

FITCH RATES CHELAN COUNTY PUBLIC UTILITY DIST.'S (WASHINGTON) \$134MM SUB CONSOLIDATED SYS REVS 'AA'

Fitch Ratings-New York-24 April 2007: Fitch has assigned an 'AA' rating to Chelan County Public Utility District No. 1, Washington's (the district) \$93.8 million in auction rate subordinate consolidated system revenue bonds, series 2007A and up to \$40 million fixed rate subordinated consolidated system revenue bonds, series 2007B (subject to AMT) and series 2007C (non-AMT). The bonds are secured by the net revenues of the 'consolidated system', which includes the district's electric distribution, water, wastewater, telecom, and the Lake Chelan hydroelectric production systems. In addition, Fitch affirms the 'AA' rating on Chelan's associated \$636 million outstanding senior hydro consolidated system revenue bonds, \$291.3 million of Rock Island project revenue bonds, and \$11.8 million Rocky Reach project revenue bonds. The Rating Outlook is Stable.

The series 2007A (subject to AMT) will be used to refund a portion of the outstanding senior hydro consolidated system revenue bonds (series 1996A, B, C, D, and 1997A[I-V]). Proceeds from the 2007B/C bonds will finance a portion of the capital expenditures at the district. The 2007B/C are scheduled to price May 10 and the 2007A bonds May 30, with Lehman Brothers as lead underwriter. The rating for the 2007 bonds reflects the unenhanced rating as both series are expected to be insured by the 'AAA' rated monoline bond insurers, XL Capital Assurance (series 2007A) and Financial Security Assurance Inc. (series 2007B/C).

Despite Chelan's various senior, subordinate, consolidated and project liens, Fitch rates all long term obligations 'AA'. While the distribution system and hydro generating projects are accounted for and financed separately, Fitch still views them as an integrated system. Additionally, the senior consolidated system lien is now closed and there are cross default provisions in the subordinated consolidated debt resolution that further link certain liens in the unlikely event of default. The district's operating lien going forward is the subordinated consolidated system lien.

The district's high credit quality stems from its considerably low cost hydroelectric power resources, very competitive retail rates (average of 3.0 cents per kwh), solid financial performance, with ample cash reserves, and successful federal operating relicensing of two of their three hydroprojects thus far. Credit risks are few and manageable including attaining FERC approval to renew the operating license for Chelan's Rocky Reach hydroproject (anticipated this year), the distribution system's considerable reliance on net margins from surplus wholesale power sales, and the risk that federal/state fish protection regulations could change and affect operations at the hydroelectric projects.

Chelan's low power costs reflect its ownership of three hydroelectric projects along the Columbia River (Rock Island, Rocky Reach and Lake Chelan projects), which have a combined generating capacity of nearly 2000 MW. The average cost of hydro production for these facilities was an exceptionally low \$16 per mwh in 2006, which compares very well against the largest hydropower producer in the pacific northwest, Bonneville Power Administration, at closer to \$30/mwh. Roughly 44% of the hydroprojects' output is currently allocated for use by the district, including power purchased by Alcoa, with the remaining 56% allocated via long-term take-or-pay agreements to several northwest utilities (including Puget Sound Energy, Inc., Portland General Electric Col, PacifiCorp, and Avista Corp.).

Given the district's allocation of hydropower, the distribution system is long power at most times of the year, except for the coldest winter days. As a result, the district weathered the northwest severe drought conditions and power crisis of 2000-2001 better than most of their peers. Prospectively, the district will have ample hydropower resource allocation to meet native load growth for the foreseeable future.

With respect to the federal relicensing of Rocky Reach hydroelectric project, Chelan is in the final stages of FERC's review process and a decision is anticipated later this year. To Chelan's

management's credit, the development of the habitat conservation plans for Rocky Reach and Rock Island, not only set a boundary on future fish protection expenditures but also seems to have helped move the FERC review process along somewhat smoother.

A final note, the 2007 bonds will be issued under a new subordinated consolidated system master resolution. Under the new subordinated resolution, the district made an effort to tighten bond covenants that were somewhat loose in the senior consolidated lien. The key changes to the resolution include: an adjusted, more encompassing rate covenant, a stronger additional bonds test, the creation of a rate stabilization fund, and the addition of a more standardized flow of funds. With the new rate covenant resolution calculation, the district's debt service coverage figures will decline in comparison to prior years' coverages, pursuant to the senior lien consolidated resolution coverage. The new resolution rate covenant calculation is more conservative as it also includes total debt and revenues associated with senior consolidated system bonds that were issued by the district, but then loaned to the hydroprojects, which are cost of service projects. While the 2007A bonds will be used to refund a portion of senior consolidated system debt, the district currently has no plans to refund any additional senior consolidated system bonds at this time.

Chelan County PUD No. 1 is an integrated electricity provider, with approximately 44,400 retail customers in central Washington. The retail distribution system is part of Chelan's 'consolidate system' and further includes: a small water and wastewater system (5000 user/ 440 users), a fiber optics system (4800 end users), and the Lake Chelan hydroelectric project (48 MW). As mentioned above, the district also owns two other large hydroelectric projects, the Rock Island and Rocky Reach projects, which may be separately financed and are accounted for separately.

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