

MANAGEMENT DISCUSSION AND ANALYSIS – WATER UTILITY

As management of Glendale *Water & Power* (a department of the City of Glendale), we offer the readers of the City of Glendale Water Enterprise Fund (Water Utility) financial statements, a fund of the City, this narrative overview and analysis of the financial activities of the Water Enterprise for the fiscal year ended June 30, 2005. We encourage readers to consider the information presented here in conjunction with the accompanying basic financial statements. All amounts, unless otherwise indicated, are expressed in thousands of dollars.

Financial Highlights

During fiscal year 2005, the region experienced one of the wettest years in history. The Water Utility had a 4.5% decrease in total water operating revenues – directly attributed to the 4.5% decline in water consumption. Operating expenses remained relatively unchanged due to the offsetting effects of the increase in production expenses and the decrease in depreciation expenses. The increase in production expenses was due to the increased cost of purchased water supplied by MWD, and the increased cost of electricity for pumping water through the transmission and distribution system. The decrease in depreciation expenses resulted from the retirements of assets. Net operating revenues were \$4,725. Total net assets increased by \$3,115 after adding net non-operating revenues of \$2,109 and subtracting \$3,719 in Transfers to the City's General Fund.

The assets of the Water Utility exceeded its liabilities at the close of fiscal year 2005 by \$85,149. Of this amount, \$9,567 was unrestricted and may be used to meet the Water Utility's ongoing obligations to creditors and customers. At the end of the fiscal year, this unrestricted net assets represented 38% of annual operating expenses for 2005.

Overview of the Basic Financial Statements

This discussion and analysis is intended to serve as an introduction to the City of Glendale Water Utility financial statements. The Water Utility is a business-type activity of the City, and its activities are recorded in a separate enterprise fund. These financial statements include only the activities for the City of Glendale Water Utility and provide comparative information for the last two fiscal years. Information on city-wide financial results is available in the City of Glendale's Comprehensive Annual Financial Report.

The City of Glendale Water Utility's financial statements comprise two components: 1) financial statements and 2) notes to the financial statements. In addition, this report also contains other

supplementary information to provide the reader additional information about the Water Utility, including sales statistics and other relevant data. Included as part of the financial statements are three separate statements which collectively provide an indication of the Water Utility's financial health.

The *Statement of Net Assets* presents information on assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial condition of the utility is improving or deteriorating.

The *Statement of Revenues, Expenses and Changes in Net Assets* presents information showing how the Water Utility's net assets changed during the most recent two fiscal years. Results of operations are recorded under the accrual basis of accounting whereby transactions are reported as underlying events occur, regardless of the timing of cash flows. Thus, revenues and expenses are reported in these statements for some items that will result in cash flows in future fiscal periods, i.e. accounts payable and accounts receivable. The accrual basis of accounting and is more fully described in the accompanying Notes to the Financial Statements.

The *Statement of Cash Flows* presents the flows of cash and cash equivalents during the last two fiscal years, including certain restricted amounts.

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 **XX to XX** of this report.

Financial Analysis

As noted earlier, net assets may serve over time as a useful indicator of the Water Utility's financial position. In the case of the Water Utility, assets exceeded liabilities by \$85,149 at the close of the most recent fiscal year. A portion of the Utility's net assets (88.8%) reflects its investment in capital assets, such as production, transmission, and distribution facilities, less any related outstanding debt used to acquire those assets. The Water Utility uses these capital assets to provide services to customers; consequently, these assets are not available for future spending. Resources needed to repay the outstanding debt shown on the balance sheet must come from other sources such as operations, since the capital assets themselves cannot be used to liquidate these long-term liabilities.

There are no current external restrictions on the Water Utility's net assets that limit how they may be used.

The Unrestricted portion of the Utility’s net assets (11.2%) may be used to meet the Water Utility’s ongoing obligations to creditors and customers.

Net Assets – Water Utility

The Water Utility’s net assets as of June 30 are as follows:

	<u>2005</u>	<u>2004</u>
Current and Noncurrent Assets	\$ 12,614	\$ 15,078
Capital Assets	<u>75,582</u>	<u>70,016</u>
 Total Assets	 <u><u>88,196</u></u>	 <u><u>85,094</u></u>
 Other Liabilities	 <u>3,047</u>	 <u>3,060</u>
 Total Liabilities	 <u><u>3,047</u></u>	 <u><u>3,060</u></u>
 Net Assets:		
Invested in capital assets, net of related del	75,582	70,016
Unrestricted	<u>9,567</u>	<u>12,018</u>
 Total Net Assets	 <u><u>\$ 85,149</u></u>	 <u><u>\$ 82,034</u></u>

The Water Utility’s net assets increased by \$3,115 during the current fiscal year.

