CITY OF VERNON, CALIFORNIA

Annual Financial Report

Fiscal Year Ended June 30, 2008

CITY OF VERNON
For the Fiscal Year Ended June 30, 2008

Table of Contents

Page(s)

FINANCIAL SECTION:

Independent Auditor's Report 1

Management's Discussion and Analysis (Required Supplementary Information-Unaudited) 3

Basic Financial Statements:

Government-wide Financial Statements:
Statement of Net Assets 18
Statement of Activities 19

Fund Financial Statements:
Governmental Funds:
Balance Sheet 20
Reconciliation of the Governmental Funds Balance Sheet to the Statement of Net Assets-Governmental Activities 21
Statement of Revenues, Expenditures, and Changes in Fund Balances 22
Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balances to the Statement of Activities-Governmental Activities 23

Proprietary Funds:
Statement of Fund Net Assets (Deficit) 24
Statement of Revenues, Expenses, and Changes in Fund Net Assets (Deficit) 25
Statement of Cash Flows 26

Notes to the Basic Financial Statements 27-67

Required Supplementary Information (Other than Management's Discussion and Analysis-Unaudited):

General Fund Budgetary Comparison Schedule 68
Notes to General Fund Budgetary Comparison Schedule 69
Schedule of Funding Progress 70

MACIAS GINI & O'CONNELL LLP
CERTIFIED PUBLIC ACCOUNTANTS & MANAGEMENT CONSULTANTS

3000 S Street, Suite 300
Sacramento, CA 95816
916.928.4600

2175 N. California Boulevard, Suite 645
Walnut Creek, CA 94596
925.274.0190

515 S. Figueroa Street, Suite 325
Los Angeles, CA 90071
213.286.6400

402 West Broadway, Suite 400
San Diego, CA 92101
619.573.1112

INDEPENDENT AUDITOR'S REPORT

City Council
City of Vernon, California

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Vernon, California (City) as of and for the fiscal year ended June 30, 2008, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. 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 City'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 the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City as of June 30, 2008, and the respective changes in financial position and, where applicable, cash flows thereof for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1 to the basic financial statements, the City adopted the provisions of Governmental Standards Accounting Board (GASB) Statement No. 50, *Pension Disclosures – An Amendment of GASB Statements No. 25 and No. 27*, and GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, for the fiscal year ended June 30, 2008. The adoption of GASB Statement No. 53 required the City to restate beginning net assets at July 1, 2007, as discussed in Note 16 to the basic financial statements.

The management's discussion and analysis, budgetary comparison information, and the schedule of funding progress on pages 3 through 17, pages 68 and 69, and page 70, respectively, are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Macias Gini & O'Connell LLP

Certified Public Accountants

Los Angeles, California
December 1, 2008

CITY OF VERNON, CALIFORNIA
Management's Discussion and Analysis
For the Fiscal Year Ended June 30, 2008
(Unaudited)

As management of the City of Vernon ("the City"), we offer readers of the financial statements this narrative overview and analysis of the financial activities of the City for the fiscal year ended June 30, 2008.

OVERVIEW OF FINANCIAL STATEMENTS

This discussion and analysis are intended to serve as an introduction to the City's basic financial statements. The City's basic financial statements comprise three components: (i) government-wide financial statements, (ii) fund financial statements, and (iii) notes to the basic financial statements.

Government-wide financial statements.

The *government-wide financial statements* are designed to provide readers with a broad overview of the City's finances, in a manner similar to a private-sector business.

The *statement of net assets* presents information on all of the City's assets and liabilities, with the difference between the two reported as *net assets*. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the City is improving or deteriorating.

The *statement of activities* presents information showing how the City's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, *regardless of the timing of related cash flows*. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave).

Both of the government-wide financial statements distinguish functions of the City that are principally supported by taxes (*governmental activities*) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (*business-type activities*). The governmental activities of the City include general government, public safety, public works, and health services. The business-type activities of the City include the Light and Power Department, Gas Department, Water Department and Fiber Optic Department.

The government-wide financial statements can be found on pages 18-19 of this report.

Fund financial statements*.*

A *fund* is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The City, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the City can be divided into two categories: governmental funds and proprietary funds.

Governmental funds.

Governmental funds are used to account for essentially the same functions reported as *governmental activities* in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on *near-term inflows and outflows of spendable resources*, as well as on *balances of spendable resources* available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for *governmental funds* with similar information presented for *governmental activities* in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental funds balance sheet and the governmental funds statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between *governmental funds* and *governmental activities*.

The City adopts an annual appropriated budget for its General Fund. A budgetary comparison schedule has been provided for the general fund to demonstrate compliance with this budget (See page 68).

The basic governmental funds financial statements can be found on pages 20-23 of this report.

Proprietary funds*.*

The City maintains two different types of proprietary funds. *Enterprise funds* are used to report the same functions presented as *business-type activities* in the government-wide financial statements. The City uses enterprise funds to account for its Light and Power Department, Gas Department, Water Department and Fiber Optic Department. *Internal service funds* are an accounting device used to accumulate and allocate costs internally among the City's various functions. The City uses internal service funds to account for its fleet of vehicles, insurance, and retirement. Because these services predominantly benefit governmental rather than business-type functions, they have been included within *governmental activities* in the government-wide financial statements.

Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail. The proprietary fund financial statements provide separate information for the Light and Power Fund and the Gas Fund, which are considered to be major funds of the City. Conversely, the internal service funds are combined into a single, aggregated presentation in the proprietary fund financial statements.

The basic proprietary funds financial statements can be found on pages 24-26 of this report.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

City's Net Assets

The table below summarizes the City's net assets for the current fiscal year ended June 30, 2008 and prior fiscal year ended June 30, 2007. The details of the current year's summary can be found on page 18 of this report.

City of Vernon
Net Assets
June 30, 2008 and 2007

	Governmental Activities		Business-type Activities		Totals	
	2008	2007	2008	2007	2008	2007
Assets:						
Current and other assets	$ 116,693,602	$ 88,198,432	$ 594,379,617	$ 535,129,809	$ 711,073,219	$ 623,328,241
Restricted assets	8,537,162	16,672,971	52,790,753	36,790,554	61,327,915	53,463,525
Capital assets	82,175,165	77,264,367	145,563,905	341,161,303	227,739,070	418,425,670
Total assets	207,405,929	182,135,770	792,734,275	913,081,666	1,000,140,204	1,095,217,436
Liabilities						
Current liabilities	43,531,160	10,829,223	150,566,234	47,653,510	194,097,394	58,482,733
Long-term liabilities	53,697,942	53,268,046	458,375,473	669,899,866	512,073,415	723,167,912
Total liabilities	97,229,102	64,097,269	608,941,707	717,553,376	706,170,809	781,650,645
Net Assets:						
Invested in capital assets, net of related debt	40,831,552	45,990,540	145,563,956	159,027,663	186,395,508	205,018,203
Restricted	6,021,539	3,701,902	48,378,388	35,972,139	54,399,927	39,674,041
Unrestricted	63,323,736	68,346,059	(10,149,776) *	528,488	53,173,960	68,874,547
Total net assets	$ 110,176,827	$ 118,038,501	$ 183,792,568	$ 195,528,290	$ 293,969,395	$ 313,566,791

* Business-type activities' negative unrestricted net assets is due to Gas Fund's cost of capital assets that were advanced by other funds. The Gas Fund expects to repay the advances from future operating revenues from customers.

The assets of the City exceeded its liabilities at the close of the most recent fiscal year by $293,969,395 (*net assets*). Of this amount, $53,173,960 (*unrestricted net assets*) may be used to meet the City's ongoing obligations to citizens and creditors.

The City is able to report positive balances in all categories of net assets for the government as a whole.

The category of the City's net assets with the largest balance totaling $186,395,508 (63%) represents resources that are invested in capital assets, net of related debt.

The second largest category of net assets, totaling $54,399,927 (19%) represents the City's restricted assets, which is restricted for special purposes and payment of long-term debt.

The last remaining category of net assets, $53,173,960 (18%) represents unrestricted net assets that can be used to meet the City's ongoing obligations to its citizens and creditors.

Governmental activities, net assets:

- Current and other assets increased $28,495,170 from the prior year due primarily to an increase in cash and investments of $12,813,963 and an increase in land held for resale of $38,718,003 offset by a decrease in escrow deposits of $26,200,000 which was used to purchase land.
- Restricted assets decreased $8,135,809 from the prior year due primarily to the Redevelopment Agency Fund's use of restricted funds for redevelopment projects.
- Capital assets increased $4,910,798 from the prior year due primarily to an increase in construction in progress by the Redevelopment Agency Fund for redevelopment projects.
- Current liabilities increased $32,701,937 from the prior year due primarily to notes issued by the Industrial Development Fund for the purpose of acquiring land held for resale for new utility customers.
- Unrestricted net assets decreased $5,022,323 from the prior year due primarily to a decrease in investment in capital assets, net of related debt, of $5,158,988, increase in restricted net assets of $2,319,637, and a decrease in net assets from the activities for the year of $7,605,933.

