SOUTHWESTERN POWER ADMINISTRATION

ANNUAL REPORT 2008

THIS PAGE INTENTIONALLY LEFT BLANK

TABLE OF CONTENTS

©Published December 2010.


ltec

The Honorable Dr. Steven Chu
Secretary of Energy
Washington, D.C. 20585

Dear Secretary Chu,

I am pleased to present the financial statements and operating data for Southwestern Power Administration (Southwestern) for Fiscal Year (FY) 2008.

In FY 2008, Southwestern delivered over 7.3 billion kilowatt-hours of energy to its wholesale customers – nearly 31% more than average due to numerous record rainfall amounts in the southwest region.

These record amounts produced revenues which exceeded the average annual revenue requirement by nearly $20 million and resulted in over $200 million in economic benefits to the region.

Yet even as Southwestern exceeded its goals of marketing and delivering Federal hydroelectric power to our customers, we stayed focused on safety, security, and reliability.

For example, we maintained our nearly 1,400 miles of high-voltage transmission lines, substations, and communications sites while achieving a Recordable Accident Frequency Rate of 0.0, a record that reflects Southwestern's safety achievement of no recordable injuries for every 200,000 hours worked.

We kept our rights-of-way secure from vegetation and other obstacles, work that not only supports our mission but also promotes reliability of the regional and National grid.

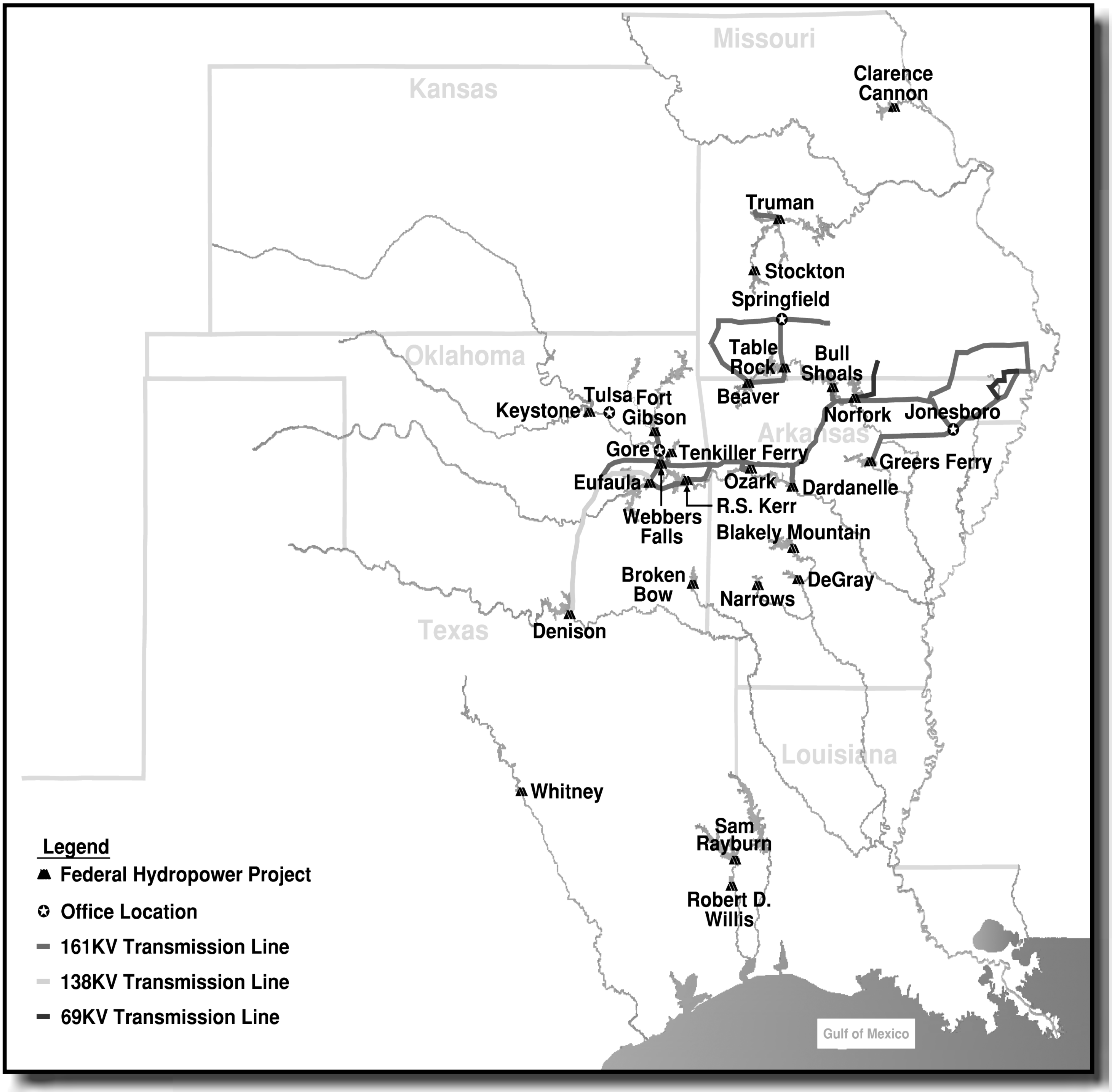
We exceeded all North American Electric Reliability Corporation (NERC) Control Performance Standards (CPS-1 and CPS-2), and maintained regulation and reserve obligations and reactive reserve margins to ensure the reliability of the bulk electric system, even during extended periods of restricted hydro operations due to unusually high project inflows.

