

JAMES CITY SERVICE AUTHORITY
(A Component Unit of the County of James City, Virginia)
Management's Discussion and Analysis
June 30, 2004 and 2003

This section of the James City Service Authority's (the Authority or JCSA) annual financial report presents our discussion and analysis of the Authority's financial performance during fiscal year ended June 30, 2004.

Financial Highlights for Fiscal Year 2004

- * The Authority's total net assets were \$131.4 million, which represents a 6.0% increase from 2003.
- * The Authority's total operating expenses before depreciation and amortization increased by 8.2% from 2003, and total operating revenues increased by 9.7%.
- * In September 2003, the Authority experienced effects from Hurricane Isabel. Costs related to this storm totaled \$209,444. Revenue was received from insurance and FEMA to offset these costs.

Overview of the Financial Statements

The financial section of this report has two components – Management's Discussion and Analysis (this section) and the basic financial statements. The basic financial statements are comprised of Balance Sheets, Statements of Revenues, Expenses and Changes in Net Assets, Statements of Cash Flows and Notes to Basic Financial Statements. The Authority implemented the provisions of Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, as of July 1, 2001, which established new requirements and a new reporting model for the annual financial reports of state and local governments.

The Authority is accounted for under the economic resources measurement focus and the accrual basis of accounting similar to an enterprise fund. Accordingly, revenues are recognized in the period earned and expenses are recognized when they are incurred. Enterprise funds are used to account for activities that are financed and operated similar to those often found in the private sector.

Financial Analysis

The difference between assets and liabilities, net assets, is one way to measure financial health or financial position. Over time, increases and decreases in net assets are one indicator of whether its financial health is improving or deteriorating. However, you will need to also consider other non-financial factors, such as changes in economic conditions, population and service area growth, and new or changed legislation.

The Authority's net assets increased from last year by \$7.4 million. This increase is primarily related to the contribution of water and sewer systems to the Authority.

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Condensed Balance Sheet Information at June 30

	2004	2003	2002	2004 vs. 2003	
				\$ Change	% Change
Capital assets	\$ 119,563,991	104,224,338	93,778,956	15,339,653	14.7%
Current and other assets	29,268,942	38,513,373	24,644,916	(9,244,431)	-24.0%
Total assets	\$ 148,832,933	142,737,711	118,423,872	6,095,222	4.3%
Current liabilities	\$ 3,381,193	3,865,005	1,838,761	(483,812)	-12.5%
Long-term liabilities	14,092,467	14,958,591	135,302	(866,124)	-5.8%
Total liabilities	17,473,660	18,823,596	1,974,063	(1,349,936)	-7.2%
Net assets:					
Invested in capital assets, net of related debt	104,781,826	88,966,049	93,778,956	15,815,777	17.8%
Restricted for capital projects	3,155,428	15,048,381	—	(11,892,953)	-79.0%
Unrestricted	23,422,019	19,899,685	22,670,853	3,522,334	17.7%
Total net assets	131,359,273	123,914,115	116,449,809	7,445,158	6.0%
	\$ 148,832,933	142,737,711	118,423,872	6,095,222	4.3%

The change in net assets can also be determined by reviewing the following condensed statements of revenues, expenses and changes in net assets information.

Condensed Statements of Revenues, Expenses and Changes in Net Assets Information

	2004	2003	2002	2004 vs. 2003	
				\$ Change	% Change
Water and sewer services	\$ 8,027,991	7,596,532	7,726,102	431,459	5.7%
Miscellaneous	442,554	460,601	404,324	(18,047)	-3.9%
Reimbursement for storm costs	371,538	—	—	371,538	100.0%
Water and sewer facility fees	4,914,512	4,030,744	3,567,289	883,768	21.9%
Nonoperating revenues	186,082	302,872	692,832	(116,790)	-38.6%
Total revenues	13,942,677	12,390,749	12,390,547	1,551,928	12.5%
Salaries	687,155	607,509	439,208	79,646	13.1%
Fringe benefits	229,833	137,091	131,892	92,742	67.6%
Operating supplies	271,026	265,937	311,839	5,089	1.9%
Maintenance of buildings and equipment	690,678	714,515	1,361,873	(23,837)	-3.3%
Special services	4,212,422	3,860,843	4,378,091	351,579	9.1%
Utilities	431,373	430,235	443,079	1,138	0.3%
Water purchases	341,726	441,101	229,495	(99,375)	-22.5%
Storm costs	209,444	—	—	209,444	100.0%
Other	54,965	130,420	98,973	(75,455)	-57.9%
Depreciation and amortization	4,119,963	3,856,524	3,566,260	263,439	6.8%
Nonoperating expenses	482,695	178,843	88,058	303,852	169.9%
Total expenses	11,731,280	10,623,018	11,048,768	1,108,262	10.4%
Excess of revenues over expenses	2,211,397	1,767,731	1,341,779	443,666	25.1%
Capital contributions	5,233,761	5,696,575	5,485,529	(462,814)	-8.1%
Change in net assets	7,445,158	7,464,306	6,827,308	(19,148)	-0.3%
Net assets at beginning of year	123,914,115	116,449,809	109,622,501	7,464,306	6.4%
Net assets at end of year	\$ 131,359,273	123,914,115	116,449,809	7,445,158	6.0%

