



**GAS ENTERPRISE FUND OF THE CITY OF LONG BEACH**

Financial Statements

September 30, 2007 and 2006

(With Independent Auditors' Report Thereon)

# GAS ENTERPRISE FUND OF THE CITY OF LONG BEACH

## Table of Contents

	<b>Page</b>
Independent Auditors' Report	1
Financial Statements:	
Statements of Net Assets	3
Statements of Revenues, Expenses, and Changes in Fund Net Assets	4
Statements of Cash Flows	5
Notes to Financial Statements	6



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## **Independent Auditors' Report**

The Honorable Mayor and City Council  
The Citizens of the City of Long Beach, California:

We have audited the accompanying financial statements of the Gas Enterprise Fund of the City of Long Beach, California (Gas Enterprise Fund), an enterprise fund of the City of Long Beach, California (the City), as of and for the years ended September 30, 2007 and 2006, as listed in the table of contents. These financial statements are the responsibility of the City. 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 Gas Enterprise Fund'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.

As discussed more fully in note 1, the accompanying financial statements of the Gas Enterprise Fund are intended to present the financial position and the changes in financial position and cash flows attributable to the Gas Enterprise Fund. They do not purport to, and do not, present fairly the financial position of the City of Long Beach, California, as of September 30, 2007 and 2006, and the changes in its financial position and, where applicable, its cash flows thereof for the years then ended in conformity with U.S. generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Gas Enterprise Fund of the City of Long Beach, California, as of September 30, 2007 and 2006, and the changes in its financial position and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued our report dated May 8, 2008 on our consideration of the Gas Enterprise Fund's internal control over financial reporting and on 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 or on 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 considered in assessing the results of our audits.

The management of the Gas Enterprise Fund of the City of Long Beach has not presented management's discussion and analysis that U.S. generally accepted accounting principles require to supplement, although not to be part of, the basic financial statements.

KPMG LLP

May 8, 2008

**GAS ENTERPRISE FUND OF THE CITY OF LONG BEACH**

Statements of Net Assets

September 30, 2007 and 2006

(In thousands)

<b>Assets</b>	<b>2007</b>	<b>2006</b>
	<hr/>	<hr/>
Current assets:		
Pooled cash and cash equivalents (note 2)	\$ 6,029	10,812
Customer accounts receivable, net of allowance for doubtful accounts of \$490 and \$448 at September 30, 2007 and 2006, respectively	2,822	3,235
Due from the City of Long Beach	733	698
Inventory	1,128	1,024
	<hr/>	<hr/>
Total current assets	10,712	15,769
Noncurrent assets:		
Restricted assets (note 2):		
Pooled cash and cash equivalents (note 2)	4,632	4,093
Nonpooled investments	650	650
Advance to Tidelands Enterprise Fund (note 3)	4,213	4,946
Capital assets (note 4):		
Nondepreciable	6,399	5,399
Depreciable, net	66,890	59,875
	<hr/>	<hr/>
Total capital assets, net	73,289	65,274
Total noncurrent assets	<hr/>	<hr/>
	82,784	74,963
Total assets	<hr/>	<hr/>
	93,496	90,732
	<hr/>	<hr/>
<b>Liabilities</b>		
Current liabilities:		
Accounts payable	5,241	9,911
Accrued wages payable	408	365
Due to the City of Long Beach	201	180
Deferred revenues	540	567
Amounts payable from restricted assets:		
Accrued interest payable	25	29
Current portion of long-term debt (note 5)	925	905
Customer deposits	1,852	1,822
	<hr/>	<hr/>
Total current liabilities	9,192	13,779
Long-term debt, net of current portion (note 5)	19,925	13,350
Less unamortized discount/deferred cost	(91)	(107)
	<hr/>	<hr/>
Net long-term debt	19,834	13,243
Total liabilities	<hr/>	<hr/>
	29,026	27,022
	<hr/>	<hr/>
<b>Net Assets</b>		
Invested in capital assets, net of related debt	53,649	51,125
Restricted for capital projects	1,468	2,107
Restricted for debt service	819	785
Unrestricted	8,534	9,693
	<hr/>	<hr/>
Total net assets	\$ 64,470	63,710
	<hr/>	<hr/>

See accompanying notes to financial statements.

## GAS ENTERPRISE FUND OF THE CITY OF LONG BEACH

### Statements of Revenues, Expenses, and Changes in Fund Net Assets

Years ended September 30, 2007 and 2006

(In thousands)

	<u>2007</u>	<u>2006</u>
Operating revenues:		
Sale of gas (note 7)	\$ 92,316	100,305
Other service charges	7,332	7,176
Total operating revenues	<u>99,648</u>	<u>107,481</u>
Operating expenses:		
Purchase of gas (note 7)	61,273	69,643
Personal services	12,895	11,610
Customer service and general	10,575	10,091
Provision for doubtful accounts	409	366
Depreciation expense (note 4)	3,098	3,242
Total operating expenses	<u>88,250</u>	<u>94,952</u>
Operating income	<u>11,398</u>	<u>12,529</u>
Nonoperating income (expense):		
Interest income	1,057	674
Interest expense	(626)	(401)
Loss on disposition of property	(441)	(443)
Other income, net	774	497
Total nonoperating income, net	<u>764</u>	<u>327</u>
Net income before transfers	12,162	12,856
Transfers to other City departments (note 6)	<u>(11,402)</u>	<u>(17,001)</u>
Change in net assets	760	(4,145)
Total net assets, beginning of year	<u>63,710</u>	<u>67,855</u>
Total net assets, end of year	<u>\$ 64,470</u>	<u>63,710</u>

See accompanying notes to financial statements.

