

**GUAM POWER AUTHORITY**

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**FINANCIAL STATEMENTS AND  
ADDITIONAL INFORMATION AND  
INDEPENDENT AUDITORS' REPORT**

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**YEARS ENDED SEPTEMBER 30, 2004 AND 2003**

## INDEPENDENT AUDITORS' REPORT

### Consolidated Commission on Utilities:

We have audited the accompanying balance sheets of Guam Power Authority (GPA), a component unit of the Government of Guam, as of September 30, 2004 and 2003, and the related statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of GPA's management. Our responsibility is to express an opinion 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 and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, 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 opinion.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of Guam Power Authority as of September 30, 2004 and 2003, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in note 4 to the financial statements, three agencies of the Government of Guam have substantial accounts receivable balances with GPA that have been outstanding for several years. These receivables total approximately \$31 million at September 30, 2004. Collection of these receivables is dependent on adequate funding to be provided by the Government of Guam to these agencies or successful issuance of bonds by the Government of Guam. At present, the likelihood of a successful bond issuance by the Government of Guam is not determinable. The write down of the receivables at September 30, 2004 would likely place GPA in technical default on its outstanding bonds payable. A bond default would raise substantial doubt about GPA's ability to continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

The Management's Discussion and Analysis on pages 1-5 is not a required part of the basic financial statements but is supplementary information required by the GASB. This supplementary information is the responsibility of GPA's management. We have applied certain limited procedures to such information, which consisted principally of inquiries of management regarding the methods of measurements and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying supplementary schedules on pages 29 through 31, for the years ended September 30, 2004 and 2003, are presented for purposes of additional analysis and are not a required part of the basic financial statements. These schedules are the responsibility of GPA's management. Such information has been subjected to the audit procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued our report dated May 23, 2005, on our consideration of the GPA's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

*Deloitte + Touche LLP*

May 23, 2005

# GUAM POWER AUTHORITY

## Management Discussion and Analysis Year Ended September 30, 2004

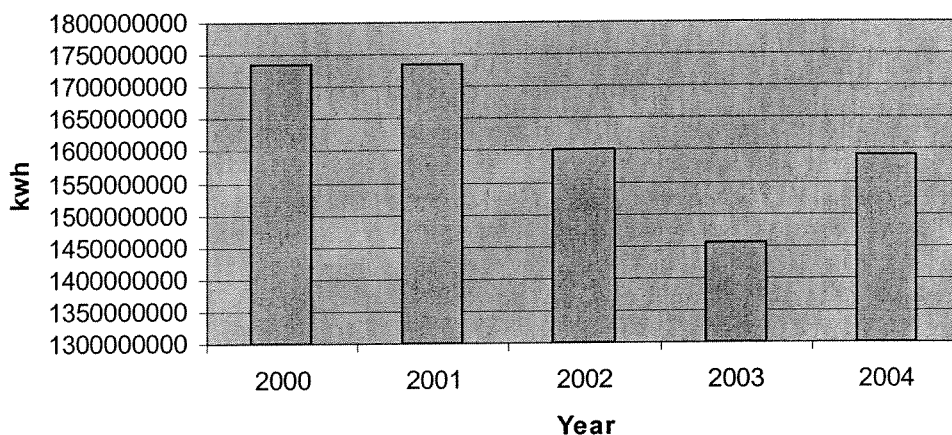
### Introduction

The defining moment for the Guam Power Authority has been the change in governance that took place January 2, 2003. An elected Consolidated Commission on Utilities (CCU) was elected as the governing board for the Guam Power Authority. Prior to that the board was appointed by and subject to oversight of the Governor of Guam. The change in governance led to a change in management. This discussion will highlight many of the changes that have taken place under the new management team.

### Economic Conditions

Guam has not seen any significant economic growth since the early 1990's. The last five years have been especially challenging as the economy has been impacted by several external events. Fiscal Year 2004 saw a reversal of some negative trends in key economic indicators for the island. They are also reflected in GPA's kWh sales numbers which are shown below:

**KWH Sales Last 5 Years**



GPA's net loss of \$9.2 million was a disappointment to the Authority and is representative of the dilemma it faces. Under normal circumstances, GPA would take aggressive measures to rectify its cash challenges either through cost cutting or rate increases. However, because the island is in the beginning stages of an economic recovery, management is concerned that aggressive cost cutting may leave GPA unprepared for the anticipated growth and rate increases may serve as a deterrent to economic expansion. Additionally, the Utility's ratepayers have been burdened by an increase in GPA's levelized energy adjustment clause (LEAC) which is set bi-annually to allow GPA to recover its fuel costs. GPA management is monitoring its sales very carefully and is in the process of hiring a consultant to update the Authority's load forecast. By the time the forecast is complete, GPA should have a more clear understanding of future energy demand and will be in a better position to take appropriate actions with respect to its bottom line.

Additionally, there were a few transactions that related to prior years which had a significant impact on the financial statements. GPA suffered damage to a fuel line which led to an oil spill. GPA incurred substantial costs related to the loss and has not received confirmation from its insurer that reimbursement is forthcoming. GPA has reserved approximately \$3.4 million pending the resolution of this claim. Additionally, the Government of Guam contested the number streetlights that were being charged to government accounts. GPA conducted a power pole and streetlight inventory count during the year. The results indicated that GPA had been over billing the government for streetlight charges since 2001. This led to a charge of approximately \$2.8 million against revenues during FY04. Also,

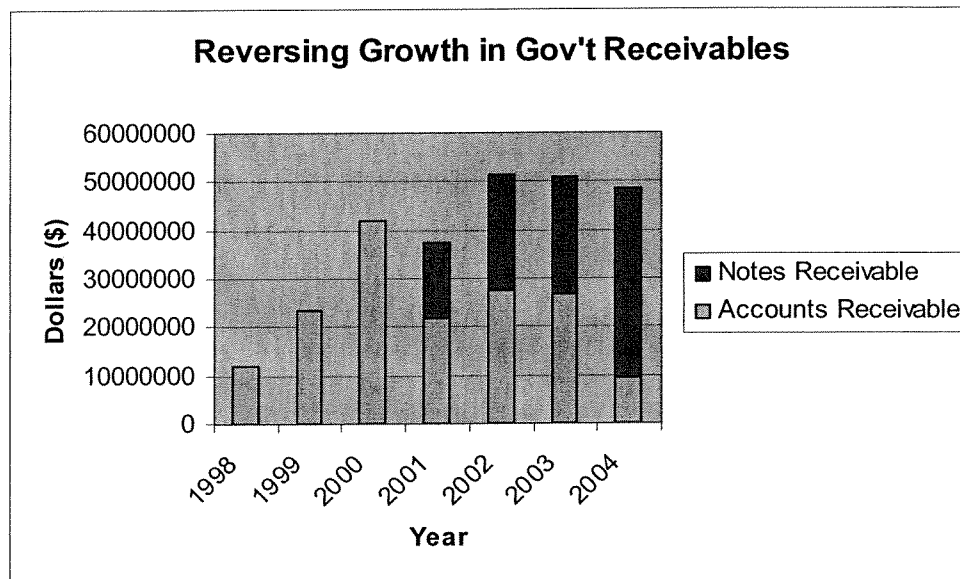
## GUAM POWER AUTHORITY

### Management Discussion and Analysis Year Ended September 30, 2004

new legislation required GPA to set up a liability for partial vesting of sick leave benefits for employees in the Government of Guam Defined Contribution Retirement Plan resulting in an expense of \$.6 million. Finally, a change in the unfunded actuarial liability for the Government of Guam defined benefit retirement plan resulted in a charge of nearly \$1.5 million. The first three of these transactions are one time adjustments to correct some long outstanding problems and react to new legislation. These transactions will not have any significant impact on future financial statements. The change in the unfunded actuarial liability was completed using information from an actuarial study that was released in March 2005.

#### Government Receivables

Before the change in governance, receivables from the Government of Guam had been steadily increasing as the payment stream from a few key agencies had been inconsistent at best. One of the first actions of the CCU was to establish a policy that the Government of Guam must be held to the same customer rules as other GPA customers. The Commission entered into an agreement with the Government wherein past due billings from the Government would be paid through the issuance of general obligation bonds. The Government was required to keep current on its bills on a go forward basis. There were a few occasions during the year in which government agencies were disconnected for their failure to keep their bills current. The policy has ended the growth in government receivables and there has been a decline in total receivables from the Government since the change in governance as the graph below shows:



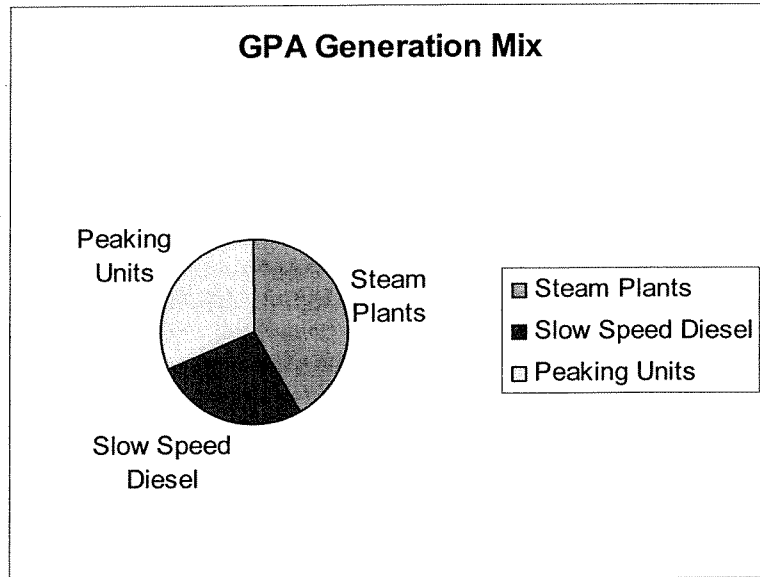
The plan to collect on the past due billings has been held up in court due to a challenge by Guam's Attorney General, therefore, GPA management is negotiating promissory notes with the government agencies to insure the payment stream to repay the amounts owed even if the general obligation bond is not issued.