Changes Net Assets – Water Utility

The Water Utility’s changes in net assets for the year ended June 30 are as follows:

	<u>2005</u>	<u>2004</u>
Revenues:		
Retail sales, net	\$ 29,698	\$ 30,928
Adjustable Rate Adjustment	55	449
Interest Income	295	111
Other revenues and grants	1,493	1,498
Capital contributions	<u>321</u>	<u>287</u>
Total Revenues	<u><u>31,862</u></u>	<u><u>33,273</u></u>
Expenses:		
Production	18,118	17,689
Transmission and distribution	2,645	2,700
Customer accounting and sales	2,167	2,041
Depreciation	<u>2,098</u>	<u>2,590</u>
Total Expenses	<u>25,028</u>	<u>25,021</u>
Transfers to the City's General Fund	<u>3,719</u>	<u>3,232</u>
Total Expenses and transfers	<u>28,747</u>	<u>28,253</u>
Changes in net assets	<u><u>3,115</u></u>	<u><u>5,020</u></u>
Total net assets, beginning of year	<u>82,034</u>	<u>77,014</u>
Total net assets, end of year	<u>\$ 85,149</u>	<u>\$ 82,034</u>

Revenues by Source – Water Utility

Retail sales (residential, commercial, industrial and other sales) continued to be the primary revenue source for the Water Utility, making up 93% of total revenue. Retail sales showed a decrease of 4.5% from the prior year, the result of a 4.5% decline in consumption during one of the wettest years in history.

The Adjustable Rate Adjustment recognized as revenues the difference between the adjustable water rate revenues collected from retail customers and the costs of purchased water from MWD and the electricity for pumping water through the transmission and distribution system.

Investment income increased by \$185, or 166% above the prior year level. The increase was

related to favorable market conditions that resulted in higher earnings for the Water Utility's investment portfolio.

Capital contributions increased 12% from prior year levels. The increased amount over prior year reflected an increased level of construction projects funded by others, primarily by retail customers.

Grants decreased by \$103, or 26% compared to the prior year level, reflecting the decrease in grant funds received from EPA for water quality projects.

Expenses by Source – Water Utility

Total expenses for the Water Utility remained relatively unchanged.

Production expenses comprising primarily of MWD water supply cost increased by 2.4%. Transmission and distribution expenses decreased by 2% as a result of the decrease in consumption. Depreciation expense decreased by 19% as old assets were retired while increased capital expenses recorded as construction in progress, the depreciation expenses for which would be incurred in future periods after they are capitalized.

Transfers to the City's General Fund are based on a formula representing a certain percentage of total retail revenues. Transfers to the City's General Fund increased by \$487, reflecting an increase in the percentage.

Capital Assets and Debt Administration

Capital Assets

The Water Utility's investment in capital assets as of June 30, 2005 totaled \$75,582 (net of accumulated depreciation). This included investments in production, transmission, and distribution related facilities, as well as general items such as office equipment, furniture, etc. This fiscal year showed an 8% increase in capital assets over the prior year as the implementation of long-term infrastructure improvement programs began.

The Water Utility’s capital assets as of June 30 are as follows:

	2005	2004
Production	\$ 24,100	\$ 22,513
Transmission and distribution	83,575	79,507
General	12,769	11,336
Less: Accumulated depreciation	<u>(44,862)</u>	<u>(43,340)</u>
Total	<u>\$ 75,582</u>	<u>\$ 70,016</u>

Long-Term Debt

As of June 30, 2005, the Water Utility had no long-term debt outstanding.

Economic Factors and Rates

Although inflationary trends in the Glendale region remained relatively low, the Water Utility’s cost escalation is not strictly attributable to inflation. One of the main drivers of the increase in costs relates to the drought conditions the region has been experiencing for several years. This has resulted in additional costs to purchase water, much more costly than the groundwater supply. In addition, the costs of the long-term capital improvement programs to improve the aging infrastructure will place additional pressure on the Water Utility’s financial conditions.

Recognizing the need for long-term financial planning for the Water Utility, City Council adopted the Water Cash Reserve Policy in December 2003 to provide the foundation for strengthening the financial health of the Water Utility. The policy identifies and plans for meeting working capital and contingency needs during emergencies and disasters, as well as expected future capital needs for system improvement.

There was no rate increase during the last two fiscal years.

Requests for Information

This financial report is designed to provide a general overview of the Water Utility’s finances. Questions concerning any information provided in this report or requests for additional financial information should be addressed to the Director of Glendale *Water & Power* – 141 North Glendale Avenue, Level 4, Glendale, California 91206.