Business-type activities, net assets:

- Current and other assets increased $59,249,808 from the prior year due primarily to an increase in Light and Power Fund's deferred outflow of $59,903,859 which represents an offset to an equal amount of derivative liabilities for derivative instruments which are considered to be effective as of the end of the current fiscal year.
- Restricted assets increased $16,000,199 from the prior year due primarily to an increase in cash restricted for capacity payments of $27,995,280 and a decrease in cash restricted for debt service of $15,589,031.
- Capital assets decreased $195,597,398 from the prior year due primarily to the sale of generating and transmission assets.
- Current liabilities increased $102,912,724 from the prior year due primarily to an increase in derivative liabilities of $93,360,425. The increase in derivative liabilities was due to the City's early implementation of GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments,* in the current fiscal year although the pronouncement was not required to be implemented until the fiscal year 2010. The early implementation of GASB 53 enables the City to report the fair value of its derivative instruments as of the end of the current fiscal year.

- Long-term liabilities decreased $211,524,393 from the prior year due primarily to a decrease in bonds payable, net, of $281,140,199 offset by an increase in deferred gain from the sale of generation assets of $71,230,473 which will be used to offset capacity expense payable to the buyer of the generation assets over the life of a tolling agreement with the buyer.
- Investment in capital assets, net of related debt, decreased $13,463,707 from the prior year due primarily to a decrease in capital assets of $195,597,398 offset by a decrease in cash restricted for debt service of $15,589,031 and a decrease in related debt of $199,557,636 due to the sale of generation and transmission assets proceeds used for the extinguishment of related debt.
- Unrestricted net assets decreased $10,678,264 from the prior year due primarily to a decrease in net assets from the activities for the year of $8,021,577. The decrease in net assets from the activities for the year were due primarily to the operating income of $4,862,384, investment income of $4,858,995, gain from the sale of generation and transmission assets of $64,091,699, offset by a loss on early termination of debt of $13,487,833, interest expense of $36,231,101, decrease in fair value of investments of $28,741,824, and a net operating transfer out of $3,373,897.

Changes in Net Assets

The table below summarizes the City's changes in net assets over the current and prior fiscal years. The details of the current year's changes in net assets can be found on page 19 of this report.

City of Vernon
Changes in Net Assets
For the Fiscal Years Ended June 30, 2008 and 2007

	Governmental Activities		Business-type Activities		Totals	
	2008	2007	2008	2007	2008	2007
Revenues						
Program Revenues						
Charges for services	$ 10,875,572	$ 10,868,533			$ 10,875,572	$ 10,868,533
Light and power			$ 147,262,646	$ 138,057,770	147,262,646	138,057,770
Gas			27,730,435	11,054,332	27,730,435	11,054,332
Other			7,430,230	7,629,380	7,430,230	7,629,380
Operating grants and contributions	539,854	272,107	-	-	539,854	272,107
General Revenues						
Taxes	19,408,565	17,908,039	-	-	19,408,565	17,908,039
State allocations	5,651,207	5,078,317	-	-	5,651,207	5,078,317
Investment income	727,243	2,079,705	(23,882,829) *	8,146,667	(23,155,586)	10,226,372
Gain on sale of property	2,790,813	11,515,195	-	-	2,790,813	11,515,195
Other revenues	1,036,315	1,585,653	-	1,036,427	1,036,315	2,622,080
Total revenues	41,029,569	49,307,549	158,540,482	165,924,576	199,570,051	215,232,125
Expenses						
Governmental activities						
General government	19,381,699	12,554,529	-	-	19,381,699	12,554,529
Public safety	22,993,043	20,333,160	-	-	22,993,043	20,333,160
Public works	5,261,193	5,338,251	-	-	5,261,193	5,338,251
Health services	1,599,106	1,398,458	-	-	1,599,106	1,398,458
Interest on long-term debt	2,774,358	1,962,574	-	-	2,774,358	1,962,574
Business-type activities						
Light and Power	-	-	182,819,295	151,788,112	182,819,295	151,788,112
Gas	-	-	24,743,547	11,791,046	24,743,547	11,791,046
Other	-	-	6,229,186	5,308,059	6,229,186	5,308,059
Total expenses	52,009,399	41,586,972	213,792,028	168,887,217	265,801,427	210,474,189
Special Items						
Business-type activities						
Light and Power						
Gain on sale of generation and transmission assets	-	-	64,091,699	-	64,091,699	-
Loss on early termination of debt	-	-	(13,487,833)	-	(13,487,833)	-
Total special items	-	-	50,603,866	-	50,603,866	-
Increase (decrease) in net assets before transfers	(10,979,830)	7,720,577	(4,647,680)	(2,962,641)	(15,627,510)	4,757,936
Transfers	3,373,897	(1,834,173)	(3,373,897)	1,834,173	-	-
Increase (decrease) in net assets	(7,605,933)	5,886,404	(8,021,577)	(1,128,468)	(15,627,510)	4,757,936
Net assets- beginning of year, restated (See Note 16) **	117,782,760	112,152,097	191,814,145	196,656,758	309,596,905	308,808,855
Net assets- end of year	$ 110,176,827	$ 118,038,501	$ 183,792,568	$ 195,528,290	$ 293,969,395	$ 313,566,791

* Business-type activities' negative revenue of $23,882,829 is due to $4,858,995 of investment income, $1,627,884 of net increase in fair value of investments, and $30,369,708 of net decrease in fair value of derivative instruments.
** For comparative purposes, fiscal year 2007 balances were not restated to reflect the implementation of GASB Statement No. 53.

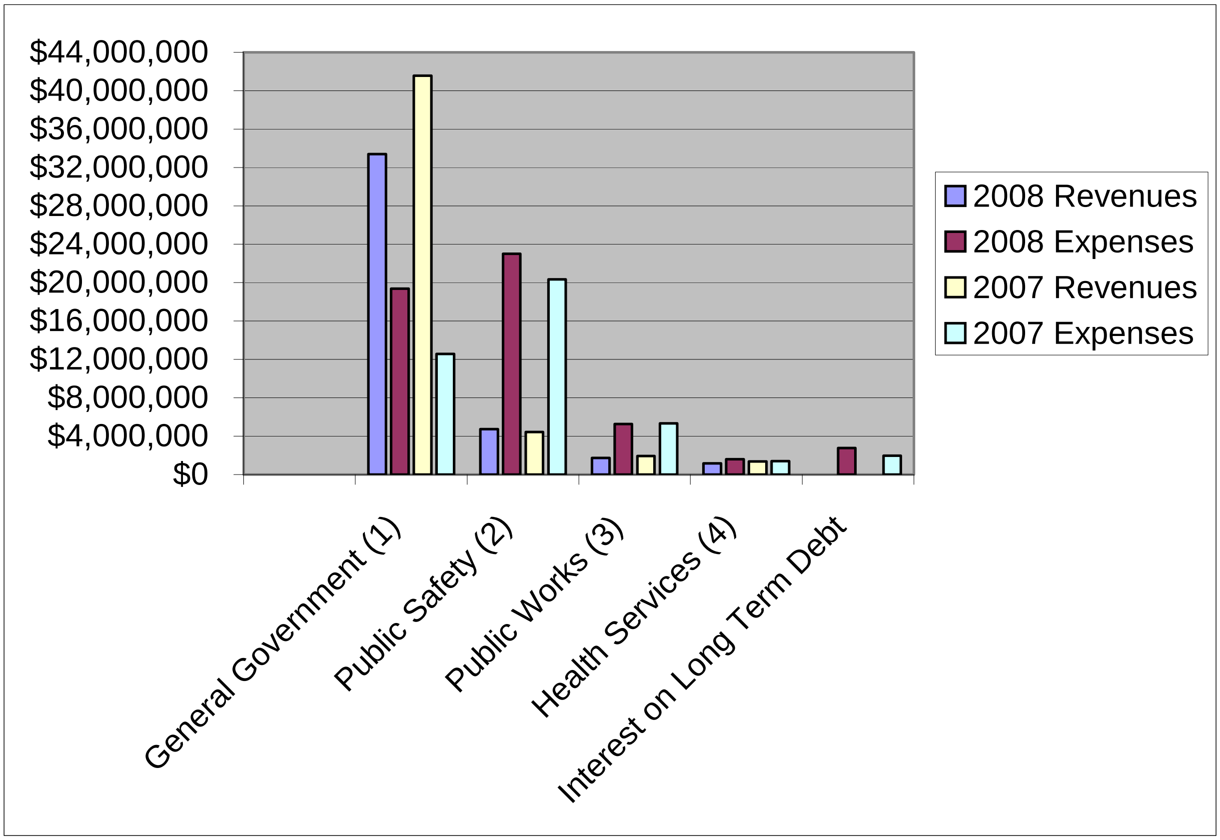
Governmental activities' net assets decreased by $7,605,933 and business-type activities' net assets decreased by $8,021,577 for a net decrease of $15,627,510 for the City. The decrease in the governmental activities was caused by the governmental activities reporting a $10,979,830 decrease in net asset before transfers and a $3,373,897 transfer in from the business-type activities.