# GUAM POWER AUTHORITY

Management Discussion and Analysis  
Year Ended September 30, 2004

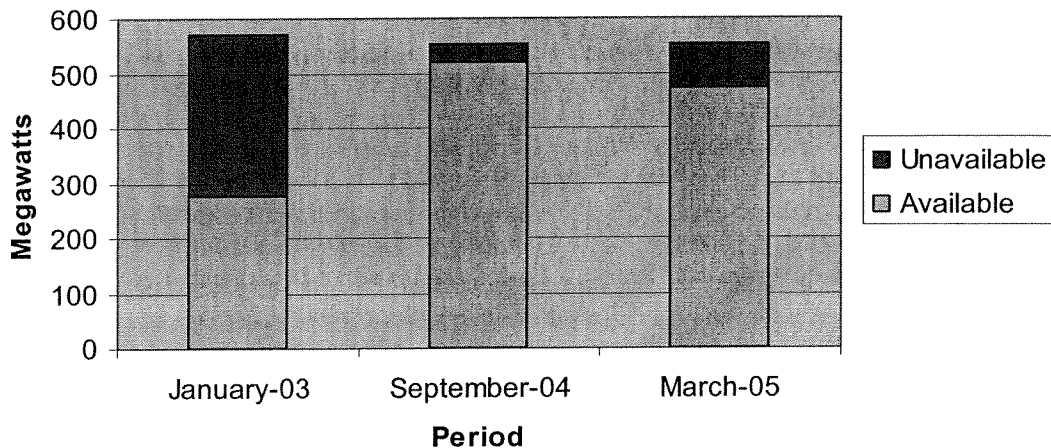
## Rehabilitation of Generation Facilities

The chart below shows the mix of generation facilities:



When the Commission took control of the utilities, the Authority had an operational capacity of 276 mW. A major focus of the new management has been to restore availability of some of the most efficient generation plants and reduce the need for the utility to burn diesel fuel which is significantly more costly. The steam plants and slow speed diesel plants each burn sulfur oil. The improvement in unit availability is demonstrated in the graph below.

## Availability of Generation Units



# GUAM POWER AUTHORITY

## Management Discussion and Analysis Year Ended September 30, 2004

The Guam Power Authority's power bill is primarily made up of a base rate and a fuel factor. GPA utilizes a levelized energy adjustment clause (LEAC) which is adjusted every six months to recover GPA's fuel costs.

### Significant Challenge

The significant challenge that is facing the Authority is related to the fact that GPA is a fossil fuel dependent utility. GPA has a fuel hedging program in place, however, GPA has found the current fuel markets to be very challenging and is currently in an unhedged position.

### Future Financing

GPA is also conducting a feasibility study to determine if sea water air cooling technology would be beneficial for the Authority's customers. GPA's preliminary estimates indicate this technology could provide a net reduction in operating costs if undertaken. If the results of the study are favorable, GPA may pursue a small bond issuance in Fiscal Year 2006.

### Table of Financial Data

MILLIONS OF DOLLARS	2004	2003	Variance
Assets:			
Current Assets	\$149.2	\$164.0	(9.0%)
Non-current investments	27.4	27.5	(0.4%)
Other non-current assets	47.6	50.7	(6.1%)
Utility Plant	557.2	568.1	(1.9%)
Liabilities			
Current liabilities	68.3	80.1	(14.7%)
Non-current liabilities	561.9	569.7	(1.4%)
Net Assets			
Invested in capital assets net of related debt	8.2	10.8	(24.1%)
Restricted	60.8	72.7	(16.4%)
Unrestricted	82.2	77.0	6.8%

MILLIONS OF DOLLARS	2004	2003	Variance
Revenues	\$226.4	\$192.4	17.7%
Total Operating and Maintenance expense	193.1	163.9	17.9%
Operating earnings	33.3	28.5	16.8%
Interest income	2.9	2.7	7.4%
Other revenues and (expense)	(45.4)	(55.4)	(18.1%)
Loss before capital contributions	(9.2)	(24.2)	(61.9%)
Capital contributions	0.0	0.3	(100.0%)
(Decrease) increase in net assets	(9.2)	(23.9)	(61.5%)

# **GUAM POWER AUTHORITY**

## **Management Discussion and Analysis Year Ended September 30, 2004**

### **Results of Operations**

#### ***2004 Compared with 2003***

- The reduction in current assets was the result of drawdowns of GPA's Construction Fund and reductions in Accounts Receivable.
- The significant event affecting liabilities was the payoff of a short term loan taken out by GPA in the aftermath of Typhoon Pongsona.
- Guam Power Authority revenues increased by \$34.0 million, or 17.7% in 2004 as compared with 2003. This is due to increased fuel revenues of \$22.6 million and base rate revenues increased by \$11.4 million.
- Total Operating and maintenance expenses of \$193.1 million for 2004 were \$29.2 million or 17.9% higher than the prior year. This is due to increases in fuel costs of \$22.6 million, increases in other production of \$3.6 million due to maintenance of the base load units and an increase of \$2.9 million in transmission and distribution costs due to maintenance.
- Interest income in 2004 increased by \$0.2 million or 7.4% compared to 2003. Interest on investments was stable in 2004.
- Other expenses, net of other revenues, decreased by \$10.0 million or 18.1% from prior year due to typhoon expenses incurred in fiscal year 2003.
- Losses before capital contributions decreased by \$15.0 million or 61.9%.

### **Conclusion**

There remains much work yet to be done; however, GPA believes the new governance model has placed the utility in a position to continue to strengthen the Utility and to take advantage of future opportunities. Major issues currently being addressed include the conversion of overhead lines to underground, the system reliability study to reduce power plant and line related outages, the refurbishment of remaining non-base load generation capacity, the replacement of the transportation fleet, the preventive maintenance of substations and manpower training and retention.

# GUAM POWER AUTHORITY

Balance Sheets  
September 30, 2004 and 2003

<u>ASSETS</u>	<u>2004</u>	<u>2003</u>
Utility plant, at cost:		
Electric plant in service	\$ 778,573,057	\$ 767,672,108
Construction work in progress	25,273,272	22,551,695
Less accumulated depreciation	<u>(246,608,978)</u>	<u>(222,137,558)</u>
Total utility plant	<u>557,237,351</u>	<u>568,086,245</u>
Bond reserve funds (trustee)	<u>27,393,130</u>	<u>27,484,000</u>
Current assets:		
Cash and investments:		
Held by trustee:		
Interest and principal funds for debt repayment	17,605,643	16,918,602
Bond indenture funds for restricted purposes	26,692,296	33,176,699
Held by Guam Power Authority:		
Bond indenture funds	<u>20,173,431</u>	<u>11,058,655</u>
Total cash and cash equivalents	<u>64,471,370</u>	<u>61,153,956</u>
Accounts receivable	41,136,226	53,497,170
Current installments of long-term receivables	<u>7,608,860</u>	<u>6,176,693</u>
Total current receivables	48,745,086	59,673,863
Materials and supplies inventory	15,847,828	17,238,286
Fuel inventory	16,526,785	16,958,924
Prepaid expenses	1,347,697	707,290
Current portion of deferred fuel costs	<u>2,222,015</u>	<u>8,326,862</u>
Total current assets	<u>149,160,781</u>	<u>164,059,181</u>
Other non-current assets:		
Accounts receivable, less current installments	31,622,764	32,958,745
Non-current deferred fuel costs	3,582,757	4,700,000
Unamortized debt issuance costs	4,957,694	5,124,898
Cancelled unit, net of amortization	1,113,057	1,235,232
Deferred asset, net	4,143,125	4,302,476
Other	<u>2,183,922</u>	<u>2,375,353</u>
Total other assets	<u>47,603,319</u>	<u>50,696,704</u>
	<u>\$ 781,394,581</u>	<u>\$ 810,326,130</u>

See accompanying notes to financial statements.

