CITY OF CLEVELAND, OHIO

DEPARTMENT OF PUBLIC UTILITIES
DIVISION OF CLEVELAND PUBLIC POWER

REPORT ON AUDITS OF FINANCIAL STATEMENTS
For the years ended December 31, 2007 and 2006

CITY OF CLEVELAND, OHIO

DEPARTMENT OF PUBLIC UTILITIES
DIVISION OF CLEVELAND PUBLIC POWER

TABLE OF CONTENTS

	Page
Independent Accountants' Report	1-2
Management's Discussion and Analysis	3-14
Balance Sheets	16-17
Statements of Revenues, Expenses and Changes in Net Assets	19
Statements of Cash Flows	20-21
Notes to Financial Statements	22-38

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Mary Taylor, CPA
Auditor of State

INDEPENDENT ACCOUNTANTS' REPORT

Division of Cleveland Public Power
Department of Public Utilities
City of Cleveland
Cuyahoga County
601 Lakeside Avenue
Cleveland, Ohio 44114

To the Honorable Frank G. Jackson, Mayor, Members of Council, and the Audit Committee:

We have audited the accompanying basic financial statements of the Division of Cleveland Public Power, Department of Public Utilities, City of Cleveland, Cuyahoga County, Ohio, (the Division) as of and for the years ended December 31, 2007 and December 31, 2006, as listed in the table of contents. These financial statements are the responsibility of the Division's management. Our responsibility is to express opinions on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to reasonably assure 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 audits provide a reasonable basis for our opinions.

As discussed in Note A, the financial statements present only the Division and do not purport to, and do not, present fairly the financial position of the City of Cleveland as of December 31, 2007 and December 31, 2006, and the respective changes in its financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Division of Cleveland Public Power, Department of Public Utilities, City of Cleveland, Cuyahoga County, Ohio, as of December 31, 2007 and December 31, 2006, and the respective changes in financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Lausche Building / 615 Superior Ave., NW / Twelfth Floor / Cleveland, OH 44113-1801
Telephone: (216) 787-3665 (800) 626-2297 Fax: (216) 787-3361
www.auditor.state.oh.us

Management's Discussion and Analysis is not a required part of the basic financial statements but is supplementary information the accounting principles generally accepted in the United States of America requires. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Mary Taylor

Mary Taylor, CPA
Auditor of State

June 4, 2008

CITY OF CLEVELAND, OHIO
DEPARTMENT OF PUBLIC UTILITIES
DIVISION OF CLEVELAND PUBLIC POWER

MANAGEMENT'S DISCUSSION AND ANALYSIS

GENERAL

As management of the City of Cleveland’s (the “City”) Department of Public Utilities, Division of Cleveland Public Power (the “Division”), we offer readers of the Division’s financial statements this narrative overview and analysis of the financial activities of the Division for the years ended December 31, 2007 and 2006. Please read this information in conjunction with the Division’s financial statements and footnotes that begin on page 16.

The Division was created in 1906 and charged with the responsibility of the distribution of electricity and related electric service to customers within its service areas. The Division operates a municipal electric system that is the largest in the State of Ohio and the thirty-seventh largest in the United States. The Division serves an area that is bound by the City limits and presently serves approximately 76,000 customers.

The Division is one of the very few municipal electric companies in the United States that competes with an investor-owned utility, in this case First Energy Corporation’s Cleveland Electric Illuminating Co. (CEI).

According to the 2000 census reports, the City’s population is approximately 478,000 people. There are approximately 224,000 residential dwelling units and 11,000 commercial units. The Division has distribution facilities in about 60% of the geographical area of the City, primarily on the east side.

The Division obtains substantially all of its power and energy requirements through agreements with various regional utilities and other power suppliers for power delivered through CEI interconnections. The balance of the Division's power and energy requirements are satisfied with production from the Division's three combustion turbine generating units and various arrangements for the exchange of short-term power and energy. To reduce its reliance on the wholesale market, the Division intends to participate in three generation projects through its membership in American Municipal Power-Ohio ("AMP-Ohio"), a nonprofit corporation comprised of municipal utilities. These plants, if constructed, are expected to be completed and operational in 2012 and 2013.

COMPARISON OF CURRENT YEAR’S AND PRIOR YEARS’ DATA

FINANCIAL HIGHLIGHTS

- The assets of the Division exceeded its liabilities (net assets) by $197,178,000, $186,575,000 and $178,867,000 at December 31, 2007, 2006 and 2005, respectively. Of these amounts, $72,648,000, $72,461,000 and $71,938,000 are unrestricted net assets at December 31, 2007, 2006 and 2005, respectively, that may be used to meet the Division’s ongoing obligations to customers and creditors.

- The Division’s total net assets increased by $10,603,000 and $7,708,000 during 2007 and 2006, respectively, and decreased by $1,114,000 during 2005. Operating revenue increased by $8,824,000 or 6.0%. Purchased power increased by $3,777,000 or 4.7% and total operating expenses increased by $5,816,000 or 4.4% for 2007. In addition, investment income increased by $1,132,000 or 38.6% whereas interest expense increased by $1,977,000 or 21.7% and amortization of bond issuance costs and discounts decreased by $932,000 or 52.5%, due to the bond refinancing completed in August 2006.

FINANCIAL HIGHLIGHTS (Continued)

- During 2007, the Division had an increase in capital assets, net of accumulated depreciation of $4,744,000. The principal capital expenditures in 2007 were for defective pole replacements, replacing and upgrading distribution feeders, work on the Euclid Corridor Transportation Project, purchase of vehicles, expansion of the Ridge Road substation and the continued implementation of automated meters. The automated meters allow for more accurate billing of consumption, more timely reading of meters and a reduction in man-hours associated with meter reading.

- The Division's total long-term bonded debt decreased by $8,045,000 and $12,255,000 for the years ended December 31, 2007 and 2006, respectively. These decreases are attributed to scheduled debt service payments to bondholders in both years, coupled with a refunding of bonds in 2006.

- In 2005, the Division was impacted by the introduction of Seams Elimination Cost Adjustment (SECA), which was mandated by the Federal Energy Regulatory Commission (FERC), see Footnote L. The Division paid SECA charges to Midwest Independent System Operator (MISO) from December 2004 to March 2006. In 2007, the Division received a SECA refund of $2,808,000 and have received $5,026,000 as of December 31, 2007. There is a likelihood that an additional $700,000 SECA refund might be received in 2008.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the Division's basic financial statements. The accompanying financial statements present financial information for the City's Division of Cleveland Public Power Fund, in which the City accounts for the operations of the Department of Public Utilities, Division of Cleveland Public Power. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The City, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

The Division of Cleveland Public Power Fund is considered an enterprise fund because the operations of the Division are similar to a private sector business enterprise. Accordingly, in accounting for the activities of the Division, the economic resources measurement focus and accrual basis of accounting is used. This is similar to businesses in the private sector.

The basic financial statements of the Division can be found on pages 16 – 21 of this report. The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the basic financial statements. The notes to the financial statements can be found on pages 22 - 38 of this report.

CONDENSED BALANCE SHEET INFORMATION

Provided below is condensed balance sheet information for the Division as of December 31, 2007, 2006 and 2005.

	2007	2006	2005
		(In thousands)	
Assets:			
Capital assets, net of accumulated depreciation	$ 313,866	$ 309,122	$ 303,761
Restricted assets	3,972	21,079	30,933
Unamortized bond issuance costs	2,330	2,590	1,737
Current assets	89,943	71,135	67,647
Total assets	410,111	403,926	404,078
Net Assets and Liabilities:			
Net assets:			
Invested in capital assets, net of related debt	119,606	109,695	95,977
Restricted for capital projects	1,522	1,461	4,534
Restricted for debt service	3,402	2,958	6,418
Unrestricted	72,648	72,461	71,938
Total net assets	197,178	186,575	178,867
Liabilities:			
Long-term obligations	186,658	192,193	197,692
Current liabilities	26,275	25,158	27,519
Total liabilities	212,933	217,351	225,211
Total net assets and liabilities	$ 410,111	$ 403,926	$ 404,078

Restricted assets*:* The Division's restricted assets decreased by $17,107,000 and $9,854,000 in 2007 and 2006, respectively, primarily due to purchases of capital assets, increased spending on capital projects and the reclassification of the incremental charges account to current assets.

Current assets: The Division's current assets increased by $18,808,000 and $3,488,000 in 2007 and 2006, respectively. The increase in 2007 is mainly due to the following:

- An increase in current cash and cash equivalents and investments of $22,091,000 resulting from increased billing and improved collections from the concerted effort to reduce tampering and the reduction in the threshold for disconnection. An increase in the Division's overall cash position created an increase in investment income. Cash and cash equivalents also increased from the reclassification of the incremental charges account.

CONDENSED BALANCE SHEET INFORMATION (Continued)

- The decrease in net accounts receivable of $3,796,000 in 2007 is due to increased collection activity and the receipt of a $2,518,000 SECA refund from American Electric Power recorded as a receivable in 2006.