MANAGEMENT DISCUSSION AND ANALYSIS – WATER UTILITY

WATER

Statements of Net Assets

Years Ending June 30 2005 and 2004

	<u>2005</u>	<u>2004</u>
Assets		
Current assets:		
Cash and invested cash	\$ 3,800,967	\$ 3,321,634
Imprest cash	1,000	1,000
Interest receivable	63,800	63,961
Accounts receivable, net	1,781,635	2,267,676
Unbilled receivable	2,598,137	2,235,385
Due from other agencies	74,756	-
Inventories	-	287,555
Total current assets	<u>8,320,295</u>	<u>8,177,211</u>
Noncurrent assets:		
Designated & invested cash	<u>4,294,000</u>	<u>6,900,000</u>
Total noncurrent assets	<u>4,294,000</u>	<u>6,900,000</u>
Capital assets:		
Land	1,006,999	622,568
Buildings and improvements	70,765,043	65,176,218
Machinery and equipment	39,821,864	39,116,575
Bldg & impro accm depreciation	(44,861,872)	(43,340,356)
Construction in progress	<u>8,849,775</u>	<u>8,441,285</u>
Total capital assets	<u>75,581,809</u>	<u>70,016,290</u>
Total assets	<u><u>88,196,104</u></u>	<u><u>85,093,501</u></u>
Liabilities and Net Assets		
Current liabilities:		
Accounts payable	1,570,046	1,774,710
Contracts-retained amount due	279,330	237,130
Accrued wages and withholding	138,323	135,380
Compensated absences	25,000	-
Deposits	<u>454,691</u>	<u>510,423</u>
Total current liabilities	<u>2,467,390</u>	<u>2,657,643</u>
Noncurrent liabilities:		
Compensated absences	513,457	402,003
Post employment benefits	<u>66,172</u>	<u>-</u>
Total noncurrent liabilities	<u>579,629</u>	<u>402,003</u>
Total liabilities	<u>3,047,019</u>	<u>3,059,646</u>
Net assets:		
Investment in general FA	75,581,809	70,016,291
Restricted		
Unrestricted	<u>9,567,276</u>	<u>12,017,564</u>
Total net assets	<u>\$ 85,149,085</u>	<u>\$ 82,033,855</u>

Water Fund

Statement of Revenues, Expenses and Changes in Net Assets
 Years Ending June 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Operating revenues		
Water Metered Sales	\$ 28,056,678	\$ 29,053,832
Water Private Fire	320,157	366,201
Water Other Sales	291,254	488,161
Water-Capital	1,029,466	1,019,780
Water Adjustment Revenue	55,416	449,049
Miscellaneous revenues	1,203,138	1,105,021
	<u>30,956,109</u>	<u>32,482,044</u>
Operating expenses:		
Production	18,118,239	17,688,757
Transmission	2,645,343	2,700,185
Customer accounting and sales	2,166,504	2,041,492
Depreciation	2,098,030	2,590,462
	<u>25,028,116</u>	<u>25,020,896</u>
Operating income	<u>5,927,993</u>	<u>7,461,148</u>
Non operating revenues		
Interest revenue	295,496	110,966
Grant revenue	289,933	392,930
Contribution in aid	320,929	286,807
	<u>906,358</u>	<u>790,703</u>
Total non operating revenues, net	<u>906,358</u>	<u>790,703</u>
Income before transfers	<u>6,834,351</u>	<u>8,251,851</u>
Transfer out:		
Transfer-General Fund	<u>(3,719,121)</u>	<u>(3,231,833)</u>
Total transfer	<u>(3,719,121)</u>	<u>(3,231,833)</u>
Change in net assets	3,115,230	5,020,018
Total Net asset, July 1	<u>82,033,855</u>	<u>77,013,837</u>
Total net assets, June 30	<u>\$ 85,149,085</u>	<u>\$ 82,033,855</u>