# GUAM POWER AUTHORITY

Balance Sheets, Continued  
September 30, 2004 and 2003

<u>LIABILITIES AND NET ASSETS</u>	<u>2004</u>	<u>2003</u>
Current liabilities:		
Short-term debt	\$ 20,000,000	\$ 25,000,000
Current maturities of long-term debt	5,935,000	5,680,000
Current obligations under capital leases	4,398,150	3,903,260
Accounts payable:		
Operations	15,033,998	17,545,475
Fuel	4,084,782	9,275,554
Navy	55,982	19,000
Accrued payroll and employees' benefits	2,241,060	1,308,507
Accrued COLA/supplemental annuities	-	952,120
Current portion of employees' annual leave	1,479,102	1,231,124
Interest payable	11,723,548	11,909,032
Customer deposits	3,331,782	3,338,339
Total current liabilities	68,283,404	80,162,411
Long-term debt, less current maturities	390,713,116	395,460,691
Employees' annual leave, less current portion	917,912	1,461,243
Retirement fund deferred contributions	5,049,406	3,492,116
Obligations under capital leases, less current portion	149,122,246	153,520,187
Provision for self-insurance	891,364	-
Deferred revenues, net	15,184,458	15,768,476
Total liabilities	630,161,906	649,865,124
Commitments and contingencies		
Net assets:		
Invested in capital assets, net of related debt	8,181,896	10,757,339
Restricted	60,845,586	72,713,032
Unrestricted	82,205,193	76,990,635
Total net assets	151,232,675	160,461,006
	\$ 781,394,581	\$ 810,326,130

See accompanying notes to financial statements.

# GUAM POWER AUTHORITY

## Statements of Revenues, Expenses and Changes in Net Assets Years Ended September 30, 2004 and 2003

	<u>2004</u>	<u>2003</u>
Revenues:		
Sales of electricity	\$ 225,299,741	\$ 190,536,282
Miscellaneous	<u>1,075,899</u>	<u>1,910,108</u>
Total revenues	<u>226,375,640</u>	<u>192,446,390</u>
Operating and maintenance expenses:		
Production fuel	95,266,939	72,709,107
Other production	<u>19,986,627</u>	<u>16,335,766</u>
	115,253,566	89,044,873
Administrative and general	23,889,866	24,349,885
Depreciation	24,603,493	24,135,225
Energy conversion costs	16,542,375	17,048,535
Transmission and distribution	9,419,690	5,846,001
Customer accounting	<u>3,368,927</u>	<u>3,508,141</u>
Total operating and maintenance expenses	<u>193,077,917</u>	<u>163,932,660</u>
Operating earnings	<u>33,297,723</u>	<u>28,513,730</u>
Other revenues (expense):		
Interest revenue	2,935,964	2,720,686
Allowance for funds used during construction	1,641,578	1,066,125
COLA/supplemental annuities	(793,351)	(683,432)
Consulting services	(4,960)	(892,768)
Other expense	(122,175)	(122,175)
Loss due to typhoon	(65,795)	(11,014,894)
Oil spill costs	(3,414,842)	-
Interest expense	<u>(42,702,473)</u>	<u>(43,810,976)</u>
Total other expenses	<u>(42,526,054)</u>	<u>(52,737,434)</u>
Loss before capital contributions	(9,228,331)	(24,223,704)
Capital contributions:		
Grants from the United States Government	<u>-</u>	<u>280,295</u>
Decrease in net assets	(9,228,331)	(23,943,409)
Total net assets at beginning of year	<u>160,461,006</u>	<u>184,404,415</u>
Total net assets at end of year	<u><u>\$ 151,232,675</u></u>	<u><u>\$ 160,461,006</u></u>

See accompanying notes to financial statements.

# GUAM POWER AUTHORITY

## Statements of Cash Flows Years Ended September 30, 2004 and 2003

<u>Increase (decrease) in cash and cash equivalents</u>	<u>2004</u>	<u>2003</u>
Cash flows from operating activities:		
Cash received from customers	\$ 225,797,359	\$ 190,000,493
Cash payments to suppliers for goods and services	(143,979,719)	(113,184,662)
Cash payments to employees for services	(24,409,718)	(23,083,588)
Net cash provided by operating activities	<u>57,407,922</u>	<u>53,732,243</u>
Cash flows from investing activities:		
Change in bond reserve funds	90,870	(687)
Interest and dividends on investments and bank accounts	2,935,963	2,720,686
Net cash provided by investing activities	<u>3,026,833</u>	<u>2,719,999</u>
Cash flows from noncapital financing activities:		
Issuance of (principal paid on) short-term debt	(5,000,000)	2,088,000
Interest paid on short-term debt and deposits	(266,158)	(452,325)
Net cash (used in) provided by noncapital financing activities	<u>(5,266,158)</u>	<u>1,635,675</u>
Cash flows from capital and related financing activities:		
Acquisition of utility plant	(13,428,043)	(5,493,434)
Contributions received	-	280,295
Principal paid on bonds and other long-term debt	(4,492,575)	(5,124,297)
Interest paid on bonds and other long-term debt	(21,799,077)	(23,912,560)
Principal paid on capital leases	(3,903,052)	(3,465,090)
Interest paid on capital leases	(19,181,143)	(19,619,213)
Oil spill costs paid	(2,125,327)	-
Typhoon expenditures	(1,018,353)	(25,402,146)
FEMA receipts	14,096,387	10,667,701
Net cash used in capital and related financing activities	<u>(51,851,183)</u>	<u>(72,068,744)</u>
Net increase (decrease) in cash and cash equivalents	3,317,414	(13,980,827)
Cash and cash equivalents at beginning of year	<u>61,153,956</u>	<u>75,134,783</u>
Cash and cash equivalents at end of year	<u>\$ 64,471,370</u>	<u>\$ 61,153,956</u>

See accompanying notes to financial statements.

# GUAM POWER AUTHORITY

## Statements of Cash Flows, Continued Years Ended September 30, 2004 and 2003

	<u>2004</u>	<u>2003</u>
<u>Reconciliation of operating earnings to net cash provided by operating activities:</u>		
Operating earnings	\$ 33,297,723	\$ 28,513,730
Other expense	(4,960)	(892,768)
Adjustments to reconcile operating earnings to net cash provided by operating activities:		
Depreciation	24,603,493	24,135,225
Bad debt	1,200,000	1,200,000
COLA/supplemental annuities paid	(1,745,471)	(801,862)
Difference between retirement expense and funding	1,557,290	1,756,858
(Increase) decrease in assets:		
Accounts receivable	(2,079,071)	(3,876,628)
Materials and supplies inventory	1,390,458	(307,408)
Fuel inventory	432,139	(3,344,383)
Prepaid expenses	(640,407)	674,474
Deferred fuel costs	7,222,090	(6,431,640)
Other assets	191,431	381,732
Increase (decrease) in liabilities:		
Accounts payable - fuel	(5,190,772)	6,314,593
Accounts payable - operations	(3,800,992)	5,225,541
Accounts payable - Navy	36,982	(316,863)
Customer deposits	(6,557)	230,731
Deferred credits	(584,018)	(584,018)
Accrued payroll and employees' benefits	932,553	572,053
Employees' annual leave	(295,353)	(260,754)
Provision for self-insurance	891,364	1,543,630
Net cash provided by operating activities	<u>\$ 57,407,922</u>	<u>\$ 53,732,243</u>

See accompanying notes to financial statements.

# GUAM POWER AUTHORITY

Notes to Financial Statements  
September 30, 2004 and 2003

## (1) Organization and Summary of Significant Accounting Policies

### Organization

The Guam Power Authority (GPA) is a component unit of the Government of Guam (GovGuam). GPA provides electrical services on Guam to residential, commercial and Government of Guam customers, and to the U.S. Navy under a customer supplier agreement. GPA is subject to the regulations of the Public Utility Commission of Guam (PUC) and has adopted the Uniform System of Accounts prescribed by the Federal Energy Regulatory Commission (FERC). Because of the rate-making process, certain differences arise in the application of accounting principles generally accepted in the United States of America between regulated and non-regulated businesses. Such differences mainly concern the time at which various items enter into the determination of net earnings in order to follow the principle of matching costs and revenues.

### Basis of Accounting

GPA utilizes the flow of economic resources measurement focus. Its financial statements are prepared in accordance with accounting principles generally accepted in the United States of America as applied to governmental units using the accrual basis of accounting. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. GASB Statement No. 20, "Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting" requires that proprietary activities apply all applicable GASB pronouncements as well as Statements and Interpretations issued by the Financial Accounting Standards Board (FASB), Accounting Principle Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989. GPA has implemented GASB 20 and elected not to apply FASB Statements and Interpretations issued after November 30, 1989.

### Net Assets

Net assets represent the residual interest in GPA's assets after liabilities are deducted and consist of four sections: invested in capital assets, net of related debt; restricted expendable and nonexpendable, and unrestricted. Net assets invested in capital assets, net of debt include capital assets, restricted and unrestricted, net of accumulated depreciation, reduced by outstanding debt net of debt service reserve. Net assets are reported as restricted when constraints are imposed by third parties or enabling legislation. All of GPA's restricted net assets are expendable. All other net assets are unrestricted.