Finally, we continued our partnerships with the Department of Energy, the U.S. Army Corps of Engineers, our customers, and other Federal power stakeholders, partnerships that are vital to our continued success in marketing and delivering carbon-free, renewable, and domestically produced energy to our customers and to the Nation.

Sincerely,

Jon Worthington
Administrator

SOUTHWESTERN SYSTEM MAP



ABOUT SOUTHWESTERN

Southwestern was established in 1943 by the Secretary of the Interior as a Federal Agency that today operates within the Department of Energy as authorized by Section 5 of the Flood Control Act of 1944.

As one of four Power Marketing Administrations in the United States, Southwestern markets hydroelectric power in Arkansas, Kansas, Louisiana, Missouri, Oklahoma, and Texas from 24 U.S. Army Corps of Engineers multipurpose dams with a generating capacity of approximately 2,174 MW.

By law, Southwestern's power is marketed and delivered to not-for-profit municipal utilities and rural electric cooperatives. Southwestern has over one hundred such "preference" customers, and these entities ultimately serve over eight million end-use customers.

Southwestern operates and maintains 1,380 miles (2,220 km) of high-voltage transmission lines, substations, and a communications system that includes microwave, VHF radio, and state-of-the-art fiber optics. Staff members work from offices located in Gore, Oklahoma; Jonesboro, Arkansas; Springfield, Missouri; and Tulsa, Oklahoma. Power scheduling and plant dispatching are conducted on a 24-hour basis by staff in the Springfield Operations Center.

Annual revenue for Southwestern has averaged approximately $146 million over the last five years. This revenue is used to pay the cost of operating and maintaining the generation and transmission facilities and to repay the principal and interest on the Federal investment.

MISSION

Southwestern Power Administration's mission is to market and reliably deliver Federal hydroelectric power with preference to public bodies and cooperatives.

This is accomplished by maximizing the use of Federal assets to repay the Federal investment and participating with other water resource users in an effort to balance their diverse interests with power needs within broad parameters set by the U.S. Army Corps of Engineers, and implementing public policy.

VISION

Southwestern has an open and trusting partnership with its customers in meeting their business expectations for operation of the Federal hydropower system, and with the American public in meeting its financial obligations while providing good stewardship of regional water resources. The Southwestern work force is cost-conscious, team-based, and empowered to meet customer expectations.

AUTHORIZATION

The Flood Control Act of 1944 (58 Stat. 887, 890; 16 U.S.C.A. 825s) is Southwestern's main authorizing legislation. Through Section 5 of this Act and a series of Executive Orders, Southwestern's Administrator is authorized to "transmit and dispose of … power and energy in such manner as to encourage the most widespread use thereof at the lowest possible rates to consumers consistent with sound business principles." Southwestern is also authorized to draw up rate schedules for such power and energy, with the goal of recovering, with interest, the investment of the American people.

SOUTHWESTER FEDERAL POWER SYSTEM ENERGY PRODUCTION

Project	Fiscal Year On-Line Date	Installed Capacity (kW)	Estimated Annual Energy* (Millions kWh)	Actual Net Energy (Millions kWh)
Beaver	1965	112,000	172	161
Blakely Mountain	1956	75,000	169	119
Broken Bow	1970	100,000	129	186
Bull Shoals	1953	340,000	785	1,158
Clarence Cannon	1985	58,000	90	145
Dardanelle	1965	140,000	613	728
De Gray	1972	68,000	97	106
Denison	1945	70,000	219	195
Eufaula	1965	90,000	260	377
Ft Gibson	1953	45,000	191	313
Greers Ferry	1964	96,000	189	320
Harry S Truman	1982	**160,000	244	418
Keystone	1968	70,000	228	371
Narrows	1950	25,500	30	43
Norfork	1944	80,550	184	228
Ozark	1973	100,000	429	307
Robert D Willis	1989	7,350	37	14
Robert S Kerr	1971	110,000	459	750
Sam Rayburn	1966	52,000	114	80
Stockton	1973	45,200	55	94
Table Rock	1959	200,000	495	835
Tenkiller	1954	39,100	95	174
Webbers Falls	1974	60,000	213	240
Whitney	1955	30,000	73	40
Total		**2,173,700**	**5,570**	**7,402**

* For each of the 24 projects in Southwestern's marketing area, a planning study was conducted by the U.S. Army Corps of Engineers prior to construction to forecast the quantity of energy that could be produced under average hydrological conditions. The term "Estimated Annual Energy" used in the table above represents the quantity of this forecasted energy on an annual basis.

** Only 53,300 kW have been declared in commercial operation.

These pages contain unaudited supplementary information.

FEDERAL INVESTMENT IN TRANSMISSION FACILITIES IN SERVICE

	2008	2007
Total Cumulative Repayable Investment	$268,545,518	$260,508,866
Total Cumulative Unpaid Investment	$61,098,871	$62,395,481
Total Cumulative Investment Paid	$207,446,647	$198,113,385

ANNUAL REPAYMENT STATUS

	2008	2007
Revenues	**$52,351,741**	**$53,944,718**
Expenses		
Operations and Maintenance	29,937,660	27,067,111
Purchased power and service charge	10,025,622	19,287,886
Interest	3,055,197	2,985,001
Total Expenses	**$43,018,479**	**$49,339,998**
Revenue applied to Amortization (Annual Amortization)	**$9,333,262**	**$4,604,720**