## GAS ENTERPRISE FUND OF THE CITY OF LONG BEACH

### Statements of Cash Flows

Years ended September 30, 2007 and 2006

(In thousands)

	<b>2007</b>	<b>2006</b>
Cash flows from operating activities:		
Cash received from customers	\$ 99,656	107,558
Cash paid to employees	(12,650)	(11,385)
Cash paid to suppliers	(76,802)	(78,556)
Net cash provided by operating activities	10,204	17,617
Cash flows used in noncapital financing activities:		
Transfer to other City departments	(11,402)	(17,001)
Other income	774	497
Net cash used in noncapital financing activities	(10,628)	(16,504)
Cash flows from capital and related financing activities:		
Proceeds from other funds under due from City of Long Beach	698	663
Payments for capital acquisitions	(11,555)	(10,396)
Principal repayments of long term debt	(905)	(885)
Interest paid	(615)	(393)
Proceeds from issuance of long-term obligation	7,500	7,755
Net cash used in capital and related financing activities	(4,877)	(3,256)
Cash flows from investing activities:		
Payments for investments	—	114
Interest income	1,057	674
Net cash provided by investing activities	1,057	788
Net decrease in cash and cash equivalents	(4,244)	(1,355)
Cash and cash equivalents, beginning of year	14,905	16,260
Cash and cash equivalents, end of year	\$ 10,661	14,905
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	\$ 11,398	12,529
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation expense	3,098	3,242
Decrease in customer accounts receivable, net	414	383
Increase in inventory	(104)	(12)
Increase (decrease) in accounts payable	(4,670)	1,336
Decrease in accrued wages payable	43	47
Increase in due to City of Long Beach	21	32
Increase (decrease) in deferred revenues	(26)	182
Increase (decrease) in customer deposits	30	(122)
Total adjustments	(1,194)	5,088
Net cash provided by operating activities	\$ 10,204	17,617

See accompanying notes to financial statements.

## **GAS ENTERPRISE FUND OF THE CITY OF LONG BEACH**

Notes to Financial Statements

September 30, 2007 and 2006

### **(1) Description of Gas Utility Operation and Summary of Significant Accounting Policies**

The following is a summary of the significant accounting policies of the Gas Enterprise Fund of the City of Long Beach (Gas Enterprise Fund).

#### **(a) General**

The Long Beach Gas Department (the Department) was established in 1924 under a provision of the City Charter of the City of Long Beach, California (City). The Department's purpose is to regulate and control the use, sale, and distribution of natural gas by the City. These activities are accounted for in the City's Gas Enterprise Fund. To accomplish its stated purpose, the Gas Enterprise Fund purchases natural gas on the open market and then distributes it to approximately more than 145,000 commercial and residential customers. Natural gas rates are established by the Long Beach City Council and are based on prevailing natural gas rates.

Natural gas is purchased by the City under long-term natural gas contracts from both local and out-of-state sources and is transported through Southern California Gas Company's pipelines on behalf of the City. Natural gas is then delivered to customers' homes and businesses via the City's 1,800 miles of gas pipeline infrastructure.

In October 1998, the Long Beach City Council approved the direct pass-through of natural gas commodity costs to customers allowing the City to fully recover this actual cost. The methodology is used by other gas utilities in California.

Effective October 1, 2005, the Department, the Southeast Resource Recovery Facility (SERRF), and the Long Beach Department of Oil Properties consolidated as one city department and became collectively known as Long Beach Gas and Oil.

#### **(b) Reporting Entity**

The Gas Enterprise Fund is part of the overall financial reporting entity of the City. As a proprietary fund of the City, the Gas Enterprise Fund's financial operations are included in the City's Comprehensive Annual Financial Report (CAFR). The City's CAFR may be obtained by contacting the City's Department of Financial Management at 333 W. Ocean Blvd., Long Beach, California 90802.

The Gas Enterprise Fund's revenues are collected through the City's customer billing system and its expenditures are paid through the City's disbursement system and are, therefore, subject to the City's internal control procedures.