<u>Governmental activities, changes in net assets:</u>

Governmental activities decreased the City's net assets by $7,605,933. This is a decrease of $13,492,337 from the prior year. The key reasons for this decrease and change in net assets are as follows:

- In the prior year, the governmental funds transferred a net of $1,834,173 to the enterprise funds. In the current year, the enterprise funds transferred a net of $3,373,897 to the governmental funds. The main reason for this transfer was enterprise funds' in-lieu tax payments to the general fund.
- In the current year, governmental funds had proceeds of $20,174,780 and a resulting gain on sale of property of $2,790,813, which is $8,724,383 less than the prior year.
- In the prior year, the governmental funds received swap termination proceeds of $818,280.
- In the current year, program expenses for general government were $6,827,170 higher than in the prior year mainly due to the following:
    - In the prior year, $3,415,075 of claims liability (Workers' Compensation) was reported as a reduction in expenses due to a change in actuarial estimate and an adjustment related to case reserves.
    - In the current year, contract services were $1,434,962 higher than in the prior year due to additional redevelopment and industrial development projects.
- In the current year, program expenses for public safety were $2,659,883 higher than in the prior year due to higher payroll costs.
- In the current year, program expense for interest was $811,784 higher than the prior year due to higher interest basis swap payments made in the current year (See page 51 for additional information on basis swap).

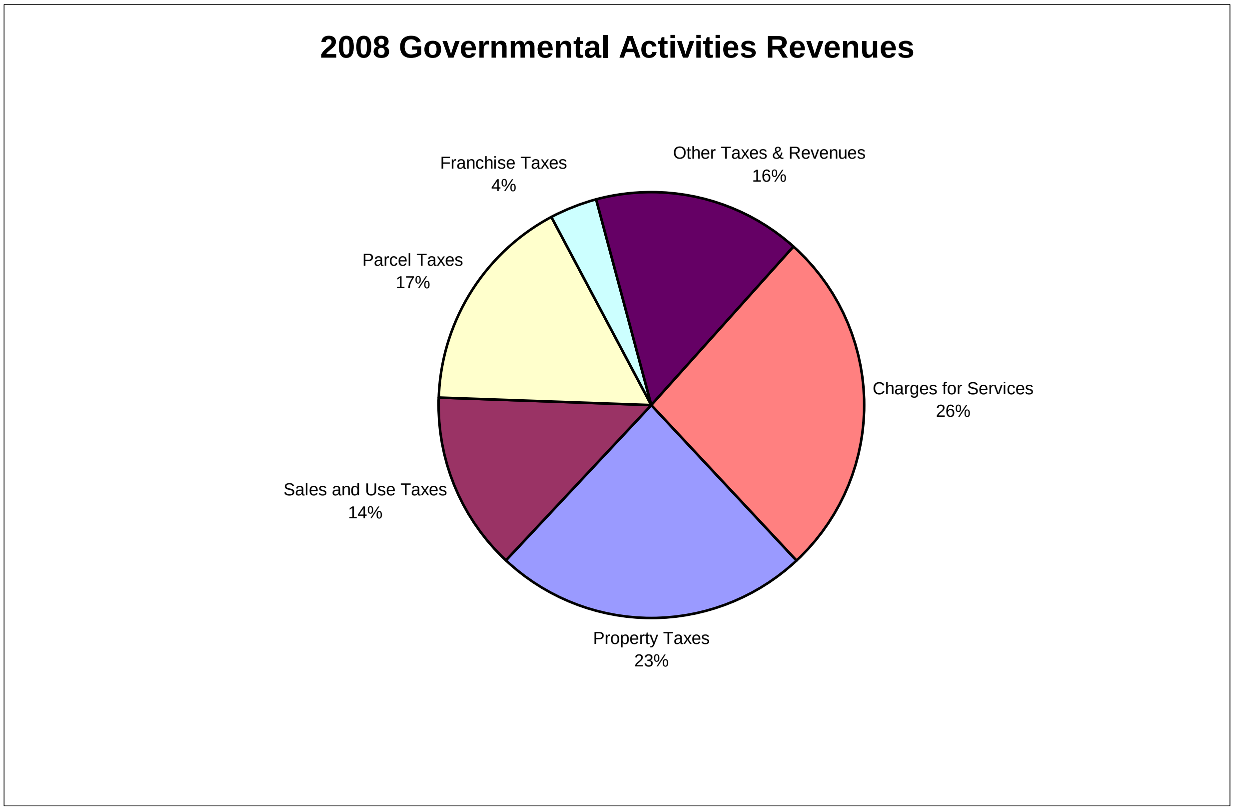
Revenues and Expenses — Governmental Activities
For the Fiscal Years Ended June 30, 2008 and 2007

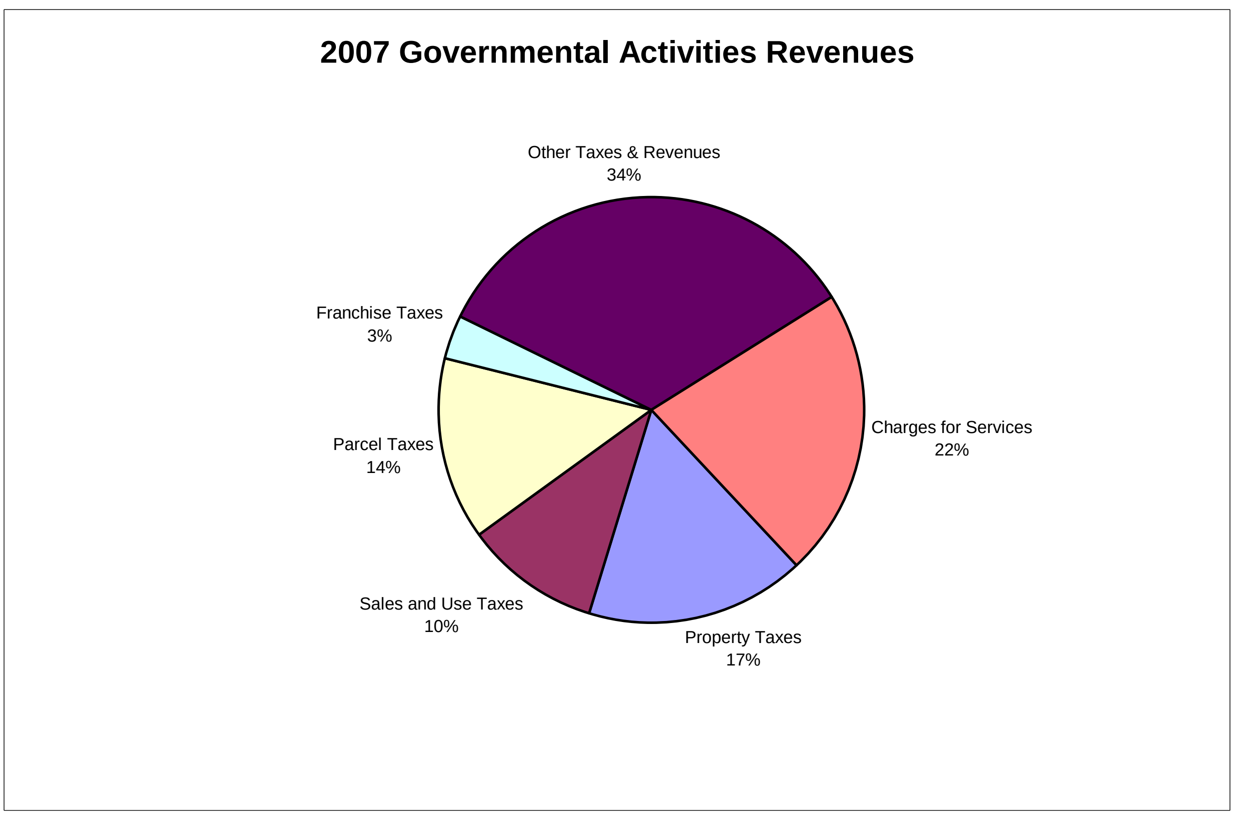


Governmental activities consist of the following departments:

(1) General Government:	(2) Public Safety	(3) Public Works	(4) Health Services
a. City Council	a. Police	a. Administrative, Engineering, and Planning	a. Health
b. City Administrator	b. Prisoner Care	b. Building Regulations	b. Solid Waste
c. City Clerk	c. Fire	c. Street Lighting	c. Hazardous Waste
d. Finance	d. Civil Defense	d. Street Operations	
e. Legal		e. Garage	
f. Elections		f. Warehouse	
g. Treasurer		g. Municipal Housing	
h. Business Services and Purchasing			
i. Personnel			
j. Employee Relations			
k. Redevelopment			
l. City Attorney			
m. Insurance			
n. Communications			
o. Library			
p. Street Lighting			
q. General Government Building			
r. Parcel Tax			