SOURCE AND DISTRIBUTION OF ENERGY

Energy Source	Millions kWh	% of Total
Generated by Corps Plants	7,401.8	97.1%
Interchange	135.8	1.8%
Losses Purchases	76.7	1.0%
Direct Purchases	6.1	0.1%
Contract Exchange	0.1	0.0%
Total	**7,620.5**	**100.0%**

Energy Distribution	Millions kWh	% of Total
Cooperatives	4,963.6	65.1%
Municipalities	2,142.4	28.1%
Government Agencies	227.4	3.0%
Losses	166.4	2.2%
Interchange	118.7	1.6%
Utility Companies / Other	2.0	0.0%
Total	**7,620.5**	**100.0%**

FY 2008 - DETAIL OF BILLINGS TO CUSTOMERS

	Capacity (kW)	Energy Delivered (kWh)	Billings for Power Sales (Dollars)
Distribution Cooperatives			
Beauregard Electric Cooperative, Inc	7,900	29,700,045	659,467
Claiborne Electric Cooperative, Inc	4,900	18,421,547	409,035
Concordia Electric Cooperative, Inc	4,300	16,165,848	358,950
Dixie Electric Membership Corporation	16,300	61,279,842	1,360,672
Jefferson Davis Electric Cooperative, Inc	3,600	13,534,197	300,517
Kaw Valley Electric Cooperative, Inc	1,000	3,586,000	81,195
Nemaha-Marshall Electric Cooperative Association	1,000	3,586,000	81,195
Northeast Louisiana Power Cooperative, Inc	4,100	15,413,947	342,255
Pointe Coupee Electric Membership Corporation	2,700	10,150,646	225,387
South Louisiana Electric Cooperative Association	8,000	30,075,997	667,815
Southwest Louisiana Electric Membership Corporation	22,400	84,212,790	1,869,881
Valley Electric Membership Corporation	9,400	35,339,294	784,682
Washington-St Tammany Electric Cooperative, Inc	7,800	29,324,097	651,119
Total	**93,400**	**350,790,250**	**7,792,170**
Generation and Transmission Cooperatives			
Arkansas Electric Cooperative Corporation	189,000	698,435,000	15,520,104
Associated Electric Cooperative, Inc	478,000	1,814,205,000	39,718,331
Brazos Electric Power Cooperative, Inc	35,200	59,778,000	1,904,185
Kansas Electric Power Cooperative, Inc	100,000	378,409,000	8,350,892
Northeast Texas Electric Cooperative, Inc	127,500	421,951,000	9,723,277
Rayburn Country Electric Cooperative, Inc	44,100	124,955,873	2,730,471
Sam Rayburn Dam Electric Cooperative, Inc	52,000	79,923,000	3,456,696
Tex-La Electric Cooperative of Texas, Inc	28,200	79,529,127	1,737,114
Western Farmers Electric Cooperative	260,000	955,594,000	21,276,632
Total	**1,314,000**	**4,612,780,000**	**104,417,702**
Joint Action Agencies			
Kansas Municipal Energy Agency*	11,200	40,508,000	908,570
Louisiana Energy and Power Authority**	12,900	37,326,000	970,698
Sam Rayburn Municipal Power Agency***	7,350	14,272,670	815,580
Total	**31,450**	**92,106,670**	**2,694,848**
Government Agencies			
Fort Sill Military Reservation, Ft Sill, Oklahoma	36,700	136,340,370	3,022,647
McAlester Army Ammunition Plant, McAlester, Oklahoma	2,688	9,985,910	221,386
Vance Air Force Base, Enid, Oklahoma	5,900	21,611,951	480,651
WAPA Interchange Settlement		59,496,000	2,642,920
Total	**45,288**	**227,434,231**	**6,367,604**
SPP Reserve Sharing Companies			
	0	1,975,000	143,683
Total	**0**	**1,975,000**	**143,683**

* Served 24 Municipals with Federal Allocations in FY 2008.
** Served 7 Municipals with Federal Allocations in FY 2008.
*** Has Federal Allocation.

These pages contain unaudited supplementary information.