MANAGEMENT DISCUSSION AND ANALYSIS – WATER UTILITY

Water Fund

Statement of Cash Flows

Years Ending June 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Cash flows from operating activities:		
Cash from customers	\$ 31,004,642	\$ 32,076,277
Cash paid to employees	(2,894,840)	(2,721,301)
Cash paid to suppliers	(19,760,318)	(19,500,750)
Net cash provided by operating activities	<u>8,349,484</u>	<u>9,854,226</u>
Cash flows from noncapital financing activities:		
Operating transfers out	(3,719,121)	(3,231,833)
Operating grant received	289,933	392,930
Net cash provided by noncapital financing activities	<u>(3,429,188)</u>	<u>(2,838,903)</u>
Cash flows from capital and related financing activities:		
Contribution in aid	320,929	286,807
Acquisition of property, plant, and equipment	(7,663,549)	(6,202,152)
Net cash (used in) capital and related financing activities	<u>(7,342,620)</u>	<u>(5,915,345)</u>
Cash provided by investing activities - interest received	295,657	92,560
Net increase (decrease) in cash and cash equivalents	(2,126,667)	1,192,538
Cash and cash equivalents at beginning of year	<u>10,222,634</u>	<u>9,030,096</u>
Cash and cash equivalents at end of year	<u><u>8,095,967</u></u>	<u><u>10,222,634</u></u>
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	<u>5,927,993</u>	<u>7,461,148</u>
Adjustments to reconcile operating income to net cash provided (used) by operating activities:		
Depreciation	2,098,030	2,590,462
(Increase)Decrease Accounts receivable net	486,040	(694,448)
(Increase)Decrease Unbilled receivable	(362,752)	288,679
(Increase)Decrease Due from other agencies	(74,756)	-
(Increase)Decrease Inventories	287,555	31,643
Increase(Decrease) Accrued salaries and withholding	2,943	22,739
Increase(Decrease) Compensated absences	136,454	71,622
Increase(Decrease) Post employment benefit	66,172	-
Increase(Decrease) Accounts payable	(204,663)	38,911
Increase(Decrease) Contracts - retention	42,200	139,418
Increase(Decrease) Deposits	(55,732)	(95,948)
Total adjustments	<u>2,421,491</u>	<u>2,393,078</u>
Net cash provided (used) by operating activities	<u><u>\$ 8,349,484</u></u>	<u><u>\$ 9,854,226</u></u>
Noncash investing, capital, and financing activities:		
Contributions of capital assets from government		
Increase in fair value of investments	(99,334)	(105,814)

Notes to Financial Statements

1. Summary of Significant Accounting Policies

The following is a summary of significant accounting policies of the City of Glendale (the City) as they pertain to the Water Enterprise Fund.

Funds and Account Groups

The basic accounting and reporting entity of the City is a “fund.” A fund is defined as an independent fiscal and accounting entity with a self-balancing set of accounts for recording cash and other resources together with all related liabilities, obligations, reserves and equities that are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions or limitations.

Basis of Presentation

The City’s Water Enterprise Fund (the Fund) is used to account for the construction, operation and maintenance of the City-owned water utility. The Fund is considered to be enterprise funds, proprietary fund types, as defined under accounting principles generally accepted in the United States of America. The measurement focus is upon financial position, changes in financial position and cash flows. Accordingly, the accrual basis of accounting is followed by the Fund. In accordance with Government Accounting Standards Board (GASB) statement No. 20, Accounting and Financial Reporting for Proprietary Funds and Other Government Entities that Use Proprietary Fund Accounting, the Fund has elected to apply all applicable pronouncements of the Financial Accounting Standards Board (FASB) including those issued on or before November 30, 1989, except for those pronouncements which conflict with or contradict GASB pronouncements. The Fund is included in the City’s Comprehensive Annual Financial Report (CAFR), and therefore, these financial statements do not purport to represent the financial position and changes in financial position of the City.

Cash and Investments

The City values its cash and investments in accordance with the provisions of Government Accounting Standard Board (GASB) Statement No. 31, “Accounting and Financial Reporting for

Certain Investments and External Investments Pools (GASB 31),” which requires governmental entities, including governmental external investment pools, to report certain investments at fair value in the statement of net assets/balance sheet and recognize the corresponding change in the fair value of investments in the year in which the change occurred. Fair value is determined using published market prices.

The City manages its pooled idle cash and investments under a formal investment policy that is reviewed by the Investment Committee and adopted by the City Council and that follow the guidelines of the State of California Government Code. Individual investments cannot be identified with any single fund because the City may be required to liquidate its investments at any time to cover large outlays required in excess of normal operating needs. Funds must request large outlays in advance in order that the City Treasurer will have the funding available.

Interest income from the investment of pooled cash is allocated to all funds, except Capital Improvement Funds on a monthly basis based upon the prior month end cash balance of the fund as a percent of the month end total pooled cash balance. The City normally holds the investment to term; therefore no realized gain/loss is recorded.

All cash and investments are held in the City’s cash management pool. Therefore, for purposes of the combined statement of cash flows for the Proprietary Funds, the City considers all cash, investments, imprest cash and cash with fiscal agents to be cash and cash equivalents.

Capital Assets

The capital assets of the Fund is capitalized at historical cost. Donated assets representing utility service assets, which are donated to the City by independent contractors, are recorded at actual installation cost to the donor. Depreciation for both purchased and contributed assets are computed using a straight-line method, based upon average estimated useful life of an asset.

A summary of the useful lives of the capital assets of the Fund is as follows:

Production plant	15 to 40 years
Transmission & distribution plant	25 to 75 years
General plant	10 to 50 years

Inventories

Inventories, consisting primarily of construction and maintenance materials and tools for the production and distribution system of the Water utility, are carried at weighted average cost.