Revenues by Source — Governmental Activities
For the Fiscal Years Ended June 30, 2008 and 2007

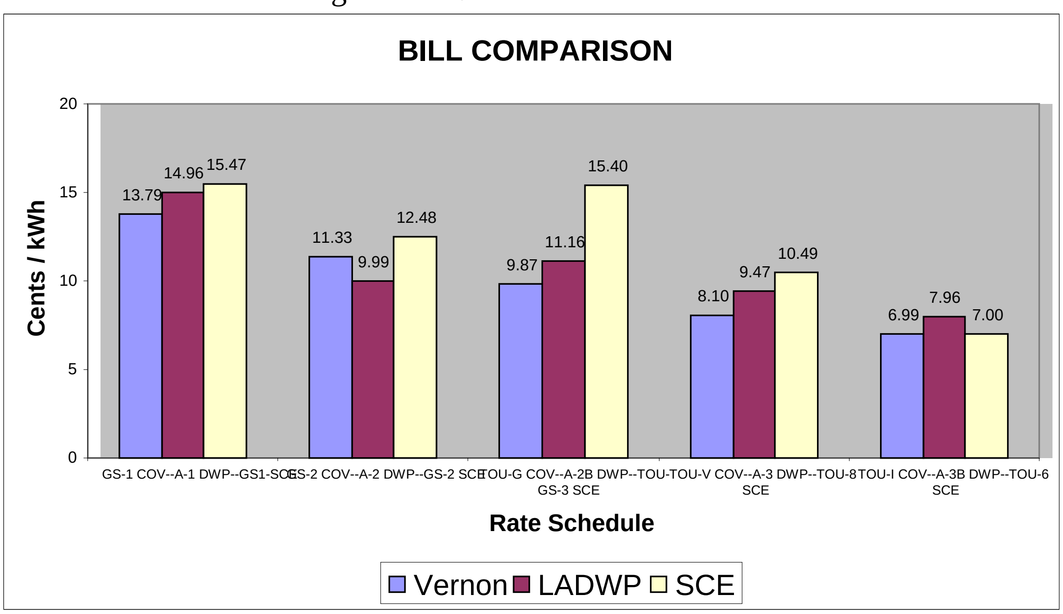




Business-type activities, changes in net assets:

Business-type activities decreased the City's net assets by $4,647,680 before transfers. The key reasons for this decrease in change in net assets are as follows:

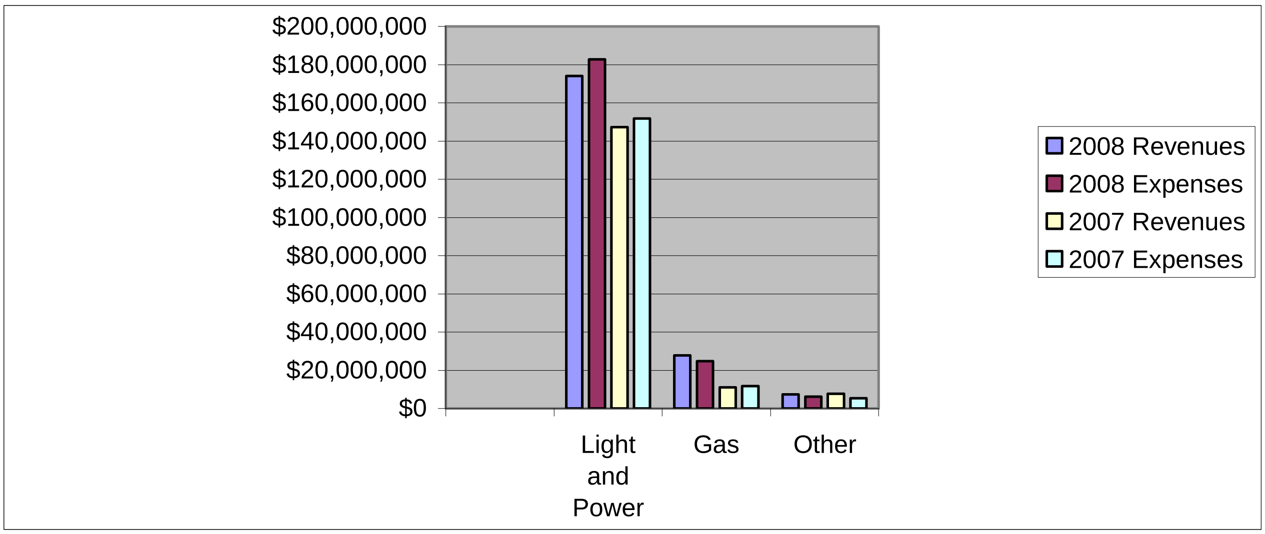
- Light and Power Fund sold its generation, transmission, and other assets for a net gain of $64,091,699 (See major capital asset events on page 15 and Note 11).
- Light and Power's operating revenue was $147,262,646 for the current year which is $9,204,876 higher than the previous year. This increase in revenue was mainly due to an increase in wholesale power sales.
- Light and Power's depreciation and amortization expense was $11,053,493 for the current year, which is $561,170 lower than the previous year. This decrease was mainly due to the generation and transmission assets being sold in late fiscal year 2008.
- Light and Power's cost of sales was $135,534,701 for the current year which is $23,587,878 higher then the previous year. This increase was mainly due to an increase in the unit price of wholesale energy purchased during the year.
    - The benefits of low cost electricity are passed on to the City's electric customers who enjoy some of the lowest rates in the Los Angeles area. Two of the larger entities providing electric service in the Los Angeles area are Los Angeles Department of Water and Power (LADWP) and Southern California Edison (SCE). The following chart provides the City's comparison of average charges per kilowatt hour (kWh) for some of the more commonly used rate schedules in the Los Angeles area.



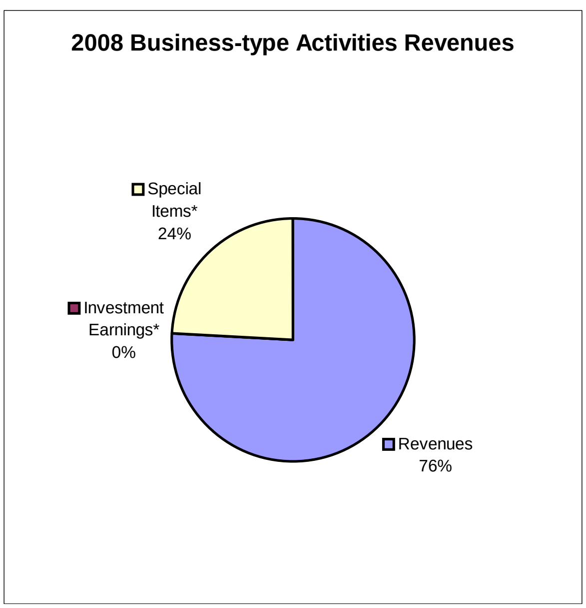
City of Vernon (COV) rate schedules:
GS-1: Small general service.
GS-2: Large general service with maximum monthly demand of 500kW or higher.
TOU-G: Time of use service with maximum monthly demand between 100 kW and 500 kW.
TOU-V: Time of use service with maximum monthly demand of 500 kW or higher.
TOU-I: Interruptible loads of at least 50 percent of maximum monthly demand, which must be at least 7,500 kW during period of interruption.

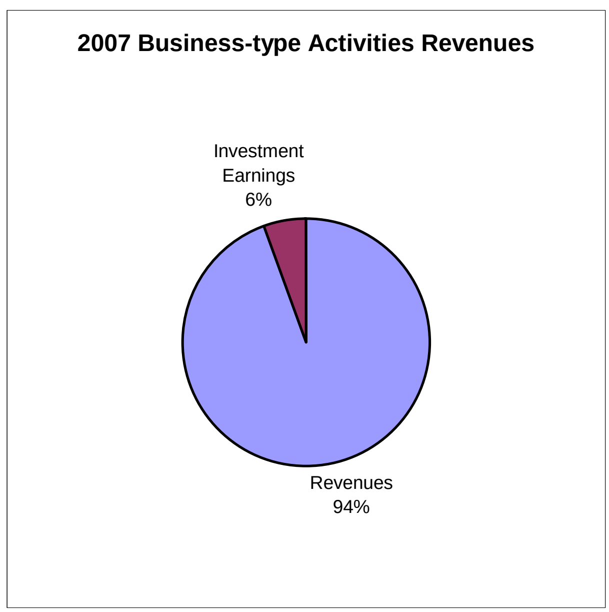
- Gas Fund's total operating revenues and expenses were $27,730,435 and $24,743,547, respectively, in the current year. The total operating revenues and expenses were $16,676,103 and $12,952,501, respectively, higher as compared to the prior year. In the current year, the Gas Fund procured natural gas for the Light and Power Fund and started providing natural gas services to its City customers.