- Net materials and supplies increased by $439,000 due to the increase in the quantity and value in cable in stores on hand at year end.

Capital assets: The Division's investment in capital assets as of December 31, 2007 amounted to $313,866,000 (net of accumulated depreciation). The total increase in the Division's investment in net capital assets for the current year was $4,744,000. A summary of the activity in the Division's capital assets during the year ended December 31, 2007 is as follows:

	Balance January 1, 2007	Additions	Reductions	Balance December 31, 2007
	(In thousands)			
Land	$ 4,863	$	$	$ 4,863
Land improvements	2,759			2,759
Utility plant	408,633	7,178	(280)	415,531
Buildings, structures and improvements	42,278			42,278
Furniture, fixtures, equipment and vehicles	42,882	3,653	(2,575)	43,960
Construction in progress	23,720	19,658	(7,527)	35,851
Total	525,135	30,489	(10,382)	545,242
Less: Accumulated depreciation	(216,013)	(17,056)	1,693	(231,376)
Capital assets, net	$ 309,122	$ 13,433	$ (8,689)	$ 313,866

CONDENSED BALANCE SHEET INFORMATION (Continued)

A summary of the activity in the Division's capital assets during the year ended December 31, 2006 is as follows:

	Balance January 1, 2006	Additions	Reductions	Balance December 31, 2006
	(In thousands)			
Land	$ 4,863	$	$	$ 4,863
Land improvements	2,759			2,759
Utility plant	403,120	5,513		408,633
Buildings, structures and improvements	42,278			42,278
Furniture, fixtures, equipment and vehicles	42,904	1,782	(1,804)	42,882
Construction in progress	8,181	21,174	(5,635)	23,720
Total	504,105	28,469	(7,439)	525,135
Less: Accumulated depreciation	(200,344)	(16,713)	1,044	(216,013)
Capital assets, net	$ 303,761	$ 11,756	$ (6,395)	$ 309,122

The principal capital expenditures during 2007 included the following:

- Euclid Corridor - $4,456,000
- Related engineering and overhead expense capitalized - $3,627,000
- Ridge Road Substation construction - $3,375,000
- Vehicles purchased - $1,526,000
- Pole replacement - $1,100,000
- Meters - $879,000
- Transformers - $863,000
- Distribution Engineering - $565,000
- Lake Road refurbishment - $447,000
- Distribution Feeders - $300,000

Additional information on the Division's capital assets, including commitments made for future capital expenditures, can be found in Notes A and D to the basic financial statements.

CONDENSED BALANCE SHEET INFORMATION (Continued)

Current liabilities increased by $1,117,000 in 2007 mainly due to the $290,000 increase in the current portion of long-term debt, the $458,000 increase in Due to other City of Cleveland Departments, Divisions or Funds and the $389,000 increase in current portion of accrued wages and benefits.

Long-term debt: The long-term obligation decrease of $5,535,000 in 2007 is attributed to scheduled debt service payments.

At December 31, 2007, the Division had total debt outstanding of $220,345,000. All bonds are backed by the revenues generated by the Division.

The Division issued revenue bonds in the public capital markets in the late 1980's and early 1990's to finance a substantial expansion to its service territory. The Division also issued bonds in mid 2006 to refinance a portion of its long term debt. This outstanding debt is being retired in accordance with repayment schedules through 2024.

The activity in the Division's debt obligations outstanding during the year ended December 31, 2007 is summarized below (excluding unamortized discounts, premiums and losses on debt refundings):

	Balance January 1, 2007	Debt Issued	Debt Refunded	Debt Retired	Balance December 31, 2007
			(In thousands)		
Mortgage Revenue Bonds:					
Mortgage Revenue Bonds 1994 A	$ 33,875	$	$	$ (965)	$ 32,910
Mortgage Revenue Bonds 1996	4,730			(850)	3,880
Mortgage Revenue Bonds 1998	31,145			(3,430)	27,715
Mortgage Revenue Bonds 2001	30,755			(2,800)	27,955
Mortgage Revenue Bonds 2006 A-1	95,265				95,265
Mortgage Revenue Bonds 2006 A-2	12,295				12,295
Mortgage Revenue Bonds 2006 B	20,325				20,325
Total	$ 228,390	$ -	$ -	$ (8,045)	$ 220,345

CONDENSED BALANCE SHEET INFORMATION (Continued)

The activity in the Division's debt obligations outstanding during the year ended December 31, 2006 is summarized below (excluding unamortized discounts, premiums and losses on debt refundings):

	Balance January 1, 2006	Debt Issued	Debt Refunded	Debt Retired	Balance December 31, 2006
			(In thousands)		
Mortgage Revenue Bonds:					
Mortgage Revenue Bonds 1994 A	$ 48,335	$	$ (14,460)	$	$ 33,875
Mortgage Revenue Bonds 1996	120,190		(114,655)	(805)	4,730
Mortgage Revenue Bonds 1998	38,655			(7,510)	31,145
Mortgage Revenue Bonds 2001	33,465			(2,710)	30,755
Mortgage Revenue Bonds 2006 A-1		95,265			95,265
Mortgage Revenue Bonds 2006 A-2		12,295			12,295
Mortgage Revenue Bonds 2006 B		20,325			20,325
Total	$ 240,645	$ 127,885	$ (129,115)	$ (11,025)	$ 228,390

The bond ratings for the Division's outstanding revenue bonds are as follows:

Moody's Investors Service	Standard & Poor's
A2	A-

The ratio of net revenue available for debt service to debt service requirements (revenue bond coverage) is a useful indicator of the Division's debt position to management, customers and creditors. The Division's revenue bond coverage for 2007, 2006 and 2005 was 223%, 179%, and 178%, respectively. Additional information on the Division's long-term debt can be found in Note B to the basic financial statements on pages 25 - 29.

Net Assets: Net assets serve as a useful indicator of a government's financial position. In the case of the Division, assets exceeded liabilities by $197,178,000, $186,575,000 and $178,867,000 at December 31, 2007, 2006 and 2005, respectively.

A large portion of the Division's net assets, $119,606,000 (61%) and $109,695,000 (59%) at December 31, 2007 and 2006, respectively, reflects its investment in capital assets (e.g., land, buildings, utility plant, furniture, fixtures, vehicles and equipment), net of accumulated depreciation, less any related, still-outstanding debt used to acquire those assets. The Division uses these capital assets to provide services to its customers. Consequently, these assets are not available for future spending.

Although the Division's investment in 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 resources, since the capital assets themselves cannot be used to liquidate these liabilities.

CONDENSED BALANCE SHEET INFORMATION (Continued)

An additional portion of the Division's net assets of $4,924,000 (2%) and $4,419,000 (2%) at December 31, 2007 and 2006, respectively, represents resources that are subject to external restrictions. These funds are set aside for the payment of revenue bonds or represent unspent bond proceeds relating to capital projects. The remaining balance of unrestricted net assets, $72,648,000 (37%) and $72,461,000 (39%) at December 31, 2007 and 2006, respectively, may be used to meet the Division's ongoing obligations to customers and creditors.

CONDENSED STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS INFORMATION

The Division's operations during 2007 increased its net assets by $10,603,000 as compared to an increase in net assets of $7,708,000 in 2006. Provided below are key elements of the Division's results of operations as of and for the years ended December 31, 2007, 2006 and 2005:

	2007	2006	2005
		(In thousands)	
Operating revenues	$ 155,171	$ 146,347	$ 150,263
Operating expenses	137,471	131,655	142,336
Operating income	17,700	14,692	7,927
Non-Operating Revenue (Expense):			
Investment income	4,061	2,929	1,883
Interest expense	(11,073)	(9,096)	(10,289)
Amortization of bond issuance costs and discount	(843)	(1,775)	(2,124)
Workers compensation refund	15	10	8
(Loss) gain on disposal of capital assets	(2)	2	2
Other	732	946	1,079
Total non-operating revenue (expense), net	(7,110)	(6,984)	(9,441)
Income (loss) before other contributions	10,590	7,708	(1,514)
Capital and other contributions	13		400
Increase (Decrease) in net assets	10,603	7,708	(1,114)
Net assets, beginning of year	186,575	178,867	179,981
Net assets, end of year	$ 197,178	$ 186,575	$ 178,867

- In 2007, operating revenues increased by $8,824,000. The increase is related to a 3% increase in kilowatt hours sold, the increase in purchased power costs passed through via the energy adjustment charge and the more accurate billing of consumption resulting from the implementation of the automated meters.

CONDENSED STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS INFORMATION (Continued)

- In 2006, operating revenues decreased by $3,916,000 largely related to a 4% decrease in kilowatt-hours sold due to a cooler than normal summer. However, there has been a significant improvement in collections as cash receipts for 2006 increased by $2,729,000 over 2005. Much of the improvement could be attributed to collection policy changes, such as lowering the dollar threshold for delinquent customers, and requiring full payment for restoring electric service for customers that have been disconnected for non-payment.

