered with the state will be treated the same as married spouses, to the extent that treatment is not in conflict with federal laws (Chapter 521, Laws of 2009).

For Fiscal Year 2010, covered payroll was $1.9 billion. Employer and employee contributions were $157.5 and $157.5 million respectively, for a total of $315 million. These contribution amounts represent approximately 8.4 percent each of covered payroll for employers and employees.

The plans have a supplemental payment component which guarantees a minimum retirement benefit based upon a one-time calculation at each employee's retirement date. Institutions make direct payments to qualifying retirees when the retirement benefits provided by the fund sponsors do not meet the benefit goals. The supplemental component is financed on a pay-as-you-go basis.

An actuarial valuation of the supplemental component of the Higher Education Retirement plans was done at the end of Fiscal Year 2009. The previous valuation was performed in 2007.

The Unfunded Actuarial Accrued Liability (UAAL) calculated as of June 30, 2009 and 2007 was $336.5 million and $127.8 million, respectively, and is amortized over a 14.5-year period.

The Annual Required Contribution (ARC) of $43.5 million consists of amortization of the UAL ($25.6 million) and normal cost (or current cost) ($16.8 million).

The UAL and ARC were established using the entry age normal cost method. The actuarial assumptions included an investment rate of return of 6 to 8 percent and projected salary increases ranging from 2 to 4 percent. Approximately $1.8 billion and $1.4 billion of payroll were covered under these plans during 2009 and 2007, respectively.

The following table reflects the activity in the Net Pension Obligation (NPO) for the years ended June 30 (expressed in millions):

| | 2010 | 2009 | 2008 |
|---|---|---|---|
| Annual required contribution | $43.5 | $43.1 | $16.6 |
| Payments to beneficiaries | (3.7) | (1.9) | (1.9) |
| Increase (decrease) in NPO | 39.8 | 41.2 | 14.6 |
| NPO at beginning of year | 79.8 | 38.6 | 24.0 |
| NPO at end of year | $119.6 | $79.8 | $38.6 |

## K. PLAN NET ASSETS AND CHANGES IN PLAN NET ASSETS

The Combining Statement of Plan Net Assets that follows presents the principal components of receivables, investments, and liabilities. The Combining Statement of Changes in Plan Net Assets presents the additions and deductions to plan net assets.

## Combining Statement of Plan Net Assets
## Pension and Other Employee Benefit Funds

June 30, 2010
(expressed in thousands)

continued

| | PERS Plan 1 | PERS Plan 2/3 Defined Benefit | PERS Plan 3 Defined Contribution | TRS Plan 1 | TRS Plan 2/3 Defined Benefit | TRS Plan 3 Defined Contribution |
|---|---|---|---|---|---|---|
| **ASSETS** | | | | | | |
| Cash and pooled investments | $ 40,303 | $ 90,339 | $ 142 | $ 34,431 | $ 44,989 | $ 4,534 |
| Receivables: | | | | | | |
| Employer accounts receivable | 3,603 | 34,456 | 4,260 | 2,952 | 16,782 | 21,842 |
| Member accounts receivable (net of allowance) | 789 | 161 | - | 434 | 4 | - |
| Due from other funds | 5 | 10 | - | 2 | 8 | - |
| Due from other pension and other employee benefit funds | 521 | - | 219 | 583 | - | 17 |
| Interest and dividends | 24,471 | 52,331 | 2,514 | 20,542 | 17,702 | 7,729 |
| Investment trades pending | 521,337 | 1,141,999 | 26,782 | 437,631 | 459,668 | 82,342 |
| Total Receivables | 550,726 | 1,228,957 | 33,775 | 462,144 | 494,164 | 111,930 |
| Investments, Noncurrent: | | | | | | |
| Public equity | 2,660,448 | 5,691,087 | 273,348 | 2,233,284 | 1,925,537 | 2,418,949 |
| Fixed income | 1,703,105 | 3,643,190 | 174,985 | 1,429,653 | 1,232,646 | 537,992 |
| Private equity | 1,964,012 | 4,201,309 | 201,792 | 1,648,668 | 1,421,482 | 620,409 |
| Real estate | 1,083,902 | 2,318,625 | 111,365 | 909,870 | 784,490 | 342,392 |
| Security lending | 531,207 | 1,136,330 | 54,579 | 445,916 | 384,469 | 167,802 |
| Liquidity | 141,248 | 326,283 | 602,657 | 120,975 | 111,289 | 58,893 |
| Tangible assets | 88,407 | 189,116 | 9,083 | 74,212 | 63,986 | 27,927 |
| Total Investments, Noncurrent | 8,172,329 | 17,505,940 | 1,427,809 | 6,862,578 | 5,923,899 | 4,174,364 |
| **Total Assets** | 8,763,358 | 18,825,236 | 1,461,726 | 7,359,153 | 6,463,052 | 4,290,828 |
| **LIABILITIES** | | | | | | |
| Obligations under security lending agreements | 531,207 | 1,136,330 | 54,579 | 445,916 | 384,469 | 167,802 |
| Accrued liabilities | 608,027 | 1,320,167 | 32,770 | 510,919 | 530,861 | 97,702 |
| Due to other funds | 102 | 726 | - | 90 | 414 | - |
| Due to other pension and other employee benefit funds | - | 597 | 5 | - | 583 | 16 |
| Unearned revenues | 148 | 399 | - | 438 | 1 | - |
| **Total Liabilities** | 1,139,484 | 2,458,219 | 87,354 | 957,363 | 916,328 | 265,520 |
| **NET ASSETS** | | | | | | |
| Net assets held in trust for: | | | | | | |
| Pension Benefits (Schedule of Funding Progress by Plan begins on Page 161) | 7,623,874 | 16,367,017 | 1,374,372 | 6,401,790 | 5,546,724 | 4,025,308 |
| Deferred compensation participants | - | - | - | - | - | - |
| **Total Net Assets** | $ 7,623,874 | $ 16,367,017 | $ 1,374,372 | $ 6,401,790 | $ 5,546,724 | $ 4,025,308 |

## Combining Statement of Plan Net Assets
## Pension and Other Employee Benefit Funds

June 30, 2010
(expressed in thousands)

continued

| | SERS Plan 2/3 Defined Benefit | SERS Plan 3 Defined Contribution | LEOFF Plan 1 | LEOFF Plan 2 | WSPRS Plan 1/2 | PSERS Plan 2 |
|---|---|---|---|---|---|---|
| **ASSETS** | | | | | | |
| Cash and pooled investments | $ 17,684 | $ 1,076 | $ 24,268 | $ 27,485 | $ 4,679 | $ 777 |
| Receivables: | | | | | | |
| Employer accounts receivable | 6,438 | 5,192 | 3 | 14,276 | 415 | 1,528 |
| Member accounts receivable (net of allowance) | 2 | - | 44 | 61 | - | - |
| Due from other funds | 6 | - | 2 | 3 | 1 | 1 |
| Due from other pension and other employee benefit funds | 277 | 9 | - | - | - | - |
| Interest and dividends | 7,138 | 2,453 | 14,709 | 16,203 | 2,447 | 283 |
| Investment trades pending | 178,313 | 26,131 | 313,412 | 345,290 | 52,127 | 6,028 |
| Total Receivables | 192,174 | 33,785 | 328,170 | 375,833 | 54,990 | 7,840 |
| Investments, Noncurrent: | | | | | | |
| Public equity | 776,602 | 548,110 | 1,599,381 | 1,762,056 | 266,007 | 30,763 |
| Fixed income | 497,147 | 170,731 | 1,023,855 | 1,127,993 | 170,287 | 19,693 |
| Private equity | 573,308 | 196,886 | 1,180,704 | 1,300,796 | 196,374 | 22,710 |
| Real estate | 316,398 | 108,658 | 651,609 | 717,885 | 108,375 | 12,533 |
| Security lending | 155,063 | 53,252 | 319,346 | 351,827 | 53,113 | 6,142 |
| Liquidity | 44,552 | 18,004 | 86,319 | 109,868 | 14,894 | 4,319 |
| Tangible assets | 25,807 | 8,863 | 53,147 | 58,553 | 8,839 | 1,022 |
| Total Investments, Noncurrent | 2,388,877 | 1,104,504 | 4,914,361 | 5,428,978 | 817,889 | 97,182 |
| **Total Assets** | 2,598,735 | 1,139,365 | 5,266,799 | 5,832,296 | 877,558 | 105,799 |
| **LIABILITIES** | | | | | | |
| Obligations under security lending agreements | 155,063 | 53,252 | 319,346 | 351,827 | 53,113 | 6,142 |
| Accrued liabilities | 206,037 | 32,550 | 362,282 | 398,793 | 60,378 | 6,961 |
| Due to other funds | 173 | 5 | 34 | 164 | 15 | 18 |
| Due to other pension and other employee benefit funds | 115 | 277 | - | - | - | 33 |
| Unearned revenues | 2 | - | - | 99 | - | - |
| **Total Liabilities** | 361,390 | 86,084 | 681,662 | 750,883 | 113,506 | 13,154 |
| **NET ASSETS** | | | | | | |
| Net assets held in trust for: | | | | | | |
| Pension Benefits (Schedule of Funding Progress by Plan begins on Page 161) | 2,237,345 | 1,053,281 | 4,585,137 | 5,081,413 | 764,052 | 92,645 |
| Deferred compensation participants | - | - | - | - | - | - |
| **Total Net Assets** | $ 2,237,345 | $ 1,053,281 | $ 4,585,137 | $ 5,081,413 | $ 764,052 | $ 92,645 |

## Combining Statement of Plan Net Assets
## Pension and Other Employee Benefit Funds

June 30, 2010
(expressed in thousands)

concluded

| | JRS | JRA | Judges | VFFRPF | Deferred Compensation | Total |
|---|---|---|---|---|---|---|
| **ASSETS** | | | | | | |
| Cash and pooled investments | $ 294 | $ 8 | $ 2,811 | $ 21,970 | $ 1,409 | $ 317,199 |
| Receivables: | | | | | | |
| Employer accounts receivable | 5 | - | - | - | - | 111,752 |
| Member accounts receivable (net of allowance) | - | - | - | - | 1,065 | 2,560 |
| Due from other funds | 1 | - | 6 | 17 | 17 | 79 |
| Due from other pension and other employee benefit funds | - | - | - | - | - | 1,626 |
| Interest and dividends | - | - | - | 395 | - | 168,917 |
| Investment trades pending | - | - | - | 8,408 | - | 3,599,468 |
| Total Receivables | 6 | - | 6 | 8,820 | 1,082 | 3,884,402 |
| Investments, Noncurrent: | | | | | | |
| Public equity | - | 11,433 | - | 42,909 | 2,446,418 | 22,686,332 |
| Fixed income | - | - | - | 27,468 | - | 11,758,745 |
| Private equity | - | - | - | 31,676 | - | 13,560,126 |
| Real estate | - | - | - | 17,482 | - | 7,483,584 |
| Security lending | - | - | - | 8,568 | - | 3,667,614 |
| Liquidity | 3,568 | - | 11 | 2,336 | 5 | 1,645,221 |
| Tangible assets | - | - | - | 1,426 | - | 610,388 |
| Total Investments, Noncurrent | 3,568 | 11,433 | 11 | 131,865 | 2,446,423 | 61,412,010 |
| **Total Assets** | 3,868 | 11,441 | 2,828 | 162,655 | 2,448,914 | 65,613,611 |
| **LIABILITIES** | | | | | | |
| Obligations under security lending agreements | - | - | - | 8,568 | - | 3,667,614 |
| Accrued liabilities | 30 | - | 3 | 9,703 | 21 | 4,177,204 |
| Due to other funds | - | - | 3 | 3 | 16 | 1,763 |
| Due to other pension and other employee benefit funds | - | - | - | - | - | 1,626 |
| Unearned revenues | - | - | - | - | - | 1,087 |
| **Total Liabilities** | 30 | - | 6 | 18,274 | 37 | 7,849,294 |
| **NET ASSETS** | | | | | | |
| Net assets held in trust for: | | | | | | |
| Pension Benefits (Schedule of Funding Progress by Plan begins on Page 161) | 3,838 | 11,441 | 2,822 | 144,381 | - | 55,315,440 |
| Deferred compensation participants | - | - | - | - | 2,448,877 | 2,448,877 |
| **Total Net Assets** | $ 3,838 | $ 11,441 | $ 2,822 | $ 144,381 | $ 2,448,877 | $ 57,764,317 |