Revenues and Expenses — Business-type Activities
For the Fiscal Years Ended June 30, 2008 and 2007



Revenues by Source — Business-type Activities
For the Fiscal Years Ended June 30, 2008 and 2007





* For the breakdown of special items and investment earnings, see page 8.

FINANCIAL ANALYSIS OF THE GOVERNMENTAL FUNDS

As noted earlier, the City uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

The fund accounting financial statements can be found on pages 20-23 of this report.

Governmental funds.

The focus of the City's *governmental funds* is to provide information on near-term inflows, outflows, and balances of *spendable* resources. Such information is useful in assessing the City's financing requirements. In particular, *unreserved fund balance* may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

At the end of the current fiscal year, the City's governmental funds reported combined ending fund balances of $93,012,968 (See page 20), an increase of $9,031,075 in comparison with the prior year (See page 22). Approximately 86% of total fund balance amount, $80,077,508, constitutes *unreserved fund balance*, which is available for spending at the City's discretion. The remainder of fund balance, $12,935,460, is *reserved* to indicate that it is not available for new spending because it has already been committed (i) to liquidate contracts and purchase orders of the current period $5,532,654, (ii) to be used for debt service $5,730,867, (iii) to be used for various redevelopment projects in or benefiting the Redevelopment Agency Fund's Industrial Redevelopment Project area, $538,399, and (iv) for a variety of other purposes $1,133,540.

The General Fund is the operating fund of the City. At the end of the current fiscal year, the total fund balance was $1,291,507 with a deficit in unreserved fund balance of $1,838,571 (See page 20). At the end of the current fiscal year, the total fund balance was 3% as compared to the total expenditures for the year. However, as the operating fund of the City, the General Fund will be supported by the resources of the City.

Proprietary funds.

The City's proprietary funds provide the same type of information found in the government-wide financial statements, but in more detail.

Unrestricted net assets for the Light and Power Fund at the end of the year amounted to $14,622,346 (See page 24). Unrestricted net assets of the Gas Fund at the end of the year amounted to a deficit of $27,045,599. Unrestricted net assets of the non-major enterprise funds (Water Fund and Fiber Optic Fund) amounted to $2,273,477. This deficit balance in unrestricted net assets for the Gas Fund is primarily due to the Gas Fund heavily invested in capital assets for which it has not yet recovered the cost of capital invested. The natural gas lines are currently operational and the Gas Fund expects to eliminate this deficit balance through increased revenues from customers on future gas sales.

Total increase (decrease) in net assets for the Light and Power Fund, Gas Fund, and Other Enterprise Funds were ($11,986,455), $2,986,888, and $977,990, respectively (See page 25). Other factors concerning the finances of these funds have already been addressed in the discussion of the City's business-type activities.

GOVERNMENTAL FUNDS AND BUDGETARY HIGHLIGHTS

For the current year, the City’s original and final budget for General Fund expenditures was $49,964,627. The General Fund’s total positive variance between the final budgeted amount and actual amount for expenditures was $2,051,835. The key reasons for this variance were excess appropriations of $1,053,672 in General Government’s legal and contract services expenditures, $672,041 in Public Works’ salaries and contract services expenditures, and $559,421 in Capital Outlay (See page 68).

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital assets.

The City's investment in capital assets for its governmental and business-type activities as of June 30, 2008, amounts to $227,739,070 (net of accumulated depreciation). This investment in capital assets includes land, buildings, utilities system improvements, machinery and equipment, and infrastructure such as roads. The total decrease in the City's investment in capital assets for the current fiscal year was $190,686,600 (net of depreciation of $13,837,320), primarily due to the sale of generating and transmission assets.

Major capital asset events during the current fiscal year included the following:

- Light and Power Fund sold its generation, transmission, and other assets for $382,758,731 with the book value of the generation and transmission assets of $198,258,596 and other assets of $27,063,036 for a total gain of $157,437,100 of which $64,091,699 was recorded as a gain on sale of capital assets and $11,605,990 was recorded as a reduction in capacity expense (See Note 11 for additional information on the City’s commitments to the buyer of the generation assets under a power purchase tolling agreement) and $81,839,411 was deferred to reduce capacity expense in future years.
- The General Fund sold one parcel of land which originally cost $5,794,543 for a total gain of $1,736,242.
- The Redevelopment Agency Fund sold one parcel of land to the Industrial Development Fund at cost of $11,589,424 for the development of the land by the Industrial Development Fund.
- Light and Power Fund made $10,320,249 of additions to capital assets for production plant, transmission plant, distribution plant, and general plant and a $7,501,849 addition to construction in progress for the Southeast Region Energy Project.

There were no significant construction commitments outstanding as of June 30, 2008.

Additional information on the City's capital assets can be found in Note 5 on pages 41-44 of this report.

Outstanding debt

During the current year, the City extinguished the following debt with the proceeds from the sale of its generation, transmission, and other assets (See Note 11 for additional information on the sale of assets):

- $90,150,000 Electric System Revenue Bonds, 2004 Series A
- $83,575,000 Electric System Revenue Bonds, 2004 Series B
- $39,875,000 Electric System Revenue Bonds, 2004 Series C
- $57,850,000 Electric System Revenue Bonds, 2004 Series D

As of June 30, 2008, the following debt remains outstanding:

- $49,420,000 RDA Industrial Redevelopment Project Tax Allocation Bonds, 2005 Series
- $190,050,000 Vernon Gas Project Variable Rate Revenue Bonds, 2006 Series A
- $109,730,000 Vernon Gas Project Variable Rate Revenue Bonds, 2006 Series B
- $109,695,000 Vernon Gas Project Variable Rate Revenue Bonds, 2006 Series C

The 2005 RDA Industrial Redevelopment Project Tax Allocation Bonds were issued to provide funds to (i) finance various redevelopment projects in or benefiting the Agency's Industrial Redevelopment Project area, (ii) fund the reserve requirement for the Series 2005 Bonds, and (iii) pay the costs of issuance related to the Series 2005 Bonds.

The 2006 Vernon Gas Project Variable Rate Revenue Bonds were issued for the express purpose of purchasing a forward supply of natural gas fuel for the City's electrical generating station to operate as a hedge against future market volatility in natural gas.

As of June 30, 2008, all bonds issued by the Vernon Redevelopment Agency and Authority had an insured rating of AA by S&P and A2 by Moody's. However, during the Fiscal Year 2008 and subsequently thereafter, S&P and Moody's made numerous rating changes on the Vernon Redevelopment Agency and Authority bonds. Below is a summary of such rating changes.

- In June 2008, S&P downgraded the bond insurer MBIA, the bond insurer for the 2005 Series and 2006 Series, to AA from AAA. As a result of such rating action, the insured rating of the Vernon Redevelopment Agency 2005 Series and the Authority's 2006 Series was lowered to AA from AAA.
- In June 2008, Moody's downgraded the bond insurer MBIA, the bond insurer for the 2005 Series and 2006 Series, to A2 from Aaa. As a result of such rating action, the insured rating of the Vernon Redevelopment Agency 2005 Series and the Authority's 2006 Series was lowered to A2 from Aaa.
- In September 2008, S&P increased the underlying rating of the City's electric system to A- from BBB+.

- In November 2008, Moody's downgraded the bond insurer MBIA, the bond insurer for the 2005 Series and 2006 Series, to Baa1. As a result of such rating action, the insured rating of the Vernon Redevelopment Agency 2005 Series was lowered to Baa1. However, the insured rating on the Authority's 2006 Series was lowered A3, the underlying rating of the City's electric system by Moody's.

Additional information on the City's long-term debt can be found in Note 6 on pages 44-47 of this report.

ECONOMIC FACTORS AND NEW YEAR'S BUDGET AND RATES

These factors were considered in preparing the City's budget for the 2009 fiscal year.

- The City's Electric System has experienced volatility in the cost of natural gas since the disruption of the California energy markets in 2001 and 2002, with unusual volatility from 2006 to the present. In response, a fuel cost adjustment billing factor went into effect on July 1, 2008 and will be added to all retail customer bills (See Note 15 for additional information).
- In August 2008, the City entered into an agreement to acquire land for the potential development of wind and solar renewable resources (See Note 15 for additional information).
- In September 2008, the City issued $43,765,000 of 2008 Taxable Series A Electric System Revenue Bonds (See Note 15, Subsequent Events, for additional information).
- The fair value of the City's derivative liabilities was $93,549,686 as of June 30, 2008. As of October 31, 2008, the fair value of the City's derivative liabilities was $53,586,136 (See Note 7 and 15 for additional information).
- The City is strictly industrial and does not maintain an unemployment rate study of its small population. However, the unemployment rate of adjacent communities is currently 7.6%. This compares favorably to the state's average unemployment rate of 7.7% but unfavorably to the national average unemployment rate of 6.1%.
- The occupancy rate of the City's central business district has remained at 98% for the current year.
- Inflationary trends in the region compare favorably to national indices.

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of the City's finances for all those with an interest in the City's finances. Questions concerning any of the information provided in this report of requests for additional financial information should be addressed to the Director of Finance, City of Vernon, 4305 Santa Fe Avenue, Vernon, California, 90058.