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Investment income was down this year from last due to the interest rates continuing to remain at a low rate of return. Expenses increased from last year by 10.4%, which is due to costs associated with Hurricane Isabel and interest payments on the revenue bond. Revenues increased 12.5% from last year, which was mainly a result of a rate increase in water and sewer service as well as customer growth.

Capital Assets

At the end of fiscal year 2004, the Authority had invested \$119,563,991 in a broad range of capital assets, including land and land improvements, water and sewer systems, office fixtures and equipment, and automotive equipment. This amount represents a 14.7% net increase from last year. This increase was primarily the result of the contribution of water and sewer systems to the Authority during fiscal year 2004. Construction in progress also increased by 30.7% over last year. This increase is mostly a result of costs incurred for the final phase of the Supervisory Control and Data Acquisition System, construction of a groundwater treatment facility located at 4321 John Tyler Highway, replacement of waterlines in First Colony, and the replacement of lift station 1-2 located at 3900 John Tyler Highway.

The following table summarizes the Authority's capital assets at June 30, 2004 and 2003:

	<u>2004</u>	<u>2003</u>
Utility plant:		
Land and land rights	\$ 910,138	887,638
Water and sewer systems	148,684,658	132,987,980
Total utility plant	<u>149,594,796</u>	<u>133,875,618</u>
Non-utility plant:		
Land	1,580,428	1,580,428
Central shop	1,955,674	1,955,674
Office fixtures and equipment	761,881	738,056
Land improvements	13,183	13,183
Automotive equipment	1,733,139	1,674,653
Total non-utility plant	<u>6,044,305</u>	<u>5,961,994</u>
Construction in progress	15,357,443	11,749,571
Less accumulated depreciation	<u>51,432,553</u>	<u>47,362,845</u>
Net capital assets	<u>\$ 119,563,991</u>	<u>104,224,338</u>

Debt Administration

At the close of the current fiscal year, the Authority's total outstanding debt was \$14,215,000. During fiscal year 2003, the Authority issued revenue bonds in the amount of \$14,650,000 to finance a groundwater treatment facility, wells and water transmission lines and to provide for the costs of issuing the bonds and funding any necessary reserves. The revenue bonds ratings are Aaa from Moody's and AAA from Standard & Poor's rating services based on the municipal bond insurance policy by the Insurer. The Series 2003 bonds have been assigned an underlying rating of AA by Standard & Poor's and of A1 by Moody's without giving effect to the issuance of the municipal bond insurance policy by the Insurer. These ratings allowed the Authority to borrow at lower interest rates.

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Economic Factors and Next Year Budgets and Rates

During the current fiscal year, the unrestricted net assets increased to \$23.4 million. The Authority did not appropriate any of this for spending during fiscal year 2005. However, the Authority did increase some water and sewer service retail rates for fiscal year 2005 to cover spending.

Overall, the portion of the budget for water operations is projected to increase by 21.5% in fiscal 2005 from the 2004 budget level. Water service charge revenues are projected to increase with customer growth. In addition, increases in the inverted block rate structure were adopted to cover the increase in spending. The second block of 15,000 to 30,000 gallons increased from \$2.60 to \$2.70 per 1,000 gallons. The third block of 30,000 or more gallons increased from \$7.45 to \$7.60 per 1,000 gallons. Nonresidential also increased from \$2.60 to \$2.70 per 1,000 gallons. There was no rate change in the first residential block.

The water operation expenses reflect an increase for the new Groundwater Treatment Plant operating expenses, as this becomes fully operational during fiscal year 2005. Personnel expenses include two new full-time permanent positions.

Overall, the fiscal year 2005 sewer operation budget will increase 10.8% from 2004. The revenue increase is due to a proposed sewer rate increase to \$2.70 from \$2.50 per 1,000 gallons to adequately fund the sewer operation and restore the Capital Improvements Program contribution.

The sewer operation reflects an increase to direct sewer expenses primarily for infrastructure maintenance and utilities. A total of \$342,091 will be transferred from sewer operations to the Capital Improvements Program for repair, renewal, and replacement costs.

Contacting the Authority's Financial Management

This financial report is designed to provide our customers and creditors with a general overview of the Authority's finances and to demonstrate the Authority's accountability for the money it receives. Questions concerning this report or requests for additional information should be directed to the James City County Department of Financial and Management Services, 101-F Mounts Bay Road, P.O. Box 8784, Williamsburg, Virginia 23187-8784.