- In 2007, operating expenses increased $5,816,000. The increase is related to a $3,777,000 increase in purchased power costs associated with the additional kilowatt hours sold, and an increase of $1,313,000 in operations expenses attributed mainly to an increase of approximately $1,000,000 in administrative and other services expense.

- In 2006, operating expenses decreased by $10,681,000 primarily due to a $9,600,000 decrease in purchased power costs of which $5,339,000 was attributable to the ending of SECA payments in 2006 and a decrease of $1,486,000 in maintenance expense.

FACTORS EXPECTED TO IMPACT THE DIVISION'S FUTURE FINANCIAL POSITION OR RESULTS OF OPERATIONS

As a municipally-owned utility, the Division's mission is to improve the quality of life in the City of Cleveland by providing reliable, affordable energy and energy services to the residents and businesses of the City. In December 2006, the Division finalized its 5-year Strategic Business Plan ("SBP"). The SBP was prepared with the assistance of an independent consultant and addressed factors likely to impact the Division over the 2007-2012 period. The Division and the consultant analyzed federal and state regulatory and legislative developments, forecasted power costs, considered competitive factors as affected by the local regional transmission organization developments, and analyzed internal organization structure, strengths, weaknesses, threats, and opportunities. The consultant made ten recommendations that are intended to improve the Division's processes and strategically position the Division to address the major competitive factors likely to impact the Division .

One of the strategic recommendations from the SBP was to enhance infrastructure to increase customer capacity and improve reliability. As a result, the Division issued the Series 2008 Bonds to fund the Capacity Expansion Program. The Capacity Expansion Program includes three major components. It is designed to support and improve the Division's electric system reliability and provide for future load growth opportunities.

FACTORS EXPECTED TO IMPACT THE DIVISION'S FUTURE FINANCIAL POSITION OR RESULTS OF OPERATIONS (Continued)

Fourth Interconnect. The first component is the addition of the fourth 138kV interconnection with the FirstEnergy transmission system (the "Fourth Interconnect"). Increased capacity from the new distribution substations and their distribution circuits will allow the Division to transfer load from the existing distribution system to new circuits and provide electric service to future customers.

Southern Project. The second component of the Capacity Expansion Program includes the extension of the southern 138kV transmission system and addition of a 138/13.8 kV substation (the "Southern Project"). The proposed extension will complete a continuous transmission ring around the Division's system. The Southern Project also includes the construction of a new distribution substation. It will allow the Division to extend its electric service to serve potential customers in parts of the southern and western areas of the City that are outside the Division's current footprint as well as areas that are within the Division's current footprint but presently lack sufficient capacity.

Lake Road Project. The third component of the Capacity Expansion Program is the expansion of the Lake Road 11.5kV Substation and the 11.5kV system downtown (the "Lake Road Project"). The proposed expansion will allow the Division to serve new customers throughout the downtown areas including the Quadrangle, Flats, and Warehouse districts.

Anticipated Cost. The estimated cost of the Capacity Expansion Program is as follows:

Fourth Interconnect in 2009	$ 5.0 million
Southern Project in 2010	26.9 million
Lake Road Project in 2010	34.1 million
Total:	$66.0 million

On April 22, 2008, the Division issued $93,712,880 of Public Power System Revenue Bonds, Series 2008, primarily to fund the aforementioned system expansion. Of this amount, $21,105,000 was used to refund the $20,325,000 Series 2006B Public Power System Refunding Revenue Variable Rate Bonds. The remaining amount of $72,607,880 will be used to fund the system expansion, to pay capitalized interest and costs of issuance. Of this amount, $44,705,000 was issued as current interest bonds and $27,902,880 was issued as capital appreciation bonds.

In conjunction with the bonds issued in April 2008, Standard & Poor's affirmed the A- rating and revised their outlook from negative to stable. Moody's Investor Services affirmed their A2 rating.

The Division is focusing its marketing efforts on those sections of the City that were part of its earlier system expansion to increase the density of customers served. As the Division competes with CEI in these areas, density is measured as the number of the Division's customers on a given street versus the total customers available on that street. Additional customers can be added with little extra expense.

FACTORS EXPECTED TO IMPACT THE DIVISION'S FUTURE FINANCIAL POSITION OR RESULTS OF OPERATIONS (Continued)

The Division purchases most of its power requirements via contracts in the power markets. The Division intends to reduce its dependence on the purchased power market by acquiring interests in certain generating facilities. The Division's long term base load supply will include a mix of power provided by participation in AMP-Ohio's base load coal-fired project, the AMP-Ohio hydroelectric projects, and the Prairie State project. The Division will purchase 80 MW from AMP-Ohio's base load coal-fired project that is expected to be in operation in 2013. The Division is currently scheduled to purchase 35 MW from AMP-Ohio's hydroelectric projects that are expected to be in operation in 2011 and 2012. The Division will purchase up to 25 MW from AMP-Ohio's share of the Prairie State project that is projected to be on-line in 2011-2012. The Division is also investigating local opportunities to add alternative energy resources to its portfolio. The actual costs of these power purchases are passed through to its customers via an Energy Adjustment Charge on its bills. As power costs rise, sales revenue will also increase commensurately. These projects will not impact the Division financially unless actual power costs push the Division's billing rates significantly above those of its competition.

In February 2000, Cleveland City Council approved a change in the method of calculating the Energy Adjustment Charge that resulted in an increase to customers of about 4%, the proceeds of which were used for debt reduction and pole replacements from the passage of the charge to November 30, 2005. The increase is scheduled to end December 31, 2008. The Division intends, subject to approval by City Council, to continue this charge either in its present form or as part of base rates. Effective December 1, 2005, the proceeds of the increase, which was $13,561,000 in 2007, are no longer earmarked for a specific purpose, but the Division maintains a fund with about $11,824,000 of historic receipts that remains earmarked by City Council for debt reduction and pole replacements.

The Division owns and operates approximately 46,000 street lights in its service area and provides street lighting service to its customer, the City of Cleveland, under a published rate schedule. CEI owns, operates, and maintains the remaining 18,000 street lights in the City. The Division has negotiated the purchase of the CEI street lights for $4,000,000 and has obtained necessary legislation to authorize the transfer. CEI will continue to provide the power to street lights where the Division lacks distribution facilities but will charge an energy-based rate under CEI's tariff for municipally-owned street lights. The Division intends to continue to charge the City the current CEI rate for the newly acquired lights for a transition period, after which the lights will be billed at the Division's then-current standard rate. In addition to adding a new revenue stream, the transfer will enable the City to avoid CEI's proposed new street lighting tariff charges, potentially affecting the General Fund, and will allow for improved maintenance of the new lights by increasing responsiveness.

In early 2001, Ohio Electric Choice legislation created a new kilowatt-hour excise tax on electric power distributed to end users of electricity in the State by both investor-owned and municipal utilities. For municipal utilities, the state law requires the utility to remit the tax receipts to the municipality's General Fund. Under legislation passed in late 2007, the General Fund will transfer annually 50% of the kWh tax receipts to the Division beginning in 2008. This amount, estimated at $3,000,000, is earmarked to be used towards the acquisition of CEI's street lights in 2008.

ADDITIONAL INFORMATION

This financial report is designed to provide a general overview of the Division's finances. Questions concerning any of the information provided in this report or requests for additional information should be addressed to the Office of the Finance Director, City Hall, Room 104, 601 Lakeside Avenue, Cleveland, Ohio 44114.

BASIC FINANCIAL STATEMENTS

CITY OF CLEVELAND, OHIO

DEPARTMENT OF PUBLIC UTILITIES
DIVISION OF CLEVELAND PUBLIC POWER
BALANCE SHEETS
December 31, 2007 and 2006

	(*In thousands*) 2007	2006
ASSETS		
CAPITAL ASSETS		
Land	$ 4,863	$ 4,863
Land improvements	2,759	2,759
Utility plant	415,531	408,633
Buildings, structures and improvements	42,278	42,278
Furniture, fixtures, equipment and vehicles	43,960	42,882
	509,391	501,415
Less: Accumulated depreciation	(231,376)	(216,013)
	278,015	285,402
Construction in progress	35,851	23,720
CAPITAL ASSETS, NET	313,866	309,122
RESTRICTED ASSETS		
Cash and cash equivalents	2,578	7,903
Investments	1,383	13,162
Accrued interest receivable	11	14
TOTAL RESTRICTED ASSETS	3,972	21,079
UNAMORTIZED BOND ISSUANCE COSTS	2,330	2,590
CURRENT ASSETS		
Cash and cash equivalents	23,808	10,442
Restricted cash and cash equivalents	964	1,272
Investments	37,108	28,383
Receivables:		
Accounts receivable - net of allowance for doubtful accounts of $2,169,000 in 2007 and $1,338,000 in 2006	15,986	19,782
Unbilled revenue	2,111	1,943
Due from other City of Cleveland departments, divisions or funds	2,566	2,532
Accrued interest receivable	474	318
Materials and supplies - at average cost, net of allowance for obsolescence of $749,000 in 2007 and 2006	6,848	6,409
Prepaid expenses	78	54
TOTAL CURRENT ASSETS	89,943	71,135
TOTAL ASSETS	$ 410,111	$ 403,926