#### **(c) Implementation of New Accounting Pronouncements**

The following summarizes recent Governmental Accounting Standards Board (GASB) pronouncements and their impact, if any, on the financial statements:

In June 2004, GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, which addresses how state and local governments should account for and report their costs and obligations related to postemployment healthcare and other nonpension benefits. Collectively, these benefits are commonly referred to as



## **GAS ENTERPRISE FUND OF THE CITY OF LONG BEACH**

### Notes to Financial Statements

September 30, 2007 and 2006

other post-employment benefits, or OPEB. The statement generally requires that employers account for and report the annual cost of OPEB and the outstanding obligations and commitments related to OPEB in essentially the same manner as they currently do for pensions. Annual OPEB costs for most employers will be based on actuarially determined amounts that, if paid on an ongoing basis, generally would provide sufficient resources to pay benefits as they come due. This statement's provisions may be applied prospectively and do not require governments to fund their OPEB plans. An employer may establish its OPEB liability at zero as of the beginning of the initial year of implementation; however, the unfunded actuarial liability is required to be amortized over future periods. This statement also establishes disclosure requirements for information about the plans in which an employer participates, the funding policy followed, the actuarial valuation process and assumptions, and, for certain employers, the extent to which the plan has been funded over time. The City will implement GASB Statement No. 45 in fiscal year ended September 30, 2009.

In September 2007, GASB issued Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*. This statement establishes criteria that governments will use to determine whether certain transactions should be regarded as a sale and reported as revenue or regarded as collateralized borrowing and recorded as a liability. Examples of such transactions include the sale of delinquent taxes, certain mortgages, student loans, or future revenue such as those from tobacco settlement agreements. The statement also includes provisions that stipulate that governments should not revalue assets that are transferred between financial reporting entity components. The requirements of this statement are effective for the financial statements for periods beginning after December 15, 2007. The City plans on implementing GASB Statement No. 48 for the fiscal year ending September 30, 2008.

In November 2006, GASB issued Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*. This statement addresses accounting and reporting standards for pollution remediation obligation, including contamination. The statement focuses on current and potential detrimental effects of existing pollution through participation in pollution remediation activities, such as site assessment and clean-up, but excludes pollution prevention and control obligation with respect to current operation and future remediation activities that may be required with asset retirements such as landfill closures or "nuclear power plant" decommissioning. The requirements of this statement are effective for financial statements periods beginning after December 15, 2007 and include measurement of pollution remediation liabilities at the beginning of the fiscal period as to restate beginning net asset. Governments with sufficient objective and verifiable information to apply the expected cash flow technique to measurements in prior periods are required to apply the provisions retroactively for all periods presented. The City plans on implementing GASB No. 49 for the fiscal year ended September 30, 2009.

**(d) Measurement Focus and Basis of Accounting**

The accompanying financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

The Gas Enterprise Fund generally follows private sector standards of accounting and financial reporting issued on or before November 30, 1989 to the extent that such standards do not conflict

## **GAS ENTERPRISE FUND OF THE CITY OF LONG BEACH**

Notes to Financial Statements

September 30, 2007 and 2006

with or contradict guidance of the GASB. The City and, by consequence, the Gas Enterprise Fund also have the option of following subsequent private sector guidance for their business-type activities and enterprise funds, subject to the same limitation. The City and the Gas Enterprise Fund have elected not to follow subsequent private sector guidance.

Operating revenues consist of charges to customers for services provided; the costs of providing such services are considered to be operating expenses and all other revenues and expenses are considered to be nonoperative in nature. In keeping with City policy, unbilled service receivables are not recognized, as their effect on a year-to-year basis is not material. Revenues collected in advance such as customer deposits are recorded as deferred revenue, a liability account, for financial statement purposes. Revenue is recognized in the fiscal year in which the earnings process is complete.

**(e) *Pooled Cash, Cash Equivalents, and Other Investments***

In order to maximize investment return, the Gas Enterprise Fund pools its available general cash with that of the City. The City's cash management pool is used essentially as a demand deposit account by the participating units; therefore, the Gas Enterprise Fund has defined cash and cash equivalents as pooled cash and investments, including restricted pooled cash and investments. Investment decisions are made by the City Treasurer and approved by a general investment committee whose membership includes a member of the management group of the Gas Enterprise Fund.

Interest income and realized gains and losses arising from such pooled cash and investments are apportioned to each participating unit based on the relationship of an individual unit's respective daily cash balances to aggregated pooled cash and investments. The Gas Enterprise Fund's share of pooled cash and investments, as of September 30, 2007 and 2006, is stated at fair value. The value of each investment is based on independent third-party pricing provided to the City (note 2).

**(f) *Inventories***

Inventories of supplies are stated at the lower of average cost or market determined on a first-in, first-out basis.

**(g) *Restricted Assets***

Amounts designated for bond indenture requirements and refunding customer deposits are recorded as restricted assets. Related liabilities of the Gas Enterprise Fund are identified as amounts payable from restricted assets when such obligations are incurred. Proceeds from commercial paper issuance, which are reserved for capital projects, are likewise recorded as restricted assets.