### Accounting Estimates

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

# GUAM POWER AUTHORITY

Notes to Financial Statements  
September 30, 2004 and 2003

## (1) Organization and Summary of Significant Accounting Policies, Continued

### Utility Plant

Utility Plant is stated at cost which, as to certain plant transferred from the power division of the Public Utility Agency of Guam in 1969, is based on estimated cost as determined by an independent appraiser. Cost includes an allowance on certain projects for funds used during construction of specific power generation plants based on the net cost of borrowed funds used for construction purposes. The cost of utility plant retired or otherwise disposed of, plus removal costs less salvage value, is charged to accumulated depreciation. Contributions in aid of construction are deducted from the cost of the utility plant. Current policy is to capitalize items over \$500.

### Depreciation

Depreciation is computed under the straight-line method over the estimated useful lives of the respective assets (5-50 years for plant assets).

### Inventory Valuation

Materials and supplies inventories and fuel inventories are stated at the lower of cost (using the weighted average and the first-in, first-out method, respectively) or market.

### Cash and Cash Equivalents

Cash and cash equivalents include cash on hand, cash in banks, certificates of deposit, money market accounts and U.S. treasury bills with original maturities of 90 days or less in the interest and principal funds for debt repayment, the bond indenture funds, and the self-insurance fund. Cash and cash equivalents do not include money market accounts in bond reserve funds held by bond trustees.

### Compensated Absences

Compensated absences are accrued and reported as a liability in the period earned. Annual leave expected to be paid out within the next fiscal year is accrued and is included in current liabilities. All annual leave credit is convertible to pay upon termination of employment. During the year ended September 30, 2003, Public Law 27-05 was implemented reducing the maximum accumulation amount of annual leave to 320 hours. Any annual leave earned in excess of 320 hours but not to exceed 100 hours as of February 28, 2003 shall be credited to the employee's sick leave. Pursuant to Public Law 27-106, employees who have accumulated annual leave in excess of three hundred twenty (320) hours as of February 28, 2003 may carry over their excess and shall use the excess amount of leave prior to retirement or termination from service. At the time of retirement or termination of service, that portion permitted to be credited to sick leave shall be so credited and the remainder of the excess leave, if any, shall be lost. Public Law 27-106 does not allow lump sum compensation or retirement credit for annual leave in excess of three hundred twenty (320) hours.

# GUAM POWER AUTHORITY

Notes to Financial Statements  
September 30, 2004 and 2003

## (1) Organization and Summary of Significant Accounting Policies, Continued

### Compensated Absences, Continued

Public Law 26-86 allows members of the Defined Contribution Retirement System to receive a lump sum payment of one-half of their accumulated sick leave upon retirement. GPA has accrued an estimated liability of \$613,212 at September 30, 2004 for potential future sick leave payments as a result of this law. However, this amount is an estimate and actual payout may be materially different than estimated.

### Deferred Asset and Deferred Revenues

The deferred asset and deferred revenues arose as a result of the Bond Reserve Fund Forward Delivery Agreement entered into in September 2000. The deferred asset represents termination fees and closing costs and the deferred revenues represent the gross proceeds that will be deferred and amortized on a straight line basis over the average remaining life of the 1993 and 1999 bonds.

### Sales of Electricity

Sales of electricity are recorded as billed to customers on a monthly cycle billing basis. At the end of each month, unbilled revenues are accrued for each cycle based on the most recent cycle billing. Unbilled receivables at September 30, 2004 and 2003 are \$5,245,318 and \$4,648,519, respectively.

### Derivative Instruments

In June 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 133, *Accounting for Derivative Instruments and Hedging Activities* (SFAS 133), which was subsequently amended in June 2000 by SFAS 138, *Accounting for Certain Derivative Instruments and Certain Hedging Activities*. These statements establish accounting and reporting requirements for derivative instruments and for hedging activities. These standards require that an entity recognize the fair value of all derivative instruments as either assets or liabilities in the balance sheet with the offsetting gains or losses recognized in earnings. These standards permit the deferral of hedge gains and losses, under specific hedge accounting provisions, until the hedged transaction is realized. These statements also provide an exception for certain derivative transactions that meet the criteria of "normal purchases and normal sales". Transactions that can be excepted from these statements are those that provide for the purchase or sale of something other than a financial or derivative instrument that will be delivered in quantities expected to be used or sold by the entity over a reasonable period in the normal course of business.

Transactions entered into during the years ended September 30, 2004 and 2003, qualify for the "normal purchases and normal sales" exception and include commodity transactions for the purchase of fuel. Accordingly, SFAS 133 and 138 do not have a significant impact on the financial position or results of operations of GPA since all transactions will be excluded under the "normal purchases and sales" exception.

# GUAM POWER AUTHORITY

Notes to Financial Statements  
September 30, 2004 and 2003

## (1) Summary of Significant Accounting Policies, Continued

### Fuel Oil Costs

Fuel oil costs increase or decrease billings to customers based on price changes in fuel oil purchased by GPA. Under or over recoveries of fuel oil costs are recorded as deferred fuel cost assets or liabilities, respectively, in the accompanying balance sheets, and are recovered or deducted in future billings to customers based on the Levelized Energy Adjustment Clause (LEAC) approved by the PUC in January of 1996. Historically, GPA charged its customers for fuel as a separate line item, which was adjusted on a monthly basis. The LEAC resulted in the conversion of the monthly fuel charge to a levelized fuel charge, which is reviewed and adjusted by the PUC on a bi-annual basis. GPA is only permitted to recover its actual fuel costs. Cumulative unrecovered fuel costs are \$5,804,772 and \$13,026,862 at September 30, 2004 and 2003, respectively.

### Allowance for Funds Used During Construction

The allowance for funds used during construction (AFUDC) is provided only for construction projects of more than \$50,000, which require a minimum of 90 days to complete. AFUDC is computed using the interest expense on directly assignable borrowings to finance the projects less interest income on the related unused borrowings which have been invested. AFUDC is provided only during the period in which such projects are undergoing activities to prepare them for their intended use.

### Unamortized Debt Issuance Costs

Unamortized debt issuance costs include costs related to the issuance of the Series 1993 and Series 1999 bonds and tax exempt commercial paper notes. These costs are being amortized on the straight line method over the life of the applicable debt, which approximates the effective interest method.

### Canceled Unit

The canceled unit account consists of costs incurred in the refurbishment of the Weber Power Barge. The barge refurbishment project was abandoned during the year ended September 30, 1994. These costs are being amortized on a straight-line basis over the life of the bonds used to finance the refurbishment costs.

### New Accounting Standards

For fiscal year 2005, GPA will be implementing GASB Statement No. 40, *Deposit and Investment Risk Disclosures* (an amendment of GASB Statement No. 3), and GASB Statement No. 42, *Accounting and Reporting for Impairment of Capital Assets and for Insurance Recoveries*. GPA has not evaluated the financial statement impact of these Statements.

### Reclassifications

Certain account balances in the 2003 financial statements have been reclassified to correspond with the 2004 presentation.

# GUAM POWER AUTHORITY

Notes to Financial Statements  
September 30, 2004 and 2003

## (2) Concentrations of Credit Risk

Financial instruments which potentially subject GPA to concentrations of credit risk consist principally of cash demand deposits and accounts receivable.

At September 30, 2004 and 2003, GPA has cash deposits in bank accounts that exceed federal depository insurance limits. GPA has not experienced any losses in such accounts.

Substantially all of GPA's customer accounts receivable are from individuals, companies and government agencies based in Guam. GPA establishes an allowance for doubtful accounts based on management's evaluation of potential uncollectible accounts receivable.

## (3) Cash and Investments

The bond indenture agreements for the 1993 and 1999 series revenue bonds (note 6) require the establishment of special funds to be held and administered by trustees and by GPA. In addition, proceeds from borrowings to finance generation and transmission facility construction are maintained by GPA in construction accounts. Funds in these accounts are required by loan agreement or public law to be used for generation and transmission facility construction.

At September 30, 2004 and 2003, investments and cash held by trustees and by GPA in these funds and accounts are as follows:

	2004			<u>Total</u>
	<u>Held By Trustee</u>	<u>Held By GPA</u>		
	<u>Interest and Principal Funds</u>	<u>Bond Indenture Funds</u>	<u>Bond Indenture Funds</u>	
Construction funds	\$ -	\$ 26,692,296 *	\$ -	\$ 26,692,296
Interest and principal funds	17,605,643	-	-	17,605,643
Working capital funds	-	-	17,373,356	17,373,356
Revenue funds	-	-	943,760	943,760
Self-insurance funds	-	-	891,364	891,364
Operating funds	-	-	889,439	889,439
Surplus funds	-	-	75,512	75,512
	<u>17,605,643</u>	<u>26,692,296</u>	<u>20,173,431</u>	64,471,370
Bond Reserve Funds				<u>27,393,130</u>
				\$ <u>91,864,500</u>

# GUAM POWER AUTHORITY

## Notes to Financial Statements September 30, 2004 and 2003

### (3) Cash and Investments, Continued

	2003			Total
	Held By Trustee		Held By GPA	
	Interest and Principal Funds	Bond Indenture Funds	Bond Indenture Funds	
Construction funds	\$ -	\$ 33,176,699	\$ -	\$ 33,176,699
Interest and principal funds	16,918,602	-	-	16,918,602
Working capital fund	-	-	2,502,452	2,502,452
Revenue fund	-	-	3,670,961	3,670,961
Operating funds	-	-	3,813,106	3,813,106
Surplus funds	-	-	1,072,136	1,072,136
	<u>16,918,602</u>	<u>33,176,699</u>	<u>11,058,655</u>	61,153,956
Bond Reserve Funds				<u>27,484,000</u>
				\$ <u>88,637,956</u>

Investments in debt securities are carried at cost or amortized cost which approximates market value at September 30, 2004 and 2003. Market values shown below implicitly include accrued interest for debt securities.