(Continued)

CITY OF CLEVELAND, OHIO

DEPARTMENT OF PUBLIC UTILITIES
DIVISION OF CLEVELAND PUBLIC POWER
BALANCE SHEETS
December 31, 2007 and 2006

	(In thousands) 2007	2006
NET ASSETS AND LIABILITIES		
NET ASSETS		
Invested in capital assets, net of related debt	$ 119,606	$ 109,695
Restricted for capital projects	1,522	1,461
Restricted for debt service	3,402	2,958
Unrestricted	72,648	72,461
TOTAL NET ASSETS	197,178	186,575
LIABILITIES		
LONG-TERM OBLIGATIONS-excluding amounts due within one year:		
Revenue bonds	185,925	191,383
Accrued wages and benefits	733	810
TOTAL LONG-TERM OBLIGATIONS	186,658	192,193
CURRENT LIABILITIES		
Current portion of long-term debt, due within one year	8,335	8,045
Accounts payable	8,616	8,459
Current payable from restricted assets	964	1,272
Due to other City of Cleveland departments, divisions or funds	1,522	1,064
Accrued interest payable	1,054	1,084
Current portion of accrued wages and benefits	4,178	3,789
Other accrued expenses	438	445
Customer deposits and other liabilities	1,168	1,000
TOTAL CURRENT LIABILITIES	26,275	25,158
TOTAL LIABILITIES	212,933	217,351
TOTAL NET ASSETS AND LIABILITIES	$ 410,111	$ 403,926

See notes to financial statements. (Concluded)

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CITY OF CLEVELAND, OHIO

DEPARTMENT OF PUBLIC UTILITIES
DIVISION OF CLEVELAND PUBLIC POWER
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
For the Years Ended December 31, 2007 and 2006

	(*In thousands*)	
	2007	**2006**
OPERATING REVENUES		
Charges for services	$ 155,171	$ 146,347
TOTAL OPERATING REVENUES	155,171	146,347
OPERATING EXPENSES		
Purchased power	83,523	79,746
Operations	19,247	17,934
Maintenance	17,645	17,262
Depreciation	17,056	16,713
TOTAL OPERATING EXPENSES	137,471	131,655
OPERATING INCOME	17,700	14,692
NON-OPERATING REVENUE (EXPENSE)		
Investment income	4,061	2,929
Interest expense	(11,073)	(9,096)
Amortization of bond issuance costs and discounts	(843)	(1,775)
Workers compensation refund	15	10
Gain on disposal of capital assets	(2)	2
Other	732	946
TOTAL NON-OPERATING REVENUE (EXPENSE), NET	(7,110)	(6,984)
INCOME (LOSS) BEFORE OTHER CONTRIBUTIONS	10,590	7,708
Capital and other contributions	13	
INCREASE (DECREASE) IN NET ASSETS	10,603	7,708
NET ASSETS, BEGINNING OF YEAR	186,575	178,867
NET ASSETS, END OF YEAR	$ 197,178	$ 186,575

See notes to financial statements.

CITY OF CLEVELAND, OHIO

DEPARTMENT OF PUBLIC UTILITIES
DIVISION OF CLEVELAND PUBLIC POWER
STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 2007 and 2006

	2007	2006
	(In thousands)	
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash received from customers	$ 160,224	$ 152,881
Cash payments to suppliers for goods or services	(9,526)	(6,774)
Cash payments to employees for services	(22,862)	(25,469)
Cash payments for purchased power	(83,339)	(82,080)
Electric excise tax payments to agency fund	(5,498)	(5,237)
NET CASH PROVIDED BY OPERATING ACTIVITIES	38,999	33,321
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Grants	13	
Workers compensation refund	15	10
NET CASH PROVIDED BY NONCAPITAL FINANCING ACTIVITIES	28	10
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Proceeds from sale of revenue bonds		131,644
Acquisition and construction of capital assets	(20,827)	(23,006)
Principal paid on long-term debt	(8,045)	(11,025)
Interest paid on long-term debt	(8,966)	(8,144)
Cash paid to escrow agent for refunding		(131,110)
NET CASH USED FOR CAPITAL AND RELATED FINANCING ACTIVITIES	(37,838)	(41,641)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of investment securities	(31,167)	(23,309)
Proceeds from sale and maturity of investment securities	34,719	27,041
Interest received on investments	2,992	3,026
NET CASH PROVIDED BY INVESTING ACTIVITIES	6,544	6,758
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	7,733	(1,552)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	19,617	21,169
CASH AND CASH EQUIVALENTS, END OF YEAR	$ 27,350	$ 19,617

(Continued)

CITY OF CLEVELAND, OHIO

DEPARTMENT OF PUBLIC UTILITIES
DIVISION OF CLEVELAND PUBLIC POWER
STATEMENTS OF CASH FLOWS

For the Years Ended December 31, 2007 and 2006

	(In thousands) 2007	2006
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
OPERATING INCOME	$ 17,700	$ 14,692
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	17,056	16,713
Changes in assets and liabilities:		
Accounts receivable, net	3,796	1,383
Unbilled revenue	(168)	228
Due from other City of Cleveland departments, divisions or funds	(34)	198
Materials and supplies, net	(439)	(700)
Accounts payable	157	480
Due to other City of Cleveland departments, divisions or funds	458	157
Accrued wages and benefits	312	112
Other accrued expenses	(7)	10
Customer deposits and other liabilities	168	48
TOTAL ADJUSTMENTS	21,299	18,629
NET CASH PROVIDED BY OPERATING ACTIVITIES	$ 38,999	$ 33,321

See notes to financial statements.

(Concluded)

NOTES TO FINANCIAL STATEMENTS
For the Years Ended December 31, 2007 and 2006

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Division of Cleveland Public Power (Division) is reported as an enterprise fund of the City of Cleveland's (City) Department of Public Utilities and is a part of the City's primary government. The Division was created for the purpose of supplying electrical services to customers within the City. The following is a summary of the more significant accounting policies.

Reporting Model and Basis of Accounting: The accounting policies and financial reporting practices of the Division comply with accounting principles generally accepted in the United States of America applicable to governmental units. Beginning January 1, 2002, the Division changed its financial reporting to comply with GASB Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments*. In May 2004, the GASB issued Statement No. 44, *Economic Condition Reporting: The Statistical Section*, which is effective for the year ended December 31, 2006. The Division has determined that GASB Statement No. 44 has no impact on its financial statements as of December 31, 2006. In June 2005, the GASB issued Statement No. 47, *Accounting for Termination Benefits*, which is effective for the year ended December 31, 2006. The Division has determined that GASB Statement No. 47 has no impact on its financial statements as of December 31, 2006. In June 2004, GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions,* which is effective for the year ended December 31, 2007. The Division has determined that GASB Statement No. 45 has no impact on its financial statements as of December 31, 2007. Effective January 1, 2007, the City implemented GASB Statement No. 48 "*Sales and Pledges of Receivables and Intra-Entity Transfers of Assets and Future Revenues*", which is effective for the year ended December 31, 2007. GASB Statement No. 48 established criteria to ascertain whether certain transactions should be regarded as sales or as collateralized borrowings, as well as disclosure requirements for future revenues that are pledged and sold. The implementation of GASB Statement No. 48 did not have an effect on the financial statements of the Division; however, additional disclosure related to revenues pledged for the repayment of revenue bonds has been provided in Note B.

The Division's net assets are accounted for in the accompanying balance sheet and the net assets are divided into the following categories:

- Amount invested in capital assets, net of related debt.
- Amount restricted for capital projects.
- Amount restricted for debt service.
- Remaining unrestricted amount.

In addition, certain additional financial information regarding the Division is included in these footnotes. The implementation of the new GASB statements did not result in a change in the Division's beginning net asset/equity balance as previously reported.

Basis of Accounting: The Division's financial statements are prepared under the accrual basis of accounting. Under this method, revenues are recognized when earned and measurable and expenses are recognized as incurred. Under GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Activities*, all Proprietary Funds will continue to follow Financial Accounting Standards Board (FASB) standards issued on

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

or before November 30, 1989. However, from that date forward, Proprietary Funds will have the option of either; 1) choosing not to apply future FASB standards (including amendments of earlier pronouncements), or 2) continuing to follow new FASB pronouncements (unless they conflict with GASB pronouncements). The Division has chosen not to apply future FASB standards.

Revenues: Revenues are derived primarily from sales of electricity to residential, commercial and industrial customers based upon actual consumption. Electricity rates are authorized by City Council and billings are made on a cyclical basis. Estimates for services between the end of the various cycles and the end of the year are recorded as unbilled revenue.