## Combining Statement of Changes in Plan Net Assets
## Pension and Other Employee Benefit Funds

For the Fiscal Year Ended June 30, 2010
(expressed in thousands)

continued

| | PERS Plan 1 | PERS Plan 2/3 Defined Benefit | PERS Plan 3 Defined Contribution | TRS Plan 1 | TRS Plan 2/3 Defined Benefit | TRS Plan 3 Defined Contribution |
|---|---|---|---|---|---|---|
| **ADDITIONS** | | | | | | |
| Contributions: | | | | | | |
| Employers | $ 154,023 | $ 327,460 | $ - | $ 112,731 | $ 164,959 | $ - |
| Members | 40,995 | 271,550 | 92,665 | 24,631 | 21,694 | 254,197 |
| State | - | - | - | - | - | - |
| Participants | - | - | - | - | - | - |
| Total Contributions | 195,018 | 599,010 | 92,665 | 137,362 | 186,653 | 254,197 |
| Investment Income: | | | | | | |
| Net appreciation (depreciation) in fair value | 779,778 | 1,468,001 | 115,690 | 646,234 | 494,914 | 366,324 |
| Interest and dividends | 232,804 | 467,351 | 23,316 | 194,268 | 157,322 | 70,415 |
| Less: investment expenses | (32,244) | (67,251) | (3,980) | (27,017) | (22,867) | (11,927) |
| Net investment income (loss) | 980,338 | 1,868,101 | 135,026 | 813,485 | 629,369 | 424,812 |
| Transfers from other pension plans | 1 | 11,611 | 4,926 | 5 | 724 | 598 |
| Other additions | - | - | - | - | - | - |
| **Total Additions** | 1,175,357 | 2,478,722 | 232,617 | 950,852 | 816,746 | 679,607 |
| **DEDUCTIONS** | | | | | | |
| Pension benefits | 1,111,386 | 251,765 | 79 | 859,250 | 55,654 | 257 |
| Pension refunds | 4,946 | 31,425 | 41,724 | 1,505 | 2,868 | 71,665 |
| Transfers to other pension plans | 1 | 5,085 | 4,926 | 1 | 198 | 1,084 |
| Administrative expenses | 372 | 698 | - | 175 | 207 | - |
| Distributions to participants | - | - | - | - | - | - |
| **Total Deductions** | 1,116,705 | 288,973 | 46,729 | 860,931 | 58,927 | 73,006 |
| **Net Increase (Decrease)** | 58,652 | 2,189,749 | 185,888 | 89,921 | 757,819 | 606,601 |
| **Net Assets - Beginning** | 7,565,222 | 14,177,268 | 1,188,484 | 6,311,869 | 4,788,905 | 3,418,707 |
| **Net Assets - Ending** | $ 7,623,874 | $ 16,367,017 | $ 1,374,372 | $ 6,401,790 | $ 5,546,724 | $ 4,025,308 |

## Combining Statement of Changes in Plan Net Assets
## Pension and Other Employee Benefit Funds

For the Fiscal Year Ended June 30, 2010
(expressed in thousands)

continued

| | SERS Plan 2/3 Defined Benefit | SERS Plan 3 Defined Contribution | LEOFF Plan 1 | LEOFF Plan 2 | WSPRS Plan 1/2 | PSERS Plan 2 |
|---|---|---|---|---|---|---|
| **ADDITIONS** | | | | | | |
| Contributions: | | | | | | |
| Employers | $ 62,090 | $ - | $ 49 | $ 76,998 | $ 5,271 | $ 15,237 |
| Members | 20,227 | 60,328 | 1,676 | 133,122 | 5,198 | 15,214 |
| State | - | - | - | 51,376 | - | - |
| Participants | - | - | - | - | - | - |
| Total Contributions | 82,317 | 60,328 | 1,725 | 261,496 | 10,469 | 30,451 |
| Investment Income: | | | | | | |
| Net appreciation (depreciation) in fair value | 200,935 | 89,503 | 449,181 | 445,838 | 72,119 | 5,525 |
| Interest and dividends | 63,796 | 22,472 | 136,935 | 143,480 | 22,388 | 2,178 |
| Less: investment expenses | (9,216) | (3,496) | (19,285) | (20,815) | (3,172) | (345) |
| Net investment income (loss) | 255,515 | 108,479 | 566,831 | 568,503 | 91,335 | 7,358 |
| Transfers from other pension plans | 431 | 445 | 112 | 1,010 | 10 | 32 |
| Other additions | - | - | - | - | - | - |
| **Total Additions** | 338,263 | 169,252 | 568,668 | 831,009 | 101,814 | 37,841 |
| **DEDUCTIONS** | | | | | | |
| Pension benefits | 34,449 | 91 | 338,231 | 46,158 | 36,116 | 18 |
| Pension refunds | 2,125 | 33,916 | 14 | 10,947 | 126 | 928 |
| Transfers to other pension plans | 8,082 | 416 | - | 112 | - | - |
| Administrative expenses | 74 | - | 34 | 1,078 | 12 | 7 |
| Distributions to participants | - | - | - | - | - | - |
| **Total Deductions** | 44,730 | 34,423 | 338,279 | 58,295 | 36,254 | 953 |
| **Net Increase (Decrease)** | 293,533 | 134,829 | 230,389 | 772,714 | 65,560 | 36,888 |
| **Net Assets - Beginning** | 1,943,812 | 918,452 | 4,354,748 | 4,308,699 | 698,492 | 55,757 |
| **Net Assets - Ending** | $ 2,237,345 | $ 1,053,281 | $ 4,585,137 | $ 5,081,413 | $ 764,052 | $ 92,645 |

## Combining Statement of Changes in Plan Net Assets
## Pension and Other Employee Benefit Funds

For the Fiscal Year Ended June 30, 2010
(expressed in thousands)

concluded

| | JRS | JRA | Judges | VFFRPF | Deferred Compensation | Total |
|---|---|---|---|---|---|---|
| **ADDITIONS** | | | | | | |
| Contributions: | | | | | | |
| Employers | $ 79 | $ 43 | $ - | $ 1,103 | $ - | $ 920,043 |
| Members | 79 | 43 | - | 45 | - | 941,664 |
| State | 11,570 | - | - | 5,685 | - | 68,631 |
| Participants | - | - | - | - | 185,120 | 185,120 |
| Total Contributions | 11,728 | 86 | - | 6,833 | 185,120 | 2,115,458 |
| Investment Income: | | | | | | |
| Net appreciation (depreciation) in fair value | (2) | 773 | (14) | 9,179 | 162,186 | 5,306,164 |
| Interest and dividends | 17 | 233 | 62 | 3,919 | 45,408 | 1,586,364 |
| Less: investment expenses | (4) | (22) | - | (502) | (4,543) | (226,686) |
| Net investment income (loss) | 11 | 984 | 48 | 12,596 | 203,051 | 6,665,842 |
| Transfers from other pension plans | - | - | - | - | - | 19,905 |
| Other additions | - | 3 | - | - | 1,145 | 1,148 |
| **Total Additions** | 11,739 | 1,073 | 48 | 19,429 | 389,316 | 8,802,353 |
| **DEDUCTIONS** | | | | | | |
| Pension benefits | 9,722 | 389 | 500 | 10,104 | - | 2,754,169 |
| Pension refunds | - | - | - | 18 | - | 202,207 |
| Transfers to other pension plans | - | - | - | - | - | 19,905 |
| Administrative expenses | 1 | - | - | 8 | - | 2,666 |
| Distributions to participants | - | - | - | - | 108,578 | 108,578 |
| **Total Deductions** | 9,723 | 389 | 500 | 10,130 | 108,578 | 3,087,525 |
| **Net Increase (Decrease)** | 2,016 | 684 | (452) | 9,299 | 280,738 | 5,714,828 |
| **Net Assets - Beginning** | 1,822 | 10,757 | 3,274 | 135,082 | 2,168,139 | 52,049,489 |
| **Net Assets - Ending** | $ 3,838 | $ 11,441 | $ 2,822 | $ 144,381 | $ 2,448,877 | $ 57,764,317 |

# Note 12
## Other Postemployment Benefits

### Plan Description and Funding Policy

In addition to pension benefits as described in Note 11, the state, through the Health Care Authority (HCA), administers an agent multiple-employer other postemployment benefit plan (OPEB). Per RCW 41.05.065, the Public Employees Benefits Board (PEBB) created within the Health Care Authority, is authorized to design benefits and determine the terms and conditions of employee and retired employee participation and coverage, including establishment of eligibility criteria for both active and retired employees. PEBB programs include medical, dental, life and long-term disability.

Employers participating in the PEBB plan include the state (which includes general government agencies and higher education institutions), 57 of the state's K-12 schools and educational service districts (ESDs) and 206 political subdivisions and tribal governments. Additionally, the PEBB plan is available to the retirees of the remaining 244 K-12 schools and ESDs. As of June 2010, membership in the PEBB plan consisted of the following:

| | Active Employees | Retirees[1] | Total |
|---|---|---|---|
| State | 111,374 | 26,181 | 137,555 |
| K-12 schools and ESDs[2] | 2,198 | 27,378 | 29,576 |
| Political subdivisions | 11,554 | 1,116 | 12,670 |
| Total | 125,126 | 54,675 | 179,801 |

[1]Retirees include retired employees, surviving spouses, and terminated members entitled to a benefit.
[2]In Fiscal Year 2010, there were 99,239 full-time equivalent active employees in the 244 K-12 schools and ESDs that elected to limit participation in PEBB only to their retirees.

For Fiscal Year 2010, the estimated monthly cost for PEBB benefits for active employees (average across all plans and tiers) is as follows:

| Required Premium[3] | |
|---|---|
| Medical | $758 |
| Dental | 76 |
| Life | 5 |
| Long-term disability | 2 |
| Total | $841 |
| Employer contribution | $755 |
| Employee contribution | 86 |
| Total | $841 |

[3]Per 2010 Index Rate Model 3.3.

The relationship between the PEBB OPEB plan and its member employers and their employees and retirees is not formalized in a contract or plan document. Rather, the benefits are provided in accordance with a substantive plan. A substantive plan is one in which the plan terms are understood by the employers and plan members. This understanding is based on communications between the HCA, employers and plan members and the historical pattern of practice with regard to the sharing of benefit costs.

The PEBB retiree OPEB plan is available to employees who elect to continue coverage and pay the administratively established premiums at the time they retire under the provisions of the retirement system to which they belong. Retirees' access to PEBB plans depends on the retirement eligibility of their respective retirement system. PEBB members are covered in the following retirement systems: PERS, PSERS, TRS, SERS, WSPRS, and Higher Education.

Per RCW 41.05.022, retirees who are not yet eligible for Medicare benefits may continue participation in the state's Non-Medicare community-rated health insurance risk pool on a self-pay basis. Retirees in the Non-Medicare risk pool receive an implicit subsidy. The implicit subsidy exists because retired members pay a premium based on a claims experience for active employees and other Non-Medicare retirees. The subsidy is valued using the difference between the age-based claims costs and the premium. In Calendar Year 2009 the average weighted implicit subsidy was valued at $272 per member per month, and in Calendar Year 2010 the average weighted implicit subsidy is projected to be $273 per member per month.

Retirees who are enrolled in both Parts A and B of Medicare may participate in the state's Medicare community-rated health insurance risk pool. Medicare retirees receive an explicit subsidy in the form of reduced premiums. Annually, the Health Care Authority administrator recommends an amount for the next calendar year's explicit subsidy for inclusion in the Governor's budget. In Calendar Year 2009, the explicit subsidy was $183 per member per month, and in Calendar Year 2010 the explicit subsidy is $183 per member per month.

Retirees participating in the PEBB life insurance program received an explicit subsidy of $5 per member per month in Calendar Year 2009. The explicit subsidy is also $5 per member per month in Calendar Year 2010.

Administrative costs as well as implicit and explicit subsidies are funded by required contributions from participating employers. The subsidies provide monetary assistance for medical and life insurance benefits.

Contributions are set each biennium as part of the budget process. In Fiscal Year 2010, the cost of the subsidies was approximately 6.7 percent of the cost of benefits for active employees. The benefits are funded on a pay-as-you-go basis.

Each participating employer in the plan is required to disclose additional information with regard to funding policy, the employer's annual OPEB costs and contributions made, the funded status and funding progress of the employers individual plan and actuarial methods and assumptions used.

The PEBB OPEB plan is accounted for as an agency fund on an accrual basis. The plan has no investments or other assets. The PEBB OPEB plan does not issue a publicly available financial report.

For information on the results of an actuarial valuation of the employer provided subsidies associated with the PEBB plan, refer to: http://osa.leg.wa.gov/Actuarial_services/OPEB/OPEB.htm.

### Annual OPEB Cost and Net OPEB Obligation

The state's (general government agencies and higher education institutions) annual other postemployment benefit (OPEB) cost (expense) is calculated based on the annual required contribution (ARC) of the state as the employer, an amount actuarially determined in accordance with the parameters of GASB Statement No. 45.

The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed 30 years.

The following tables show the components of the state's annual OPEB cost for Fiscal Year 2010, the amount actually contributed to the plan, and changes in the state's Net OPEB Obligation (NOO) (expressed in thousands):

| | |
|---|---|
| Annual required contribution | $349,326 |
| Interest on Net OPEB Obligation | 22,210 |
| Amortization of Net OPEB Obligation | (17,116) |
| Annual OPEB cost (expense) | 354,420 |
| Contributions made | (70,099) |
| Increase in Net OPEB Obligation | 284,321 |
| Net OPEB Obligation - beginning of year | 493,551 |
| Net OPEB Obligation - end of year* | $777,872 |
| *estimated | |

The state's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for Fiscal Years 2008, 2009 and 2010 were as follows (expressed in thousands):

| Fiscal Year Ended | Annual OPEB Cost | Percentage of Annual OPEB Cost Contributed | Net OPEB Obligation |
|---|---|---|---|
| 6/30/10 | $354,420 | 19.78% | $777,872 |
| 6/30/09 | 334,374 | 25.92% | 493,551 |
| 6/30/08 | 313,970 | 21.69% | 245,855 |

### Funded Status and Funding Progress

The funded status of the plan as of January 1, 2009, the latest date for which information is available, was as follows (expressed in thousands):

| | |
|---|---|
| Actuarial accrued liability (AAL) | $3,786,869 |
| Actuarial value of plan assets | - |
| Unfunded actuarial accrued liability (UAAL) | $3,786,869 |

| | |
|---|---|
| Funded ratio (actuarial value of plan assets/AAL) | 0.00% |
| Covered payroll (active plan members) | $5,678,422 |
| UAAL as a percentage of covered payroll | 66.69% |

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trends. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

### Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the terms of the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

Significant methods and assumptions were as follows:

| | |
|---|---|
| Actuarial valuation date | January 1, 2009 |
| Actuarial cost method | Projected Unit Credit (PUC) |
| Amortization method | Closed, level percentage of projected payroll amortization method |
| Remaining amortization period | 30 years |
| Asset valuation method | n/a - no assets |
| Actuarial assumptions: | |
| Investment rate of return | 4.5% |
| Projected salary increases | 4.5% |
| Health care inflation rate | 7.0% initial rate, 5% ultimate rate in 2067 |
| Inflation rate | 3.5% |

# Note 13
## Commitments and Contingencies

### A. CONSTRUCTION AND OTHER COMMITMENTS

Outstanding commitments related to state infrastructure and facility construction, improvement, and/or renovation totaled $5.3 billion at June 30, 2010.