CITY OF VERNON, CALIFORNIA

Statement of Net Assets

June 30, 2008

	Governmental Activities	Business-type Activities	Total
ASSETS:			
Cash and investments	$ 15,546,820	$ 164,889,312	$ 180,436,132
Receivables, net of allowances of $50,000			
for business-type activities	2,426,220	9,854,252	12,280,472
Accrued unbilled revenue	-	8,015,898	8,015,898
Accrued interest receivable	9,517	599,114	608,631
Inventories	770,592	60,314	830,906
Internal balances	31,901,242	(31,901,242)	-
Prepaid natural gas	-	368,725,587	368,725,587
Deposits and prepaid expenses	89,515	16,770	106,285
Restricted cash and investments	8,537,162	52,790,753	61,327,915
Note receivable	-	3,566,803	3,566,803
Bond issuance costs	2,210,390	7,665,132	9,875,522
Other assets	25,021,303	61,760	25,083,063
Derivative assets	-	2,922,058	2,922,058
Deferred outflows	-	59,903,859	59,903,859
Land held for resale	38,718,003	-	38,718,003
Capital assets:			
Nondepreciable	46,474,053	20,107,636	66,581,689
Depreciable, net	35,701,112	125,456,269	161,157,381
Total assets	207,405,929	792,734,275	1,000,140,204
LIABILITIES:			
Accounts payable	6,227,491	16,365,979	22,593,470
Accrued wages and benefits	1,999,739	367,754	2,367,493
Customer deposits and funds held for others	264,122	662,211	926,333
Unearned revenue	164,633	-	164,633
Derivative liabilities	189,261	93,360,425	93,549,686
Bond interest	663,800	4,683,505	5,347,305
Note interest	112,492	-	112,492
Long-term liabilities:			
Due within one year:			
Legal settlement payable	-	1,866,667	1,866,667
Bonds payable, net	44,345	22,330,000	22,374,345
Notes payable	30,273,750	-	30,273,750
Deferred gain from sale of generation assets	-	10,608,938	10,608,938
Claims payable	1,754,466	-	1,754,466
Compensated absences	1,837,061	320,755	2,157,816
Due in more than one year:			
Bonds payable, net	50,189,011	387,145,000	437,334,011
Deferred gain from sale of generation assets	-	71,230,473	71,230,473
Claims payable	3,508,931	-	3,508,931
Total liabilities	97,229,102	608,941,707	706,170,809
NET ASSETS:			
Invested in capital assets, net of related debt	40,831,552	145,563,956	186,395,508
Restricted for:			
Grants	290,672	-	290,672
Debt service	5,730,867	20,383,108	26,113,975
Capacity payments	-	27,995,280	27,995,280
Unrestricted	63,323,736	(10,149,776)	53,173,960
Total net assets	$ 110,176,827	$ 183,792,568	$ 293,969,395

See accompanying notes to the basic financial statements.

CITY OF VERNON, CALIFORNIA
Statement of Activities
For the Fiscal Year Ended June 30, 2008

	Program Revenues			Net (Expenses) Revenues and Change in Net Assets		
	Expenses	Charges for Services	Operating Grants and Contributions	Governmental Activities	Business-type Activities	Total
FUNCTION/PROGRAM ACTIVITIES:						
Governmental activities:						
General government	$ 19,381,699	$ 3,236,812	$ 539,854	$ (15,605,033)	$ -	$ (15,605,033)
Public safety	22,993,043	4,740,743	-	(18,252,300)	-	(18,252,300)
Public works	5,261,193	1,730,596	-	(3,530,597)	-	(3,530,597)
Health services	1,599,106	1,167,421	-	(431,685)	-	(431,685)
Interest on long-term debt	2,774,358	-	-	(2,774,358)	-	(2,774,358)
Total governmental activities	52,009,399	10,875,572	539,854	(40,593,973)	-	(40,593,973)
Business-type activities:						
Light and power	182,819,295	147,262,646	-	-	(35,556,649)	(35,556,649)
Gas	24,743,547	27,730,435	-	-	2,986,888	2,986,888
Other	6,229,186	7,430,230	-	-	1,201,044	1,201,044
Total business-type activities	213,792,028	182,423,311	-	-	(31,368,717)	(31,368,717)
Total	$ 265,801,427	$ 193,298,883	$ 539,854	(40,593,973)	(31,368,717)	(71,962,690)
General Revenues:						
Property taxes				9,762,840	-	9,762,840
Parcel taxes				6,832,688	-	6,832,688
Franchise taxes				1,451,760	-	1,451,760
Business license taxes				1,041,176	-	1,041,176
Other license taxes				320,101	-	320,101
Investment income				571,137	4,858,995	5,430,132
Net increase (decrease) in fair value of investments				156,106	(28,741,824)	(28,585,718)
State contribution - sales and use taxes				5,651,207	-	5,651,207
Gain on sale of property				2,790,813	-	2,790,813
Other revenues				1,036,315	-	1,036,315
Special items:						
Gain on sale of generation and transmission assets				-	64,091,699	64,091,699
Loss on early termination of debt				-	(13,487,833)	(13,487,833)
Transfers				3,373,897	(3,373,897)	-
Total general revenues, special items, and transfers				32,988,040	23,347,140	56,335,180
Change in net assets				(7,605,933)	(8,021,577)	(15,627,510)
NET ASSETS, BEGINNING OF YEAR, RESTATED				117,782,760	191,814,145	309,596,905
NET ASSETS, END OF YEAR				$ 110,176,827	$ 183,792,568	$ 293,969,395

See accompanying notes to the basic financial statements.

CITY OF VERNON, CALIFORNIA

Balance Sheet
Governmental Funds
June 30, 2008

	General Fund	Redevelopment Agency Fund	Industrial Development Fund	Other Governmental Funds	Total Governmental Funds
ASSETS:					
Cash and investments	$ 3,091,735	$ 7,547,070	$ -	$ 4,679,685	$ 15,318,490
Receivables	1,961,486	201,230	100,000	163,504	2,426,220
Accrued interest receivable	1,834	7,683	-	-	9,517
Due from other funds	15,588,782	862,611	-	24,041,683	40,493,076
Inventories	770,592	-	-	-	770,592
Restricted cash and investments	297,597	4,720,956	3,518,609	-	8,537,162
Other assets	89,515	25,021,303	-	-	25,110,818
Land held for resale	-	-	38,718,003	-	38,718,003
Total assets	$ 21,801,541	$ 38,360,853	$ 42,336,612	$ 28,884,872	$ 131,383,878
LIABILITIES AND FUND BALANCES:					
Liabilities:					
Accounts payable	$ 2,814,499	$ 2,939,815	$ 329,042	$ 66,174	$ 6,149,530
Accrued wages and benefits	1,969,162	-	17,928	12,649	1,999,739
Due to other funds	-	-	3,363,528	-	3,363,528
Advances from other funds	14,774,667	-	-	5,979	14,780,646
Customer deposits and funds held for others	264,122	-	-	-	264,122
Deferred revenue	687,584	-	11,125,761	-	11,813,345
Total liabilities	20,510,034	2,939,815	14,836,259	84,802	38,370,910
Fund balances:					
Reserved for:					
Federal forfeiture funds	290,672	-	-	-	290,672
Inventories	770,592	-	-	-	770,592
Encumbrances	1,996,538	2,761,800	703,439	70,877	5,532,654
Employee loans receivable	72,276	-	-	-	72,276
Debt service	-	4,182,557	1,548,310	-	5,730,867
Redevelopment projects	-	538,399	-	-	538,399
Unreserved	(1,838,571)	27,938,282	25,248,604	-	51,348,315
Unreserved, reported in nonmajor:					
Special revenue funds	-	-	-	28,729,193	28,729,193
Total fund balances	1,291,507	35,421,038	27,500,353	28,800,070	93,012,968
Total liabilities and fund balances	$ 21,801,541	$ 38,360,853	$ 42,336,612	$ 28,884,872	$ 131,383,878

See accompanying notes to the basic financial statements.

CITY OF VERNON, CALIFORNIA
Reconciliation of the Governmental Funds Balance Sheet to the
Statement of Net Assets - Governmental Activities
June 30, 2008

Fund balances - total governmental funds (page 20)	$	93,012,968
Amounts reported for governmental activities in the statement of net assets are different because:		
Capital assets used in governmental activities are not financial resources and therefore are not reported in the governmental funds.		82,175,165
Because the focus of governmental funds is on short-term financing, some assets will not be available to pay for current period expenditures. Those assets are offset by deferred revenue in the governmental funds		11,125,761
Other assets used in governmental activities do not consume current financial resources and therefore are not reported in the governmental fund.		
Unamortized bond issuance costs		2,210,390
Compensated absences are not due and payable in the current period and therefore are not reported in the funds.		(1,837,061)
Internal service funds are used by management to charge the costs of employee benefits for health insurance, workers compensation, etc., to individual funds. The assets and liabilities of these funds are included in governmental activities in the statement of net assets		4,439,312
Long-term liabilities are not due and payable in the current period and therefore are not reported in the governmental fund.		
Bonds payable		(49,420,000)
Bond interest payable		(663,800)
Unamortized bond premium		(813,356)
Note payable		(30,273,750)
Note interest payable		(112,492)
Derivative liabilites		(189,261)
The City recognized uncollected property taxes that were earned but unavailable as of June 30, 2008.		522,951
Net assets of governmental activities (page 19)	$	110,176,827

See accompanying notes to the basic financial statements.