Statement of Cash Flows: The Division utilizes the direct method of reporting for the statement of cash flows as defined by the GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Non-expendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*. In a statement of cash flows, cash receipts and cash payments are classified according to operating, non-capital financing, capital and related financing, and investment activities.

Cash and Cash Equivalents: Cash and cash equivalents represent cash on hand and cash deposits maintained by the City Treasurer on behalf of the Division. Cash equivalents are defined as highly liquid investments with maturity of three months or less when purchased and include certificates of deposit, U.S. Treasury Bills, State Treasury Asset Reserve of Ohio (STAROhio) and repurchase agreements. The City's policy is to enter into repurchase agreements with local commercial banks and to obtain confirmation of securities pledged.

Investments: The Division follows the provisions of GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and External Investment Pools*, which requires governmental entities to report certain investments at fair value in the balance sheet and recognize the corresponding change in the fair value of investments in the year in which the change occurred. The fair value is based on quoted market prices.

The City has invested funds in STAROhio during fiscal year 2007 and 2006. STAROhio is an investment pool managed by the State Treasurer's Office, which allows governments within the State to pool their funds for investment purposes. STAROhio is not registered with the SEC as an investment company, but does operate in a manner consistent with Rule 2a7 of the Investment Company Act of 1940. Investments in STAROhio are valued at STAROhio's share price, which is the price the investment could be sold for on December 31, 2007 and 2006.

Restricted Assets: Proceeds from debt and amounts set aside in various fund accounts for payment of revenue bonds are classified as restricted assets since their use is limited by the bond indentures.

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Capital Assets and Depreciation: Capital assets are stated on the basis of historical cost, or, if contributed, at fair market value as of the date received. Depreciation is computed by allocating the cost of capital assets over the estimated useful lives of the assets using the straight-line method. A capital asset is defined as a tangible item with a useful life in excess of one year and an individual cost of more than $5,000 for furniture, fixtures, equipment, and vehicles, and $10,000 for all other assets. When capital assets are disposed, the cost and related accumulated depreciation are removed from the accounts with gains or losses on disposition being reflected in operations. The estimated useful lives are as follows:

Utility plant	10 to 50 years
Land improvements	42 to 48 years
Buildings, structures and improvements	10 to 47 years
Furniture, fixtures, equipment, and vehicles	5 to 40 years

The Division's policy is to capitalize interest on construction projects up to the point in time that the project is substantially completed. Capitalized interest is included in the cost of the assets and is depreciated on the straight-line basis over the estimated useful lives of such assets. The Division applies Statement of Financial Accounting Standards No. 62, *Capitalization of Interest Cost in Situations Involving Certain Tax-Exempt Borrowings and Certain Gifts and Grants,* for its revenue bonds. This statement requires capitalization of interest cost of eligible borrowings less interest earned on investment of the related bond proceeds from the date of borrowing until the assets constructed from the bond proceeds are ready for their intended use.

For 2007 and 2006 total interest costs incurred amounted to $11,631,000 and $9,534,000 respectively, of which $555,000 and $344,000, respectively, was capitalized, net of interest income of $3,000 in 2007 and $94,000 in 2006.

Bond Issuance Costs, Discounts and Unamortized Losses on Debt Refundings: Bond issuance costs are initially recorded as deferred expenses and unamortized original issuance discounts are netted against long-term debt. Both are amortized over the lives of the related bonds. Unamortized losses on debt refundings are netted against long-term debt and are amortized over the shorter of the remaining life of the defeased bond or the newly issued bond.

Compensated Absences: The Division accrues for compensated absences such as vacation, sick leave and compensatory time using the termination payment method specified under GASB Statement No. 16, *Accounting for Compensated Absences*. These amounts are recorded as accrued wages and benefits in the accompanying balance sheets. The portion of the compensated absence liability that is not expected to be paid out within one year is reported as a long-term liability.

Normally, all vacation time is to be taken in the year available. The Division allows employees to carryover up to 80 hours of vacation from one year to the next with proper approval. Sick days not taken may be accumulated until retirement. An employee is paid one-third of accumulated sick leave upon retirement, calculated at the three-year average base salary rate, with the balance being forfeited.

NOTE B - LONG-TERM DEBT

Long-term debt outstanding at December 31, 2007 and 2006 is as follows:

	Interest Rate	Original Issuance	2007	2006
			(In thousands)	
Mortgage Revenue Bonds:				
Series 1994 A, due through 2013	Zero Coupon	$ 219,105	$ 32,910	$ 33,875
Series 1996, due through 2011	5.25%-6.00%	123,720	3,880	4,730
Series 1998, due through 2017	4.10%-5.25%	44,840	27,715	31,145
Series 2001, due through 2016	3.75%-5.50%	41,925	27,955	30,755
Series 2006 A-1, due through 2024	4.25%-5.00%	95,265	95,265	95,265
Series 2006 A-2, due through 2017	5.00%	12,295	12,295	12,295
Series 2006 B, due through 2024	Auction Rates	20,325	20,325	20,325
		$ 557,475	$ 220,345	$ 228,390
Less:				
Unamortized discount-zero coupon bonds			(6,299)	(7,221)
Unamortized premium-current interest bonds (net)			3,810	4,148
Unamortized loss on debt refunding			(23,596)	(25,889)
Current portion			(8,335)	(8,045)
Total Long-Term Debt			$ 185,925	$ 191,383

Summary: Changes in long-term obligations for the year ended December 31, 2007 are as follows:

	Balance January 1, 2007	Increase	Decrease	Balance December 31, 2007	Due Within One Year
			(In thousands)		
Mortgage Revenue Bonds:					
Series 1994 A, due through 2013	$ 33,875	$	$ (965)	$ 32,910	$ 3,905
Series 1996, due through 2011	4,730		(850)	3,880	895
Series 1998, due through 2017	31,145		(3,430)	27,715	630
Series 2001, due through 2016	30,755		(2,800)	27,955	2,905
Series 2006 A-1, due through 2024	95,265			95,265	
Series 2006 A-2, due through 2017	12,295			12,295	
Series 2006 B, due through 2024	20,325			20,325	
Total revenue bonds	228,390		(8,045)	220,345	8,335
Accrued wages and benefits	4,599	339	(27)	4,911	4,178
Total	$ 232,989	$ 339	$ (8,072)	$ 225,256	$ 12,513

NOTE B - LONG-TERM DEBT (Continued)

Summary: Changes in long-term obligations for the year ended December 31, 2006 are as follows:

	Balance January 1, 2006	Increase	Decrease	Balance December 31, 2006	Due Within One Year
			(In thousands)		
Mortgage Revenue Bonds:					
Series 1994 A, due through 2013	$ 48,335	$	$ (14,460)	$ 33,875	$ 965
Series 1996, due through 2011	120,190		(115,460)	4,730	850
Series 1998, due through 2017	38,655		(7,510)	31,145	3,430
Series 2001, due through 2016	33,465		(2,710)	30,755	2,800
Series 2006 A-1, due through 2024		95,265		95,265	
Series 2006 A-2, due through 2017		12,295		12,295	
Series 2006 B, due through 2024		20,325		20,325	
Total revenue bonds	240,645	127,885	(140,140)	228,390	8,045
Accrued wages and benefits	4,487	112		4,599	3,789
Total	$ 245,132	$ 127,997	$ (140,140)	$ 232,989	$ 11,834

Minimum principal and interest payments on long-term debt are as follows:

	Principal	Interest	Total
		(In thousands)	
2008	$ 8,335	$ 9,336	$ 17,671
2009	8,530	9,150	17,680
2010	8,725	8,950	17,675
2011	11,210	8,731	19,941
2012	11,480	8,513	19,993
2013-2017	61,215	36,819	98,034
2018-2022	75,620	20,504	96,124
2023-2024	35,230	2,663	37,893
Total	$ 220,345	$ 104,666	$ 325,011

The City has pledged future Power System revenues, net of specified operating expenses, to repay $220,345,000 in various public power system revenue bonds issued in various years since 1994. Proceeds from the bonds provided financing for public power system operations. The bonds are payable from public power system net revenues and are payable through 2024. Annual principal and interest payments on the bonds are expected to require less than 45 percent of net revenues. The total principal and interest remaining to be paid on the various Power System Revenue Bonds is $325,011,000. Principal and interest paid for the current year and total net revenues were $17,413,159 and $38,817,000, respectively.