Compensated Absences

The Water Fund has a fully funded liability for earned but unused accumulated vacation and overtime. As of June 30, 2005 and 2004, the Water Fund had \$538,457 and \$402,003, respectively, of the Water employees’ earned unused accumulated vacation and overtime.

Post-Employment Benefit

All City Employees, including employees of Water Enterprise Fund, that are eligible for retirement with accumulated sick leave are entitled to convert their sick leave hours valued at the rate stated in their respective MOU or Ordinance, into a Retiree Health Savings Plan (RHSP). This RHSP account is controlled by the retiree and money deposited into the account is non-taxable. Money withdrawn from this account, when used for eligible medical expenses as specified in IRS Publication 502 are non-taxable to the retiree. As of June 30, 2005 and 2004, \$5,730,795 and \$5,061,393 had been set-aside in the Internal Service Fund-Employee benefits Fund of the City related to such benefits.

Unbilled Receivables

The Fund record utility services delivered to customers but not billed. As of June 30, 2005 and 2004, the Water Fund’s unbilled receivables were \$2,598,137 and \$2,235,385, respectively.

Deposits

The Fund requires all new or existing utility customers that have not or failed to establish their credit worthiness with the Fund to place a deposit. The deposits are refunded after these customers establish their credit worthiness to the Fund.

Contracts - Retained Amount Due

The Fund records 10% of each progress payment on construction contracts. These retained amounts are not released until final inspection is completed and sufficient time has elapsed for sub-contractors to file claims against the contractor.

Transfers

The City's charter provides for certain percentages of operating revenues in the Water Fund to be transferred to the City's General Fund and have been reflected in the financial statements as transfers out.

Net Assets

Net assets represent the difference between assets and liabilities. Net assets invested in capital assets, net of related debt, consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any borrowings used for the acquisition, construction or improvement of those assets. Net assets invested in capital assets, net of related debt, excludes unspent debt proceeds. Net assets are reported as restricted when there are limitations imposed on their use either through the enabling legislation adopted by the City or through external restrictions imposed by creditors, grantors or laws or regulations of other governments.

The City first applied restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

Revenue Recognition

The Water Utility uses the accrual basis of accounting. Revenues are recognized when earned and expenses are recognized when incurred. Water Utility customers are billed either monthly or bi-monthly. Unbilled water service charges are recorded at year-end and are included in accounts receivable.

An allowance for doubtful accounts is maintained for utility and miscellaneous accounts receivable. The balance in this account is adjusted at fiscal year-end to approximate the amount anticipated to be uncollectible.

Budgets and Budgetary Accounting

The Water Utility presents and the City Council adopts an annual budget. The proposed budget includes estimated expenses and forecasted revenues. The City Council adopts the Water Utility's budget in June each year via a resolution.

2. Cash and Invested Cash

Cash resources of the individual funds are combined to form a pool of cash and investments, which is managed by the City Treasurer under a formal investment policy that is reviewed by the Investment Committee and adopted annually by the City Council. Therefore, individual investments cannot be identified with any single fund. The Fund's interest in this pool is entirely insured or collateralized as of June 30, 2005. Income from the investment of pooled cash is allocated to the Fund on a monthly basis, based upon the month-end cash balance of the fund as a percent of the month-end total pooled cash balance. Of this total, \$8,095,967 and \$10,221,634 pertains to the Water Fund for fiscal year 2005 and 2004, respectively. Invested cash is stated at the fair value. An increase (decrease) in the fair value of investments is recognized as an increase (decrease) to Interest Income Revenue. The City normally holds the investment to term; therefore, no realized gain/loss is recorded. All cash and investments are held in the City's cash management pool. Therefore, for purpose of the combined statement of cash flows for the Proprietary Funds, the City consider all cash, investment, imprest cash and cash with fiscal agents to be cash and cash equivalents.

City of Glendale Cash and investments pool at fiscal year end consist of the following:

	2005	2004
Investments	\$ 558,306,802	\$ 565,955,722
Cash with fiscal agents	18,622,859	15,186,778
	<u>576,929,661</u>	<u>581,142,500</u>
Cash on hand	(649,867)	6,494,160
Total	<u>\$ 576,279,794</u>	<u>\$ 587,636,660</u>

The following amounts are reflected in the City of Glendale’s government-wide statement of net assets:

	<u>2005</u>	<u>2004</u>
Cash and investments	\$ 439,805,054	\$ 410,329,623
Imprest cash	28,930	37,280
Cash with fiscal agents	18,622,859	15,186,778
Investment-gas/electric commodity	3,945,569	3,882,979
Designated cash and investments	<u>113,877,382</u>	<u>158,200,000</u>
Total	<u>\$ 576,279,794</u>	<u>\$ 587,636,660</u>