CITY OF VERNON, CALIFORNIA

Statement of Revenues, Expenditures and Changes in Fund Balances

Governmental Funds

For the Fiscal Year Ended June 30, 2008

	General Fund	Redevelopment Agency Funds	Industrial Development Fund	Other Governmental Funds	Total Governmental Funds
REVENUES:					
Taxes	$ 10,675,889	$ 7,789,207	$ -	$ 6,054,578	$ 24,519,674
Special assessments	772,086	-	-	-	772,086
Licenses and permits	1,236,622	-	-	304,593	1,541,215
Fines, forfeitures and penalties	249,235	-	-	-	249,235
Investment income	159,421	463,510	37,722	-	660,653
Intergovernmental revenues	539,854	-	-	-	539,854
Charges for services to enterprise funds	8,861,811	-	-	-	8,861,811
Other revenues	1,428,699	-	-	-	1,428,699
Total revenues	23,923,617	8,252,717	37,722	6,359,171	38,573,227
EXPENDITURES:					
General government	13,919,675	914,106	811,434	29,114	15,674,329
Public safety	21,630,258	-	-	97,619	21,727,877
Public works	4,971,701	-	-	-	4,971,701
Health services	1,421,492	-	-	89,625	1,511,117
Capital outlay	3,155,167	31,968,577	763,226	88,882	35,975,852
Interest on bonds	-	2,276,590	542,113	-	2,818,703
Total expenditures	45,098,293	35,159,273	2,116,773	305,240	82,679,579
Excess (deficiency) of revenues over (under) expenditures	(21,174,676)	(26,906,556)	(2,079,051)	6,053,931	(44,106,352)
Other financing sources (uses):					
Proceeds from land	-	-	1,054,571	-	1,054,571
Sale of property	7,530,785	11,589,424	-	-	19,120,209
Proceeds from long-term debt	-	-	30,273,750	-	30,273,750
Transfers in	3,401,651	-	-	17,573,644	20,975,295
Transfers out	(16,509,727)	(27,754)	(1,748,917)	-	(18,286,398)
Total other financing sources (uses)	(5,577,291)	11,561,670	29,579,404	17,573,644	53,137,427
NET CHANGE IN FUND BALANCES	(26,751,967)	(15,344,886)	27,500,353	23,627,575	9,031,075
FUND BALANCES, BEGINNING OF YEAR	28,043,474	50,765,924	-	5,172,495	83,981,893
FUND BALANCES, END OF YEAR	$ 1,291,507	$ 35,421,038	$ 27,500,353	$ 28,800,070	$ 93,012,968

See accompanying notes to the basic financial statements.

CITY OF VERNON, CALIFORNIA
Reconciliation of the Statement of Revenues, Expenditures, and
Changes in Fund Balances of Governmental Funds to the
Statement of Activities - Governmental Activities
For the Fiscal Year Ended June 30, 2008

Net change in fund balances - total governmental funds (page 22)		$ 9,031,075
Amounts reported for governmental activities in the statement of activities are different because:		
Expenditures for capital assets	$ 35,975,852	
Less current year depreciation	(2,555,326)	33,420,526
Change in long-term compensated absences		272,292
The effect of various miscellaneous transactions involving capital assets (i.e., sales, trade-ins, and donations) is to decrease net assets.		
Sale of and gain on capital assets		(17,383,967)
Internal service funds are used by management to charge the costs of certain activities to individual funds. The change in net assets of the internal service funds is reported with governmental activities.		(2,261,359)
Other assets used in governmental activities do not consume current financial resources and therefore are not reported in the governmental fund.		
Change in unamortized bond issuance costs		(120,514)
Long-term debt proceeds provide current financial resources to governmental funds, but issuing debt increase long-term liabilities in the statement of net assets.		
Issuance of notes		(30,273,750)
Some expenses in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in the governmental funds.		
Change in unamortized bond premium		44,345
Change in fair value of derivative liabilities		66,480
Change in note interest payable		(112,492)
Revenue timing differences result in less revenue in government-wide statement of activities.		(288,569)
Change in net assets of governmental activities (page 19)		$ (7,605,933)

See accompanying notes to the basic financial statements.

CITY OF VERNON, CALIFORNIA
Statement of Fund Net Assets (Deficit)
Proprietary Funds
June 30, 2008

	Business-type Activities Enterprise Funds				Governmental Activities - Internal Service Funds
	Light and Power Fund	Gas Fund	Other Enterprise Funds	Totals	
ASSETS:					
Current assets:					
Cash and investments	$ 164,889,312	$ -	$ -	$ 164,889,312	$ 228,330
Accounts receivable, net of allowances of $50,000	8,671,157	824,978	358,117	9,854,252	-
Accrued unbilled revenue	6,833,316	625,845	556,737	8,015,898	-
Accrued interest receivable	599,114	-	-	599,114	-
Bond issuance costs	562,297	-	-	562,297	-
Due from other funds	-	4,022,107	7,551,011	11,573,118	9,552,340
Inventories	-	60,314	-	60,314	-
Prepaid natural gas	28,578,343	-	-	28,578,343	-
Notes receivable	298,309	-	-	298,309	-
Deposits and prepaid expenses	16,770	-	-	16,770	-
Restricted cash and investments	12,869,178	-	-	12,869,178	-
Derivative assets	2,922,058	-	-	2,922,058	-
Deferred outflows	59,903,859	-	-	59,903,859	-
Other assets	61,760	-	-	61,760	-
Total current assets	286,205,473	5,533,244	8,465,865	300,204,582	9,780,670
Noncurrent assets:					
Restricted cash and investments	39,921,575	-	-	39,921,575	-
Advances to other funds	45,321,078	-	-	45,321,078	-
Prepaid natural gas	340,147,244	-	-	340,147,244	-
Note receivable	3,268,494	-	-	3,268,494	-
Bond issuance costs	7,102,835	-	-	7,102,835	-
Capital assets:					
Nondepreciable	20,062,636	-	45,000	20,107,636	-
Depreciable, net	94,235,549	22,770,562	8,450,158	125,456,269	-
Total noncurrent assets	550,059,411	22,770,562	8,495,158	581,325,131	-
Total assets	836,264,884	28,303,806	16,961,023	881,529,713	9,780,670
LIABILITIES:					
Accounts payable	8,537,198	7,318,514	510,267	16,365,979	77,961
Accrued wages and benefits	273,060	12,662	82,032	367,754	-
Customer deposits	437,797	6,000	218,414	662,211	-
Due to other funds	58,255,006	-	-	58,255,006	-
Bond interest	4,683,505	-	-	4,683,505	-
Long-term liabilities:					
Due within one year:					
Claims payable	-	-	-	-	1,754,466
Deferred gain from sale of generation assets	10,608,938	-	-	10,608,938	-
Derivative liabilities	93,360,425	-	-	93,360,425	-
Legal settlement payable	1,866,667	-	-	1,866,667	-
Bonds payable, net	22,330,000	-	-	22,330,000	-
Compensated absences	237,845	3,092	79,818	320,755	-
Total current liabilities	200,590,441	7,340,268	890,531	208,821,240	1,832,427
Due in more than one year:					
Claims payable	-	-	-	-	3,508,931
Advances from other funds	-	25,238,575	5,301,857	30,540,432	-
Deferred gain from sale of generation assets	71,230,473	-	-	71,230,473	-
Bonds payable, net	387,145,000	-	-	387,145,000	-
Total noncurrent liabilities	458,375,473	25,238,575	5,301,857	488,915,905	3,508,931
Total liabilities	658,965,914	32,578,843	6,192,388	697,737,145	5,341,358
NET ASSETS:					
Invested in capital assets, net of related debt	114,298,236	22,770,562	8,495,158	145,563,956	-
Restricted for debt service	20,383,108	-	-	20,383,108	-
Restricted for capacity payments	27,995,280	-	-	27,995,280	-
Unrestricted (deficit)	14,622,346	(27,045,599)	2,273,477	(10,149,776)	4,439,312
Total net assets (deficit)	$ 177,298,970	$ (4,275,037)	$ 10,768,635	$ 183,792,568	$ 4,439,312

See accompanying notes to the basic financial statements.