	<u>2004</u>	<u>2003</u>
Cash on hand, in demand and time deposits and money market accounts	\$ 64,471,370	\$ 61,153,956
Federal National Mortgage Association discount notes	<u>27,393,130</u>	<u>27,484,000</u>
	\$ <u>91,864,500</u>	\$ <u>88,637,956</u>

Credit risk associated with investments is categorized into three levels generally described as follows:

- Category 1 - Insured or registered, or securities held by GPA or its agent in GPA's name.
- Category 2 - Uninsured and unregistered, or securities held by a party other than GPA or its agent, but in GPA's name.
- Category 3 - Uninsured and unregistered, with securities held by a party other than GPA and not in GPA's name.

Demand and time deposits and money market accounts held in GPA's name are non-categorized investments in accordance with Governmental Accounting Standards Board (GASB) Statement No. 3. As of September 30, 2004 and 2003, funds held by trustees amounting to \$17,605,644 and \$16,918,602, respectively, are classified as Category 1 investments in accordance with GASB No. 3. As of September 30, 2004 and 2003, funds held by trustees amounting to \$27,393,130 and \$27,484,000, respectively, are classified as Category 3 investments in accordance with GASB No. 3. The Category 3 investments are held and registered in the name of U.S. Bank as Co-Trustee for GPA. The balance of the investments is classified as Category 2 investments.

Bank balances of demand and time deposits and money market accounts held in the name of GPA totaled \$19,154,159 and \$6,315,558 as of September 30, 2004 and 2003, respectively. Of this amount, \$534,074 and \$406,418 were covered by federal depository and national credit union administration insurance as of September 30, 2004 and 2003, respectively, \$18,467,983 and \$5,742,620 were uninsured and uncollateralized, and \$152,102 and \$166,520 were held on hand for the change fund and petty cash.

# GUAM POWER AUTHORITY

Notes to Financial Statements  
September 30, 2004 and 2003

## (4) Receivables

Accounts receivable at September 30, 2004 and 2003, are summarized as follows:

	<u>2004</u>	<u>2003</u>
Customers:		
Private	\$ 32,008,259	\$ 30,473,505
Government	<u>9,326,241</u>	<u>11,579,579</u>
	41,334,500	42,053,084
Federal Emergency Management Agency claims	3,836,447	17,162,058
Insurance claim	1,465,777	-
Others	4,063,456	4,844,925
Interest	417,568	374,930
U.S. Navy	<u>4,706,429</u>	<u>2,594,887</u>
	55,824,177	67,029,884
Less allowance for doubtful receivables	<u>(14,687,951)</u>	<u>(13,532,714)</u>
	\$ <u>41,136,226</u>	\$ <u>53,497,170</u>

## Long-Term Receivables

Long-term receivables at September 30, 2004 and 2003 consisted of the following:

	<u>2004</u>	<u>2003</u>
Installment payment agreement receivable from the GovGuam Department of Education (DOE), due in 84 monthly installments of \$100,000 beginning May 2002, including interest at 4.47% per annum, renegotiated in July 2004 to additional current receivables of \$2,797,264, payable in three \$500,000 payments in July, August, September 2004, thirteen monthly installments of \$100,000 starting October 2004, with monthly installments increasing by \$25,000 annually each November until payments reach \$200,000 in November 2008, interest at 4.47% per annum, with the final installment due in July 2013.	\$ 14,527,330	\$ 12,753,409
Note receivable from the GovGuam Department of Public Works (DPW), due in 60 monthly installments of \$75,000, beginning May 2002, including interest at 4.35%, per annum, with the final installment payment due in April 2007, uncollateralized.	10,124,204	9,767,178
Note receivable from the Guam Memorial Hospital Authority (GMHA), due in 48 monthly installments of \$45,695, beginning October 13, 2001, including interest at 4.47% per annum, with a final installment payment due in September 2005, uncollateralized.	1,090,081	1,421,129

# GUAM POWER AUTHORITY

Notes to Financial Statements  
September 30, 2004 and 2003

## (4) Receivables, Continued

### Long-Term Receivables, Continued

	<u>2004</u>	<u>2003</u>
Receivable due from Guam Waterworks Authority, payable monthly from an 11.5% water rate surcharge, interest at 4.3%, uncollateralized.	13,490,009	15,193,722
	39,231,624	39,135,438
Less current portion	<u>7,608,860</u>	<u>6,176,693</u>
	\$ <u>31,622,764</u>	\$ <u>32,958,745</u>

Future maturities of long-term receivables are summarized as follows:

<u>Year ending September 30,</u>	<u>Amount</u>
2005	\$ 7,608,860
2006	4,771,794
2007	10,109,232
2008	6,433,279
2009	1,953,398
Thereafter	<u>8,355,061</u>
	\$ <u>39,231,624</u>

The DOE, DPW and GMHA receivables resulted from the conversion of past due receivables from these entities into notes receivable in 2001. In April 2002, the DOE and DPW notes were renegotiated to convert the outstanding note balances plus current receivable balances into new notes receivable.

In April 2003, Public Law 27-19, which authorized the Government of Guam to borrow up to \$218 million including \$30 million to pay the Guam Power Authority for past due notes receivable and power bills was signed into law by the Governor of Guam. Shortly after passage of the law, the Attorney General of Guam expressed concerns on whether the Government had enough room in its debt ceiling to borrow \$218 million and refused to sign the bond indenture agreement approving the form of the contract. In June 2003, the Governor proposed legislation to satisfy the concerns of the Attorney General which was passed into law as Public Law 27-21. The Attorney General continued to contest the legality of the indenture. In July 2003, the Guam Economic Development and Commerce Authority (GEDCA) filed a request for a declaratory judgment with the Supreme Court of Guam. Later that month the Supreme Court issued a ruling in favor of GEDCA and the Governor's position. A few days later, the Attorney General filed an appeal with the United States Ninth Circuit Court of Appeals. Arguments were heard before the Court of Appeals in May 2004. The decision of the Court is pending.

In July 2004, the note receivable from DOE was renegotiated again to convert the old note receivable plus current receivables of \$2,797,264 into a new installment agreement of \$15,855,083.

# GUAM POWER AUTHORITY

## Notes to Financial Statements September 30, 2004 and 2003

### (4) Receivables, Continued

#### Long-Term Receivables, Continued

At September 30, 2004, the installment agreement for DOE is current. The GMHA and DPW notes receivable are significantly delinquent with only minimal payments made on the DPW note since its inception. In addition, there are questions being raised as to whether the DPW note is legal and binding. There is no long-term funding source to repay the DOE, DPW and GMHA receivables. Collectibility of these receivables is dependent on adequate funding being provided by the Government of Guam General Fund and other funding sources or the issuance of the bonds discussed in the preceding paragraph.

### (5) Short-Term Debt

Short-term debt at September 30, 2004 and 2003, is as follows:

	<u>2004</u>	<u>2003</u>
Tax exempt commercial paper note issued in August 1998, interest at 1.2% and 0.9% at September 30, 2004 and 2003, respectively. The note is collateralized by a pledge of revenues subordinate to the bondholders under GPA's bond issues.	\$ 20,000,000	\$ 20,000,000
Ninety-day notes payable drawn on a \$10 million bank line of credit, interest at 1.25% over index at September 30, 2003, payable at maturity, uncollateralized, originally due May 11, 2003 but rolled over until February 10, 2004.	<u>-</u>	<u>5,000,000</u>
	<u>\$ 20,000,000</u>	<u>\$ 25,000,000</u>

Changes in short-term debt for the years ended September 30, 2004 and 2003 are as follows:

	Outstanding September 30, <u>2003</u>	<u>Increases</u>	<u>Decreases</u>	Outstanding September 30, <u>2004</u>
Tax exempt commercial paper	\$ 20,000,000	\$ -	\$ -	\$ 20,000,000
Ninety-day notes payable	<u>5,000,000</u>	<u>-</u>	<u>5,000,000</u>	<u>-</u>
	<u>\$ 25,000,000</u>	<u>\$ -</u>	<u>\$ 5,000,000</u>	<u>\$ 20,000,000</u>
	Outstanding September 30, <u>2002</u>	<u>Increases</u>	<u>Decreases</u>	Outstanding September 30, <u>2003</u>
Tax exempt commercial paper	\$ 20,000,000	\$ -	\$ -	\$ 20,000,000
Thirty-day notes payable	2,912,000	-	2,912,000	-
Ninety-day notes payable	<u>-</u>	<u>5,000,000</u>	<u>-</u>	<u>5,000,000</u>
	<u>\$ 22,912,000</u>	<u>\$ 5,000,000</u>	<u>\$ 2,912,000</u>	<u>\$ 25,000,000</u>