### B. SUMMARY OF SIGNIFICANT LITIGATION

#### Pending Litigation

The state and its agencies are parties to numerous routine legal proceedings that normally occur in governmental operations. At any given point, there may be numerous lawsuits involving the implementation of specific state programs that could significantly impact expenditures and potentially have future budgetary impact.

The state is the defendant in a number of cases alleging inadequate funding of state programs or services. Claims include: funding inadequacies and inequities in both basic and special education; inadequate funding for care of the disabled and elderly; inadequate funding for the provision of mental health services to children. Collective claims in these programmatic and service cases exceed $350 million. Adverse rulings in these cases could result in significant future costs.

The Department of Revenue routinely has claims for refunds in various stages of administrative and legal review. Claims for refunds are approximately $234 million. In addition, the state is defending cases challenging the constitutionality of certain taxes that fund discrete state programs.

The Washington State Department of Transportation (WSDOT) is a defendant in a number of lawsuits related to environmental clean-up and habitat restoration/enhancement associated with highway construction projects and storm water discharge from state highways. In addition, the Department of Natural Resources is defending contribution claims for clean-up costs connected to runoff from historic mining activity. While estimates are not available for all lawsuits, claims for damages will likely exceed $19 million. If the efforts of the plaintiffs are successful, the financial impact could be significant and would need to be addressed in future budgets.

The state is the defendant in numerous lawsuits by employees accusing the state of various infractions of law or contract. These suits claim back pay and damages in excess of $62 million. Additionally, the state is being sued as a result of the legislative repeal of the gain sharing provision associated with select state pension plans. No reliable estimate of damage is currently available.

The state is contesting these lawsuits and the outcomes are uncertain at this time.

#### Tobacco Settlement

In November 1998, Washington joined 45 other states in a Master Settlement Agreement (MSA) with the nation's largest tobacco manufacturers to provide restitution for monies spent under health care programs for the treatment of smoking-related illnesses.

Washington's share of the settlement was approximately $116.8 million in Fiscal Year 2010 and is subject to various offsets, reductions, and adjustments.

Beginning in 2008, Washington received the first of ten "strategic contribution payments" under the MSA. This payment is subject to the same offsets, reductions, and adjustments as are applicable to the base payment. The 2010 strategic contribution payment was approximately $40.7 million.

In 2006, 2007, 2008, and 2009, determinations were made under a process established by the MSA that disadvantages experienced by manufacturers as a result of participating in the MSA were a significant factor contributing to market share losses by those manufacturers.

These determinations related to sales data for the years 2003, 2004, 2005, and 2006. Washington faces a potential "nonparticipating manufacturer (NPM) adjustment" of between $0 and $130 million for the year 2003, $0 and $137 million for the year 2004, $0 and $131 million for the year 2005, and $0 and $119 million for the year 2006.

Washington and 37 other states each filed court actions seeking a declaration that they had diligently enforced their escrow statutes. In the Consent Decree, the King County Superior Court retained jurisdiction to enforce and interpret the MSA as to Washington.

The participating manufacturers oppose having the diligent enforcement issue decided by numerous state courts. They believe the issue is governed by an arbitration clause in the MSA that they claim requires a panel of arbitrators to decide, in a single national proceeding, whether individual states diligently enforced their own statutes.

The King County Superior Court heard Washington's motion and, in late September 2006, entered an order compelling arbitration and dismissing the state's action. Washington's appeal was dismissed and the trial court's order compelling arbitration is now final. With the exception of Montana, all states will participate in a single national arbitration of the NPM Adjustment dispute.

The dispute will be presented to a three-member panel of retired Article III judges. The panel is in place and some preliminary hearings have been held. Hearings on individual state cases will begin in 2011, but no specific dates for any state hearings have been set.

The arbitration will comprise some presentations made by the states collectively, but each state will also have to respond to claims by the participating manufacturers that the state was not diligent in enforcing its Qualifying Statute and present its individual case for diligence in enforcing its Qualifying Statute. The panel will not issue its decision as to any individual state until the entire arbitration with all states has been completed.

## C. FEDERAL ASSISTANCE

The state has received federal financial assistance for specific purposes that are generally subject to review or audit by the grantor agencies.

Entitlement to this assistance is generally conditional upon compliance with the terms and conditions of grant agreements and applicable federal regulations, including the expenditure of assistance for allowable purposes. Any disallowance resulting from a review or audit may become a liability of the state.

The state does estimate and recognize a claims and judgments liability for disallowances when determined by the grantor agency or for probable disallowances based on experience pertaining to these grants; however, these recognized liabilities and any unrecognized disallowances are considered immaterial to the state's overall financial condition.

## D. ARBITRAGE REBATE

Rebatable arbitrage is defined by the Internal Revenue Service Code Section 148 as earnings on investments purchased from the gross proceeds of a bond issue that are in excess of the amount that would have been earned if the investments were invested at a yield equal to the yield on the bond issue.

The rebatable arbitrage must be paid to the federal government. State agencies and universities responsible for investments from bond proceeds carefully monitor their investments to restrict earnings to a yield less than the bond issue, and therefore limit any state arbitrage liability. The state estimates that rebatable arbitrage liability, if any, will be immaterial to its overall financial condition.

## E. OTHER COMMITMENTS AND CONTINGENCIES

### School Bond Guarantee Program

Washington voters passed a constitutional amendment in November 1999, creating the Washington State School Bond Guarantee Program.

The program's purpose is to provide savings to state taxpayers by pledging the full faith and credit of the state of Washington to the full and timely payment of voter-approved school district general obligation bonds

in the event a school district is unable to make a payment.

The issuing school district remains responsible for the repayment of the bonds, including any payment the state makes under the guarantee.

The State Treasurer introduced the School Bond Guarantee Program in March 2000. At the end of Fiscal Year 2010, the state had guaranteed 211 school districts' voter-approved general obligation debt with 193 districts having a total outstanding principal of $7.97 billion. The state estimates that school bond guarantee liability, if any, will be immaterial to its overall financial condition.

### Local Option Capital Asset Lending Program

On September 1, 1998, the state lease-purchase program was extended to local governments seeking low cost financing of essential equipment. The Local Option Capital Assets Lending (LOCAL) program allows local governments to pool their financing requests together with Washington State agencies in Certificates of Participation (COPs). Refer to Note 7.B for the state's COP disclosure.

These COPs do not constitute a debt or pledge of the faith and credit of the state; rather, local governments pledge their full faith and credit in a general obligation pledge.

In the event that any local government fails to make any payment, the state is obligated to withhold an amount sufficient to make such payment from the local government's share, if any, of state revenues or other amounts authorized or required by law to be distributed by the state to such local government, if otherwise legally permissible.

Upon failure of any local government to make a payment, the state is further obligated, to the extent of legally available appropriated funds to make such payment on behalf of such local government. The local government remains obligated to make all COP payments and reimburse the state for any conditional payments.

As of June 30, 2010, outstanding certificates of participation notes totaled $83 million for 181 local governments participating in LOCAL. The state estimates that LOCAL program liability, if any, will be immaterial to its overall financial condition.

### Office Building Lease

The 2009 Legislature authorized the state to lease-develop an office building in Olympia, Washington. On June 29, 2009, the state entered into a ground lease and a lease agreement with FYI Properties (FYI), a Washington nonprofit corporation. The agreements call for FYI to design and construct an office building and to finance it with tax-exempt obligations that meet the requirements of Revenue Ruling 63-20 and Revenue Procedure 82-26 issued by the Internal Revenue Service. The state is required to make monthly payments that equal the required debt service on the bonds upon substantial completion of the project estimated to be July 2011. Additional amounts may also be due per the terms of the lease agreement. The lease agreements provide the state with options to purchase the building during the term of the lease and transfer ownership of the building to the state at the end of the lease. The office building will be occupied starting in Fiscal Year 2012.

# Note 14
## Subsequent Events

### A. BOND ISSUES

In July 2010, the state issued:

- $347.3 million in various purpose general obligation bonds to fund various state capital projects, including state, institutions of higher education, and public school facilities; multimodal transportation projects; state and local water supply projects; and conservation and outdoor recreation projects.
- $365.6 million to refund various purpose general obligation bonds.
- $118.2 million in taxable bonds to fund certain taxable projects including: low-income housing projects, and local government and economic development infrastructure projects.

In September 2010, the state refunded:

- $401.4 million in general obligation bonds, which were used for various purposes.
- $394 million in motor vehicle fuel tax general obligation bonds.

In October 2010, the University of Washington issued $165 million in general revenue and refunding bonds. This included $20.3 million in tax-exempt revenue and refunding bonds (Series 2010A), and $144.7 million in taxable Build America revenue bonds (Series 2010B). Part of the proceeds from Series 2010A were used to partially refund 2002 housing and dining revenue and refunding bonds. The remaining proceeds from Series 2010A, and all of the proceeds from Series 2010B were used to pay off $35 million in commercial paper and fund a variety of projects including renovation and expansion of education facilities.

In November 2010, Washington Biomedical Research Facilities 3 (a blended component unit of the University of Washington), expects to issue approximately $165 million in revenue bonds. The bond proceeds will fund the construction of a research facility that the University will occupy through a long-term lease arrangement.

In November 2010, Central Washington University issued $34.5 million in revenue bonds for the construction of a residence hall, which included $32 million in taxable Build America revenue bonds.

In December 2010, Washington State University expects to issue $38.8 million in revenue bonds for housing and dining projects.

## B. CERTIFICATES OF PARTICIPATION

In August 2010, the state issued $9.3 million to refund Certificates of Participation.

In November 2010, the state issued $50 million in Certificates of Participation to fund various state and local government real estate and equipment purchases.

## C. CONVENTION AND TRADE CENTER

The 2010 State Legislature enacted Substitute Senate Bill 6889 which authorized King County to create a public facilities district to acquire, own and operate a convention and trade center. The bill provides for the transfer of the state Convention and Trade Center, an enterprise fund of the state, to the public facilities district created in July 2010 by King County Ordinance 16883.

Section 8 of the Substitute Senate Bill 6889 sets forth a number of conditions that must be met prior to the transfer occurring including the redemption, prepayment or legal defeasance of all outstanding debt of the state related to the state Convention and Trade Center. The public facilities district plans to issue debt during November 2010 and use the proceeds to satisfy outstanding state bonds, certificates of participation and financing contracts related to the state convention and trade center. The bill provides that all conditions of the transfer must occur prior to June 30, 2011.

## D. RESOLVED LITIGATION

Jim A. Tobin v. Department of Labor & Industries was settled by the Supreme Court on August 12, 2010 in favor of the plaintiff. This case is primarily about distribution of money recovered from third parties. Chapter 51.24 RCW allows workers injured by non-employer third parties to file personal injury claims against those responsible parties. "Any recovery" in such an action is subject to distribution under a complex statutory formula. The current distribution formula includes third party damages for pain and suffering. The plaintiff of this case argued that pain and suffering damages must be excluded from distribution. Upon notification of the Supreme Court decision in favor of Jim A. Tobin, an increase in the amount of $165.8 million was recorded in claims payable liabilities in the Workers' Compensation Fund.

## E. GENERAL ELECTION

There were measures on the state's November 2, 2010 general election ballot that addressed state laws related to state operations, state imposed taxes and fees, and the calculation of the state debt limitation. These measures, if passed, could impact the state fiscally. Election results are not final or official until certified. By law December 2, 2010 is the last day for the Office of the Secretary of State to certify General Election returns. Information is posted as available on the Secretary of State's website at: http://www.sos.wa.gov.