**(h) *Capital Assets***

The cost of additions to property, plant, and equipment and replacement of retired property is capitalized. The cost of constructed assets includes labor, materials, interest, and allocated indirect expenses such as engineering, supervision, and construction and transportation equipment. The cost of minor replacements is regarded as a period cost and is expensed as incurred. Upon retirement or sale, the costs of the affected plant assets as well as the related accumulated depreciation are

## GAS ENTERPRISE FUND OF THE CITY OF LONG BEACH

Notes to Financial Statements

September 30, 2007 and 2006

removed from the Gas Enterprise Fund's accounting records. Resulting gains or losses are recognized as a component of the change in net assets in the year of removal (note 4).

Depreciation of capital assets is provided using the straight-line method over the estimated service lives of the assets, as follows:

Building, structures, and improvements	10 to 50 years
Transmission and distribution equipment	35 to 50 years
Other machinery and equipment	5 to 30 years

Contributed assets are recorded at fair market value when received.

**(i) *Compensated Absences***

Vacation and sick leave benefits are paid through a citywide Employee Benefits Internal Service Fund administered by the City. The cost of these benefits is recognized by the Gas Enterprise Fund through regular payroll burden charges from the Employee Benefits Internal Service Fund based on estimates of benefits earned for vacation pay and sick leave.

**(j) *Pension Plan***

All full time Gas Enterprise Fund employees are members of the State of California Public Employees' Retirement System (CalPERS), a statewide plan available to most municipalities in the state. CalPERS acts as a common investment and administrative agent for cities in California. The Gas Enterprise Fund is billed by the City for its share of pension costs based upon rates established by CalPERS for the City's general employees. No separate pension benefit obligation is calculated for the Gas Enterprise Fund; accordingly, no obligation is presented herein.

Contribution requirements of plan members and the City are established and maybe amended by CalPERS. Effective October 1, 2006, the City contribution payments to CalPERS' Miscellaneous Plans are at 12.012% plus the employee rate of 9.000% and 8.000%. Miscellaneous employees paid 2.000% to CalPERS, that when added to the 6.000% paid by the City makes up the 8.000% employee rate, which was effective March 4, 2006. Management employees pay 1.000% of the 8.000% to CalPERS and the City pays 7.000%. Effective in fiscal year 2007, all miscellaneous employees in tier one and tier two pay 2.000% of the 8.000%. Miscellaneous employees in tier three pay 2.000% of the 7.000% employee rate.

The Gas Enterprise Fund's contributions to CalPERS were \$1,696,131, \$1,477,458, and \$1,151,573 for fiscal years 2007, 2006 and 2005, respectively, which was equal to the annual required contributions. Further information regarding the City's participation in CalPERS may be found in the City's CAFR.

**(k) *Use of Estimates***

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amount

**GAS ENTERPRISE FUND OF THE CITY OF LONG BEACH**

Notes to Financial Statements

September 30, 2007 and 2006

of assets and liabilities as of the date of the financial statements. Actual results could differ from those estimates.

**(l) Reclassifications**

Certain amounts reported in fiscal year 2006 have been reclassified to conform to the fiscal year 2007 presentation. Such reclassifications had no effect on the previously reported change in net assets.

**(m) Net Assets**

The Gas Enterprise Fund has adopted a policy of generally utilizing restricted funds, prior to unrestricted funds, when an expense is incurred for purposes for which both are available.

The Gas Enterprise Fund's net assets are classified into the following net asset categories:

Invested in Capital Assets, Net of Related Debt – Capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction, or improvement of those assets.

Restricted – Amounts designated for bond indenture requirements and refunding customer deposits. Related liabilities of the Gas Enterprise Fund are identified as amounts payable from restricted assets when such obligations are incurred. Proceeds from commercial paper issuance, which are reserved for capital projects, are likewise recorded as restricted assets.

Unrestricted – All other categories of net assets.

**(2) Pooled Cash and Cash Equivalents**

As of September 30, 2007 and 2006, the Gas Enterprise Fund's pooled cash and cash equivalents amounted to \$10,661,000 and \$14,905,000, respectively, which represented 0.632% and 1.036%, respectively, of the City's cash management pool of \$1,686,441,000 and \$1,438,522,000, respectively. Cash and investments as of September 30, 2007 are classified in the accompanying statements of net assets as follows (in thousands):

	<u>2007</u>	<u>2006</u>
Pooled cash and cash equivalents	\$ 10,661	14,905
Nonpooled cash and investments	650	650
Total cash and investments	<u>\$ 11,311</u>	<u>15,555</u>

**GAS ENTERPRISE FUND OF THE CITY OF LONG BEACH**

Notes to Financial Statements

September 30, 2007 and 2006

**(a) Investments Authorized by the California Government Code and the City's Investment Policy**

The table below identifies the investment types that are authorized for the City by the City's investment policy. The table also identifies certain provisions of the City's investment policy that address interest rate risk, credit risk, and concentration of credit risk. This table does not address debt proceeds held by bond trustees that are governed by the provisions of debt agreements of the City, rather than the general provision of the California Government Code or the City's investment policy.

