

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, 2004. 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

Fiscal year 2004 saw increased water sales resulting from warmer weather than in the prior year. Total water consumption grew by 3% resulting in a 4% increase in total operating revenue. Operating expenses increased by 8% primarily due to the increased cost of water supplied by MWD, and the increased cost of electricity for pumping water through the transmission and distribution system. Net operating revenue was \$6,356. Total net assets increased by \$5,020 after adding net non-operating revenue of \$1,896 and less \$3,232 in Transfers to the City's General Fund.

The assets of the Water Utility exceeded its liabilities at the close of the most recent fiscal year by \$82,034. Of this amount, \$12,018 was unrestricted and may be used to meet the Fund's ongoing obligations to creditors and customers. At the end of the fiscal year, the unrestricted net assets represented 48% of annual operating expenses for 2004.

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 that collectively provide an indication of the Water Utility's financial health.

The **Balance Sheets** present 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 **Statements of Revenues, Expenses and Changes in Net Assets** present 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 is more fully described in the accompanying Notes to the Financial Statements.

The **Statements of Cash Flows** present 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 72 to 81 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 \$82,034 at the close of the most recent fiscal year. A portion of the Utility's net assets (85.4%) 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 (14.6%) 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:

	2004	2003
Current and other assets	15,077	13,492
Capital assets	70,016	66,405
Total assets	85,094	79,897
Long-term debt	-	-
Other liabilities	3,060	2,883
Total liabilities	3,060	2,883
Net assets:		
Invested in capital assets, net of related debt	70,016	66,405
Restricted	-	-
Unrestricted	12,018	10,609
Total net assets	82,034	77,014

The Water Utility's net assets increased by \$5,020 during the current fiscal year. The increase is primarily a result of increased retail revenues from increased consumption.

Changes in Net Assets – Water Utility

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

	2004	2003
Revenues		
Retail sales, net	30,928	30,846
Adjustable rate adjustment	449	787
Interest income	111	320
Other revenues and grants	1,498	1,206
Capital contributions	287	200
Total revenues	33,273	33,359
Expenses		
Production	17,689	16,618
Transmission and distribution	2,700	1,977
Customer accounting and sales	2,041	1,831
Depreciation	2,590	2,738
Interest expense	-	-
Total expenses	25,021	23,164
Transfers to the City's general fund	3,232	3,082
Total expenses and transfers	28,253	26,246
Changes in net assets	5,020	7,113
Total net assets, beginning of year	77,014	69,901
Total net assets, end of year	82,034	77,014

Revenues by Source – Water Utility

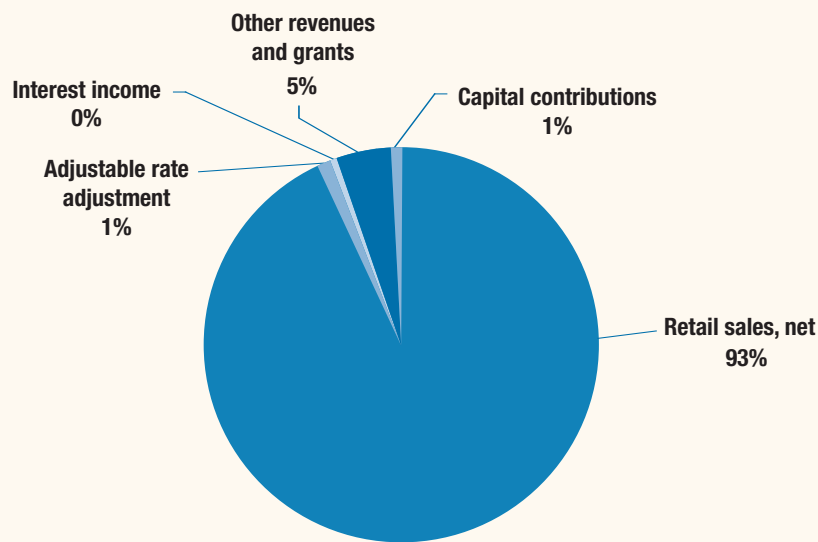
Retail sales (residential, commercial, industrial and other sales) continue to be the primary revenue source for the Water Utility, making up 93% of total revenue. Retail sales showed an increase of 4% from the prior year due to a 3.1% consumption growth as a result of warmer weather than in the prior year, offset by a decrease in accrued unbilled revenues.

The Adjustable Rate Adjustment recognizes the deficit between the adjustable water rate charged to customers and the costs of MWD water supply and electricity for pumping.

Investment income decreased by \$209, or 65% below the prior year level. The decrease is related to market conditions that continue to be poor, resulting in lower earnings for the Water Utility's investment portfolio.

Capital contributions increased 43% from prior year levels. The increased amount over the prior year reflects an increased level of construction projects funded by others, primarily by retail customers.

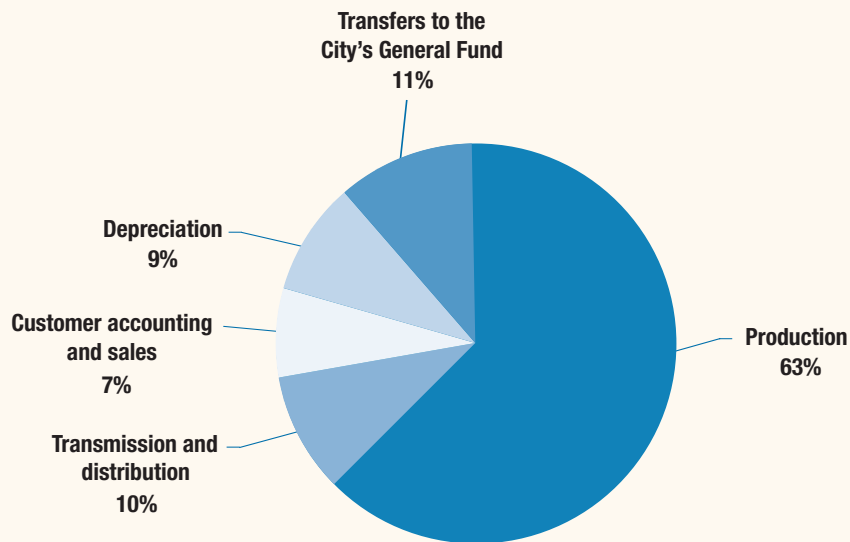
Other revenues and grants increased by \$292, or 24% over the prior year level primarily due to the increased grant funding from EPA for water quality projects.



Expenses by Source – Water Utility

Total expenses for the Water Utility increased by 8.0%. Increase in consumption resulted in a corresponding increase in operating expenses. Production expenses comprising primarily of MWD water supply cost increased by 6.4%. Transmission and distribution expenses increased by 36.6% as a result of transporting more water through the system and increased electricity cost for pumping. Customer accounting and sales expenses increased by 11.5% after returning to the full staffing level. Depreciation expense decreased slightly as old assets were retired while increased capital expenses recorded as construction in progress did not require depreciation until future periods.

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 \$150, reflecting an increase in both the percentage and total retail revenues.



Capital Assets and Debt Administration

Capital Assets

The Water Utility's investment in capital assets as of June 30, 2004 totals to \$70,016 (net of accumulated depreciation). This includes investments in production, transmission, and distribution related facilities, as well as general items such as office equipment, furniture, etc. This fiscal year showed a 5.4% 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:

	2004	2003
Production	22,513	23,324
Transmission and distribution	79,507	74,660
General	11,336	9,544
Less: Accumulated depreciation	(43,340)	(41,124)
Total	70,016	66,404

Long-Term Debt

As of June 30, 2004, 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.