NOTE B – LONG-TERM DEBT (Continued)

On August 17, 2006, the City issued $95,265,000 of Public Power System Refunding Revenue Bonds, Series 2006A-1, $12,295,000 of Public Power System Refunding Revenue Bonds, Series 2006A-2 and $20,325,000 Public Power System Refunding Revenue Variable Rate Bonds, Series 2006B. The Bonds were issued to refund $114,655,000 of Public Power System First Mortgage Revenue Refunding Bonds, Series 1996, Sub-Series 1 and $14,460,000 of Public Power System First Mortgage Revenue Bonds, Series 1994A. Net proceeds of the bonds, including related premium, in the total amount of $131,109,631 will be used to pay the principal, interest and premium on the refunded bonds. As a result, the refunded bonds are considered to be defeased and the liability for these bonds has been removed from long term debt. The City completed the refunding to reduce its debt service payments over the next ten years and to obtain an economic gain (the difference between the present values of the old and new debt service payments) of approximately $5.4 million. The Series 2006B Bonds were issued as variable rate debt (auction rate securities). The City entered into a basis swap on a portion of the Series 2006A-1 Bonds at the time of issuance of the bonds.

***Interest Rate Swap Transaction*:**

Terms: Simultaneously with the issuance of the City's $95,265,000 Series 2006A-1 Public Power System Refunding Revenue Bonds on August 17, 2006, the City entered into a floating-to-floating rate basis swap agreement on an initial notional amount of $70,455,000 which is equal to a portion of the total declining balance of the Series 2006A-1 Bonds. Lehman Brothers Special Financing, Inc. is the counterparty on the transaction. Under the swap agreement for the Series 2006A-1 Bonds, the City pays the counterparty a floating rate based on the Securities Industry and Financial Markets Association (SIFMA) index. The counterparty is also a floating rate payor, paying the City 67% of one month LIBOR plus a spread of 46.25 basis points. Net payments are exchanged quarterly on each February 15, May 15, August 15 and November 15. The obligation of the City to make periodic payments (but not any termination payment) is secured by a pledge of and lien on the net revenues of the Public Power System on a parity with the pledge and lien securing the payment of debt service on the bonds.

Objective: The City entered into the swap in order to maximize the savings associated with the refunding of the bonds. The actual overall savings to be realized by the Public Power System will depend upon the net payments received under the swap agreement.

Basis Risk: By entering into a swap based upon the 30 day LIBOR rate of interest, the City has undertaken basis risk associated with a change in tax rates and structure. While the average relationship between LIBOR (taxable) and SIFMA (tax-exempt) interest rates has been 67%, this relationship may not continue to apply. The payments received from the counterparty may be less than the amount owed to the counterparty resulting in any increase in debt service over the fixed rate on the bonds. A reduction in federal income tax rates might increase the percentage relationship between SIFMA and LIBOR and may potentially increase the cost of financing.

Counterparty Risk: The City selected a highly rated counterparty in order to minimize this risk. However, over the long term it is possible that the credit strength of Lehman Brothers could change and this event could trigger a termination payment on the part of the City.

NOTE B - LONG-TERM DEBT (Continued)

Termination Risk: The swap agreement may be terminated prior to its stated termination date under certain circumstances. Upon termination, a payment may be owed by the Division to Lehman Brothers or by Lehman Brothers to the Division, depending upon the prevailing economic circumstances at the time of the termination.

Fair Value: The fair value of the swap at December 31, 2007 as reported by Lehman Brothers totaled $364,000, which would be payable by Lehman Brothers to the City.

During September 2005, the Division utilized incremental charges to defease certain Mortgage Revenue Bonds that were due November 15, 2005 by placing $4,790,000 relating to principal and $120,000 relating to interest in an irrevocable trust to provide for the debt service payments. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the Division's financial statements. As a result of the Series 2006 advance refunding, there was $11,040,000 Series 1994A defeased debt outstanding at December 31, 2007.

Revenue Bonds are payable from the revenues derived from operations of the public power system, after the payment of all operating and maintenance expenses (net revenues). The bonds are collateralized by a pledge of and lien on such net revenues plus a first mortgage lien upon all property of the public power system, including any improvements, additions, replacements, and extensions thereto.

The indenture requires that, at all times, the Division will charge rates and fees for the products and services of the public power system. Revenues will be at least sufficient to provide funds for the payment in each year of the necessary operating and maintenance expenses of the power system and in an amount equal to 1.25 times the payments of principal and interest on the revenue bonds then outstanding and due in that year. As of December 31, 2007 and 2006, the Division was in compliance with the terms and requirements of the bond indenture. The indenture establishes the following fund accounts for the application of revenues:

***Revenue Fund*:** All revenues will be deposited into this fund and will be used for payment of current operating expenses and deposits into other funds.

***Debt Service Fund*:** Monthly deposits will be made from the revenue fund to cover succeeding principal and interest payments as they become due on the Revenue Bonds.

***Debt Service Reserve Fund*:** Deposits will be made to this fund if the amount in the debt service fund at any time is less than the debt service reserve requirement. However, the Division has elected, pursuant to provisions of the indenture governing the Division's bonds, to satisfy the bond reserve requirement with a surety bond in an aggregate amount at least equal to the bond reserve requirement.

***Renewal and Replacement Fund*:** The balance in this fund is maintained at $1,000,000 and is to be applied against the cost of repair or replacement of capital assets in order to maintain the system.

NOTE B - LONG-TERM DEBT (Continued)

***Construction Fund*:** The proceeds from Series 1994 and Series 1991 Bonds of $79,386,000 and $12,050,000, respectively, were deposited into this fund to be used, along with earnings from investments of amounts held therein, for the payment of capital costs. As of December 31, 2007, the Division had no outstanding commitments for future constructions that will be funded by available bond proceeds and operating revenue as opposed to $4,439,000 as of December 31, 2006. Capital costs include all costs of additions, extensions, renewals, replacements, alterations, betterments and any other capital improvements to the system. Amounts held in this fund are subject to a lien in favor of bondholders and may be used to pay principal of outstanding bonds to the extent that amounts in all other funds are insufficient. No payment needs to be made into a fund if the amounts in such fund are equal to the required fund balance, if any.

Amounts held in trust may be invested by the City Treasurer or the Trustee in permitted investments. However, the use of funds is limited by the bond indenture and, accordingly, the amounts are classified as restricted assets in the financial statements.

NOTE C - DEPOSITS AND INVESTMENTS

Deposits: At December 31, 2007 and 2006, the Division's carrying amount of deposits totaled $4,682,000 and $2,484,000, respectively, and the Division's bank balances totaled $5,231,000 and $2,697,000, respectively. The differences represent normal reconciling items. Based on the criteria described in GASB Statement No.3, *Deposits with Financial Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements* and GASB Statement No. 40, *Deposit and Investments Risk Disclosures – an Amendment to GASB Statement No. 3*, $5,231,000 and $2,697,000 of the bank balances at December 31, 2007 and 2006, respectively, were insured or collateralized with securities held by the City or by its agent in the City's name.

Custodial credit risk for deposits is the risk that in the event of bank failure, the Division will not be able to recover deposits or collateral for securities that are in possession of an outside party. At year end, the Division's deposits were fully insured or collateralized. All deposits are collateralized with eligible securities pledged and deposited either with the City or with a qualified trustee by the financial institution as security for repayment of all public monies deposited in the financial institution whose market value at all times is equal to at least 110% of the carrying value of the deposits being secured.

Investments: The City's investment policies are governed by State statutes and City ordinances which authorize the City to invest in obligations of the U.S. Treasury, agencies and instrumentalities; bonds and other State obligations; certificates of deposit; U.S. Government Money Market Mutual Funds; STAROhio; guaranteed investment contracts; and repurchase transactions. Such repurchase transactions must be purchased from financial institutions or registered broker/dealers. Repurchase transactions are not to exceed a period of one year and confirmation of securities pledged must be obtained.

Under City policy, investments are limited to repurchase agreements, U.S. Government securities, certificates of deposit, investments in certain money market mutual funds, and STAROhio. Generally, investments are recorded in segregated accounts by way of book entry through the banks' commercial or trust department and are kept at the Federal Reserve Bank in the depository institutions' separate custodial account for the City,

NOTE C - DEPOSITS AND INVESTMENTS (Continued)

apart from the assets of the depository institution. Ohio statute prohibits the use of Reverse Repurchase Agreements.

Investment securities are exposed to various risks such as interest rate, market and credit. Market values of securities fluctuate based on the magnitude of changing market conditions; significant changes in market conditions could materially affect the portfolio value.

Interest rate risk: As a means of limiting its exposure to fair value losses caused by rising interest rates, the Division invests primarily in short-term investments maturing within five years from the date of purchase. The intent is to avoid the need to sell securities prior to maturity. Investment maturities are disclosed in the table on the following page.

Custodial Credit Risk: For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Division will not be able to recover the value of the investments or collateral securities that are in the possession of an outside party. The Division does not have an investment policy dealing with investment custodial credit risk beyond the requirement in the State statute.

Credit Risk: The Division's investments as of December 31, 2007 and 2006 include U.S. Agencies, Victory Federal Money Market Funds, Allegiant Government Money Market Funds, STAROhio and mutual funds. The Division maintains the highest ratings for its investments. Investments in FHLMC, FNMA, FFCB and FHLB agency securities are rated AAA by Standard & Poor's. Investments in the Victory Money Market Fund, and STAROhio carry a rating of AAAm, which is the highest money market fund rating given by Standard & Poor's. Ohio law requires that STAROhio maintain the highest rating provided by at least one nationally recognized standard rating service. The Division has no investment policy that would further limit its investment choices.