FY 2008 - DETAIL OF BILLINGS TO CUSTOMERS

	Capacity (kW)	Energy Delivered (kWh)	Billings for Power Sales (Dollars)
Municipalities			
Alexandria, Louisiana	10,700	38,484,000	868,598
Anthony, Kansas	300	1,087,000	24,506
Augusta, Arkansas	3,700	13,279,000	300,621
Bentonville, Arkansas	18,000	67,210,000	1,485,852
Carthage, Missouri	7,000	25,439,000	604,603
Clarksville, Arkansas	19,100	68,882,000	1,554,014
Coffeyville, Kansas	1,900	7,020,000	155,964
Comanche, Oklahoma	4,200	15,185,454	341,330
Copan, Oklahoma	2,500	9,038,961	203,173
Duncan, Oklahoma	32,500	117,506,487	2,641,243
Eldorado, Oklahoma	1,300	4,700,260	105,650
Fulton, Missouri	3,000	10,828,000	244,270
Goltry, Oklahoma	900	3,254,026	73,142
Granite, Oklahoma	2,300	8,315,845	186,919
Hermann, Missouri	5,800	21,164,000	474,276
Higginsville, Missouri	3,000	10,991,000	246,210
Hominy, Oklahoma	10,000	36,155,845	812,690
Jonesboro, Arkansas	80,000	294,194,106	6,617,705
Jonesville, Louisiana	500	1,879,750	41,738
Kansas City, Kansas	38,600	137,868,000	3,088,929
Kennett, Missouri	11,000	40,436,000	954,902
Lafayette, Louisiana	18,600	41,752,000	1,306,335
Lamar, Missouri	12,000	44,104,000	987,622
Lexington, Oklahoma	4,100	14,823,895	333,203
Malden, Missouri	5,000	18,387,133	431,607
Manitou, Oklahoma	600	2,169,349	48,761
Minden, Louisiana	2,400	8,742,000	196,224
Natchitoches, Louisiana	2,600	8,984,000	206,636
New Madrid, Missouri	4,500	16,588,000	386,092
Nixa, Missouri	5,300	19,919,000	461,232
Olustee, Oklahoma	700	2,530,910	56,888
Paragould, Arkansas	50,500	185,710,028	4,359,226
Paris, Arkansas	10,800	39,560,865	879,835
Piggott, Arkansas	4,900	18,019,391	422,975
Poplar Bluff, Missouri	39,500	145,258,342	3,409,692
Purcell, Oklahoma	14,500	52,144,291	1,175,787
Ruston, Louisiana	4,900	16,645,000	379,909
Ryan, Oklahoma	1,900	6,869,608	154,411
Sikeston, Missouri	33,800	120,889,000	2,946,796
Skiatook, Oklahoma	11,000	40,623,000	902,794
Spiro, Oklahoma	4,000	14,462,337	325,076
Springfield, Missouri	50,000	187,922,000	4,171,306
Thayer, Missouri	2,800	10,028,000	227,106
Walters, Oklahoma	6,400	23,139,738	520,122
West Plains, Missouri	15,000	55,293,000	1,289,398
Wetumka, Oklahoma	2,600	9,400,519	211,300
Yale, Oklahoma	3,700	13,377,659	300,695
Total	**568,400**	**2,050,261,799**	**47,117,363**

Total Capacity (kW)	**2,052,538**
Total Energy (kWh)	**7,335,347,950***
Total Billings ($)	**168,533,371**

* Includes approximately 2.3 billion kilowatt-hours of off-peak, non-firm energy. Southwestern's composite cost for 1,200 hours of firm capacity and firm peaking energy was $0.05136/kWh in FY 2008.

Department of Energy
Southwestern Power Administration
One West Third Street
Tulsa, Oklahoma 74103-3502

December 2010

To the Users of the Southwestern Federal Power System Financial Statements:

The Financial Statements included in this 2008 Annual Report of the Southwestern Power Administration (Southwestern) are stand-alone Financial Statements and do not include the power portion of the U.S. Army Corps of Engineers (Corps) in the six Districts in which Southwestern markets power.

It is our goal in the near future to supplement this 2008 Annual Report by publishing audited Southwestern and Corps Consolidated Financial Statements.

Respectfully,

Gary L. Swartzlander
Assistant Administrator
Office of Corporate Services/CFO
Southwestern Power Administration

SOUTHWESTERN POWER ADMINISTRATION

Financial Statements

September 30, 2008 and 2007

SOUTHWESTERN POWER ADMINISTRATION

Statements of Assets, Federal Investment, and Liabilities

September 30, 2008 and 2007

Assets	**2008**	**2007**
Utility plant:		
Plant in service	$ 268,545,518	260,508,866
Accumulated depreciation	(129,707,253)	(118,999,239)
Construction work in progress	17,009,102	18,534,234
Net utility plant	155,847,367	160,043,861
Current assets:		
Cash	30,487,717	33,866,520
Accounts receivable	16,305,470	14,953,653
Materials and supplies, at average cost	2,387,349	2,650,311
Total current assets	49,180,536	51,470,484
Banking exchange receivables	3,920,818	1,412,075
Purchased power and banking exchange deferral	—	20,273,405
Deferred workers' compensation	3,822,791	3,788,316
Other assets	22,877,170	18,000,526
Total assets	$ 235,648,682	254,988,667
Federal Investment and Liabilities		
Federal investment:		
Congressional appropriations	$ 959,184,555	929,019,577
Interest on Federal investment	72,952,903	68,445,347
Transfer to/from other Federal agencies, net	(145,697,173)	(97,776,715)
Gross Federal investment	886,440,285	899,688,209
Funds returned to U.S. Treasury	(757,215,315)	(745,855,837)
Investment of U.S. government	129,224,970	153,832,372
Accumulated net revenues	77,739,394	79,114,146
Total Federal investment	206,964,364	232,946,518
Current liabilities:		
Accounts payable and accrued liabilities	5,844,284	6,648,757
Accrued workers' compensation	4,668,374	4,632,955
Purchased power and banking exchange deferral	6,433,094	—
Advances for construction	11,738,566	10,760,437
Commitments and contingencies (notes 4 and 5)		
Total liabilities	28,684,318	22,042,149
Total Federal investment and liabilities	$ 235,648,682	254,988,667

See accompanying notes to financial statements and accountants' review report.