# RSI
# Required Supplementary Information

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## BUDGETARY INFORMATION
# Budgetary Comparison Schedule

**General Fund**
For the Fiscal Year Ended June 30, 2010
*(expressed in thousands)*

| | General Fund | | | |
|---|---|---|---|---|
| | Original Budget 2009-11 Biennium | Final Budget 2009-11 Biennium | Actual 2009-11 Biennium | Variance with Final Budget |
| **Budgetary Fund Balance, July 1** | $ 189,310 | $ 189,310 | $ 189,310 | $ - |
| **Resources** | | | | |
| Taxes | 29,493,412 | 28,582,490 | 13,139,029 | (15,443,461) |
| Licenses, permits, and fees | 187,150 | 179,419 | 85,637 | (93,782) |
| Other contracts and grants | 359,489 | 421,747 | 177,250 | (244,497) |
| Timber sales | 5,698 | 6,990 | 4,855 | (2,135) |
| Federal grants-in-aid | 15,487,030 | 16,821,716 | 8,306,614 | (8,515,102) |
| Charges for services | 132,086 | 130,431 | 55,660 | (74,771) |
| Investment income (loss) | 10,407 | (9,993) | 327 | 10,320 |
| Miscellaneous revenue | 213,124 | 544,311 | 177,173 | (367,138) |
| Unclaimed property | 95,773 | 91,955 | 60,171 | (31,784) |
| Transfers from other funds | 1,743,577 | 1,908,951 | 1,255,073 | (653,878) |
| **Total Resources** | 47,917,056 | 48,867,327 | 23,451,099 | (25,416,228) |
| **Charges To Appropriations** | | | | |
| General government | 3,529,346 | 3,506,382 | 1,706,150 | 1,800,232 |
| Human services | 23,393,416 | 24,569,701 | 11,955,459 | 12,614,242 |
| Natural resources and recreation | 592,619 | 682,981 | 333,844 | 349,137 |
| Transportation | 100,183 | 98,775 | 46,424 | 52,351 |
| Education | 18,860,255 | 18,917,212 | 9,455,796 | 9,461,416 |
| Capital outlays | 305,525 | 334,336 | 86,891 | 247,445 |
| Transfers to other funds | 709,891 | 538,449 | 456,702 | 81,747 |
| **Total Charges To Appropriations** | 47,491,235 | 48,647,836 | 24,041,266 | 24,606,570 |
| **Excess Available For Appropriation Over (Under) Charges To Appropriations** | 425,821 | 219,491 | (590,167) | (809,658) |
| **Reconciling Items** | | | | |
| Changes in reserves (net) | - | - | 32,527 | 32,527 |
| Entity adjustments (net) | - | - | (3,427) | (3,427) |
| **Total Reconciling Items** | - | - | 29,100 | 29,100 |
| **Budgetary Fund Balance, June 30** | $ 425,821 | $ 219,491 | $ (561,067) | $ (780,558) |

## BUDGETARY INFORMATION

# Budgetary Comparison Schedule – Budget to GAAP Reconciliation

**General Fund**
For the Fiscal Year Ended June 30, 2010
*(expressed in thousands)*

| | General Fund |
|---|---|
| **Sources/Inflows of Resources** | |
| Actual amounts (budgetary basis) "Total Resources" from the Budgetary Comparison Schedule | $ 23,451,099 |
| Differences - budget to GAAP: | |
| The following items are inflows of budgetary resources but are not revenue for financial reporting purposes: | |
| Transfers from other funds | (1,255,073) |
| Budgetary fund balance at the beginning of the biennium | (189,310) |
| The following items are not inflows of budgetary resources but are revenue for financial reporting purposes: | |
| Noncash commodities and electronic food stamp benefits | 1,327,020 |
| Unanticipated receipts | 14,677 |
| Noncash revenues | (4,610) |
| Revenues collected for other governments | 30,851 |
| **Total Revenues (GAAP Basis) as Reported on the Statement of Revenues, Expenditures, and Changes in Fund Balances - Governmental Funds** | $ 23,374,654 |
| **Uses/Outflows of Resources** | |
| Actual amounts (budgetary basis) "Total Charges to Appropriations" from the Budgetary Comparison Schedule | $ 24,041,266 |
| Differences - budget to GAAP: | |
| Budgeted expenditure transfers are recorded as expenditures in the budget statement but are recorded as other financing sources (uses) for financial reporting purposes. | (1,177,642) |
| The following items are outflows of budgetary resources but are not expenditures for financial reporting purposes: | |
| Transfers to other funds | (456,702) |
| The following items are not outflows of budgetary resources but are recorded as current expenditures for financial reporting purposes: | |
| Noncash commodities and electronic food stamp benefits | 1,327,020 |
| Expenditures related to unanticipated receipts | 14,677 |
| Certificates of participation and capital lease acquisitions | 3,301 |
| Distributions to other governments | 30,851 |
| **Total Expenditures (GAAP Basis) as Reported on the Statement of Revenues, Expenditures, and Changes in Fund Balances - Governmental Funds** | $ 23,782,771 |

## BUDGETARY INFORMATION
# Budgetary Comparison Schedule

**Motor Vehicle Fund**
For the Fiscal Year Ended June 30, 2010
*(expressed in thousands)*

| | Motor Vehicle | | | |
|---|---|---|---|---|
| | Original Budget 2009-11 Biennium | Final Budget 2009-11 Biennium | Actual 2009-11 Biennium | Variance with Final Budget |
| **Budgetary Fund Balance, July 1** | $ 314,526 | $ 314,526 | $ 314,526 | $ - |
| **Resources** | | | | |
| Taxes | 2,025,279 | 1,887,778 | 966,695 | (921,083) |
| Licenses, permits, and fees | 778,724 | 752,123 | 374,857 | (377,266) |
| Other contracts and grants | 5,269 | 4,675 | 1,710 | (2,965) |
| Timber sales | - | - | 27 | 27 |
| Federal grants-in-aid | 1,061,784 | 1,256,255 | 541,398 | (714,857) |
| Charges for services | 546,092 | 556,678 | 242,283 | (314,395) |
| Investment income (loss) | 15,172 | 6,964 | 15,571 | 8,607 |
| Miscellaneous revenue | 52,097 | 56,810 | 26,110 | (30,700) |
| Transfers from other funds | 599,934 | 327,446 | 100,031 | (227,415) |
| **Total Resources** | 5,398,877 | 5,163,255 | 2,583,208 | (2,580,047) |
| **Charges To Appropriations** | | | | |
| General government | 20,780 | 22,077 | 14,240 | 7,837 |
| Natural resources and recreation | 2,493 | 2,483 | 1,053 | 1,430 |
| Transportation | 1,661,389 | 1,678,156 | 782,294 | 895,862 |
| Capital outlays | 4,534,611 | 4,871,043 | 1,927,355 | 2,943,688 |
| Transfers to other funds | 1,393,562 | 1,112,515 | 417,537 | 694,978 |
| Debt service | - | - | 18 | (18) |
| **Total Charges To Appropriations** | 7,612,835 | 7,686,274 | 3,142,497 | 4,543,777 |
| **Excess Available For Appropriation Over (Under) Charges To Appropriations** | (2,213,958) | (2,523,019) | (559,289) | 1,963,730 |
| **Reconciling Items** | | | | |
| Bond sale proceeds | 2,230,650 | 2,550,883 | 2,060,820 | (490,063) |
| Bond issue premiums | - | - | 32,569 | 32,569 |
| Refunding other debt issued | - | - | 1,710 | 1,710 |
| Payments to escrow agents for refunded other debt | - | - | (1,800) | (1,800) |
| Changes in reserves (net) | - | - | 10 | 10 |
| Entity adjustments (net) | - | - | 5,359 | 5,359 |
| **Total Reconciling Items** | 2,230,650 | 2,550,883 | 2,098,668 | (452,215) |
| **Budgetary Fund Balance, June 30** | $ 16,692 | $ 27,864 | $ 1,539,379 | $ 1,511,515 |

## BUDGETARY INFORMATION

# Budgetary Comparison Schedule – Budget to GAAP Reconciliation

**Motor Vehicle Fund**
For the Fiscal Year Ended June 30, 2010
*(expressed in thousands)*

| | Motor Vehicle Fund |
|---|---|
| **Sources/Inflows of Resources** | |
| Actual amounts (budgetary basis) "Total Resources" from the Budgetary Comparison Schedule | $ 2,583,208 |
| Differences - budget to GAAP: | |
| The following items are inflows of budgetary resources but are not revenue for financial reporting purposes: | |
| Transfers from other funds | (100,031) |
| Budgetary fund balance at the beginning of the biennium | (314,526) |
| The following items are not inflows of budgetary resources but are revenue for financial reporting purposes: | |
| Revenues collected for other governments | 237,201 |
| Unanticipated receipts | 5,761 |
| Noncash revenues | 4,706 |
| Other | 653 |
| **Total Revenues (GAAP Basis) as Reported on the Statement of Revenues, Expenditures, and Changes in Fund Balances - Governmental Funds** | $ 2,416,972 |
| **Uses/Outflows of Resources** | |
| Actual amounts (budgetary basis) "Total Charges to Appropriations" from the Budgetary Comparison Schedule | $ 3,142,497 |
| Differences - budget to GAAP: | |
| The following items are outflows of budgetary resources but are not expenditures for financial reporting purposes: | |
| Transfers to other funds | (417,537) |
| The following items are not outflows of budgetary resources but are recorded as current expenditures for financial reporting purposes: | |
| Distributions to other governments | 237,201 |
| Expenditures related to unanticipated receipts | 5,761 |
| **Total Expenditures (GAAP Basis) as Reported on the Statement of Revenues, Expenditures, and Changes in Fund Balances - Governmental Funds** | $ 2,967,922 |

# BUDGETARY INFORMATION
## Notes to Required Supplementary Information

### GENERAL BUDGETARY POLICIES AND PROCEDURES

The Governor is required to submit a budget to the state Legislature no later than December 20 of the year preceding odd-numbered year sessions of the Legislature.

The budget is a proposal for expenditures in the ensuing biennial period based upon anticipated revenues from the sources and rates existing by law at the time of submission of the budget. The Governor may additionally submit, as an appendix to the budget, a proposal for expenditures in the ensuing biennium from revenue sources derived from proposed changes in existing statutes.

The appropriated budget and any necessary supplemental budgets are legally required to be adopted through the passage of appropriation bills by the Legislature and approved by the Governor. Operating appropriations are generally made at the fund/account and agency level; however, in a few cases, appropriations are made at the fund/account and agency/program level. Operating appropriations cover either the entire biennium or a single fiscal year within the biennium. Capital appropriations are biennial and are generally made at the fund/account, agency, and project level.

The legal level of budgetary control is at the fund/account, agency, and appropriation level, with administrative controls established at lower levels of detail in certain instances. The accompanying budgetary schedules are not presented at the legal level of budgetary control. This is due to the large number of appropriations within individual agencies that would make such a presentation in the accompanying financial schedules extremely cumbersome. Section 2400.121 of the GASB Codification of Governmental Accounting and Financial Reporting Standards provides for the preparation of a separate report in these extreme cases.

For the state of Washington, a separate report has been prepared for the 2009-11 Biennium to illustrate legal budgetary compliance. Appropriated budget versus actual expenditures, and estimated versus actual revenues and other financing sources (uses) for appropriated funds at agency and appropriation level are presented in the Budget-to-Actual Detail Report for governmental funds. A copy of this report is available at the Office of Financial Management, 1110 Capitol Way SE, PO Box 43113, Olympia, Washington 98504-3113.

Legislative appropriations are strict legal limits on expenditures/expenses, and over-expenditures are prohibited. All appropriated and certain nonappropriated funds are further controlled by the executive branch through the allotment process. This process allocates the expenditure/expense plan into monthly allotments by program, source of funds, and object of expenditure. According to statute RCW 43.88.110(2), except under limited circumstances, the original allotments are approved by the Governor and may be revised on a quarterly basis and must be accompanied by an explanation of the reasons for significant changes. Because allotments are not the strict legal limit on expenditures/expenses, the budgetary schedules presented as required supplementary information (RSI) are shown on an appropriation versus actual comparison rather than an allotment versus actual comparison.

Proprietary funds typically earn revenues and incur expenses (i.e., depreciation or budgeted asset purchases) not covered by the allotment process. Budget estimates are generally made outside the allotment process according to prepared business plans. These proprietary fund business plan estimates are adjusted only at the beginning of each fiscal year.

Additional fiscal control is exercised through various means. OFM is authorized to make expenditure/expense allotments based on availability of unanticipated receipts, mainly federal government grant increases made during a fiscal year. State law does not preclude the over-expenditure of allotments, although RCW 43.88.110(3) requires that the Legislature be provided an explanation of major variances.

Operating encumbrances lapse at the end of the applicable appropriation. Capital outlay encumbrances lapse at the end of the biennium unless reappropriated by the Legislature in the ensuing biennium. Encumbrances outstanding against continuing appropriations at fiscal year-end are reported as reservations of fund balance.

### Budgetary Reporting vs. GAAP Reporting

Governmental funds are budgeted materially in conformance with GAAP. However, the presentation in the accompanying budgetary schedules is different in certain respects from the corresponding Statements of Revenues, Expenditures, and Changes in Fund Balance (governmental operating statement). In the accompanying budgetary schedules, budget and actual expenditures are reported only for appropriated activities. Expenditures are classified based on whether the appropriation is from the operating or capital budget. Expenditures funded by operating budget appropriations are reported as current expenditures classified by the function of the agency receiving the appropriation. Expenditures funded by capital budget appropriations are reported as capital outlays.

However, in the governmental operating statements, all governmental funds are included and expenditures are classified according to what was actually purchased. Capital outlays are fixed asset acquisitions such as land, buildings, and equipment. Debt service expenditures are principal and interest payments. Current expenditures are all other governmental fund expenditures classified based on the function of the agency making the expenditures.

Additionally, certain governmental activities are excluded from the budgetary schedules because they are not appropriated. These activities include activities designated as nonappropriated by the Legislature, such as the Higher Education Special Revenue Fund, Higher Education Endowment Fund, Tobacco Settlement Securitization Bond Debt Service Fund, federal surplus food commodities, electronic food stamp benefits, capital leases, note proceeds, and resources collected and distributed to other governments.

Further, certain expenditures are appropriated as operating transfers. These transfers are reported as operating transfers on the budgetary schedules and as expenditures on the governmental operating statements. The factors contributing to the differences between the Budgetary Comparison Schedule and the Statement of Revenues, Expenditures, and Changes in Fund Balance are noted in the previous Budget to GAAP reconciliation.