Information Relating to the City of Glendale Investment Pool:

Authorized Investments

Under provisions of the City’s investment policy, and in accordance with California Government Code Section 53601, the City Treasurer may invest or deposit in the following types of investments:

	<u>Maximum Maturity</u>	<u>Maximum % of Portfolio</u>
U.S. Treasuries	5 years	100%
Federal Agencies	5 years	100%
Medium Term Corporate Notes	5 years	15%
Commercial Paper (A1,P1 minimum rating)	180 days	15%
Bankers Acceptance	180 Days	30%
Negotiable Certificates of Deposit	1 year	30%
Local Agency Investment Fund (State Pool)	N/A	LAIF maximum
Money Market Mutual Funds	90 days	5%
Time Deposits	1 year	10%

Investments in Medium Term Corporate Notes may be invested in Securities rated AA or better by Moody’s or Standard and Poor’s rating services and no more than 5% of the market value of the portfolio may be invested in one corporation. Maximum participation in Bankers Acceptance is limited to 10% per bank.

Disclosure Relating to Interest Rate Risk

Interest rate risk is the risk that fluctuations in market rates may adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to the changes in market interest rates. The City manages its exposure to interest rate

risk by purchasing a combination of shorter term and longer term investments and by timing cash flows from maturities so that a portion of the portfolio is maturing or coming close to maturity evenly over time as necessary to provide the cash flow and liquidity needed for operations.

		Remaining Maturity (in Months)			
		12 Months or Less	13 to 24 Months	25 to 60 Months	More than 60 Months
Commercial Paper	\$ 12,990,571	12,990,571	-	-	-
Federal Agency Term Notes	88,396,123	43,691,250	29,877,329	14,827,544	-
Federal Agency Callable Bonds	385,539,403	44,602,869	111,798,657	229,137,877	-
Corporate Notes	35,490,245	17,925,704	8,078,693	9,485,848	-
State Investment Pool	18,957,204	18,957,204	-	-	-
Money Market Held by Fiscal Agents	16,933,256	16,933,256	-	-	-
Federal Agency Term Notes	8,880,479	8,880,479	-	-	-
Guaranteed Investment Contracts	4,909,098	-	-	-	4,909,098
Money Market	4,833,282	4,833,282	-	-	-
	\$ 576,929,661	168,814,615	149,754,679	253,451,269	4,909,098

The City assumes that callable investments will not be called.

Disclosures Relating to Credit Risks

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. The City invests only in the most risk-adverse instruments, such as AAA-rate government securities, and AAA or AA-rate corporate securities.

MANAGEMENT DISCUSSION AND ANALYSIS – WATER UTILITY

		Rating as of Year End				
		AAA	AA	Aa2	A1,P1	Unrated
Commercial Paper	\$ 12,990,571	-	-	-	12,990,571	-
Federal Agency Term Notes	88,396,123	88,396,123	-	-	-	-
Federal Agency Callable Bonds	385,539,403	385,539,403	-	-	-	-
Corporate Notes	35,490,245	24,992,435	10,497,810	-	-	-
State Investment Pool	18,957,204	-	-	-	-	18,957,204
Money Market	16,933,256	16,933,256	-	-	-	-
Held by Fiscal Agent						
Federal Agency Term Notes	8,880,479	8,880,479	-	-	-	-
Guaranteed Investment Contracts	4,909,098	-	-	4,909,098	-	-
Money Market	4,833,282	4,833,282	-	-	-	-
	\$ 576,929,661	529,579,978	10,497,810	4,909,098	12,990,571	18,957,204

Concentration on Credit Risk

The investment policy of the City contains no limitations on the amount that can be invested in any one issuer beyond that stated above. Investments in any one issuer that represent 5% or more of total City investments are as follows:

Issuer	Investment Type	Reported Amount
FHLB	Federal Agency Term Notes	\$ 51,540,938
FHLB	Federal Agency Callable Bonds	<u>248,340,822</u>
	Total	<u><u>299,881,760</u></u>
FHLMC	Federal Agency Term Notes	18,729,405
FHLMC	Federal Agency Callable Bonds	<u>66,881,618</u>
	Total	<u><u>85,611,023</u></u>
FNMA	Federal Agency Term Notes	9,806,250
FNMA	Federal Agency Callable Bonds	<u>60,509,150</u>
	Total	\$ <u><u>70,315,400</u></u>

Custodial Credit Risk

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty (e.g., broker-dealer) to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The California Government Code and the Entity's investment policy do not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits or investments, other than the following provision for deposits: The California Government Code requires that a financial institution secure deposits made by state or local governmental units by pledging securities in an undivided collateral pool held by a depository regulated under state law (unless so waived by the governmental unit). The market value of the pledged securities in the collateral pool must equal at least 110% of the total amount deposited by the public agencies. California law also allows financial institutions to secure City deposits by pledging first trust deed mortgage notes having a value of 150% of the secured public deposits.