SOUTHWESTERN POWER ADMINISTRATION

Statements of Operations and Accumulated Net Revenues

For Fiscal Years Ended September 30, 2008 and 2007

	2008	2007
Operating revenues:		
Sales of electric power:		
Cooperatives	$ 111,848,349	93,188,224
Municipalities	49,818,636	44,570,290
Federal and state agencies	6,315,621	3,034,909
Investor owned utilities	133,955	117,442
Banking exchange	4,461,135	(2,188,371)
Transmission service charges for others	19,492,431	20,468,023
Other operating income	420,256	2,252,195
Gross revenue	192,490,383	161,442,712
Net purchased power credit and banking exchange deferral	(27,059,551)	(19,865,517)
Revenue distributed to Army Corp of Engineers	(113,079,091)	(87,632,477)
Net operating revenues	52,351,741	53,944,718
Operating expenses:		
Operation and maintenance	24,327,112	20,131,610
Purchased power and banking exchange	6,924,440	16,228,918
Depreciation	12,319,983	11,180,415
Transmission service charges by others	3,101,182	3,058,968
Retirement and other employee benefit expense	3,998,579	4,056,476
Total operating expenses	50,671,296	54,656,387
Net operating revenues (expense)	1,680,445	(711,669)
Interest on Federal investment	4,050,462	3,867,004
Allowance for funds used during construction (AFUDC)	(995,265)	(882,003)
Net interest expense	3,055,197	2,985,001
Net deficit	(1,374,752)	(3,696,670)
Accumulated net revenues:		
Balance, beginning of year	79,114,146	82,810,816
Balance, end of year	$ 77,739,394	79,114,146

See accompanying notes to financial statements and accountants' review report.

SOUTHWESTERN POWER ADMINISTRATION

Statements of Cash Flows

For Fiscal Years Ended September 30, 2008 and 2007

		2008	2007
Cash flows from operating activities:			
Net deficit	$	(1,374,752)	(3,696,670)
Adjustments to reconcile net deficit to net cash provided by operating activities:			
Revenue distributed to Army Corp of Engineers		113,079,091	87,632,477
Depreciation		12,319,983	11,180,415
Benefit expense paid by other Federal agencies		1,207,536	1,367,115
Interest on Federal investment		4,507,556	5,322,172
Allowance for funds used during construction		(995,265)	(882,003)
Increase (decrease) in assets:			
Accounts receivable		(1,351,817)	(4,648,056)
Materials and supplies		262,962	50,502
Purchased power and banking exchange deferral		20,273,405	26,814,589
Banking exchange receivables		(2,508,743)	(707,166)
Deferred workers' compensation		(34,475)	(222,034)
Other assets		(4,876,644)	(12,038,628)
Increase (decrease) in liabilities:			
Accounts payable and accrued liabilities		(804,473)	(1,675,473)
Accrued workers' compensation		35,419	272,968
Purchased power and banking exchange deferral		6,433,094	—
Advances for construction		978,129	7,554,383
Net cash provided by operating activities		147,151,006	116,324,591
Cash flows from investing activity:			
Additions to utility plant		(7,128,224)	(10,009,272)
Cash flows from capital financing activities:			
Congressional appropriations		30,164,978	29,998,340
Funds returned to U.S. Treasury		(124,438,569)	(98,594,812)
Transfer to/from other Federal agencies, net		(49,127,994)	(39,963,917)
Net cash used in capital financing activities		(143,401,585)	(108,560,389)
Net decrease in cash		(3,378,803)	(2,245,070)
Cash at beginning of year		33,866,520	36,111,590
Cash at end of year	$	30,487,717	33,866,520
Supplemental disclosure of noncash financing activity:			
Portion of Funds returned to U.S. Treasury on behalf of the Army Corp of Engineers	$	113,079,091	87,632,477

See accompanying notes to financial statements and accountants' review report.

SOUTHWESTERN POWER ADMINISTRATION

Notes to Financial Statements

September 30, 2008 and 2007

(1) Summary of Significant Accounting Policies

(a) General Information and Basis of Preparation of Financial Statements

The Southwestern Federal Power System (SWFPS) encompasses the operation of 24 hydroelectric power plants maintained and operated by the U.S. Army Corps of Engineers (Corps) and the transmission and marketing of power and energy from those plants by the Southwestern Power Administration, a unit of the U.S. Department of Energy. Southwestern and the Corps are separately managed and financed and each maintains its own accounting records. Nineteen generation plants contribute to an interconnected system and five projects are used to serve specific customer loads. As discussed in note 1(g), a portion of the revenues collected by Southwestern are distributed to the Corps. The accompanying financial statements reflect solely the transmission and power marketing activities of Southwestern and thus exclude certain activities of Southwestern that are not reimbursable through the rate-making process and the generating activities of the Corps. As a result, the accompanying financial statements do not include a complete presentation of the financial position, results of operations, changes in net federal investment, and cash flows of Southwestern. Southwestern's activities that are not reimbursable through the rate-making process are described further in note 1(o).

Southwestern is subject to the accounting regulations of the Federal Energy Regulatory Commission. Accounts are maintained in accordance with accounting principles generally accepted in the United States of America as established by Financial Accounting Standards Board (FASB), the uniform system of accounts prescribed for electric utilities by the FERC, the accounting practices and standards established by the DOE, and the requirements of specific legislation and executive directives issued by government agencies. Southwestern's financial statements follow the accounting and reporting guidance contained in Statement of Financial Accounting Standards (SFAS) No. 71, Accounting for the Effects of Certain Types of Regulation. Allocation of costs and revenues to accounting periods for rate-making and regulatory purposes may differ from bases generally applied by nonregulated companies. Such allocations to meet regulatory accounting requirements are considered to be accounting principles generally accepted in the United States of America for regulated utilities provided that there is a demonstrable ability to recover any deferred costs in future rates and such costs or revenues are accounted for as regulatory assets or liabilities.

(b) Confirmation and Approval of New Rates

Southwestern is not a public utility within the jurisdiction of FERC under the Federal Power Act. Under a Delegation Order issued by the Secretary of Energy, the Administrator of Southwestern has the authority to develop power and transmission rates for Southwestern's Federal power system. Such rates can be approved on an interim basis by the Deputy Secretary of Energy. FERC has the exclusive authority to confirm, approve, and place into effect on a final basis, to remand, or to disapprove, rates developed by the Administrator.