Budgetary Fund Balance includes the following as reported on the Governmental Funds Balance Sheet: Unreserved, undesignated fund balance; and Reserved for encumbrances.

## PENSION PLAN INFORMATION
## Schedules of Funding Progress

continued

**Schedule of Funding Progress**
**Public Employees' Retirement System - Plan 1**
Valuation Years 2009 through 2004
*(dollars in millions)*

| | 2009 | 2008 | 2007 | 2006 | 2005 | 2004 |
|---|---|---|---|---|---|---|
| Actuarial valuation date | 6/30/2009 | 6/30/2008 | 6/30/2007 | 9/30/2006 | 9/30/2005 | 9/30/2004 |
| Actuarial value of plan assets | $ 9,776 | $ 9,853 | $ 9,715 | $ 9,591 | $ 9,707 | $ 9,928 |
| Actuarial accrued liability | 13,984 | 13,901 | 13,740 | 13,129 | 13,704 | 12,855 |
| Unfunded actuarial liability | 4,208 | 4,048 | 4,025 | 3,538 | 3,997 | 2,927 |
| Percentage funded | 70% | 71% | 71% | 73% | 71% | 77% |
| Covered payroll | 580 | 638 | 676 | 725 | 786 | 863 |
| Unfunded actuarial liability as a percentage of covered payroll | 726% | 634% | 595% | 488% | 509% | 339% |

*Source: Washington State Office of the State Actuary. Starting with the 2007 report the valuation date changed to June 30.*

**Schedule of Funding Progress**
**Public Employees' Retirement System - Plan 2/3**
Valuation Years 2009 through 2004
*(dollars in millions)*

| | 2009 | 2008 | 2007 | 2006 | 2005 | 2004 |
|---|---|---|---|---|---|---|
| Actuarial valuation date | 6/30/2009 | 6/30/2008 | 6/30/2007 | N/A | N/A | N/A |
| Actuarial value of plan assets | $ 18,260 | $ 16,693 | $ 14,888 | N/A | N/A | N/A |
| Actuarial accrued liability | 18,398 | 16,508 | 14,661 | N/A | N/A | N/A |
| Unfunded actuarial liability | 138 | (185) | (227) | N/A | N/A | N/A |
| Percentage funded | 99% | 101% | 102% | N/A | N/A | N/A |
| Covered payroll | 8,132 | 7,869 | 7,157 | N/A | N/A | N/A |
| Unfunded actuarial liability as a percentage of covered payroll | 2% | 0% | 0% | N/A | N/A | N/A |

PERS Plan 2/3 uses the aggregate actuarial cost method. Effective for reporting year 2007, this Schedule of Funding Progress is prepared using the entry age actuarial cost method and is intended to serve as a surrogate for the funded status and funding progress information of this plan as required by GASB Statement No. 50.

N/A indicates data not available.

*Source: Washington State Office of the State Actuary. Starting with the 2007 report the valuation date changed to June 30.*

## PENSION PLAN INFORMATION
## Schedules of Funding Progress

continued

**Schedule of Funding Progress**
**Teachers' Retirement System - Plan 1**
Valuation Years 2009 through 2004
*(dollars in millions)*

| | 2009 | 2008 | 2007 | 2006 | 2005 | 2004 |
|---|---|---|---|---|---|---|
| Actuarial valuation date | 6/30/2009 | 6/30/2008 | 6/30/2007 | 9/30/2006 | 9/30/2005 | 9/30/2004 |
| Actuarial value of plan assets | $ 8,146 | $ 8,262 | $ 8,302 | $ 8,275 | $ 8,450 | $ 8,728 |
| Actuarial accrued liability | 10,820 | 10,754 | 10,826 | 10,359 | 10,894 | 10,401 |
| Unfunded actuarial liability | 2,674 | 2,492 | 2,524 | 2,084 | 2,444 | 1,673 |
| Percentage funded | 75% | 77% | 77% | 80% | 78% | 84% |
| Covered payroll | 389 | 432 | 426 | 478 | 546 | 616 |
| Unfunded actuarial liability as a percentage of covered payroll | 687% | 577% | 592% | 436% | 448% | 272% |

*Source: Washington State Office of the State Actuary. Starting with the 2007 report the valuation date changed to June 30.*

**Schedule of Funding Progress**
**Teachers' Retirement System - Plan 2/3**
Valuation Years 2009 through 2004
*(dollars in millions)*

| | 2009 | 2008 | 2007 | 2006 | 2005 | 2004 |
|---|---|---|---|---|---|---|
| Actuarial valuation date | 6/30/2009 | 6/30/2008 | 6/30/2007 | N/A | N/A | N/A |
| Actuarial value of plan assets | $ 6,160 | $ 5,681 | $ 5,277 | N/A | N/A | N/A |
| Actuarial accrued liability | 6,048 | 5,264 | 4,682 | N/A | N/A | N/A |
| Unfunded (assets in excess of) actuarial liability | (112) | (417) | (595) | N/A | N/A | N/A |
| Percentage funded | 102% | 108% | 113% | N/A | N/A | N/A |
| Covered payroll | 3,957 | 3,621 | 3,318 | N/A | N/A | N/A |
| Unfunded actuarial liability as a percentage of covered payroll | 0% | 0% | 0% | N/A | N/A | N/A |

TRS Plan 2/3 uses the aggregate actuarial cost method. Effective for reporting year 2007, this Schedule of Funding Progress is prepared using the entry age actuarial cost method and is intended to serve as a surrogate for the funded status and funding progress information of this plan as required by GASB Statement No. 50.

N/A indicates data not available.

*Source: Washington State Office of the State Actuary. Starting with the 2007 report the valuation date changed to June 30.*

## PENSION PLAN INFORMATION
## Schedules of Funding Progress

continued

**Schedule of Funding Progress**
**School Employees' Retirement System - Plan 2/3**
Valuation Years 2009 through 2004
*(dollars in millions)*

| | 2009 | 2008 | 2007 | 2006 | 2005 | 2004 |
|---|---|---|---|---|---|---|
| Actuarial valuation date | 6/30/2009 | 6/30/2008 | 6/30/2007 | N/A | N/A | N/A |
| Actuarial value of plan assets | $ 2,503 | $ 2,303 | $ 2,133 | N/A | N/A | N/A |
| Actuarial accrued liability | 2,493 | 2,207 | 1,998 | N/A | N/A | N/A |
| Unfunded (assets in excess of) actuarial liability | (10) | (96) | (135) | N/A | N/A | N/A |
| Percentage funded | 100% | 104% | 107% | N/A | N/A | N/A |
| Covered payroll | 1,467 | 1,379 | 1,283 | N/A | N/A | N/A |
| Unfunded actuarial liability as a percentage of covered payroll | 0% | 0% | 0% | N/A | N/A | N/A |

SERS Plan 2/3 uses the aggregate actuarial cost method. Effective for reporting year 2007, this Schedule of Funding Progress is prepared using the entry age actuarial cost method and is intended to serve as a surrogate for the funded status and funding progress information of this plan as required by GASB Statement No. 50.

N/A indicates data not available.

*Source: Washington State Office of the State Actuary. Starting with the 2007 report the valuation date changed to June 30.*

**Schedule of Funding Progress**
**Law Enforcement Officers' and Fire Fighters' Retirement System - Plan 1**
Valuation Years 2009 through 2004
*(dollars in millions)*

| | 2009 | 2008 | 2007 | 2006 | 2005 | 2004 |
|---|---|---|---|---|---|---|
| Actuarial valuation date | 6/30/2009 | 6/30/2008 | 6/30/2007 | 9/30/2006 | 9/30/2005 | 9/30/2004 |
| Actuarial value of plan assets | $ 5,612 | $ 5,592 | $ 5,298 | $ 5,018 | $ 4,800 | $ 4,666 |
| Actuarial accrued liability | 4,492 | 4,368 | 4,340 | 4,309 | 4,243 | 4,266 |
| Unfunded (assets in excess of) actuarial liability | (1,120) | (1,224) | (958) | (709) | (557) | (400) |
| Percentage funded | 125% | 128% | 122% | 116% | 113% | 109% |
| Covered payroll | 33 | 37 | 43 | 48 | 56 | 64 |
| Unfunded actuarial liability as a percentage of covered payroll | 0% | 0% | 0% | N/A | N/A | N/A |

N/A indicates data not available.

*Source: Washington State Office of the State Actuary. Starting with the 2007 report the valuation date changed to June 30.*

## PENSION PLAN INFORMATION
## Schedules of Funding Progress

continued

**Schedule of Funding Progress**
**Law Enforcement Officers' and Fire Fighters' Retirement System - Plan 2**
Valuation Years 2009 through 2004
*(dollars in millions)*

| | 2009 | 2008 | 2007 | 2006 | 2005 | 2004 |
|---|---|---|---|---|---|---|
| Actuarial valuation date | 6/30/2009 | 6/30/2008 | 6/30/2007 | N/A | N/A | N/A |
| Actuarial value of plan assets | $ 5,564 | $ 5,053 | $ 4,360 | N/A | N/A | N/A |
| Actuarial accrued liability | 4,641 | 3,998 | 3,626 | N/A | N/A | N/A |
| Unfunded (assets in excess of) actuarial liability | (923) | (1,055) | (734) | N/A | N/A | N/A |
| Percentage funded | 120% | 126% | 120% | N/A | N/A | N/A |
| Covered payroll | 1,442 | 1,345 | 1,234 | N/A | N/A | N/A |
| Unfunded actuarial liability as a percentage of covered payroll | 0% | 0% | 0% | N/A | N/A | N/A |

LEOFF Plan 2 uses the aggregate actuarial cost method. Effective for reporting year 2007, this Schedule of Funding Progress is prepared using the entry age actuarial cost method and is intended to serve as a surrogate for the funded status and funding progress information of this plan as required by GASB Statement No. 50.

N/A indicates data not available.

*Source: Washington State Office of the State Actuary. Starting with the 2007 report the valuation date changed to June 30.*

**Schedule of Funding Progress**
**Washington State Patrol Retirement System - Plan 1/2**
Valuation Years 2009 through 2004
*(dollars in millions)*

| | 2009 | 2008 | 2007 | 2006 | 2005 | 2004 |
|---|---|---|---|---|---|---|
| Actuarial valuation date | 6/30/2009 | 6/30/2008 | 6/30/2007 | N/A | N/A | N/A |
| Actuarial value of plan assets | $ 900 | $ 870 | $ 800 | N/A | N/A | N/A |
| Actuarial accrued liability | 790 | 745 | 702 | N/A | N/A | N/A |
| Unfunded (assets in excess of) actuarial liability | (110) | (125) | (98) | N/A | N/A | N/A |
| Percentage funded | 114% | 117% | 114% | N/A | N/A | N/A |
| Covered payroll | 83 | 79 | 72 | N/A | N/A | N/A |
| Unfunded actuarial liability as a percentage of covered payroll | 0% | 0% | 0% | N/A | N/A | N/A |

WSPRS Plan 1/2 uses the aggregate actuarial cost method. Effective for reporting year 2007, this Schedule of Funding Progress is prepared using the entry age actuarial cost method and is intended to serve as a surrogate for the funded status and funding progress information of this plan as required by GASB Statement No. 50.

N/A indicates data not available.

*Source: Washington State Office of the State Actuary. Starting with the 2007 report the valuation date changed to June 30.*

## PENSION PLAN INFORMATION
## Schedules of Funding Progress

continued

**Schedule of Funding Progress**
**Public Safety Employees' Retirement System - Plan 2**
Valuation Years 2009 through 2004
*(dollars in millions)*

| | 2009 | 2008 | 2007 | 2006 | 2005 | 2004 |
|---|---|---|---|---|---|---|
| Actuarial valuation date | 6/30/2009 | 6/30/2008 | 6/30/2007 | N/A | N/A | N/A |
| Actuarial value of plan assets | $ 69 | $ 39 | $ 14 | N/A | N/A | N/A |
| Actuarial accrued liability | 64 | 37 | 19 | N/A | N/A | N/A |
| Unfunded (assets in excess of) actuarial liability | (5) | (2) | 6 | N/A | N/A | N/A |
| Percentage funded | 108% | 106% | 74% | N/A | N/A | N/A |
| Covered payroll | 223 | 200 | 134 | N/A | N/A | N/A |
| Unfunded actuarial liability as a percentage of covered payroll | 0% | 0% | 0% | N/A | N/A | N/A |

PSERS Plan 2 uses the aggregate actuarial cost method. Effective for reporting year 2007, this Schedule of Funding Progress is prepared using the entry age actuarial cost method and is intended to serve as a surrogate for the funded status and funding progress information of this plan as required by GASB Statement No. 50.

N/A indicates data not available.