NOTE C - DEPOSITS AND INVESTMENTS (Continued)

Concentration of Credit Risk: The Division places a limitation on the amount it may invest in any one issuer to help minimize the concentration of credit risk. The Division had the following investments at December 31, 2007 and 2006, which include those classified as cash and cash equivalents in the balance sheet in accordance with the provisions of GASB Statement No. 9, since they have a maturity of three months or less:

Type of Investment	2007 Fair Value	2007 Cost	2006 Fair Value	2006 Cost	Investment Maturities: Less than One Year	Investment Maturities: 1 - 5 Years	Investment Maturities: 5 Years or More
	(In thousands)						
U.S. Agency Obligations	$ 37,108	$ 36,783	$ 40,373	$ 40,547	$	$ 37,108	$
U.S. Treasury Bills	2,768	2,768	1,171	1,171	2,768		
Repurchase Agreements	1,173	1,173	5,819	5,819	1,173		
STAROhio	18,314	18,314	8,400	8,400	18,314		
Investment in Mutual Funds	1,796	1,796	2,915	2,915	1,796		
Total Investments	61,159	60,834	58,678	58,852	24,051	37,108	-
Total Deposits	4,682	4,682	2,484	2,484	4,682		
Total Deposits and Investments	$ 65,841	$ 65,516	$ 61,162	$ 61,336	$ 28,733	$ 37,108	$ -

As of December 31, 2007, the investments in U.S. Agency Obligations, U.S. Treasury Bills and STAROhio are approximately 61%, 5% and 30%, respectively, of the Division's total investments. As of December 31, 2006, the investments in U.S. Agency Obligations, repurchase agreements and STAROhio are approximately 69%, 10% and 14%, respectively, of the Division's total investments.

CITY OF CLEVELAND, OHIO
DEPARTMENT OF PUBLIC UTILITIES
DIVISION OF CLEVELAND PUBLIC POWER

NOTES TO FINANCIAL STATEMENTS (Continued)
For the Years Ended December 31, 2007 and 2006

NOTE D - CAPITAL ASSETS

Capital Asset Activity: Capital asset activity for the year ended December 31, 2007 was as follows:

	Balance January 1, 2007	Additions	Reductions	Balance December 31, 2007
		(In thousands)		
Capital assets, not being depreciated:				
Land	$ 4,863	$	$	$ 4,863
Construction in progress	23,720	19,658	(7,527)	35,851
Total capital assets, not being depreciated	28,583	19,658	(7,527)	40,714
Capital assets, being depreciated:				
Land improvements	2,759			2,759
Utility plant	408,633	7,178	(280)	415,531
Buildings, structures and improvements	42,278			42,278
Furniture, fixtures, equipment and vehicles	42,882	3,653	(2,575)	43,960
Total capital assets, being depreciated	496,552	10,831	(2,855)	504,528
Less: Accumulated depreciation	(216,013)	(17,056)	1,693	(231,376)
Total capital assets being depreciated, net	280,539	(6,225)	(1,162)	273,152
Capital assets, net	$ 309,122	$ 13,433	$ (8,689)	$ 313,866

Capital Asset Activity: Capital asset activity for the year ended December 31, 2006 was as follows:

	Balance January 1, 2006	Additions	Reductions	Balance December 31, 2006
		(In thousands)		
Capital assets, not being depreciated:				
Land	$ 4,863	$	$	$ 4,863
Construction in progress	8,181	21,174	(5,635)	23,720
Total capital assets, not being depreciated	13,044	21,174	(5,635)	28,583
Capital assets, being depreciated:				
Land improvements	2,759			2,759
Utility plant	403,120	5,513		408,633
Buildings, structures and improvements	42,278			42,278
Furniture, fixtures, equipment and vehicles	42,904	1,782	(1,804)	42,882
Total capital assets, being depreciated	491,061	7,295	(1,804)	496,552
Less: Accumulated depreciation	(200,344)	(16,713)	1,044	(216,013)
Total capital assets being depreciated, net	290,717	(9,418)	(760)	280,539
Capital assets, net	$ 303,761	$ 11,756	$ (6,395)	$ 309,122

NOTE D - CAPITAL ASSETS (Continued)

Commitments: The Division has outstanding commitments of approximately $20,256,000 and $30,131,000 for future capital expenditures at December 31, 2007 and 2006, respectively. It is anticipated that these commitments will be financed from the Division's cash balances; however, at the discretion of the Division, additional long-term debt may be issued in the future to finance a portion of the costs.

NOTE E - DEFINED BENEFIT PENSION PLAN

Ohio Public Employees Retirement System: All full-time employees participate in the Ohio Public Employees Retirement System (OPERS). OPERS administers three separate pension plans as described below:

1) The Traditional Pension Plan (TP) – a cost-sharing, multiple-employer defined benefit pension plan.
2) The Member-Directed Plan (MD) – a defined contribution plan in which the member invests both member and employer contributions (employer contributions vest over five years at 20% per year). Under the Member-Directed Plan, members accumulate retirement assets equal to the value of member and (vested) employer contributions plus any investment earnings.
3) The Combined Plan (CO) – a cost-sharing, multiple-employer defined benefit pension plan. Under the Combined Plan, employer contributions are invested by OPERS to provide a formula retirement benefit similar in nature to the Traditional Pension Plan benefit. Member contributions, the investment of which is self-directed by the members, accumulate retirement assets in a manner similar to the Member-Directed Plan.

OPERS provides retirement, disability, survivor and death benefits and annual cost-of-living adjustments to members of the Traditional Pension and Combined Plans. Members of the Member-Directed Plan do not qualify for ancillary benefits. Authority to establish and amend benefits is provided by state statute per Chapter 145 of the Ohio Revised Code. OPERS issues a stand-alone financial report. Interested parties may obtain a copy by making a written request to OPERS, Attention: Finance Director, 277 East Town Street, Columbus, Ohio 43215-4642, or by calling (614) 222-5601 or 1-800-222-7377.

The Ohio Revised Code provides statutory authority for member and employer contributions. For 2007, member and employer contribution rates were consistent across all three plans (TP, MD and CO). Member contribution rates were 9.5% in 2007, 9.00% in 2006 and 8.50% in 2005, and employer contribution rates were 13.85% of covered payroll in 2007, 13.70% in 2006 and 13.55% in 2005. The Division's required employer contributions to OPERS for the pension portion of all the plans for the years ending December 31, 2007, 2006 and 2005 were approximately $1,571,000, $1,747,000 and $1,776,000 each year, respectively. The required payments due in 2007, 2006 and 2005 have been made.

NOTE F - OTHER POST-EMPLOYMENT BENEFITS

Ohio Public Employees Retirement System: Ohio Public Employees Retirement System (OPERS) administers three separate pension plans: The Traditional Pension Plan (TP) – a cost-sharing, multiple-employer defined benefit pension plan; the Member-Directed Plan (MD) – a defined contribution plan; and the Combined Plan (CO) – a cost-sharing, multiple-employer defined benefit pension plan that has elements of both a defined benefit and defined contribution plan. OPERS maintains a cost-sharing multiple employer defined benefit post-employment healthcare plan, which includes a medical plan, prescription drug program and Medicare Part B premium reimbursement, to qualifying members of both the Traditional Pension and Combined Plans. Members of the Member-Directed Plan do not qualify for ancillary benefits, including post-employment health care coverage. In order to qualify for post-employment health care coverage, age and service retirees under the Traditional Pension and Combined Plans must have 10 or more years of qualifying Ohio service credit. Health care coverage for disability benefit recipients and qualified survivor benefit recipients is available. The health care coverage provided by OPERS meets the definition of an Other Post-employment Benefit (OPEB) as described in GASB Statement No. 45. The Ohio Revised Code permits, but does not mandate, OPERS to provide OPEB benefits to its eligible members and beneficiaries. Authority to establish and amend benefits is provided in Chapter 145 of the Ohio Revised Code. OPERS issues a stand-alone financial report. Interested parties may obtain a copy by making a written request to OPERS, Attention: Finance Director, 277 East Town Street, Columbus, Ohio 43215-4642, or by calling (614) 222-5601 or 1-800-222-7377.