# GUAM POWER AUTHORITY

Notes to Financial Statements  
September 30, 2004 and 2003

## (6) Long-Term Debt

Long-term debt at September 30, 2004 and 2003, is as follows:

	<u>2004</u>	<u>2003</u>
Bonds:		
1999 Series, initial face value of \$349,178,601, interest at varying rates from 3.90% to 5.25% payable semiannually in October and April, principal and mandatory sinking fund payments payable in varying annual installments commencing with a payment of \$2,950,000 in October 2000, increasing to \$26,110,000 in October 2034.	\$ 336,623,601	\$ 339,948,601
1993 Series, initial face value of \$100 million, interest at varying rates from 3.90% to 5.25% payable semiannually in October and April, principal and mandatory sinking fund payments payable in varying annual installments commencing with a payment of \$1,725,000 in October 1996, increasing to \$6,535,000 in October 2023.	<u>83,900,000</u>	<u>86,255,000</u>
	420,523,601	426,203,601
Less current maturities	<u>(5,935,000)</u>	<u>(5,680,000)</u>
	414,588,601	420,523,601
Less discount on bonds	<u>(6,136,925)</u>	<u>(6,444,752)</u>
	408,451,676	414,078,849
Loss on defeasance, net of \$4,251,390 and \$3,371,792 accumulated amortization in 2004 and 2003, respectively	<u>(17,738,560)</u>	<u>(18,618,158)</u>
	\$ <u>390,713,116</u>	\$ <u>395,460,691</u>

As of September 30, 2004, future maturities of long-term debt are as follows:

<u>Year ending September 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total Debt Service</u>
2005	\$ 5,935,000	\$ 21,548,916	\$ 27,483,916
2006	6,200,000	21,281,816	27,481,816
2007	6,480,000	21,004,916	27,484,916
2008	6,770,000	20,711,466	27,481,466
2009	7,080,000	20,400,776	27,480,776
2010 through 2014	41,098,601	96,280,276	137,378,877
2015 through 2019	53,070,000	84,340,488	137,410,488
2020 through 2024	68,130,000	69,278,413	137,408,413
2025 through 2029	87,355,000	50,060,763	137,415,763
2030 through 2035	<u>138,405,000</u>	<u>26,485,888</u>	<u>164,890,888</u>
	\$ <u>420,523,601</u>	\$ <u>431,393,718</u>	\$ <u>851,917,319</u>

Proceeds of the 1993 series bonds, face value of \$100 million, were used to finance acquisitions of additional generating capacity, to construct additional transmission facilities, and to upgrade and refurbish existing equipment.

# GUAM POWER AUTHORITY

Notes to Financial Statements  
September 30, 2004 and 2003

## (6) Long-Term Debt, Continued

Proceeds of the 1999 series bonds, face value of \$349,178,601, were used to finance new projects as specified in the bond indenture and to retire certain outstanding bonds and the commercial paper issued for the purpose of financing certain commercial paper projects.

All gross revenues of GPA have been pledged to repay the 1993 and 1999 series bond principal and interest.

Discounts associated with 1993 and 1999 bond series are being amortized using the effective interest method over the lives of the bonds.

On September 28, 2000, GPA entered into a Bond Reserve Fund Forward Delivery Agreement (the agreement) with the US Bank Trust National Association and Bank of America. In connection with the agreement, GPA received cash totaling \$13.5 million in October 2000 representing the present value amount of interest income on certain bond proceeds invested by GPA.

Based on the terms of the agreement, gross proceeds totaled \$17,521,029 while GPA incurred termination fees and closing costs totaling \$3,530,000 and \$1,250,529, respectively. The \$13.5 million in net proceeds received included \$759,500 of interest income earned as of the closing date of the agreement. The gross proceeds, termination fees and closing costs will be deferred and amortized on a straight line basis over the average remaining life of the 1993 and 1999 bonds. The gross proceeds, net of amortization, is reflected as deferred revenue in the accompanying balance sheets. The termination fees and closing costs amortization are reflected as deferred asset in the accompanying balance sheets. The current year amortization of deferred revenue and deferred asset are reflected as components of interest income and interest expense, respectively, in the accompanying statements of operations and net assets.

The following summarizes deferred revenues and deferred asset at September 30, 2004 and 2003:

	<u>2004</u>	<u>2003</u>
Deferred revenues	\$ 17,521,029	\$ 17,521,029
Accumulated amortization	<u>(2,336,571)</u>	<u>(1,752,553)</u>
	<u>\$ 15,184,458</u>	<u>\$ 15,768,476</u>
Deferred asset	\$ 4,780,529	\$ 4,780,529
Accumulated amortization	<u>(637,404)</u>	<u>(478,053)</u>
	<u>\$ 4,143,125</u>	<u>\$ 4,302,476</u>

Changes in long-term liabilities are presented as follows:

	<u>Outstanding</u> <u>Sept. 30, 2003</u>	<u>Increases</u>	<u>Decreases</u>	<u>Outstanding</u> <u>Sept. 30, 2004</u>	<u>Current</u>	<u>Noncurrent</u>
1993 Series bonds	\$ 86,255,000	\$ -	\$ 2,355,000	\$ 83,900,000	\$ 2,475,000	\$ 81,425,000
1999 Series bonds	339,948,601	-	3,325,000	336,623,601	3,460,000	333,163,601
Unamortized discount on bonds	(6,444,752)	-	(307,827)	(6,136,925)	-	(6,136,925)
Loss on defeasance of bonds	(18,618,158)	-	(879,598)	(17,738,560)	-	(17,738,560)
Obligations under capital leases	157,423,447	-	3,903,260	153,520,187	4,398,150	149,122,037

# GUAM POWER AUTHORITY

## Notes to Financial Statements September 30, 2004 and 2003

### (6) Long-Term Debt, Continued

	Outstanding Sept. 30, 2003	Increases	Decreases	Outstanding Sept. 30, 2004	Current	Noncurrent
Accrued annual leave	2,692,367	-	295,353	2,397,014	1,479,102	917,912
Accrued unfunded liability to retirement fund	3,492,116	1,557,290	-	5,049,406	-	5,049,406
Deferred revenues, net	<u>15,768,476</u>	<u>-</u>	<u>584,017</u>	<u>15,184,459</u>	<u>-</u>	<u>15,184,459</u>
	<u>\$580,517,097</u>	<u>\$ 1,557,290</u>	<u>\$ 9,275,205</u>	<u>\$ 572,799,182</u>	<u>\$11,812,252</u>	<u>\$ 560,986,930</u>
	Outstanding Sept. 30, 2002	Increases	Decreases	Outstanding Sept. 30, 2003	Current	Noncurrent
1993 Series bonds	\$ 88,495,000	\$ -	\$ 2,240,000	\$ 86,255,000	\$ 2,355,000	\$ 83,900,000
1999 Series bonds	343,148,601	-	3,200,000	339,948,601	3,325,000	336,623,601
IBM note payable	871,723	-	871,723	-	-	-
Unamortized discount on bonds	(6,752,579)	-	(307,827)	(6,444,752)	-	(6,444,752)
Loss on defeasance of bonds	(19,497,756)	-	(879,598)	(18,618,158)	-	(18,618,158)
Obligations under capital leases	160,888,537	-	3,465,090	157,423,447	3,903,260	153,520,187
Accrued annual leave	2,953,120	-	260,753	2,692,367	1,231,124	1,461,243
Accrued unfunded liability to retirement fund	1,735,258	1,756,858	-	3,492,116	-	3,492,116
Deferred revenues, net	<u>16,352,493</u>	<u>-</u>	<u>584,017</u>	<u>15,768,476</u>	<u>-</u>	<u>15,768,476</u>
	<u>\$588,194,397</u>	<u>\$ 1,756,858</u>	<u>\$ 9,434,158</u>	<u>\$580,517,097</u>	<u>\$10,814,384</u>	<u>\$569,702,713</u>

### (7) Defeased Debt

On May 1, 1999, GPA issued the 1999 Series bonds of \$349,178,601 to finance 1999 projects, to retire \$45 million in tax exempt commercial paper notes, to retire GPA's 1992 and 1994 series bonds with a total principal outstanding of \$143,660,000 and \$99,820,000, respectively, and to pay the amount currently due on the 1993 bonds totaling \$1,950,000. The proceeds for the refunding of the aforementioned bonds were transferred to an escrow agent who used the proceeds to purchase U.S. Government securities which are to be held by the escrow agent in an irrevocable trust to provide debt service payments until maturity or earlier redemption of the 1992, 1993 and 1994 bonds. The advance refunding met the requirements of an in-substance defeasance and the 1992 and 1994 bonds were removed from GPA's financial statements. The advance refunding resulted in a loss on defeasance totaling \$22,249,124 representing the difference between the reacquisition price and the carrying amount of the 1992 and 1994 bonds. The loss will be deferred and amortized over the remaining life of the 1992 and 1994 bonds and is reflected as a reduction of the bond liability in the accompanying balance sheets.