*Source: Washington State Office of the State Actuary. Starting with the 2007 report the valuation date changed to June 30.*

**Schedule of Funding Progress**
**Judicial Retirement System**
Valuation Years 2009 through 2004
*(dollars in millions)*

| | 2009 | 2008 | 2007 | 2006 | 2005 | 2004 |
|---|---|---|---|---|---|---|
| Actuarial valuation date | 6/30/2009 | 6/30/2008 | 6/30/2007 | 9/30/2006 | 9/30/2005 | 9/30/2004 |
| Actuarial value of plan assets | $ 2 | $ 1 | $ 1 | $ 0.3 | $ 2 | $ 4 |
| Actuarial accrued liability | 89 | 92 | 85 | 88 | 89 | 89 |
| Unfunded actuarial liability | 87 | 91 | 84 | 88 | 87 | 85 |
| Percentage funded | 2% | 1% | 1% | 0% | 2% | 4% |
| Covered payroll | 0.9 | 1.3 | 1.3 | 1.4 | 1.7 | 2.4 |
| Unfunded actuarial liability as a percentage of covered payroll | 9667% | 7000% | 6462% | 6286% | 5118% | 3542% |

*Source: Washington State Office of the State Actuary. Starting with the 2007 report the valuation date changed to June 30.*

## PENSION PLAN INFORMATION
## Schedules of Funding Progress

concluded

**Schedule of Funding Progress**
**Judges' Retirement Fund**
Valuation Years 2009 through 2004
*(dollars in millions)*

| | 2009 | 2008 | 2007 | 2006 | 2005 | 2004 |
|---|---|---|---|---|---|---|
| Actuarial valuation date | 6/30/2009 | 6/30/2008 | 6/30/2007 | 9/30/2006 | 9/30/2005 | 9/30/2004 |
| Actuarial value of plan assets | $ 3.3 | $ 3.6 | $ 4.0 | $ 4.1 | $ 4.2 | $ 4.4 |
| Actuarial accrued liability | 3.4 | 3.5 | 3.9 | 4.0 | 4.5 | 4.7 |
| Unfunded (assets in excess of) actuarial liability | 0.1 | (0.1) | (0.1) | (0.1) | 0.3 | 0.3 |
| Percentage funded | 97% | 103% | 103% | 103% | 93% | 94% |
| Covered payroll | - | - | - | - | - | - |
| Unfunded actuarial liability as a percentage of covered payroll | N/A | N/A | N/A | N/A | N/A | N/A |

N/A indicates data not available.

*Source: Washington State Office of the State Actuary. Starting with the 2007 report the valuation date changed to June 30.*

**Schedule of Funding Progress**
**Volunteer Fire Fighters' and Reserve Officers' Relief and Pension Fund**
Valuation Years 2009 through 2004
*(dollars in millions)*

| | 2009 | 2008 | 2007 | 2006 | 2005 | 2004 |
|---|---|---|---|---|---|---|
| Actuarial valuation date | 6/30/2009 | 6/30/2008 | 6/30/2007 | 12/31/2006 | 12/31/2005 | 12/31/2004 |
| Actuarial value of plan assets | $ 166 | $ 161 | $ 151 | $ 140 | $ 127 | $ 120 |
| Actuarial accrued liability | 163 | 153 | 141 | 142 | 140 | 115 |
| Unfunded (assets in excess of) actuarial liability | (3) | (8) | (10) | 2 | 13 | (5) |
| Percentage funded | 102% | 105% | 107% | 99% | 91% | 104% |
| Covered payroll | N/A | N/A | N/A | N/A | N/A | N/A |
| Unfunded actuarial liability as a percentage of covered payroll | N/A | N/A | N/A | N/A | N/A | N/A |

* Pension plan liability only - excludes relief benefits.

**Covered Payroll is not presented because it is not applicable since this is a volunteer organization.

N/A indicates data not available.

*Source: Washington State Office of the State Actuary. Starting with the 2007 report the valuation date changed to June 30.*

## PENSION PLAN INFORMATION

## Schedules of Contributions from Employers and Other Contributing Entities (cont'd)

**Schedules of Contributions from Employers and Other Contributing Entities**
For the Fiscal Years Ended June 30, 2010 through 2005
*(dollars in millions)*

| | 2010 | 2009 | 2008 | 2007 | 2006 | 2005 |
|---|---|---|---|---|---|---|
| **PUBLIC EMPLOYEES' RETIREMENT PLAN SYSTEM - PLAN 1** | | | | | | |
| Employers' annual required contribution | $ 627.8 | $ 620.2 | $ 453.1 | $ 397.3 | $ 438.5 | $ 340.3 |
| Employers' actual contribution | 154.0 | 325.2 | 221.8 | 118.7 | 29.6 | 22.4 |
| Percentage contributed | 25% | 52% | 49% | 30% | 7% | 7% |
| **PUBLIC EMPLOYEES' RETIREMENT PLAN SYSTEM - PLAN 2/3** | | | | | | |
| Employers' annual required contribution | $ 383.1 | $ 369.7 | $ 363.3 | $ 331.3 | $ 307.6 | $ 227.7 |
| Employers' actual contribution | 327.5 | 439.7 | 318.7 | 242.5 | 149.6 | 74.7 |
| Percentage contributed | 85% | 119% | 88% | 73% | 49% | 33% |
| **TEACHERS' RETIREMENT SYSTEM - PLAN 1** | | | | | | |
| Employers' annual required contribution | $ 406.1 | $ 391.0 | $ 294.7 | $ 249.8 | $ 287.5 | $ 224.3 |
| Employers' actual contribution | 112.7 | 178.9 | 113.1 | 60.5 | 15.1 | 8.8 |
| Percentage contributed | 28% | 46% | 38% | 24% | 5% | 4% |
| **TEACHERS' RETIREMENT SYSTEM - PLAN 2/3** | | | | | | |
| Employers' annual required contribution | $ 221.1 | $ 186.9 | $ 208.9 | $ 167.7 | $ 166.4 | $ 117.4 |
| Employers' actual contribution | 165.0 | 160.8 | 109.5 | 102.2 | 75.4 | 33.8 |
| Percentage contributed | 75% | 86% | 52% | 61% | 45% | 29% |
| **SCHOOL EMPLOYEES' RETIREMENT SYSTEM - PLAN 2/3** | | | | | | |
| Employers' annual required contribution | $ 82.3 | $ 71.5 | $ 75.8 | $ 71.5 | $ 81.4 | $ 64.0 |
| Employers' actual contribution | 62.1 | 63.5 | 52.1 | 45.9 | 30.4 | 10.2 |
| Percentage contributed | 75% | 89% | 69% | 64% | 37% | 16% |

The Annual Required Contribution (ARC) changes each year with the experience of the plans. Factors influencing the experience include changes in funding methods, assumptions, plan provisions, and economic and demographic gains and losses. The methods used to derive the ARC for this accounting disclosure are different from that used to derive the actual contributions required by law. These differences include the use of different actuarial valuations (actual contributions may be based on an earlier valuation), and different actuarial cost methods. For these reasons the actual contributions will not match the Annual Required Contributions.

*Source: Washington State Office of the State Actuary*

## PENSION PLAN INFORMATION

## Schedules of Contributions from Employers and Other Contributing Entities (cont'd)

**Schedules of Contributions from Employers and Other Contributing Entities**
For the Fiscal Years Ended June 30, 2010 through 2005
*(dollars in millions)*

| | 2010 | 2009 | 2008 | 2007 | 2006 | 2005 |
|---|---|---|---|---|---|---|
| **LAW ENFORCEMENT OFFICERS' AND FIRE FIGHTERS' RETIREMENT SYSTEM - PLAN 1** | | | | | | |
| Employers' annual required contribution | $ - | $ - | $ - | $ 0.1 | $ - | $ - |
| Employers' actual contribution | - | - | - | 0.1 | 0.1 | - |
| Percentage contributed | N/A | N/A | N/A | 100% | N/A | N/A |
| State annual required contribution | - | - | - | - | - | - |
| State actual contribution | - | - | - | - | - | - |
| Percentage contributed | N/A | N/A | N/A | N/A | N/A | N/A |
| **LAW ENFORCEMENT OFFICERS' AND FIRE FIGHTERS' RETIREMENT SYSTEM - PLAN 2** | | | | | | |
| Employers' annual required contribution* | $ 111.1 | $ 105.3 | $ 61.3 | $ 56.9 | $ 60.8 | $ 48.5 |
| Employers' actual contribution | 77.0 | 77.8 | 73.4 | 58.2 | 48.5 | 32.8 |
| Percentage contributed | 69% | 74% | 120% | 102% | 80% | 68% |
| State annual required contribution* | 44.4 | 42.1 | 40.8 | 38.0 | 40.5 | 32.3 |
| State actual contribution | 51.4 | 51.1 | 45.9 | 37.9 | 31.7 | 21.3 |
| Percentage contributed | 116% | 121% | 113% | 100% | 78% | 66% |
| **WASHINGTON STATE PATROL RETIREMENT SYSTEM** | | | | | | |
| Employers' annual required contribution | $ 6.6 | $ 5.0 | $ 6.8 | $ 5.3 | $ 6.1 | $ 3.4 |
| Employers' actual contribution | 5.3 | 6.4 | 6.1 | 3.3 | 3.1 | - |
| Percentage contributed | 80% | 128% | 90% | 62% | 51% | 0% |

N/A indicates data not available.

*The Annual Required Contribution (ARC) for the LEOFF Plan 2 presented is the Office of the State Actuary's recommended figure; the LEOFF Plan 2 Retirement Board has proposed a higher ARC of $113.5 million.

The Annual Required Contribution (ARC) changes each year with the experience of the plans. Factors influencing the experience include changes in funding methods, assumptions, plan provisions, and economic and demographic gains and losses. The methods used to derive the ARC for this accounting disclosure are different from that used to derive the actual contributions required by law. These differences include the use of different actuarial valuations (actual contributions may be based on an earlier valuation), and different actuarial cost methods. For these reasons the actual contributions will not match the Annual Required Contributions.

*Source: Washington State Office of the State Actuary*

## PENSION PLAN INFORMATION

# Schedules of Contributions from Employers and Other Contributing Entities (concl'd)

**Schedules of Contributions from Employers and Other Contributing Entities**
For the Fiscal Years Ended June 30, 2010 through 2005
*(dollars in millions)*

| | 2010 | 2009 | 2008 | 2007 | 2006 | 2005 |
|---|---|---|---|---|---|---|
| **PUBLIC SAFETY EMPLOYEES' RETIREMENT PLAN SYSTEM - PLAN 2** | | | | | | |
| Employers' annual required contribution | $ 14.8 | $ 14.3 | $ 12.4 | $ 7.1 | N/A | N/A |
| Employers' actual contribution | 15.2 | 14.5 | 11.7 | 6.6 | N/A | N/A |
| Percentage contributed | 103% | 101% | 94% | 93% | N/A | N/A |
| **JUDICIAL RETIREMENT SYSTEM** | | | | | | |
| Employers' annual required contribution | $ 20.4 | $ 21.2 | $ 26.6 | $ 37.3 | $ 27.7 | $ 21.7 |
| Employers' actual contribution | 11.6 | 10.2 | 9.6 | 9.6 | 6.7 | 6.2 |
| Percentage contributed | 57% | 48% | 36% | 26% | 24% | 29% |
| **JUDGES' RETIREMENT FUND** | | | | | | |
| Employers' annual required contribution | $ - | $ - | $ - | $ - | $ 0.1 | $ 0.1 |
| Employers' actual contribution | - | - | - | 0.3 | 0.3 | 0.5 |
| Percentage contributed | N/A | N/A | N/A | N/A | 300% | 500% |
| **VOLUNTEER FIRE FIGHTERS' AND RESERVE OFFICERS' RELIEF AND PENSION FUND** | | | | | | |
| Employers' annual required contribution | $ 1.0 | $ 1.1 | $ 1.0 | $ 1.0 | $ 1.0 | $ 0.7 |
| Employers' actual contribution | 1.0 | 1.0 | 1.0 | 1.0 | 1.0 | 0.7 |
| Percentage contributed | 100% | 91% | 100% | 100% | 100% | 100% |
| State annual required contribution | 1.8 | 1.4 | 0.9 | 2.0 | 3.6 | 1.8 |
| State actual contribution | 5.7 | 5.2 | 5.0 | 6.0 | 4.6 | 4.4 |
| Percentage contributed | 317% | 371% | 556% | 300% | 128% | 244% |

N/A indicates data not available.

The Annual Required Contribution (ARC) changes each year with the experience of the plans. Factors influencing the experience include changes in funding methods, assumptions, plan provisions, and economic and demographic gains and losses. The methods used to derive the ARC for this accounting disclosure are different from that used to derive the actual contributions required by law. These differences include the use of different actuarial valuations (actual contributions may be based on an earlier valuation), and different actuarial cost methods. For these reasons the actual contributions will not match the Annual Required Contributions.

*Source: Washington State Office of the State Actuary*

## OTHER POSTEMPLOYMENT BENEFITS INFORMATION
## Schedule of Funding Progress

**Schedule of Funding Progress**
**Other Postemployment Benefits**
Valuation Years 2009 through 2007
*(dollars in millions)*

| | 2009 | 2008 | 2007 |
|---|---|---|---|
| Actuarial valuation date | 1/1/2009 | 1/1/2008 | 1/1/2007 |
| Actuarial value of plan assets | $ - | $ - | $ - |
| Actuarial accrued liability (AAL)* | 3,787 | 4,014 | 3,800 |
| Unfunded actuarial accrued liability (UAAL) | 3,787 | 4,014 | 3,800 |
| Funded ratio | 0% | 0% | 0% |
| Covered payroll | 5,678 | 5,170 | 5,427 |
| UAAL as a percentage of covered payroll | 66.69% | 77.64% | 70.01% |

* Based on projected unit credit actuarial cost method.

*Source: Washington State Office of the State Actuary*

# INFRASTRUCTURE ASSETS REPORTED USING THE MODIFIED APPROACH

## CONDITION ASSESSMENT

The state's highway system is divided into three main categories: pavement, bridges, and rest areas. Condition information about each of these areas as well as state managed airports follows.