At June 30, 2005, the carrying amount of the City's deposits was (\$649,867) and the corresponding bank balance was \$1,073,920. The difference of \$1,723,787 was principally due to outstanding warrants, wires and deposits in transit. Of the Bank balance, \$100,000 was insured by the FDIC depository insurance and \$973,920 was uncollateralized and not insured by FDIC depository insurance.

Investment in State Investment Pool

The City is a voluntary participant in the Local Agency Investment Fund (LAIF) that is regulated by California Government Code Section 16429 under the oversight of the Treasurer of the State of California. The fair market value of the City's investment in this pool is reported in the accompanying financial statements at amounts based upon the City's pro-rata share of the fair value provided by LAIF for the entire LAIF portfolio (in relation to the amortized cost of that portfolio)

3. Self-Insurance Program

The City is self-insured for Workers' Compensation claims up to \$3,000,000 per occurrence and general public liability up to \$2,000,000 per occurrence. Additional coverage in excess of these limits has been purchased from third-party insurance companies. Workers' Compensation and

general public liability insurance protection is provided through internal service funds maintained by the City. The City is also self-insured for unemployment insurance and general auto liability through separate Internal Service Funds. The Internal Service Funds charge the Electric Fund for its estimated share of the liability. At June 30, 2005, such liability has been fully funded to the City.

A claims payable liability has been established in these funds on case basis estimates of reported claims and an estimate for claims incurred but not reported. Management believes that provisions for claims at June 30, 2005 are adequate to cover the net cost of claims incurred to date. However, such liabilities are, by necessity, based upon estimates and there can be no assurance that the ultimate cost will not exceed such estimates.

4. Pension Plan

Full-time employees of GWP participate with other City employees in the Public Employees Retirement System (PERS) of the State of California, which is an agent multiple-employer public employee retirement system. GWP's contributions represent a pro rata share of the City's contribution, including the employees' contribution that is paid by GWP, which is based on PERS's actuarial determination as of July 1 of the current fiscal year. PERS does not provide data to participating organizations in such a manner so as to facilitate separate disclosure for GWP's share of the actuarial computed pension benefit obligation, the plan's net assets available for benefit obligation and the plan's net assets available for benefits. Approximately 22% of full-time City workers are employed by GWP.

Plan Description

The City contributes to the California Public Employees' Retirement System (CalPERS), an agent multiple-employer public employee retirement system that acts as a common investment and administrative agent for participating public entities within the State of California.

All full-time employees are required to participate in CalPERS, and related benefits vest after five years of service. Upon five years of service, employees who retire at age 50 or older are entitled to receive an annual retirement benefit. The benefit is payable monthly for life. The benefit is calculated as follows: years of credited service multiplied by their highest twelve consecutive months of salary multiplied by a percentage factor. This factor is age-based – public safety employees use the 3% at age 50 factor while all others use the 2% at age 55 factor. Effective December 1, 2005 the general employees will use the 2.5% at age 55 factor. The system also provides death and disability benefits. CalPERS issues a publicly available financial report that

includes financial statements and required supplemental information of participating public entities within the state of California. Copies of the CalPERS' annual financial report may be obtained from the CalPERS Executive Office – 400 P Street, Sacramento, CA 95814.

Funding Policy

CalPERS is a contributory plan deriving funds from employee contributions as well as from employer contributions and earnings from investments. According to the plan, City employees are required to contribute 7% of annual salary for general members and 9% of annual salary for public safety members. Effective December 1, 2005 general members contribution rate will increase to 8% of reportable earnings. The City is also required to contribute at an actuarially determined rate; the current public safety rate and the current general employee rates are 24.99% and 0% respectively of annual covered payroll. The contribution requirements of plan members are established by State statute and the employer contribution rate is established and may be amended by CalPERS. The City's rate for safety members that CALPERS charges have decreased in fiscal year 2005-06 from 24.99% to 24.577%, the rate for general employees have increased from 0% to 6.289%. Effective December 1, 2005 this rate will increase from 6.289% to 9.591%