<u>Authorized investment type</u>	<u>Maximum maturity</u>	<u>Maximum percentage of portfolio</u>	<u>Maximum investment in one issuer</u>
Bonds issued by the City	5 years*	30%	None
U.S. Treasury notes, bonds, or bills	5 years*	None	None
Registered state warrants or treasury notes or bonds of the State of California	5 years*	30%	None
Local agency bonds	5 years*	30%	None
Federal agency securities	5 years*	40%	None
Banker's acceptances	180 days	40%	30%
Commercial paper	270 days	25%	10%
Negotiable certificates of deposit	5 years*	30%	10%
Time certificates of deposit	5 years*	100%	10%
Repurchase agreements	90 days	100%	None
Reverse repurchase agreements	92 days	20%	None
Securities Lending Program	92 days	20%	None
Medium-term notes	5 years*	30%	10%
Money market funds	N/A	20%	10%
Local Agency Investment Fund (LAIF)	N/A	None	\$40 million per account
Asset-backed Securities	5 years	20%	None
Mortgage-backed Securities	5 years	20%	None

\* Maximum maturity of five years unless a longer maturity is approved by the Long Beach City Council, either specifically or as part of an investment program, at least three months prior to purchase.

**(b) Investments Authorized by Debt Agreements**

Investment of debt proceeds held by bond trustee is governed by provisions of the debt agreements.

**GAS ENTERPRISE FUND OF THE CITY OF LONG BEACH**

Notes to Financial Statements

September 30, 2007 and 2006

**(c) Disclosures Relating to Interest Rate Risk**

Interest rate risk is the risk that changes in market interest rates will 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 changes in market interest rates. One of the ways that the City manages its exposure to interest rate risk is 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 closer to maturity evenly over time as necessary to provide cash flow and liquidity needed for operations.

The following schedule indicates the interest rate risk of the City's investments, which includes the amount the Gas Enterprise Fund has invested with the City as of September 30, 2007 (in thousands):

<b>Investment type</b>	<b>2007</b>		<b>2006</b>	
	<b>Amount (in thousands)</b>	<b>Weighted average maturity (in years)</b>	<b>Amount (in thousands)</b>	<b>Weighted average maturity (in years)</b>
Interdepartment Loan (Health Savrs)	\$ 3,098	11.600	\$ 3,297	12.600
U.S. Treasury notes	145,149	0.900	214,467	1.542
Federal agency securities	1,190,784	2.280	1,042,876	1.572
Medium-term notes	49,881	1.830	33,464	1.609
Short-term commercial paper	135,874	0.020	132,731	0.013
Local Agency Investment Fund LAIF	139,156	0.010	2,920	0.003
Subtotal city pool	1,663,942		1,429,755	
Cash on hand	32,878		26,811	
Outstanding checks	(10,379)		(18,044)	
Total city pool	<u>\$ 1,686,441</u>		<u>\$ 1,438,522</u>	

The Gas Enterprise Fund's nonpooled investments consist of guaranteed investment contracts held by the bond trustee and amounted to \$650,000 at September 30, 2007 and 2006. These guaranteed investment contracts do not have stated maturity dates.

**(d) Investments with Fair Values Highly Sensitive to Investment Risk**

The City had no investments that were highly sensitive to market interest rate changes as of September 30, 2007 and 2006. Highly sensitive investments are investments whose sensitivity to market interest rate fluctuations are not fully addressed by use of one of the five methods for reporting interest rate risk.

**GAS ENTERPRISE FUND OF THE CITY OF LONG BEACH**

Notes to Financial Statements

September 30, 2007 and 2006

*(e) Disclosures Relating to Credit Risk*

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. Presented below is the minimum rating required by the California Government Code, the City's investment policy, and the actual rating as of year-end for each investment type (in thousands):

Rating as of fiscal year ended September 30, 2007								
<b>City pooled investment</b>	<b>Amount (in thousands)</b>	<b>Minimum legal rating</b>	<b>Not required to be rated</b>	<b>A-1+</b>	<b>A-1</b>	<b>AAA</b>	<b>AA-</b>	<b>Unrated</b>
Interdepartment loan (Health Savrs)	\$ 3,098	N/A	\$ 3,098	—	—	—	—	—
U.S. Treasury notes	145,149	N/A	145,149	—	—	—	—	—
Federal agency securities	1,190,784	N/A	—	—	—	1,190,784	—	—
Medium-term notes	49,881	N/A	—	—	—	44,861	5,020	—
Short-term commercial paper	135,874	A	—	54,350	81,524	—	—	—
LAIF	139,156	N/A	139,156	—	—	—	—	—
Subtotal city pool	1,663,942		287,403	54,350	81,524	1,235,645	5,020	—
Cash on hand	32,878		—	—	—	—	—	32,878
Outstanding checks	(10,379)		—	—	—	—	—	(10,379)
	<u>\$ 1,686,441</u>		<u>\$ 287,403</u>	<u>54,350</u>	<u>81,524</u>	<u>1,235,645</u>	<u>5,020</u>	<u>22,499</u>

  