### Pavement Condition

The Washington State Department of Transportation (WSDOT) owns and maintains 20,498 lane miles of highway, including ramps, collectors and special use lanes. Special use lanes include High Occupancy Vehicle (HOV), climbing, chain-up, holding, slow vehicle turnout, two-way turn, weaving/speed change, bicycle, transit, truck climbing shoulder, turn and acceleration lanes. Special use and ramp/collector lane miles make up 1,927 of the total lane miles.

WSDOT has been rating pavement condition since 1969. Pavement rated in *good* condition is smooth and has few defects. Pavement in *poor* condition is characterized by cracking, patching, roughness and rutting. Pavement condition is rated using three factors: Pavement Structural Condition (PSC), International Roughness Index (IRI), and Rutting.

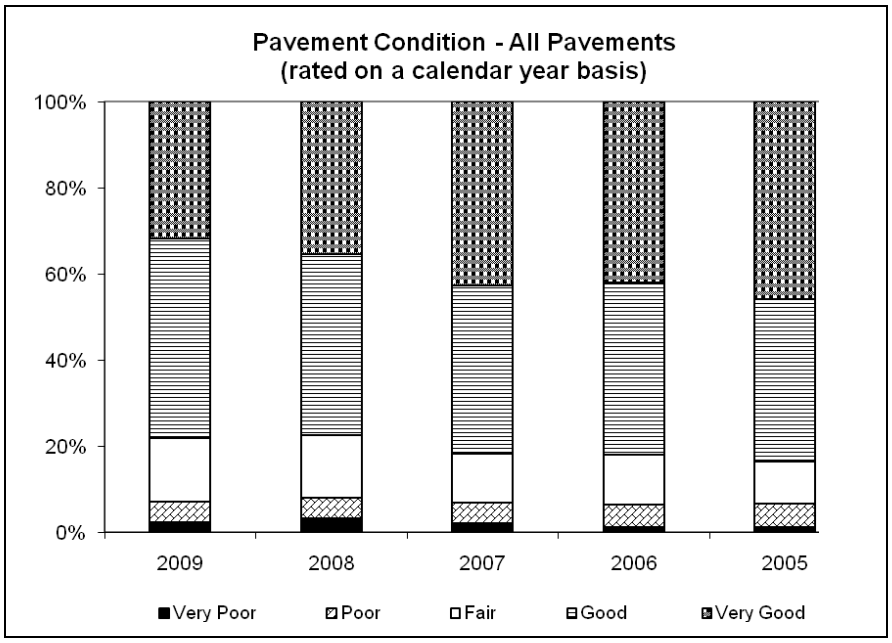
In 1993 the Legislature required WSDOT to rehabilitate pavements at the Lowest Life Cycle Cost (LLCC), which has been determined to occur at a PSC range between 40 and 60, or when triggers for roughness or rutting are met.

The trend over the last five years has shown that the percent of pavements in poor or very poor condition was fairly stable at 7 to 10 percent. WSDOT uses LLCC analysis to manage its pavement preservation program.

The principles behind LLCC are basic – if rehabilitation is done too early, pavement life is wasted; if rehabilitation is done too late, very costly repair work may be required, especially if the underlying structure is compromised. WSDOT continually looks for ways to best strike a balance between these two basic principles.

While the goal for pavements is zero miles in 'poor' condition, marginally good pavements may deteriorate into poor condition during the lag time between assessment and actual rehabilitation. As a result, a small percentage of marginally good pavements will move into the 'poor' condition category for any given assessment period.

WSDOT manages state highways targeting the LLCC per the Pavement Management System due date. While the Department has a long-term goal of no pavements in poor condition (a pavement condition index less than 40, on a 100 point scale), the current policy is to maintain 90 percent of all highway pavement types at a pavement condition index of 40 or better with no more than 10 percent of its highways at a pavement condition below 40. The most recent assessment, conducted in 2009, found that state highways were within the prescribed parameters with only 7 percent of all pavement types with a pavement condition index below 40.



WSDOT uses the following scale for Pavement Structural Condition (PSC):

| Category | PSC Range | Description |
|---|---|---|
| Very Good | 80 – 100 | Little or no distress. Example: Flexible pavement with 5 percent of wheel track length having "hairline" severity alligator cracking will have a PSC of 80. |
| Good | 60 – 80 | Early stage deterioration. Example: Flexible pavement with 15 percent of wheel track length having "hairline" alligator cracking will have a PSC of 70. |
| Fair | 40 – 60 | This is the threshold value for rehabilitation. Example: Flexible pavement with 25 percent of wheel track length having "hairline" alligator cracking will have a PSC of 50. |
| Poor | 20 – 40 | Structural deterioration. Example: Flexible pavement with 25 percent of wheel track length having "medium (spalled)" severity alligator cracking will have a PSC of 30. |
| Very Poor | 0 – 20 | Advanced structural deterioration. Example: Flexible pavement with 40 percent of wheel track length having "medium (spalled)" severity alligator cracking will have a PSC of 10. May require extensive repair and thicker overlays. |

The PSC is a measure based on distresses such as cracking and patching, which are related to the pavement's ability to carry loads. Pavements develop structural deficiencies due to truck traffic and cold weather. WSDOT attempts to program rehabilitation for pavement segments when they are projected to reach a PSC of 50. A PSC of 50 can occur due to various amounts and severity of distress. For rigid pavements (such as Portland cement concrete), a PSC of 50 represents 50 percent of the concrete slabs exhibiting joint faulting with a severity of 1/8 to 1/4 inch (faulting is the elevation difference at slab joints and results in a rough ride – particularly in large trucks). Further, a PSC of 50 can also be obtained if 25 percent of concrete slabs exhibit two to three cracks per panel.

The International Roughness Index (IRI) uses a scale in inches per mile. WSDOT considers pavements with a ride performance measure of greater than 220 inches per mile to be in poor condition. For example, new asphalt overlays typically have ride values below 75 inches per mile, which is very smooth.

Rutting is measured in inches: a pavement with more than 0.58 inches of rutting is considered in poor condition.

The three indices (PSC, IRI, and Rutting) are combined to rate a section of pavement, which is assigned the lowest category of any of the three ratings.

The following table shows the combined explanatory categories and the ratings for each index.

| Category | PSC | IRI | Rutting |
|---|---|---|---|
| Very Good | 100 – 80 | < 95 | < 0.23 |
| Good | 80 – 60 | 95 – 170 | 0.23 – 0.41 |
| Fair | 60 – 40 | 170 – 220 | 0.41 – 0.58 |
| Poor | 40 – 20 | 220 – 320 | 0.58 – 0.74 |
| Very Poor | 0 – 20 | > 320 | > 0.74 |

Since 1999, WSDOT has used an semi-automated pavement distress survey procedure. In the automated survey, high-resolution video images are collected at highway speed and these video images are then rated on special workstations at 3-6 mph speed. Use of the semi-automated procedure has resulted in a more detailed classification and recording of various distresses that are rated.

In 2009, WSDOT rated pavement condition on 16,966 of the 20,498 lane miles of highway. The following chart shows recent pavement condition ratings for the State Highway System, using the combination of the three indices described on the preceding page.

| Percentage of Pavement Lane Miles in Fair or Better Condition* | | | | | |
|---|---|---|---|---|---|
| | 2009 | 2008 | 2007 | 2006 | 2005 |
| Statewide - Chip seals | 95% | 95% | 91% | 91% | 91% |
| Statewide - Asphalt | 93% | 92% | 94% | 94% | 95% |
| Statewide - Concrete | 90% | 87% | 93% | 93% | 91% |
| Statewide - All Pavements | 93% | 92% | 93% | 94% | 93% |

| Percentage of Pavement Lane Miles in Poor or Very Poor Condition* | | | | | |
|---|---|---|---|---|---|
| | 2009 | 2008 | 2007 | 2006 | 2005 |
| Statewide - Chip seals | 5% | 5% | 9% | 9% | 9% |
| Statewide - Asphalt | 7% | 8% | 6% | 6% | 5% |
| Statewide - Concrete | 10% | 13% | 7% | 7% | 9% |
| Statewide - All Pavements | 7% | 8% | 7% | 6% | 7% |

*Calendar year data. Assessments are typically physically conducted in the summer and fall of each year, and processed during the winter and spring, with final results released in July. Years indicated are when the physical assessment was conducted.

Note: The All Pavements percentages are calculated from total lane miles inspected and are not a statistical average of the three pavement type percentages. IRI or rutting is not used for sections identified as under construction in rating distress.

More information about pavement management at WSDOT may be obtained at:
http://www.wsdot.wa.gov/biz/mats/pavement/.

## Bridge Condition

During Fiscal Year 2010, there were 3,184 state-owned vehicular structures over 20 feet in length with a total area of 45,695,870 square feet. In addition to bridges, the 3,184 structures include 97 culverts and 71 ferry terminal vehicle and pedestrian structures. (While ferry terminals are included in a depreciable asset category, they are included here with bridge condition information since they are evaluated by the WSDOT Bridge Office on a periodic basis.)

There was a net increase of 23 bridge and culvert structures in Fiscal Year 2010 due to new construction, additions of culvert structures not previously inventoried, and a sectional approach to inventory and inspection of large bridge structures such as those crossing Puget Sound and Lake Washington. Special emphasis is given to the ongoing inspection and maintenance of major bridges representing a significant public investment due to size, complexity or strategic location. All bridges are inspected every two years and underwater bridge components at least once every five years in accordance with Federal Highway Administration (FHWA) requirements.

Information related to public bridges is maintained in the Washington State Bridge Inventory System (WSBIS). This system is used to develop preservation strategies and comprehensive recommendations for maintenance and construction, and for reporting to the FHWA.

WSDOT's policy is to maintain 95 percent of its bridges at a structural condition of at least fair, meaning that all primary structural elements are sound.

The most recent assessments over the last two years found that state-owned bridges were within the prescribed parameters with 97.9 percent having a condition rating of fair or better and only 2.1 percent of bridges having a condition rating of poor. Bridges rated as poor may have structural deficiencies that restrict the weight and type of traffic allowed. Bridges that are rated as poor are not necessarily unsafe for public travel. Any bridges determined to be unsafe are closed to traffic. There is one bridge currently closed.

WSDOT's Bridge Seismic Retrofit Program prioritizes state bridges for seismic retrofit, and performs these retrofits as funding permits. Retrofit priorities are based on seismic risk of a site, structural detail deficiencies, and route importance.

The Seismic Retrofit Program includes 880 bridges that have been classified as needing retrofitting. WSDOT has fully or partially retrofitted 395 bridges. Of those, 256 are completely retrofitted, 139 are partially retrofitted. There are 13 bridges currently under contract to be retrofitted.

The following condition rating data is based on the structural sufficiency standards established in the FHWA "Recording and Coding Guide for the Structural Inventory and Appraisal of the Nation's Bridges." This structural rating relates to the evaluation of bridge superstructure, deck, substructure, structural adequacy and waterway adequacy.

Three categories of condition were established in relation to the FHWA criteria as follows:

| Category | National Bridge Inventory Code | Description |
|---|---|---|
| Good | 6, 7, or 8 | A range from no problems noted to some minor deterioration of structural elements. |
| Fair | 5 | All primary structural elements are sound but may have deficiencies such as minor section loss, deterioration, cracking, spalling or scour. |
| Poor | 4 or less | Advanced deficiencies such as section loss, deterioration, cracking, spalling, scour or seriously affected primary structural components. |

Note: Bridges rated in poor condition may be restricted for the weight and type of traffic allowed.

The following charts show the most recent condition rating of Washington State bridges:

| Percentage of Bridges in Fair or Better Condition | | | | | |
|---|---|---|---|---|---|
| **Bridge Type** | **2010** | **2009** | **2008** | **2007** | **2006** |
| Reinforced concrete (1,286 bridges in FY 2010) | 98.1% | 98.0% | 98.0% | 98.3% | 98.6% |
| Prestressed concrete (1,379 bridges in FY 2010) | 99.3% | 99.0% | 98.9% | 99.3% | 99.3% |
| Steel (370 bridges* in FY 2010) | 96.6% | 95.0% | 93.9% | 94.7% | 94.1% |
| Timber (81 bridges in FY 2010) | 80.2% | 80.4% | 71.7% | 66.3% | 68.1% |
| Statewide - All bridges (3,116 out of 3,184 bridges in FY 2010) | 97.9% | 97.5% | 97.0% | 97.4% | 97.5% |

| Percentage of Bridges in Poor Condition | | | | | |
|---|---|---|---|---|---|
| **Bridge Type** | **2010** | **2009** | **2008** | **2007** | **2006** |
| Reinforced concrete (25 bridges in FY 2010) | 1.9% | 2.0% | 2.0% | 1.7% | 1.4% |
| Prestressed concrete (10 bridges in FY 2010) | 0.7% | 1.0% | 1.1% | 0.7% | 0.7% |
| Steel (13 bridges* in FY 2010) | 3.4% | 5.0% | 6.1% | 5.3% | 5.9% |
| Timber (20 bridges in FY 2010) | 19.8% | 19.6% | 28.3% | 33.7% | 31.9% |
| Statewide - All bridges (68 out of 3,184 bridges in FY 2010) | 2.1% | 2.5% | 3.0% | 2.6% | 2.5% |

*The steel bridge ratings for Fiscal Year 2010 include 44 ferry terminal structures with 41 rated as fair or better and three ferry terminal structures rated as poor.

Note: Bridges rated as poor may have structural deficiencies that restricted the weight and type of traffic allowed. WSDOT currently has two posted bridges and 141 restricted bridges. Posted bridges have signs posted which inform of legal weight limits. Restricted bridges are those where overweight permits will not be issued for travel by overweight vehicles. This is a decrease of nine posted bridges in 2010 as compared to 2009. The number of restricted bridges decreased by one.