FERC's review is limited to: 1) whether the rates are the lowest possible consistent with sound business principles; 2) whether the revenue levels generated are sufficient to recover the costs of producing and transmitting electric energy including repayment within the period permitted by law; and 3) the assumptions and projections used in developing the rates. FERC shall reject decisions of the Administrator only if it finds them to be arbitrary, capricious or in violation of the law.

The rates in effect as of September 30, 2008 are summarized as follows:

The Integrated System rate schedules were placed into effect October 1, 2006 and were approved on a final basis by the FERC on February 27, 2007. These rate schedules incorporated a three-year phase-in of a 27.7% revenue increase and remain in effect through September 30, 2010.

The Robert D. Willis project rate required no rate action during FY 2008. The Robert D. Willis project rate was approved and confirmed by the FERC on February 23, 2007, for the period January 1, 2007 through September 30, 2010. The Sam Rayburn Dam project rate required a rate action during FY 2008, for a 22.8% revenue increase. The current rate in effect from October 1, 2007 through September 30, 2011 was confirmed and approved by the FERC on the final basis February 29, 2008.

(c) Utility, Plant, and Depreciation

Utility plant is stated at original cost. Property transferred from other government agencies is transferred at net book value. Cost includes direct labor and material, payments to contractors, indirect charges for engineering, supervision and similar overhead items, and allowance for funds used during construction. The costs of additions and betterments are capitalized. Repairs and minor replacements are charged to operation and maintenance expense. Generally, the cost of utility plant retired, together with removal costs less salvage, is charged to accumulated depreciation when the property is removed from service. Gains and losses are recognized only on sales of significant identifiable assets.

Depreciation on utility plant is computed on a straight-line basis over the estimated service lives of the various classes of property. Service lives currently range from 5 to 100 years for transmission plant and generating plant components.

(d) Cash

Cash held by Southwestern represents the unexpended balance of funds authorized by Congress, including customer advances, held at the U.S. Treasury. Cash received from the sale of power is generally deposited directly with the U.S. Treasury and is reflected as “Funds returned to U.S. Treasury” in the accompanying financial statements. Cash held for customer advances is restricted for the purposes agreed to between Southwestern and the customer.

(e) Congressional Appropriations

Southwestern receives Congressional Appropriations through DOE to finance its operation. In accordance with the Flood Control Act of 1944, Southwestern is responsible for repayment to the Federal government, with interest, of its appropriations, and the portion of Congressional Appropriations allocated to the Corps for construction and operations of the power projects.

(f) Purchased Power and Banking Exchange Deferral and Receivable

Southwestern utilizes a separate rate component (adder) to recover the cost of purchased power based upon the average purchased power costs expected to occur in the future. If the actual expenses of purchased power exceed the revenue generated from this adder, the cost is deferred for future recovery through rates. Likewise, if the expense is less than the adder, the excess revenue is deferred. In addition to the adder, Southwestern utilizes a separate rate component (adder adjustment), which is either positive or negative to address deferred expenses or excess revenues, respectively.

Southwestern has arrangements with certain customers in which excess power generated by the Corps is banked with the customer until needed by the power system and the customer has power available. The power system records a receivable for the power banked at the cost specified in the marketing arrangement. The net revenue or expense associated with banking activity is deferred until the power is returned or delivered.

(g) Operating Revenues

Operating revenues are recorded on the basis of service rendered. Rates are established under requirements of the Flood Control Act of 1944, related legislation and executive departmental directives, and are to provide sufficient revenues to meet all required repayment of system costs, including operation and maintenance expenses less depreciation, interest, and payment to the U.S. Treasury for the Federal investment in utility plant. Rates are intended to provide for recovery of the Federal investment in transmission and generating facilities within the service lives of the assets, not to exceed 50 years from the date placed in service, while operation and maintenance costs and interest on Federal investment are intended to be recovered annually.

As set forth in “Utility, Plant, and Depreciation” above, assets are being depreciated for financial reporting purposes using the straight-line method over their estimated service lives, which currently range from 5 to 100 years for transmission and generating plant components. Accordingly, annual depreciation charges are not matched with the recovery of the related capital costs and will, in the case of generating facilities, continue beyond the period within which such costs will have been recovered through rates.

While energy and transmission rates are established to recover the costs of operating the power projects, rates are also required to be at the lowest possible level, consistent with sound business principles. Over the life of the power system, accumulated net revenues represent differences between the timing of the recognition of expenses and related revenues, resulting primarily from the difference between the recognition of depreciation and the related recovery of the U.S. Treasury’s investment in utility plant. Southwestern is a Federal entity, thus at any given time the accumulated net revenue, to the extent available, is committed to the repayment of the Federal investments.

The practices followed by Southwestern are in conformity with the accounting practices and standards established by the DOE and the requirements of specific legislation and executive directives issued by government agencies. Based upon guidelines established in DOE Order RA 6120.2, revenues distributed to the Corps cover annual operating expenses including interest, with the remainder applied to the unpaid generation investment.

(h) Accounts Receivable

Southwestern's accounts receivable consists generally of receivables for power and energy sold to its customers who are primarily public bodies and cooperatives. Southwestern provides for uncollectible accounts if collection is in doubt. At September 30, 2008 and 2007, no allowance for uncollectible accounts was considered necessary.

Financial instruments, which potentially subject Southwestern to credit risk, include accounts receivable for customer purchases of power, transmission or other products and services. These receivables are primarily with a group of diverse customers that are generally large, stable and established organizations which do not represent a significant credit risk. Although Southwestern is affected by the business environment of the utility industry, management does not believe a significant risk of loss from a concentration of credit exists.