Rating as of fiscal year ended September 30, 2007								
<b>Nonpooled investment</b>	<b>Amount (in thousands)</b>	<b>Minimum legal rating</b>	<b>Not required to be rated</b>	<b>A-1+</b>	<b>A-1</b>	<b>AAA</b>	<b>AA-</b>	<b>Unrated</b>
Guaranteed investment contracts	\$ 650	N/A	\$ 650	—	—	—	—	—
Total held by bond trustees	<u>\$ 650</u>		<u>\$ 650</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>

**GAS ENTERPRISE FUND OF THE CITY OF LONG BEACH**

Notes to Financial Statements

September 30, 2007 and 2006

Rating as of fiscal year ended 2006								
<u>City-pooled investment</u>	<u>Amount (in thousands)</u>	<u>Minimum legal rating</u>	<u>Not required to be rated</u>	<u>A-1+</u>	<u>A-1</u>	<u>AAA</u>	<u>AA-</u>	<u>Unrated</u>
Interdepartment loan (Health Savrs)	\$ 3,297	N/A	\$ 3,297	—	—	—	—	—
U.S. Treasury notes	214,467	N/A	214,467	—	—	—	—	—
Federal agency securities	1,042,876	N/A	—	—	—	1,042,876	—	—
Medium-term notes	33,464	N/A	—	—	—	28,445	5,019	—
Short-term commercial paper	132,731	A	—	75,773	56,958	—	—	—
LAIF	2,920	N/A	2,920	—	—	—	—	—
Subtotal city pool	1,429,755		220,684	75,773	56,958	1,071,321	5,019	—
Cash on hand	26,811		—	—	—	—	—	26,811
Outstanding checks	(18,044)		—	—	—	—	—	(18,044)
	<u>\$ 1,438,522</u>		<u>\$ 220,684</u>	<u>75,773</u>	<u>56,958</u>	<u>1,071,321</u>	<u>5,019</u>	<u>8,767</u>

  

Rating as of fiscal year ended 2006								
<u>Nonpooled investment</u>	<u>Amount (in thousands)</u>	<u>Minimum legal rating</u>	<u>Not required to be rated</u>	<u>A-1+</u>	<u>A-1</u>	<u>AAA</u>	<u>AA-</u>	<u>Unrated</u>
Guaranteed investment contracts	\$ 650	N/A	\$ 650	—	—	—	—	—
Total held by bond trustees	<u>\$ 650</u>		<u>\$ 650</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>

**(f) Concentration of Credit Risk**

The investment policy of the City contains no limitations on the amount that can be invested in any one issuer beyond that stipulated by the California Government Code. Investments in any one issuer that represents 5% or more of the City's total pooled investments are as follows (in thousands):

<u>Issuer</u>	<u>City pooled investment type</u>	<u>Amount</u>	
		<u>2007</u>	<u>2006</u>
Federal Farm Credit Bank	Federal agency securities	\$ 89,334	181,052
Federal Home Loan Bank	Federal agency securities	354,763	241,246
Federal Home Loan Mortgage Association	Federal agency securities	307,865	266,937
Federal National Mortgage Association	Federal agency securities	438,822	353,641
U.S. Treasuries	U.S. Treasury notes and bonds	145,149	214,467
Commercial paper	Unsecured corporate debt	135,874	132,731
LAIF	State pool investment	139,156	—

**(g) Custodial Credit Risk**

Custodial credit risk for deposits is the risk that, in the event of 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



## **GAS ENTERPRISE FUND OF THE CITY OF LONG BEACH**

Notes to Financial Statements

September 30, 2007 and 2006

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 City'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 the City's deposits by pledging first trust deed mortgage notes having a value of 150% of the secured public deposits.

All securities owned by the City are deposited in trust for safekeeping with a custodial bank different from the City's primary bank except for one City-issued bond and investment in the state's LAIF.

As of September 30, 2007, the City reported cash deposits of \$32,878,000, less \$10,379,000 for checks outstanding. As of September 30, 2006, the City reported cash deposits of \$26,811,000, less \$18,044,000 for checks outstanding.

**(h) *Investment in State Investment Pool***

The City is a voluntary participant in the LAIF that is regulated by California Government Code Section 16429 under the oversight of the Treasurer of the State of California. The fair value of the City's investment in this pool is reported in the accompanying financial statements at amounts based upon the City's prorata share of the fair value provided by LAIF for the entire LAIF portfolio (in relation to the amortized cost of that portfolio). The balance available for withdrawal is based on the accounting records maintained by LAIF, which are recorded on an amortized cost basis. Included in LAIF's investment portfolio are mortgage-backed securities, loans to certain state funds, and securities with interest rates that vary according to changes in rates greater than a one-for-one basis and structured basis.

**(i) *GASB Statement No. 31***

GASB Statement No. 31, *Certain investments and External Investment-pools* requires that certain investments and external investment pools be reported at fair value. At September 30, 2007 and 2006, the effect of valuating the City's investments at fair value did not have material impact on its financial position.

**(j) *Securities Lending***

The City did not engage in any securities lending programs for the fiscal years ended September 30, 2007 and 2006. However, from time to time, the City engages in limited securities lending activities. These activities are governed by formal agreements with the City's contract bank. These agreements limit the nature and amount of the transactions, and provide for full collateralization of each transaction.