Refer to http://www.wsdot.wa.gov/commercialVehicle/Restrictions/ for more information on overweight restrictions. Any bridges determined to be unsafe are closed to traffic.

Additional information regarding the WSDOT's bridge inspection program may be obtained at:
http://www.wsdot.wa.gov/eesc/bridge/index.cfm.

## Safety Rest Area Condition

The WSDOT owns, operates, and maintains 47 developed safety rest area (SRA) facilities. Within these facilities, the Department manages the following assets: 94 buildings, 694 acres, 31 on-site public drinking water systems, 41 on-site sewage pre-treatment/treatment systems, and 20 recreational vehicle sanitary disposal facilities.

WSDOT performs SRA building and site condition assessments in odd-numbered calendar years, to determine the facility deficiencies. This biennial process, which began in 2003, helps prioritize renovation and replacement projects. Sites and buildings are divided into functional components that are assessed with a numerical rating of 1 to 5 based on guideline criteria (1 meets current standards, 5 is poor).

In addition, a weighting multiplier is applied based on the criticality of the individual component. For instance, a safety deficiency adds a weighting multiplier of ten while a department image deficiency has a weighting multiplier of two. The combined total building and site ratings are used to determine each facility's overall condition, and fall into one of five categories.

WSDOT SRA condition assessment rating parameters are not based on other state or national guidelines for safety rest areas. The model used is based on the capital facility program software already in use, with minor modifications to the rating parameters to better match the unique needs of SRA facilities. The SRA program goal is to have no more than 5 percent of the facilities rated poor.

The following charts show the most recent condition rating of Washington State safety rest areas:

| Category | 2009* | 2007 | 2005 |
|---|---|---|---|
| Percentage of facilities in fair or good condition | 97.6% | 95.2% | 95.2% |
| Percentage of facilities in poor condition | 2.4% | 4.8% | 4.8% |

*2009 percentages are based on 43 inspected SRA sites.

| Category | Description | Number of Safety Rest Areas in Category | | |
|---|---|---|---|---|
| | | 2009 | 2007 | 2005 |
| Good Condition | Facility is new construction and/or meets current standards. | 8 | 8 | 11 |
| Fair-High Condition | Facility meets current standards and/or is in adequate condition with minimal component deficiencies. | 7 | 6 | 2 |
| Fair-Mid Condition | Facility is functional, and in adequate condition with minor component deficiencies. | 11 | 6 | 9 |
| Fair-Low Condition | Facility has multiple system deficiencies. | 16 | 20 | 18 |
| Poor | Facility is at or beyond its service life, with multiple major deficiencies. | 1 | 2 | 2 |
| No Condition Assessment Data | No data in 2009 (Iron Goat, Dodge Junction, Keller Ferry, Dusty) | 4 | 5 | 0 |
| | Total | 47 | 47 | 42 |

## State Managed Airport Condition

The WSDOT Aviation Division is authorized by RCW 47.68.100 to acquire, manage and maintain airports.

Under this authority, WSDOT manages 17 airports, eight of which the Department owns. The airports are used primarily for access to small communities and emergency purposes such as fire fighting, search and rescue, and medical evacuation (one airport is used only for helicopter and search and rescue operations). The airports are also used for recreational flying activities. Most are located near or adjacent to state highways and their runways range in character from paved, to gravel or turf.

Three airports are in operational condition 12 months of the year, and the remaining 14 are operational from June to October each year. Opening and closing dates may vary depending on weather conditions. In accordance with WSDOT policy, maintenance is performed on each airport annually and inspections occur a minimum of three times per year. The use of state airports by all persons is solely at the risk of the user. Since these airports are maintained principally for emergency use, the state does not warrant the conditions at any state airport to be suitable for any other use.

The definitions below represent the classification category for state managed airports within the Washington Aviation System Plan (WASP). The system plan was adopted in 2009 as part of the Long-Term Air Transportation Study and represents the state-interest component of the statewide multimodal transportation plan. The system plan fulfills the statewide aviation planning requirements of federal government, coordinates statewide aviation planning, and identifies the program needs for public use of state airports.

| Category | Definition |
|---|---|
| Local service airport | An airport with a paved runway capable of handling aircraft with a maximum gross certificated takeoff weight of 12,500 pounds. |
| Rural essential airport | An airport with a turf, gravel or sand (unpaved) runway near access to recreational opportunities with capacity for aircraft less than 12,500 pounds. |

The following chart shows the most recent condition rating of Washington State managed airports:

**Washington Aviation System Plan (1)**

| Airport Classification | WSDOT Aviation Owned | WSDOT Aviation Managed |
|---|---|---|
| Local Airports (2) | 2 | - |
| Rural Essential Airports (3) | - | - |
| Paved runway | - | 1 |
| Turf runway | 5 | 3 |
| Gravel runway | - | 4 |
| Sand | - | 1 |
| Helicopter only | 1 | - |
| Total Airports | 8 | 9 |

| | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| Percentage of airports acceptable for general recreational use or better | 94% | 94% | 88% | 88% | 88% |
| Percentage of airports not acceptable for general recreational use or better | 6% | 6% | 12% | 12% | 12% |

(1) Eight airports are owned by WSDOT and nine are managed by WSDOT under various use/operating agreements.
(2) Local airports are acceptable for general use and serve small to medium-sized communities.
(3) Rural essential airports are acceptable for general recreation use and typically serve recreation communities and remote back country locations.

For more information about the airports which are acceptable for general recreational use or better, refer to WSDOT's website at: http://www.wsdot.wa.gov/aviation/Airports/.

## INFRASTRUCTURE ASSETS REPORTED USING THE MODIFIED APPROACH

### Comparison of Planned-to-Actual Preservation and Maintenance

For the Fiscal Years Ended June 30, 2010 through 2006
(expressed in thousands)

| | 2010 | | | 2009 | | |
|---|---|---|---|---|---|---|
| **PAVEMENT** | **Planned** | **Actual** | **Variance** | **Planned** | **Actual** | **Variance** |
| Preservation | $ 147,424 | $ 137,952 | $ 9,472 | $ 125,246 | $ 109,279 | $ 15,967 |
| Maintenance | 20,780 | 21,489 | (709) | 19,651 | 19,170 | 481 |
| **Total** | $ 168,204 | $ 159,441 | $ 8,763 | $ 144,897 | $ 128,449 | $ 16,448 |
| **BRIDGES** | | | | | | |
| Preservation | $ 40,958 | $ 30,904 | $ 10,054 | $ 63,436 | $ 16,586 | $ 46,850 |
| Maintenance | 13,532 | 13,532 | - | 13,365 | 13,406 | (41) |
| **Total** | $ 54,490 | $ 44,436 | $ 10,054 | $ 76,801 | $ 29,992 | $ 46,809 |
| **REST AREAS** | | | | | | |
| Preservation | $ 162 | $ 144 | $ 18 | $ 199 | $ 193 | $ 6 |
| Maintenance | 5,653 | 5,781 | (128) | 5,808 | 5,631 | 177 |
| **Total** | $ 5,815 | $ 5,925 | $ (110) | $ 6,007 | $ 5,824 | $ 183 |
| **AIRPORTS** | | | | | | |
| Preservation & maintenance | $ 183 | $ 159 | $ 24 | $ 146 | $ 168 | $ (22) |

In addition to increasing and improving the state highway system, WSDOT places a high priority on preserving and maintaining the current highway system. WSDOT breaks out preservation and maintenance into two separate functions. Preservation can be described as projects that maintain the structural integrity of the existing highway system including roadway pavements, safety features, bridges, and other structures/facilities. The maintenance function handles the day-to-day needs that occur such as guardrail replacement, patching pot holes, installing signs, and vegetation control.

WSDOT uses outcome based performance measures for evaluating the effectiveness of the maintenance program. The Maintenance Accountability Process (MAP) is a comprehensive planning, measuring and managing process that provides a means for communicating the impacts of policy and budget decisions on program service delivery. WSDOT uses it to identify investment choices and the effects of those choices in communicating with the Legislature and other stakeholders. The MAP measures and communicates the outcomes of 32 distinct highway maintenance activities. Maintenance results are measured via field condition surveys and reported as Level of Service (LOS) ratings, which range from A to F. LOS targets are defined in terms of the condition of various highway features (i.e. percent of guardrail on the highway system that is damaged) and are set commensurate with the level of funding provided for the WSDOT highway maintenance program. More information about MAP may be obtained at: http://www.wsdot.wa.gov/maintenance/accountability/default.htm.

WSDOT's legally authorized budgets are biennial with the even year being the first fiscal year of the biennium. Planned amounts in this schedule are not the legal legislative authorizations but are the planned expenditures for the year within the legal authorizations. Therefore, a negative variance is not an indication of overspending the WSDOT's legal authorization but indicates that more expenditure activity occurred than was initially planned. Actual expenditures may vary from the budgeted or planned amounts for a variety of reasons which include, but are not limited to, management's decision to accelerate or defer preservation or maintenance activity or reduce planned activity in response to economic forecasts.

| 2008 | | | 2007 | | | 2006 | | |
|---|---|---|---|---|---|---|---|---|
| Planned | Actual | Variance | Planned | Actual | Variance | Planned | Actual | Variance |
| $ 118,886 | $ 130,375 | $ (11,489) | $ 111,195 | $ 99,416 | $ 11,779 | $ 108,409 | $ 130,340 | $ (21,931) |
| 18,329 | 16,994 | 1,335 | 19,152 | 16,255 | 2,897 | 19,219 | 18,586 | 633 |
| $ 137,215 | $ 147,369 | $ (10,154) | $ 130,347 | $ 115,671 | $ 14,676 | $ 127,628 | $ 148,926 | $ (21,298) |
| | | | | | | | | |
| $ 11,260 | $ 23,407 | $ (12,147) | $ 21,055 | $ 20,138 | $ 917 | $ 8,434 | $ 20,338 | $ (11,904) |
| 12,427 | 12,601 | (174) | 11,553 | 11,051 | 502 | 11,552 | 11,820 | (268) |
| $ 23,687 | $ 36,008 | $ ( 12,321) | $ 32,608 | $ 31,189 | $ ,1419 | $ 19,986 | $ 32,158 | $ (12,172) |
| | | | | | | | | |
| $ 77 | $ 77 | $ - | $ 188 | $ 173 | $ 15 | $ 188 | $ 129 | $ 59 |
| 5,590 | 5,778 | (188) | 5,056 | 5,359 | (303) | 5,021 | 5,187 | (166) |
| $ 5,667 | $ 5,855 | $ (188) | $ 5,244 | $ 5,532 | $ (288) | $ 5,209 | $ 5,316 | $ (107) |
| | | | | | | | | |
| $ 146 | $ 134 | $ 12 | $ 83 | $ 200 | $ (117) | $ 83 | $ 67 | $ 16 |

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# APPENDIX E

# DTC AND ITS BOOK-ENTRY SYSTEM

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## DTC AND ITS BOOK-ENTRY SYSTEM

*The following information has been provided by DTC. The state takes no responsibility for the accuracy or completeness thereof, or for the absence of material changes in such information subsequent to the date hereof. Beneficial Owners should confirm the following with DTC or the Participants (as hereinafter defined).*

1. The Depository Trust Company ("DTC"), New York, NY, will act as securities depository for the Certificates. The Certificates 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 certificate will be issued for each Principal Payment Date of the Certificates, each in the aggregate principal amount represented by such Certificates, and will be deposited with DTC.

2. 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 3.5 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments (from over 100 countries) that DTC's participants ("Direct Participants") deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities through electronic computerized book-entry transfers and pledges between Direct Participants' accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation ("DTCC"). DTCC is the holding company for DTC, National Securities Clearing Corporation and Fixed Income Clearing Corporation, all of which are registered clearing agencies. DTCC is owned by the users of its regulated subsidiaries. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). DTC has Standard & Poor's rating of AA+. 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 (which website is not incorporated herein by reference).

3. Purchases of Certificates under the DTC system must be made by or through Direct Participants, which will receive a credit for the Certificates on DTC's records. The ownership interest of each actual purchaser of each Certificate ("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, but Beneficial Owners are 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 Certificates are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in the Certificates, except in the event that use of the book-entry system for the Certificates is discontinued.

4. To facilitate subsequent transfers, all Certificates deposited by Direct Participants with DTC are to be 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 Certificates 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 Certificates; DTC's records reflect only the identity of the Direct Participants to whose accounts such Certificates 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.

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

6. Prepayment notices shall be sent to DTC. If less than all of the Certificates of a Principal Payment Date are being prepaid, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such maturity to be prepaid.

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

8. Principal, prepayment and interest payments on the Certificates will be made to Cede & Co. or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the state or the Certificate Registrar, on the 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 are the responsibility of such Participant and not of DTC, the Fiscal Agent or the state, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of principal, prepayment and interest payments to Cede & Co. (or any other nominee as may be requested by an authorized representative of DTC) is the responsibility of the state or the Fiscal Agent, 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.

9. DTC may discontinue providing its services as depository with respect to the Certificates at any time by giving reasonable notice to the state or the Fiscal Agent. Under such circumstances, in the event that a successor depository is not obtained, Certificates are required to be printed and delivered.

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

11. The information in this appendix concerning DTC and DTC's book-entry system has been obtained from sources that the state believes to be reliable, but the state takes no responsibility for the accuracy thereof.