### (8) Employees' Retirement Plan

Employees of GPA hired before September 30, 1995 are under the Government of Guam Employees' Retirement System (a defined benefit, contributory pension plan). Employees hired after September 30, 1995, are members of the Defined Contribution Retirement System (DCRS). Until December 31, 1999 and for several limited periods after December 31, 1999, those employees who were members of the defined benefit plan with less than 20 years of service at September 30, 1995, had the option to switch to the Defined Contribution Retirement System. Otherwise, they remained under the old plan.

# GUAM POWER AUTHORITY

Notes to Financial Statements  
September 30, 2004 and 2003

## (8) Employees' Retirement Plan, Continued

The Defined Benefit Plan and the DCRS are administered by the Government of Guam Retirement Fund, to which GPA contributes based upon a fixed percentage of the payroll for those employees who are members of the Plan.

As a result of an actuarial valuations performed as of September 30, 2002, 2001 and 2000, contribution rates for the years ended September 30, 2004, 2003 and 2002, respectively, have been determined as follows:

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Normal costs (% of DB Plan payroll)	17.66%	16.42%	15.15%
Unfunded liability costs (% of total payroll)	<u>16.23%</u>	<u>22.94%</u>	<u>18.58%</u>
	33.89%	39.36%	33.73%
Employee contributions (DB Plan employees)	<u>9.50%</u>	<u>9.50%</u>	<u>9.50%</u>
	24.39%	29.86%	24.23%
Agency specific adjustments	<u>- %</u>	<u>1.91%</u>	<u>.91%</u>
Government contribution as a % of DB Plan payroll	<u>24.39%</u>	<u>31.77%</u>	<u>25.14%</u>
Government contribution as a % of total payroll	<u>20.81%</u>	<u>29.25%</u>	<u>N/A</u>

Statutory contribution rates for employer and employee contributions were 20.81% and 9.5%, respectively, for the year ended September 30, 2004. For the year ended September 30, 2003, statutory contribution rates for employer and employee contributions were initially set at 26% and 9.5%, respectively, by the Guam Legislature. The employer contribution rate was reduced to 18% by legislative action effective March 1, 2003.

The plan utilized the actuarial cost method termed "entry age normal" with an assumed rate of return of 7.5% and an assumed salary scale increase of 8.5% per annum for short service employees and 4% per annum for longer service employees. The actuarial valuation performed as of September 30, 2002, did not provide a breakdown of actuarial present value of vested and non-vested accumulated plan benefits by sponsor or net assets available for benefits by sponsor. If the actuarial valuation were performed for GPA as a separate sponsor, the accrued unfunded liability at September 30, 2004 and 2003 may be materially different than that recorded in the accompanying financial statements.

Contributions into the DCRS by members are based on an automatic deduction of 5% of the member's regular base pay. The contribution is periodically deposited into an individual annuity account within the DCRS. Employees are afforded the opportunity to select from different annuity accounts available under the DCRS.

Statutory employer contributions into the DCRS for the years ended September 30, 2004 and 2003 are determined using the same rates as the DB plan. Of the amount contributed by the employer, only 5% of the member's regular base pay is deposited into the member's individual annuity account. The remaining amount is contributed towards the unfunded liability of the defined benefit plan.

## GUAM POWER AUTHORITY

Notes to Financial Statements  
September 30, 2004 and 2003

### (8) Employees' Retirement Plan, Continued

Members of the DCRS who have completed five years of government service, have a vested balance of 100% of both member and employer contributions plus any earnings thereon.

Retirement expense for the years ended September 30, 2004, 2003 and 2002 is as follows:

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Cash contributions and accruals	\$ 3,934,842	\$ 4,824,369	\$ 4,357,628
Increase (decrease) in accrued unfunded liability to the retirement fund	<u>1,557,290</u>	<u>1,756,858</u>	<u>(110,837)</u>
	\$ <u>5,492,132</u>	\$ <u>6,581,227</u>	\$ <u>4,246,791</u>

### (9) Commitments and Contingencies

#### Capital Commitments

The 2005 capital improvement project budget is approximately \$32.3 million. GPA has also entered into agreements to purchase fuel from certain suppliers at prices yet to be determined.

#### Leases

On December 31, 2002, GPA entered into a lease agreement for its office building for an initial term of two years with a monthly rental of \$25,000, with an option to extend for three additional one-year terms.

GPA also leases fuel storage tanks for a monthly fee of \$100,000 beginning September 1998, increasing to \$107,500 in March 2003. The initial term of the lease is for a period of 10 years with an option to renew for an additional 5-year period, expiring on September 2013, at an increased monthly lease fee of \$115,650.

At September 30, 2004, future minimum lease payments for operating leases are as follows:

<u>Year ending September 30,</u>	<u>Amount</u>
2005	\$ 1,777,307
2006	1,323,188
2007	1,323,188
2008	1,323,188
2009	<u>2,766</u>
	\$ <u>5,749,637</u>

Rent expense under the aforementioned agreements totaled \$1,813,880 and \$2,163,133 during the years ended September 30, 2004 and 2003, respectively, which is included as a component of administrative and general expense in the accompanying statements of operations and retained earnings.

#### Letters of Credit

As of September 30, 2004, GPA has a \$20 million bank line of credit for purchases of parts and supplies, which is 100% collateralized by a standby letter of credit.

## GUAM POWER AUTHORITY

Notes to Financial Statements  
September 30, 2004 and 2003

### (9) Commitments and Contingencies, Continued

#### Letters of Credit, Continued

As of September 30, 2004, GPA has a \$10 million uncollateralized revolving documentary letter of credit for purchases of fuel.

As of September 30, 2004, GPA has outstanding letters of credit of approximately \$303,389, collateralized by deposits in a savings account maintained by GPA.

#### Environmental Protection Agency

On May 24, 1986, the administrator of the Environmental Protection Agency (EPA) granted a continuing exemption to GPA under the provisions of Section 325(b) of the Clean Air Act, as amended. The terms of the exemption require monitoring by EPA, certain commitments by GPA regarding fuel stocks and reporting and delineation of grounds for revocation of the exemption.

#### Environmental Remediation

On August 4, 2001, the Tanguisson Pipeline in the Mongmong/Toto area ruptured spilling black oil which contaminated an approximately 60,000 square foot area. The pipeline is operated by GPA and owned by the United States Navy. In 2004, GPA incurred clean-up costs totaling \$3,414,842, including accrued costs of \$1,289,515. Final clean-up costs may be materially different than estimated. GPA has filed a claim with its insurance company for the costs of clean up less deductibles; however, reimbursement by the insurance company is considered unlikely.

#### Litigation

GPA has several asserted and unasserted claims outstanding as of September 30, 2004. It is not possible for the management of GPA to estimate the ultimate resolution of these matters and therefore, no provision for any liability that may result from these claims has been made in the financial statements.

#### Self-Insurance

GPA self-insures its transmission and distribution (T&D) plant, because no insurance is available at reasonable rates.

As the result of a PUC Decision and Order, GPA added an insurance charge of \$.00145 per kilowatt hour to customer billings effective January 1, 1993 until a self-insurance fund balance of \$2.5 million is established. As required by the Decision and Order, GPA records the insurance charge as sales revenue and records self-insurance expense in the same amount. Insurance charge proceeds are accumulated in the restricted self-insurance fund to be used to cover uninsured or self-insured damages to the T&D plant in the event of a natural catastrophe. The self-insurance fund included in cash and cash equivalents held by GPA, is \$891,364 and \$0 at September 30, 2004 and 2003, respectively.

#### FEMA Receivables

As of September 30, 2004 and 2003, GPA has a total of \$3,836,447 and \$26,040,885, respectively, in outstanding FEMA claims for typhoon damages. GPA recorded \$3,836,447 and \$17,162,058, respectively, of the outstanding claims as accounts receivable at September 30, 2004 and 2003. In 2004, FEMA paid GPA \$8,502,556 in settlement of a claim receivable of \$10,209,382 from fiscal year 1998. The difference of \$1,706,826 was charged against typhoon loss in 2003.

## GUAM POWER AUTHORITY

Notes to Financial Statements  
September 30, 2004 and 2003

### (9) Commitments and Contingencies, Continued

#### Plant Explosion

In February 2002, an explosion severely damaged one of GPA's generation plants. In 2004, GPA incurred repair costs totaling \$1,882,662, of which \$1,465,777 will be reimbursed by insurance.

#### Hazardous Waste Assessment

Guam Public Law 20-110 requires certain entities to remit payments to a hazardous substance expense fund. There are questions as to the enforceability of the law and; accordingly, no provision has been made in the accompanying financial statements for payments to be made under this law.

### (10) Agreements with the United States Navy

On September 15, 1996, a lease agreement was entered into between GPA and the U.S. Navy (Navy) to transfer to GPA the operations, maintenance and custody of certain Navy-owned electrical transmission and distribution lines, electric power generation facilities, related structures and equipment, together with the associated land interest. The facilities are leased to GPA at no cost for a period of 50 years.

During the years ended September 30, 2004 and 2003, GPA billed the Navy approximately \$34,126,000 and \$31,564,000, respectively, for sales of electricity under a customer supplier agreement.

### (11) Energy Conversion Agreements

In September 1996, GPA entered into agreements to purchase electricity produced by generating plants constructed or refurbished and operated by three companies. The agreements have twenty year terms. At the end of the agreements, ownership of the plants and the plant improvements reverts to GPA. Under each of the agreements, GPA pays capacity and operation and maintenance costs.