**GAS ENTERPRISE FUND OF THE CITY OF LONG BEACH**

Notes to Financial Statements

September 30, 2007 and 2006

**(3) Advances to Other General City Funds**

The Gas Enterprise Fund has a long-term receivable from the City's Tidelands Enterprise Fund. Under the terms of the agreement, the Gas Enterprise Fund is to receive annual payments in an amount necessary to cover the actual debt service requirements of the Gas Utility Revenue Bonds (note 5).

**(4) Capital Assets**

Activities in capital assets for the years ended September 30, 2007 and 2006 are as follows (in thousands):

	2007				Balance, September 30, 2007
	Balance, October 1, 2006	Additions	Retirements	Transfers	
Capital assets, not being depreciated:					
Land	\$ 203	—	—	—	203
Construction in progress	5,196	11,554	—	(10,554)	6,196
Total capital assets not being depreciated	5,399	11,554	—	(10,554)	6,399
Capital assets being depreciated:					
Buildings and improvements	5,642	—	—	—	5,642
Distribution systems	119,971	—	(1,873)	10,554	128,652
Storage structures	318	—	—	—	318
Machinery and equipment	1,940	—	(157)	—	1,783
Total capital assets being depreciated	127,871	—	(2,030)	10,554	136,395
Less accumulated depreciation:					
Buildings and improvements	(3,328)	(128)	—	—	(3,456)
Distribution systems	(62,978)	(2,761)	1,496	—	(64,243)
Storage structures	(230)	(6)	—	—	(236)
Machinery and equipment	(1,460)	(203)	93	—	(1,570)
Total accumulated depreciation	(67,996)	(3,098)	1,589	—	(69,505)
Total capital assets being depreciated, net	59,875	(3,098)	(441)	10,554	66,890
Total	\$ 65,274	8,456	(441)	—	73,289

**GAS ENTERPRISE FUND OF THE CITY OF LONG BEACH**

Notes to Financial Statements

September 30, 2007 and 2006

	<b>2006</b>				<b>Balance, September 30, 2006</b>
	<b>Balance, October 1, 2005</b>	<b>Additions</b>	<b>Retirements</b>	<b>Transfers</b>	
Capital assets, not being depreciated:					
Land	\$ 203	—	—	—	203
Construction in progress	3,680	5,196	5,160	(8,840)	5,196
Total capital assets not being depreciated	<u>3,883</u>	<u>5,196</u>	<u>5,160</u>	<u>(8,840)</u>	<u>5,399</u>
Capital assets being depreciated:					
Buildings and improvements	5,676	—	(34)	—	5,642
Distribution systems	113,876	—	(2,745)	8,840	119,971
Storage structures	318	—	—	—	318
Machinery and equipment	2,019	39	(118)	—	1,940
Total capital assets being depreciated	<u>121,889</u>	<u>39</u>	<u>(2,897)</u>	<u>8,840</u>	<u>127,871</u>
Less accumulated depreciation:					
Buildings and improvements	(3,202)	(132)	6	—	(3,328)
Distribution systems	(62,322)	(3,007)	2,351	—	(62,978)
Storage structures	(223)	(7)	—	—	(230)
Machinery and equipment	(1,464)	(96)	100	—	(1,460)
Total accumulated depreciation	<u>(67,211)</u>	<u>(3,242)</u>	<u>2,457</u>	<u>—</u>	<u>(67,996)</u>
Total capital assets being depreciated, net	<u>54,678</u>	<u>(3,203)</u>	<u>(440)</u>	<u>8,840</u>	<u>59,875</u>
Total	\$ <u>58,561</u>	<u>1,993</u>	<u>4,720</u>	<u>—</u>	<u>65,274</u>

**(5) Long-Term Debt**

Long-term debt activities for the 2007 and 2006 fiscal years is are follows (in thousands):

	<b>2007</b>			<b>Balance, September 30, 2007</b>
	<b>Balance, October 1, 2006</b>	<b>Increase</b>	<b>Decrease</b>	
Long-term debt:				
2005 Commercial paper	\$ 7,755	7,500	—	15,255
2005 Gas Utility Revenue Bonds	6,500	—	(905)	5,595
Current portion of long-term debt, due within one year	(905)	(925)	905	(925)
Unamortized discount	(31)	—	5	(26)
Unamortized issuance cost	(76)	—	11	(65)
Net long-term debt	\$ <u>13,243</u>	<u>6,575</u>	<u>16</u>	<u>19,834</u>

**GAS ENTERPRISE FUND OF THE CITY OF LONG BEACH**

Notes to Financial Statements

September 30, 2007 and 2006

	<b>2006</b>			<b>Balance, September 30, 2006</b>
	<b>Balance, October 1, 2005</b>	<b>Increase</b>	<b>Decrease</b>	
Long-term debt:				
2005 Commercial paper	\$ —	7,755	—	7,755
2005 Gas Utility Revenue Bonds	7,385	—	(885)	6,500
Current portion of long-term debt, due within one year	(885)	(905)	885	(905)
Unamortized discount	(35)	—	4	(31)
Unamortized issuance cost	(83)	—	7	(76)
Net long-term debt	<u>\$ 6,382</u>	<u>6,850</u>	<u>11</u>	<u>13,243</u>