Annual Pension Cost

Contributions to CalPERS totaling \$9,832,076 were made during the fiscal year ended June 30, 2005 in accordance with actuarially determined contribution requirements through an actuarial valuation performed at June 30, 2003. The actuarial assumptions included (a) a rate of return on the investment of present and future assets of 7.75% a year compounded annually (net of administrative expenses), (b) projected salary increases that vary by duration of service ranging from 3.25% to 14.45%, (c) no additional projected salary increases attributable to seniority/merit and (d) no post retirement benefit increases. The actuarial value of the City's assets was determined using techniques that smooth the effects of short-term volatility in the market value of investments over a three year period depending on the size of investment gains and/or losses. CalPERS uses the entry-age-normal-actuarial-cost method, which is a projected-benefit-cost method. That is, it takes into account those benefits that are expected to be earned in the future as well as those already accrued. According to this cost method, the normal cost for an employee is the level amount which would fund the projected benefit if it were paid annually from date of employment until retirement. In addition, the employer's total normal cost is expressed as a level percentage of payroll. CalPERS also uses the level-percentage-of-payroll method to amortize any unfunded actuarial liabilities. Initial unfunded liabilities are amortized over a closed period that depends on the plan's date of entry into CalPERS. Subsequent plan amendments are amortized as a level percent of pay over a closed 20 year period. Gains and losses that occur in the operation of

the plan are amortized over a rolling period, which results in an amortization of 10% of unamortized gains and losses each year. If the plan’s accrued liability exceeds the actuarial value of plan assets, then the amortization payment on the total unfunded liability may not be lower than the payment calculated over a 30 year amortization.

Three Year Trend Information			
Fiscal year ending	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
6/30/03	\$561,070	100%	0
6/30/04	\$2,090,971	100%	0
6/30/05	\$9,832,076	100%	0

REQUIRED SUPPLEMENTARY INFORMATION - Schedule of Funding Progress (Unaudited)

Actuarial Valuation Date	Actuarial Value of Assets ←a→	Actuarial Liability <AAL> – Entry Age ←b→	(Unfunded AAL) / Overfunded AAL ←a-b→	Funded Ratio ←a/b→	Covered Payroll ←c→	(Unfunded AAL)/ Overfunded AAL as a Percentage of Covered Payroll ←(a-b)/c→
06/30/2001	815,521,178	687,539,962	127,981,216	118.6%	101,369,092	126.3%
06/30/2002	766,978,940	732,667,128	34,311,812	104.7%	109,853,251	31.2%
06/30/2003	770,652,222	795,007,184	(24,354,962)	96.9%	114,964,463	(21.2%)

5. Net Assets

Net assets are reported as restricted when there are limitations imposed on their use either through the enabling legislation adopted by the City or through external restrictions imposed by creditors, grantors or laws or regulations of other governments. Net assets are reported as unrestricted when there are no limitations imposed on their use.

In December of 2003, GWP management received approval from the City Council to implement a cash reserve policy for the Water Fund to ensure a long term sustainable financial health of the water operation. The policy calls for annual review of the reserves to determine if the recommended levels are sufficient. The annual review of the Cash Reserve Policy for fiscal year ending June 30, 2005, established a target of \$7,400,000 of designated cash in the following categories: \$5,700,000 for contingency reserve; and \$1,700,000 for rate stabilization reserve. As of June 30, 2005, \$4,294,000 is designated with the goal of meeting the remaining \$3,106,000 with future available cash.

6. Capital Assets

A summary of the changes in Water Fund 2004- 2005 Capital Assets is as follows:

	Balance at July 01, 2004	Additions	Retirements	Balance at June 30, 2005
Production plant	\$ 22,513,260	809,497	(777,061)	24,099,818
Transmission & distribution Plant	79,507,342	4,785,802	717,823	83,575,321
General plant	11,336,044	2,068,251	635,752	12,768,543
Total water fund	113,356,646	7,663,549	576,514	120,443,681
Less allowance for accumulated depreciation	43,340,356	2,098,030	576,514	44,861,872
Net book value of water fund	\$ 70,016,290	5,565,519	-	75,581,809

A summary of the changes in Water Fund 2003- 2004 Capital Assets is as follows:

	Balance at July 01, 2004	Additions	Retirements	Reclassification	Balance at June 30, 2005
Production plant	\$ 23,323,995	1,243,093	356,817	(1,697,011)	22,513,260
Transmission & distribution Plant	74,660,475	4,593,371	10,887	264,383	79,507,342
General plant	9,544,111	326,428	53,057	1,518,562	11,336,044
Total water fund	107,528,581	6,162,892	420,761	85,934	113,356,646
Less allowance for accumulated depreciation	41,123,987	2,590,456	420,761	46,674	43,340,356
Net book value of water fund	\$ 66,404,594	3,572,436	-	39,260	70,016,290

7. Contingent Liabilities

Litigation

The City is a defendant in several general damage and personal injury lawsuits and claims. These claims arise primarily from injuries sustained by the claimants while on property owned or maintained by the City. While litigation is by nature uncertain, management believes, based on consultation with the City Attorney, that these cases in the aggregate are not expected to result in a material adverse impact on the City. Additionally, City management believes that sufficient reserves are available to the City to cover any potential losses should an unfavorable outcome materialize.