(i) Interest on Federal Investment

Interest on repayable Federal investment is a cost mandated by the Secretary of Energy and by the FERC. Southwestern computes interest in accordance with DOE Order RA 6120.2, which provides that interest be computed on the remaining investment after revenues have been applied to recovery of costs during the year, any prior year unpaid costs, and then to Federal investment bearing the highest interest rate.

(j) Allowance for Funds Used During Construction (AFUDC)

The FERC Uniform System of Accounts defines AFUDC as the net costs for the period of construction of borrowed funds used for construction purposes and a reasonable rate on other funds when so used. While cash is not realized currently from this allowance, it is realized under the rate making process over the repayment life of the related property through increased revenues resulting from a higher recoverable investment. The interest rates used are established by law, administrative order, or administrative policy for the fiscal year during which the construction commenced (4.875% for FY 2008 and 2007).

(k) Retirement Benefits

Southwestern employees participate in one of the following contributory defined benefit plans: the Civil Service Retirement System (CSRS) or Federal Employees Retirement System (FERS). Agency contributions are based on eligible employee compensation and are submitted to benefit program trust funds administered by the Office of Personnel Management (OPM). Based on statutory contribution rates, the FY 2008 cost factor under CSRS is 25.2% of basic pay, a 0.2% increase from FY 2007. The FY 2008 cost factor under FERS is 12% of basic pay, the same as for FY 2007. The contribution levels, however, are legislatively mandated and do not reflect the current full cost requirements to fund the plans. Other retirement benefits administered by the OPM include the Federal Employees Health Benefits Program which costs $5,220 and $5,572 per enrolled employee, as of FY 2008 and FY 2007, respectively, and the Federal Employee Group Life Insurance Program which has an FY 2008 cost factor of 0.02% of basic pay, the same as for FY 2007.

In addition to the amounts contributed to the CSRS and FERS as stated above, Southwestern recorded an expense and related liability for the pension and other postretirement benefits in the financial statements of $1,216,755 and $1,367,115 for the years ended September 30, 2008 and 2007, respectively. This amount reflects the contribution made on behalf of Southwestern by OPM to the benefit program trust funds.

(l) Workers' Compensation

Workers' compensation consists of two elements: actuarial liability associated with workers' compensation cases incurred for which additional claims may still be made in the future (future claims) and a liability for expenses associated with actual claims incurred and paid by the Department of Labor (DOL), the program administrator, whom Southwestern must reimburse. The DOL and the DOE determine Southwestern's actuarial liability associated with workers' compensation cases. The actuarial liability for future claims was determined using historical benefit payment patterns and the U.S. Treasury discount rates.

The recovery of these future claims will be deferred for purposes of the rate-making process until such time as the future claims are actually submitted and paid by the DOL. Therefore, the recognition of the expense associated with this actuarially determined liability has been recorded as deferred workers compensation in the Statement of Assets, Federal Investment, and Liabilities in accordance with SFAS No. 71 to reflect the effects of the rate-making process. Southwestern has recorded $3,822,791 and $3,788,316 of actuarial liabilities as of September 30, 2008 and 2007, respectively.

(m) Income Taxes

As an agency of the U.S. government, Southwestern is exempt from all income taxes imposed by any governing body, whether it is a federal state or common wealth of the United States.

(n) Use of Estimates

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

(o) Scope of Report

The financial statements are limited in scope due to certain non-reimbursable activities that are not included in the financial statements. Southwestern has agreements with Federal and non-Federal customers to provide services on a fee basis where the fee is generally paid in advance. The operating revenues and expenses related to these services are excluded from the rate-making process. A portion of cash and advances from construction on the accompanying financial statements relate to these activities.

In December 2004, the U.S. Congress passed and the President signed the Commercial Spectrum Enhancement Act (CSEA, Title II of P.L. 108-494), creating the Spectrum Relocation Fund (SRF) to streamline the relocation of Federal systems from existing spectrum bands to accommodate commercial use by facilitating reimbursement to affected agencies of relocation costs. In FY 2007 Southwestern received $8 million in spectrum relocation funds, as approved by the Office of Management and Budget, and as reported to the Congress. SRF activity is excluded from the FY 2008 and FY 2007 financial statements. This activity is not reimbursable through the rate-making process.

(2) Regulatory Assets and Liabilities

Southwestern's regulatory assets and liabilities at September 30, 2008 and 2007, consists of the following:

		2008	2007
Regulatory assets:			
Nonfund deferred activity	$	22,739,043	17,584,239
Purchased power and banking exchange deferral		—	20,273,405
Deferred workers' compensation		3,822,791	3,788,316
Total	$	26,561,834	41,645,960
Regulatory liabilities:			
Purchased power and banking exchange deferral	$	6,433,094	—

Southwestern's financing sources include annual appropriations, Federal power receipts (Use of Receipts) and alternative financing arrangements to fund its operations. Revenues received from the sale of Federal and purchased power are generally deposited with the Treasury. However, due to fluctuations in the amount of annual appropriations received to fund maintenance, rehabilitation, and modernization of the Southwestern Federal power system facilities, Southwestern has established an alternative financing program under reimbursable authority regulations. Under agreements with customers to finance certain operational projects, a portion of the funds received from the sale of power are net billed, allowing a portion of the funds to be retained by Southwestern to finance future projects. Nonfund deferred financing activity represents the amount of alternative financing funds authorized and collected which are deferred until completion of the project at which time these assets will be classified as a transfer, expense, or capital asset.