The Ohio Revised Code provides statutory authority requiring public employers to fund post retirement health care through their contributions to OPERS. A portion of each employer’s contribution to OPERS is set aside for the funding of post retirement health care benefits. Employer contribution rates are expressed as a percentage of the covered payroll of active members, The Division’s contribution rate was 13.85% of covered payroll in 2007, 13.70% of covered payroll in 2006 and 13.55% of covered payroll in 2005. The Ohio Revised Code currently limits the employer contribution to a rate not to exceed 14.00% of covered payroll. Active members do not make contributions to the OPEB Plan. OPERS’ Post Employment Health Care Plan was established under, and is administrated in accordance with Internal Revenue Code 401(h). Each year, the OPERS Retirement Board determines the portion of the employer contribution rate that will be set aside for funding of post employment health care benefits. For 2007, the employer contribution allocated to the health care plan from January 1 through June 30, 2007 and July 1 through December 31, 2007 was 5% and 6% of covered payroll, respectively. In 2006, 4.50% of covered payroll was used to fund health care and 4.00% of covered payroll in 2005. The OPERS Retirement Board is also authorized to establish rules for the payment of a portion of the health care benefits provided, by the retiree or the surviving beneficiaries. Payment amounts vary depending on the number of covered dependents and the coverage selected. The Division’s actual contributions for 2007 which were to fund post-employment benefits were approximately $1,036,000.

The Health Care Preservation Plan (HCPP) adopted by the OPERS Retirement Board on September 9, 2004, was effective January 1, 2007. Member and employer contribution rates increased as of January 1, 2006, January 1, 2007 and January 1, 2008, which allowed additional funds to be allocated to the health care plan.

NOTE G - CONTINGENT LIABILITIES AND RISK MANAGEMENT

Contingent Liabilities: Various claims are pending against the City involving the Division for personal injuries, property damage and other matters. The City is responsible for the lawsuits. The City's management is of the opinion that ultimate settlement of such claims will not result in a material adverse effect on the Division's financial position, results of operations or cash flows.

Risk Management: The Division is exposed to various risks of loss related to torts; thefts of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Division carries insurance to cover particular liabilities and property protection. Otherwise, the Division is generally self-insured. No material losses, including incurred but not reported losses, occurred in 2007 or 2006. There were no significant decreases in any insurance coverage in 2007. In addition, there were no insurance settlements in excess of insurance coverage during the past three years.

The City provides the choice of four separate health insurance plans for its employees. These plans are provided by two different insurers through commercial insurance. Operating funds are charged a monthly rate per employee, by type of coverage. The City participates in the State of Ohio's workers' compensation retrospective rating program.

In accordance with GASB Statement No. 10, claims liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. Liabilities include an amount for claims that have been incurred but not reported. The result of the process to estimate the claims liability is not an exact amount as it depends on many complex factors, such as inflation, changes in legal doctrines, and damage awards. Accordingly, claims are re-evaluated periodically to consider the effects of inflation, recent claim settlement trends (including frequency and amount of pay-outs), and other economic and social factors. The estimate of the claims liability also includes amounts for incremental claim adjustment expenses related to specific claims and other claim adjustment expenses, regardless of whether allocated to specific claims. Estimated recoveries, for example from salvage or subrogation, are another component of the claims liability estimate. Claims liability for the Division is reported as accounts payable on the balance sheet and is immaterial.

NOTES TO FINANCIAL STATEMENTS (Continued)
For the Years Ended December 31, 2007 and 2006

NOTE H - RELATED PARTY TRANSACTIONS

Revenues and Accounts Receivable: The Division provides services to the City, including its various departments and divisions. The usual and customary rates are charged to all City departments and divisions.

Operating Expenses: The Division is provided various intra-city services. Charges are based on actual use or on a reasonable pro rata basis. The more significant costs for the years ended December 31, 2007 and 2006 are as follows:

	2007	2006
	(In thousands)	
City Administration	$ 1,131	$ 703
Telephone Exchange	687	570
Division of Water	463	434
Utilities Administration and Fiscal Control	936	654
Motor Vehicle Maintenance	484	449

NOTE I - CUYAHOGA COUNTY REAL PROPERTY TAXES

The Division is required by ordinance to keep records of the estimated property taxes which would be payable to Cuyahoga County were it subject to such taxes. The estimated property taxes for the Division, based on book value of real estate at the current tax rates, would have been approximately $1,130,000 and $1,206,000 for the years ended December 31, 2007 and 2006, respectively.

NOTE J - KILOWATT PER HOUR TAX

In May 2001, the Division started billing electric deregulation kilowatt-hour tax according to the laws of the State of Ohio. The Division billed $5,486,000 and $5,233,000 for this tax in 2007 and in 2006 respectively, of which $12,543 and $13,164 was remitted to the State. All except the State of Ohio’s portion belongs to the General Fund of the City. In March 2006, City Council passed ordinance 2068-05, which allocates 100% of the City’s share of the tax in 2007 to the General Fund of the City. Under legislation passed in December 2007, the General Fund will transfer annually 50% of the kWh tax receipts to the Division beginning in 2008. This amount, estimated at $3,000,000, is earmarked for the acquisition of CEI's street lights in 2008.

NOTE K – INCREMENTAL CHARGES

In 2000, 2002 and 2003, Cleveland City Council passed ordinances 910-98, 1886-02 and 2088-03, respectively to allow the Division to add an incremental charge for excess fuel, power production and purchased power cost.

The proceeds of the incremental charges shall be applied to the repayment of any bond obligations of the Division and the replacement of utility poles treated with copper naphthenate in the Division's distribution system.

The incremental charges were originally scheduled to end November 30, 2005, but have been extended by recent legislation to December 31, 2008. The Division intends, subject to approval by City Council to continue this charge either in its present form or as part of base rates. Effective December 1, 2005, the proceeds of the incremental charges are no longer earmarked for a specific purpose. The incremental charges billed were $13,561,000 and $13,158,000 in 2007 and 2006, respectively.

NOTE L – SEAMS ELIMINATION COST ADJUSTMENT (SECA) PAYMENTS

Between December 2004 and March 2006, the Division was required by the Federal Energy Regulatory Commission ("FERC") to pay SECA payments amounting to $10,800,000. The payments arose from a transmission restructuring effort aimed at reducing transmission costs by allowing users such as Cleveland Public Power to pay a single rate for transmission across a regional system consisting of multiple utilities. These payments, made subject to refund and the outcome of litigation proceedings, were intended as a temporary replacement for revenues previously received by transmission owners in neighboring regional systems for transmission access across their systems.

Through December 31, 2007, the Division received $5,026,000 as reimbursements for SECA payments. The Division is also pursuing an additional reimbursement of $700,000. The remaining SECA payment of $5,074,000 is eligible for pass through to the customers of the Division in future years.

NOTE M – SUBSEQUENT EVENTS

Effective April 22, 2008, the City issued $93,712,880 Public Power System Revenue Bonds, Series 2008 for Cleveland Public Power. The Division will use $72,607,880 to fund the system expansion, to pay costs of issuance and to pay capitalized interest. Of this amount issued as new money, $44,705,000 was issued as current interest bonds and $27,902,000 was issued as capital appreciation bonds.

The remaining $21,105,000 Series 2008 Bonds were issued to refund the $20,325,000 Series 2006B Public Power System Refunding Revenue Variable Rate Bonds and to pay issuance costs. The 2006B Bonds were auction rate securities insured by FGIC. Due to the credit rating downgrades of several municipal bond insurance companies (including FGIC), CPP was incurring greater interest expense on these auction rate securities than was the case prior to the credit rating downgrades. In response to this situation, City Council passed legislation on February 25, 2008 authorizing the issuance of refunding bonds. Therefore, in

NOTE M – SUBSEQUENT EVENTS (Continued)

conjunction with the issuance of CPP's new money bonds, the 2006B auction rate securities were refunded as fixed rate bonds insured by MBIA at an interest rate of 4.58%.

Auction Rate Securities

As described in Note B, above, the City has issued certain debt securities as auction rate securities (ARS). The City also has entered into various swap transactions involving some of these securities. Recent disruptions in national capital markets, including changes in the credit ratings of private companies insuring these securities on behalf of the City, have affected these securities, as described below:

i. CPP 2006B. Cleveland Public Power ARS of $20,325,000 provided for a maximum default reset of 250% of the 30 day taxable rate, due to the downgrade of the credit rating of the private company insuring the bonds on behalf of the City. The last reset on May 14, 2008, resulted in an interest rate of 6.263% upon the failed auction of that date. These bonds were refunded on April 22, 2008 as part of a $93.7 million fixed rate issue that also included additional capital funds for CPP. The fixed rate on the refunding bonds was 4.58%. The ARS was redeemed on May 22.

Mary Taylor, CPA
Auditor of State

CITY OF CLEVELAND
CLEVELAND PUBLIC POWER

CUYAHOGA COUNTY

CLERK'S CERTIFICATION
This is a true and correct copy of the report which is required to be filed in the Office of the Auditor of State pursuant to Section 117.26, Revised Code, and which is filed in Columbus, Ohio.

Susan Babbitt

CLERK OF THE BUREAU

CERTIFIED
JULY 15, 2008

88 E. Broad St. / Fourth Floor / Columbus, OH 43215-3506
Telephone: (614) 466-4514 (800) 282-0370 Fax: (614) 466-4490
www.auditor.state.oh.us