GPA has determined that the agreements to purchase electricity were in fact capital leases to acquire the plants and that the capacity payments made under the agreements were lease payments. The operations and maintenance payments under the agreements are reflected as energy conversion costs under operation and maintenance expenses.

The leases have effective interest rates ranging from 8.6% to 14.2%. Future capacity payments under these agreements are as follows:

<u>Year ending September 30,</u>	<u>Amount</u>
2005	\$ 23,084,304
2006	23,084,304
2007	23,084,304
2008	23,084,304
2009	23,084,304
2010-2014	115,421,520
2015-2019	<u>94,221,073</u>
	325,064,113

# GUAM POWER AUTHORITY

Notes to Financial Statements  
September 30, 2004 and 2003

## (11) Energy Conversion Agreements, Continued

Less amounts representing interest	<u>171,543,717</u>
	153,520,396
Less current portion	<u>4,398,150</u>
	\$ <u>149,122,246</u>

## (12) Accrued Supplemental/COLA Annuities

As required by Public Law 26-35, as amended by Public Law 26-49, GPA must pay to the Government of Guam Retirement Fund certain supplemental benefits for retirees. The supplemental benefits derive from an annual appropriation by the Guam Legislature and do not relate to covered Plan benefits.

## (13) Typhoon Damages

The island of Guam was struck by a major typhoon in July 2002 and a super typhoon in December 2002. GPA recorded estimated losses from these typhoons during the years ended September 30, 2004 and 2003 as follows:

	<u>2004</u>	<u>2003</u>
Typhoon damages	\$ 65,795	\$ 25,402,146
Charged against self-insurance fund	-	(1,543,630)
FEMA recoveries	<u>-</u>	<u>(14,550,448)</u>
Net typhoon damages	65,795	9,308,068
Settlement of typhoon Paka claim (note 9)	<u>-</u>	<u>1,706,826</u>
Loss due to typhoon	\$ <u>65,795</u>	\$ <u>11,014,894</u>

Recorded typhoon damages and related FEMA recoveries are estimated amounts. Final damages and recoveries may be materially different than estimated.

**GUAM POWER AUTHORITY**

Notes to Financial Statements  
September 30, 2004 and 2003

**(14) Utility Plant**

A summary of changes in capital assets for the years ended September 30, 2004 and 2003 is as follows:

	Beginning Balance October 1, 2003	Transfers and Additions	Transfers and Deletions	Balance Sept. 30, 2004
<b>2004</b>				
<u>Depreciable:</u>				
Intangible plant	\$ 4,353,988	\$ -	\$ -	\$ 4,353,988
Steam production plant	64,272,206	1,526,592	-	65,798,798
Other production plant	245,787,700	1,213,339	(5,521)	246,995,518
Transmission plant	106,775,848	5,638,105	(243,970)	112,169,983
Distribution plant	141,652,309	1,839,794	(288,043)	143,204,060
General plant	33,447,330	2,479,235	(1,258,582)	34,667,983
Production plant under capital lease	171,382,727	-	-	171,382,727
	767,672,108	12,697,065	(1,796,116)	778,573,057
Accumulated depreciation	(222,137,558)	(24,603,493)	132,073	(246,608,978)
	545,534,550	(11,906,428)	(1,664,043)	531,964,079
<u>Non-depreciable:</u>				
Construction work in progress	22,551,695	26,049,982	(23,328,405)	25,273,272
	<u>\$ 568,086,245</u>	<u>\$ 14,143,554</u>	<u>\$ (24,992,448)</u>	<u>\$ 557,237,351</u>
	Beginning Balance October 1, 2002	Transfers and Additions	Transfers and Deletions	Balance Sept. 30, 2003
<b>2003</b>				
<u>Depreciable:</u>				
Intangible plant	\$ 4,353,988	\$ -	\$ -	\$ 4,353,988
Steam production plant	62,776,348	1,495,858	-	64,272,206
Other production plant	245,123,180	664,520	-	245,787,700
Transmission plant	91,105,754	15,703,684	(33,590)	106,775,848
Distribution plant	132,434,035	11,642,409	(2,424,135)	141,652,309
General plant	35,531,540	436,018	(2,520,228)	33,447,330
Production plant under capital lease	171,382,727	-	-	171,382,727
	742,707,572	29,942,489	(4,977,953)	767,672,108
Accumulated depreciation	(201,818,332)	(24,135,225)	3,815,999	(222,137,558)
	540,889,240	5,807,264	(1,161,954)	545,534,550
<u>Non-depreciable:</u>				
Construction work in progress	44,446,114	35,714,490	(57,608,909)	22,551,695
	<u>\$ 585,335,354</u>	<u>\$ 41,521,754</u>	<u>\$ (58,770,863)</u>	<u>\$ 568,086,245</u>

# GUAM POWER AUTHORITY

## Schedule 1 Schedule of Sales of Electricity Years Ended September 30, 2004 and 2003

	<u>2004</u>	<u>2003</u>
Commercial	\$ 92,847,632	\$ 75,190,620
Residential	64,544,683	54,046,499
Government of Guam	33,781,275	29,735,445
U.S. Navy	<u>34,126,151</u>	<u>31,563,718</u>
	<u>\$ 225,299,741</u>	<u>\$ 190,536,282</u>

See accompanying independent auditors' report.

# GUAM POWER AUTHORITY

## Schedule 2 Schedule of Operating and Maintenance Expenses Years Ended September 30, 2004 and 2003

	2004	2003
Administrative and General:		
Salaries and wages:		
Regular pay	\$ 2,768,099	\$ 2,839,592
Overtime	30,630	27,445
Premium pay	1,375	887
Benefits	8,403,476	8,067,717
Total salaries and wages	<u>11,203,580</u>	<u>10,935,641</u>
Insurance	8,065,994	8,103,743
Contract	1,979,701	2,743,421
Communications	1,313,351	946,621
Completed work orders	-	2,344,691
Overhead allocations	27,715	19,126
Operating supplies	129,317	76,991
Travel	134,838	105,178
Other administrative expenses	17,821	15,138
Training	423,645	23,299
Office supplies	23,545	13,244
General and administrative capitalized	(426,156)	(1,751,035)
Miscellaneous	996,515	773,827
Total general and administrative	<u>\$ 23,889,866</u>	<u>\$ 24,349,885</u>
Customer Accounting:		
Salaries and wages:		
Regular pay	\$ 1,606,113	\$ 1,575,678
Overtime	65,575	61,523
Premium pay	4,055	1,282
Total salaries and wages	<u>1,675,743</u>	<u>1,638,483</u>
Bad debt	1,200,000	1,200,000
Communications	191,673	190,656
Overhead allocations	125,558	160,696
Completed work orders	125,943	270,412
Operating supplies	33,106	29,350
Contract	1,501	1,900
Office supplies	13,201	15,217
Others	2,202	1,303
Miscellaneous	-	124
Total customer accounting	<u>\$ 3,368,927</u>	<u>\$ 3,508,141</u>

See accompanying independent auditors' report.

**GUAM POWER AUTHORITY**

Schedule 2

Schedule of Operating and Maintenance Expenses, Continued  
Years Ended September 30, 2004 and 2003

	<u>2004</u>	<u>2003</u>
Fuel:		
Salaries and wages:		
Regular pay	\$ 20,346	\$ 21,265
Overtime	3,683	8,352
Premium pay	<u>70</u>	<u>175</u>
Total salaries and wages	<u>24,099</u>	<u>29,792</u>
Fuel	88,020,751	79,110,683
Deferred fuel costs	<u>7,222,089</u>	<u>(6,431,368)</u>
Total fuel costs	<u><u>\$ 95,266,939</u></u>	<u><u>\$ 72,709,107</u></u>
Other Production:		
Salaries and wages:		
Regular pay	\$ 6,340,455	\$ 6,086,349
Overtime	2,056,347	2,372,709
Premium pay	<u>141,715</u>	<u>73,639</u>
Total salaries and wages	<u>8,538,517</u>	<u>8,532,697</u>
Contract	4,147,169	3,004,768
Communications	5,416	397,887
Office supplies	14,738	2,694
Operating supplies	2,774,141	3,479,234
Overhead allocations	103,142	65,745
Completed work orders	4,394,772	852,741
Others	<u>8,732</u>	<u>-</u>
Total other production	<u><u>\$ 19,986,627</u></u>	<u><u>\$ 16,335,766</u></u>
Transmission and Distribution:		
Salaries and wages:		
Regular pay	\$ 4,160,614	\$ 3,174,556
Overtime	1,066,147	606,604
Premium pay	<u>45,461</u>	<u>18,099</u>
Total salaries and wages	<u>5,272,222</u>	<u>3,799,259</u>
Contract	86,033	286,907
Office supplies	21,602	2,108
Operating supplies	486,657	346,055
Overhead allocations	2,122,939	1,431,633
Completed work orders	<u>1,430,237</u>	<u>(19,961)</u>
Total transmission and distribution	<u><u>\$ 9,419,690</u></u>	<u><u>\$ 5,846,001</u></u>

See accompanying independent auditors' report.