Purchased power and banking exchange deferral account represents the deferral of net revenue or expenses associated with net purchased power and banking exchange activities as follows:

	Purchased power and banking exchange deferral
September 30, 2006	$ 47,087,994
Purchased power adder revenue	(24,530,776)
Purchased power expense	5,402,300
Net banking exchange	(737,041)
Net purchased power and banking exchange	(19,865,517)
Non-Federal losses paid in-kind	(8,544,778)
Interest on deferred activities and other	1,595,706
September 30, 2007	20,273,405
Purchased power adder revenue	(25,159,183)
Purchased power expense	486,531
Net banking exchange	(2,386,899)
Net purchased power and banking exchange	(27,059,551)
Interest on deferred activities and other	353,052
September 30, 2008	$ (6,433,094)

The deferred workers' compensation represents a regulatory asset that will be expensed as future claims are actually submitted and paid by the DOL (see note l (l)).

(3) Investment of U.S. Government

Construction and operation of Southwestern's transmission system are financed through Congressional Appropriations. The exceptions are capital assets funded through the alternative financing arrangements, and the funding of the construction of the Robert Douglas Willis project by non-Federal parties. The U.S. Government's investment in each generating project and each year's investment in the transmission system is to be repaid to the U.S. Treasury within the service lives of the assets, not to exceed 50 years from the time the facility is placed in service. There is no requirement for repayment of a specific amount on an annual basis.

Annual revenues are first applied to the current year operating expenses (less depreciation) and interest expense. All annual amounts for such expenses have been paid through fiscal year 2008. Remaining revenues are to be first applied to repayment of operating deficits (which include all expenses except depreciation), if any, and then to repayment of the Federal investment. To the extent possible, while still complying with the repayment period established for each increment of investment and unless otherwise required by legislation, repayment of the investment is to be accomplished by a repayment of the highest interest-bearing investment first. Interest rates applied to the unamortized initial investment of the U.S. Government in the Corps' hydroelectric plants range from 2.5% to 6.0% for unpaid facilities in service prior to FY 2008 and 4.875% for facilities placed in service during FY 2008. The rates have been set by law, by administrative order pursuant to law, or by administrative policies using the U.S. Senate Document No. 97 formula for the fiscal year during which the appropriations were requested.

(4) Commitments and Contingencies

(a) General

Based on the 2008 Integrated System Power Repayment Study prepared as of September 30, 2008, the projected increase in capital investment in 2009 is $81,687,614, which includes $11,339,400 for transmission facilities and $70,348,214 for generating facilities. The five-year investment increase projected in the 2008 Integrated System Power Repayment Study for FY 2009 through FY 2013 is estimated to cost $485,056,656.

Southwestern sells power to customers under long-term sales contracts, which range from 10 to 15 years and require Southwestern to provide a minimum of 1,200 kilowatt hours per kilowatt of peaking contract demand per year, subject to scheduling constraints outlined in each customer's contract. If sufficient power is unavailable to Southwestern from Corps hydroelectric facilities to meet these commitments, Southwestern may be required to purchase power from other sources to meet these commitments. The cost to purchase such power is recovered through the purchased power adder discussed more fully in note 1(f).

(b) Legal

Southwestern is a party to certain claims and legal actions arising in the ordinary course of business. In management's opinion, these actions will not have a material adverse effect on the financial condition or results of operations of Southwestern during fiscal year 2008 and 2007.

(5) Leases

Southwestern is obligated under a 10-year operating lease for office space. This lease consists of a 5-year firm term for the first 5-years and the option to terminate during the second 5-year term. This lease commenced January 1, 2004 and is scheduled to terminate December 31, 2013. Future minimum lease payments as of September 30, 2008 are:

Year ending September 30:		
2009	$	691,000
2010		655,000
2011		656,000
2012		677,000
2013		679,000
Total future minimum lease payments	$	3,358,000

Rent expense for operating leases during the years ended September 30, 2008 and 2007 was $625,000 and $623,000, respectively.

(6) Subsequent Events

Southwestern has evaluated subsequent events from the balance sheet date through October 4, 2010, the date at which the financial statements were available to be issued, and determined there are no other items to disclose.

THIS PAGE INTENTIONALLY LEFT BLANK

THIS PAGE INTENTIONALLY LEFT BLANK

SOUTHWESTERN POWER ADMINISTRATION ADDRESSES

WEB: www.swpa.gov

E-MAIL: info@swpa.gov

GORE MAINTENANCE
Rt. 3, Hwy. 10
Gore, OK 74435-9802
Voice: 918-489-5582
Fax: 918-489-5527

JONESBORO MAINTENANCE
305 North Floyd Street
Jonesboro, AR 72401-1908
Voice: 870-972-4686
Fax: 870-932-6153

SPRINGFIELD MAINTENANCE & OPERATIONS CENTER
2858 South Golden
Springfield, MO 65807-3207
Maintenance Numbers:
Voice: 417-881-8772
Fax: 417-891-2688
Operations Numbers:
Voice: 417-881-1820
Fax: 417-891-2683

TULSA HEADQUARTERS
One West Third Street
Tulsa, OK 74103-3502
Voice: 918-595-6600
Fax: 918-595-6656

WASHINGTON D.C. LIAISON OFFICE
U.S. Department of Energy
Room 8G-027/Forrestal
Washington, DC 20585-1615
Voice: 202-586-5581
Fax: 202-586-6261

U.S. DEPARTMENT OF ENERGY