As of September 30, 2007 and 2006, \$15,255,000 and \$7,755,000, respectively in commercial paper notes has been issued and has had interest rates ranging from 3.01% to 3.76% since their issuance. The Commercial Paper Notes, Series A and B (taxable) were authorized in an aggregate principal amount not to exceed \$35,000,000. The program termination date is July 1, 2020 unless earlier terminated or extended in accordance with program terms. The Commercial Paper Notes shall not have maturities exceeding 270 days and shall not bear interest rate in excess of the lesser of (a) 12% per annum and (b) the maximum rate of interest permitted by law. The Gas Enterprise Fund intends to refinance the Commercial Paper Notes on a long-term basis by renewal of the Commercial Paper Notes and future issuance of revenue bonds.

The 2005 Gas Utility Revenue Bonds, (2005 Bonds), are payable through August 1, 2013 with a total debt service in the amount of \$6,121,681 as of September 30, 2007. The 2005 Bonds have interest rates ranging from 2.000% to 3.125%.

Annual debt service requirements to maturity for these bonds are as follows:

	<b>Annual debt service requirements</b>		
	<b>Principal</b>	<b>Interest</b>	<b>Total</b>
Fiscal year ending September 30:			
2008	\$ 925,000	149,192	1,074,192
2009	940,000	127,546	1,067,546
2010	970,000	103,719	1,073,719
2011	990,000	77,756	1,067,756
2012	1,020,000	48,937	1,068,937
2013	750,000	19,531	769,531
Total	<u>\$ 5,595,000</u>	<u>526,681</u>	<u>6,121,681</u>

The bond agreement contains certain restrictive covenants. The Gas Enterprise Fund's management believes that the Gas Enterprise Fund has complied with these covenants during the years ended September 30, 2007 and 2006.

**GAS ENTERPRISE FUND OF THE CITY OF LONG BEACH**

Notes to Financial Statements

September 30, 2007 and 2006

**(6) Transfers to Other City Departments**

Transfers consist of the following as of September 30, 2007 and 2006 (in thousands):

	2007	2006
Transfers to:		
General Fund	\$ 11,402	17,001
Total transfers	\$ 11,402	17,001

**(7) Gas Rates**

The Gas Enterprise Fund passes along the actual cost of natural gas it provides to its customers.

The contract for full gas supply requirements was renewed with Coral Energy effective April 1, 2006 through March 31, 2009, which provides gas for a price that is competitive with surrounding utilities. This contract has a price ceiling cap of \$10.50 per decatherm, which offers protection against swings in market prices during the winter months of November through February. There is a price floor cap of \$5.50 per decatherm during all months of the year. Additionally, the price paid to local gas supplies is equal to the Southern California Gas Company's core procurement price.

**(8) Commitments and Contingencies**

The Gas Enterprise Fund is subject to claims and lawsuits arising from the normal course of business. Representatives of the City Attorney's Office routinely evaluate such claims. The management of the Gas Enterprise Fund may make provision for probable losses if deemed appropriate or upon advice of legal counsel. To the extent that such provision for damages is considered necessary, appropriate amounts are reflected in the accompanying financial statements. Based upon information obtained from the City Attorney with respect to the remaining cases, it is the opinion of management that any liability for unreserved claims and suits will not have a material impact on the financial statements of the Gas Enterprise Fund.

**(9) Subsequent Event**

The Long Beach Bond Finance Authority (the Authority) entered into a Prepaid Natural Gas Purchase and Sale Agreement with Merrill Lynch Commodity Inc. (MLCI) to acquire a supply of natural gas for delivery over a period of approximately 30 years in order to secure a fixed quantity of natural gas. The Department and the Authority entered into the supply agreement to meet a portion of the requirements of the Department's commercial and residential customers. Under this new contract, MLCI became the primary provider of natural gas for the Department effective November 1, 2007.

The Department will pay the Authority the contract price for all gas delivered or deemed delivered under the supply agreement. The contract price will be equal to the applicable index price for the month in which the gas delivery occurs, less \$0.83 per one million British Thermal Units (MMBtus) of gas delivered. The Department anticipates a prepaid gas cost savings to facilitate funding of its gas utility's infrastructure requirements over the next 30 years.

**GAS ENTERPRISE FUND OF THE CITY OF LONG BEACH**

Notes to Financial Statements

September 30, 2007 and 2006

The contract for full gas supply requirements with Coral Energy, which was renewed in April 1, 2006 and was to be in effect until March 31, 2009, was terminated and replaced with a new contract. Under the new contract, Coral Energy will continue to provide storage, scheduling, forecasting, and balancing services to the City, as well as commodity price hedging.