CITY OF VERNON, CALIFORNIA
Statement of Revenues, Expenses and Changes in Fund Net Assets (Deficit)
Proprietary Funds
For the Fiscal Year Ended June 30, 2008

	Business-type Activities Enterprise Funds				Governmental Activities - Internal Service Funds
	Light and Power Fund	Gas Fund	Other Enterprise Funds	Totals	
OPERATING REVENUES:					
Charges for services	$ 147,262,646	$ 27,730,435	$ 7,430,230	$ 182,423,311	$ 1,439,727
Total operating revenues	147,262,646	27,730,435	7,430,230	182,423,311	1,439,727
OPERATING EXPENSES:					
Cost of sales	135,534,701	24,072,362	5,685,663	165,292,726	569,677
Depreciation and amortization	11,053,493	671,185	543,523	12,268,201	-
Claims expense	-	-	-	-	1,858,086
Employee benefits	-	-	-	-	1,958,434
Total operating expenses	146,588,194	24,743,547	6,229,186	177,560,927	4,386,197
Operating income (loss)	674,452	2,986,888	1,201,044	4,862,384	(2,946,470)
NONOPERATING REVENUE (EXPENSES):					
Investment income	4,858,995	-	-	4,858,995	111
Net decrease in fair value of investments	(28,741,824)	-	-	(28,741,824)	-
Interest expense	(36,231,101)	-	-	(36,231,101)	-
Total nonoperating expenses, net	(60,113,930)	-	-	(60,113,930)	111
Income (loss) before special items and transfers	(59,439,478)	2,986,888	1,201,044	(55,251,546)	(2,946,359)
Special Items:					
Gain on sale of capital assets	64,091,699	-	-	64,091,699	-
Loss on early termination of debt	(13,487,833)	-	-	(13,487,833)	-
Transfers in	27,754	-	-	27,754	685,000
Transfers out	(3,178,597)	-	(223,054)	(3,401,651)	-
Change in net assets	(11,986,455)	2,986,888	977,990	(8,021,577)	(2,261,359)
Net assets (deficit), beginning of the year, restated	189,285,425	(7,261,925)	9,790,645	191,814,145	6,700,671
Net assets (deficit), end of the year	$ 177,298,970	$ (4,275,037)	$ 10,768,635	$ 183,792,568	$ 4,439,312

See accompanying notes to the basic financial statements.

CITY OF VERNON
Statement of Cash Flows
Proprietary Funds
For the Fiscal Year Ended June 30, 2008

	Business-type Activities - Enterprise Funds				Governmental Activities - Internal Service Funds
	Light & Power Fund	Gas Fund	Other Enterprise Funds	Total	
Cash flows from operating activities:					
Cash received from customers/other funds	$ 200,475,763	$ 18,028,840	$ 6,083,838	$ 224,588,441	$ 3,127,758
Cash paid to suppliers for goods and services	(51,035,277)	(17,366,244)	(5,517,671)	(73,919,192)	(566,617)
Cash paid to City general fund for services	(8,397,734)	-	(464,077)	(8,861,811)	-
Cash paid for employee benefits	-	-	-	-	(1,958,434)
Cash paid for claims expense	(3,200,000)	-	-	(3,200,000)	(1,146,724)
Net cash provided by (used in) operating activities	137,842,752	662,596	102,090	138,607,438	(544,017)
Cash flows from noncapital financing activities:					
Transfers received	27,754	-	-	27,754	685,000
Transfers (paid)	(3,178,597)	-	(223,054)	(3,401,651)	-
Collection of note receivable	281,317	-	-	281,317	-
Net cash provided by (used in) noncapital financing activities	(2,869,526)	-	(223,054)	(3,092,580)	685,000
Cash flows from capital and related financing activities:					
Repayment of bonds	(292,820,000)	-	-	(292,820,000)	-
Bond interest paid	(31,547,596)	-	-	(31,547,596)	-
Sale of capital assets	382,858,731	-	-	382,858,731	-
Acquisition and construction of capital assets	(16,014,761)	(662,596)	(406,946)	(17,084,303)	-
Net cash provided by (used in) capital and related financing activities	42,476,374	(662,596)	(406,946)	41,406,832	-
Cash flows from investing activities:					
Purchases and sales of investments, net	(67,137,061)	-	-	(67,137,061)	-
Investment income	4,259,881	-	-	4,259,881	111
Net cash used in and provided by investing activities	(62,877,180)	-	-	(62,877,180)	111
Net increase (decrease) in cash and cash equivalents	114,572,420	-	(527,910)	114,044,510	141,094
Cash and cash equivalents, beginning of year	55,958,250	-	527,910	56,486,160	87,236
Cash and cash equivalents, end of year	$ 170,530,670	$ -	$ -	$ 170,530,670	$ 228,330
Reconciliation of operating income to net cash provided by (used in) operating activities:					
Operating income (loss)	$ 674,452	$ 2,986,888	$ 1,201,044	4,862,384	$ (2,946,470)
Adjustments to reconcile operating income to net cash provided by (used in) operating activities:					
Depreciation and amortization	11,053,493	671,185	543,523	12,268,201	-
Provision for doubtful accounts	(1,000,000)	-	-	(1,000,000)	-
Changes in operating assets and liabilities:					
Decrease (increase) in:					
Accounts receivable	2,094,532	(804,933)	(353,422)	936,177	-
Other receivables	1,299,797	(625,845)	(58,058)	615,894	-
Inventories	577,141	(12,020)	-	565,121	-
Prepaid expenses and deposits	4,529,438	-	-	4,529,438	-
Other assets	48,319,739	-	-	48,319,739	-
Increase (decrease) in:					
Accounts payable	(5,746,082)	6,693,821	(313,608)	634,131	3,060
Claims/Legal Settlement payable	(3,200,000)	-	-	(3,200,000)	711,362
Accrued wages and benefits	26,819	6,594	19,182	52,595	-
Due (to) from other funds	(2,607,530)	(8,258,797)	(934,912)	(11,801,239)	1,688,031
Customer deposits	17,530	6,000	36,037	59,567	-
Compensated absences	(35,988)	(297)	(37,696)	(73,981)	-
Deferred revenue	81,839,411	-	-	81,839,411	-
Net cash provided by (used in) operating activities	$ 137,842,752	$ 662,596	$ 102,090	$ 138,607,438	$ (544,017)
Reconciliation of cash and cash equivalents to Statement of Net Assets					
Cash and investments	$ 164,889,312	$ -	$ -	$ 164,889,312	$ 228,330
Current restricted cash and investments	12,869,178	-	-	12,869,178	-
Noncurrent restricted cash and investments	39,921,575	-	-	39,921,575	-
Total	217,680,065	-	-	217,680,065	228,330
Less: Investments with maturities of more than 90 days	(47,149,395)	-	-	(47,149,395)	-
Total cash and cash equivalents	$ 170,530,670	$ -	$ -	$ 170,530,670	$ 228,330
Noncash Capital, Investing and Financing Activities					
Acquisition of capital assets in accounts payable	$ 1,807,337	$ -	$ -	$ 1,807,337	$ -
Decrease in fair value of investments	30,894,232	-	-	30,894,232	-
Loss on early termination of debt	13,487,833	-	-	13,487,833	-

See accompanying notes to the basic financial statements.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the City of Vernon, California (City) have been prepared in conformity with U.S. generally accepted accounting principles (GAAP). The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The more significant of the City's accounting policies are described below.

Reporting Entity

The City was incorporated on September 16, 1905 as a General Law City. Effective July 1, 1988, the City became a Charter City. The City operates under a Council-City Administrator form of government. As required by generally accepted accounting principles, the accompanying basic financial statements present the City of Vernon (primary government) and its component units, entities for which the primary government is considered to be financially accountable. In accordance with GASB Statement No. 14, the City's component units are considered blended component units. Although legally separate entities, they are, in substance, part of the City's operations, and therefore, data from these units are combined with data of the primary government.

Blended Component Units

Vernon Redevelopment Agency (RDA). The governing body of the RDA is comprised of members of the City Council and the Mayor. Among its duties, it approves the RDA's budget and appoints the management.

Separately issued financial statements for the RDA may be obtained through the City of Vernon, 4305 Santa Fe Avenue, Vernon, California, 90058.

Vernon Natural Gas Financing Authority

On April 1, 2006, the City and the RDA created the Vernon Natural Gas Financing Authority (Authority) pursuant to the Joint Powers Agreement, for the express purpose of undertaking projects and programs that promote economic development within the City. Such projects and programs include assisting the City in procuring natural gas for use as fuel for electric generating units that are part of the City's Electric System, which is accounted for in the City's Light and Power fund. During the year ended June 30, 2006, the Authority issued $430,845,000 in variable rate bonds and subsequently purchased natural gas in accordance with the Natural Gas Agreement between the Authority and the City. As a result of this financing arrangement, the debt and related asset (prepaid natural gas) associated with the Authority have been blended with the City's Light and Power fund for financial reporting purposes.

Basis of Presentation

Government-wide Financial Statements

The statement of net assets and statement of activities display information about the primary government (the City) and its component units. These statements include the financial activities of the overall government. It is the City's policy to make eliminations to minimize the double counting of internal activities, except for services rendered by governmental activities to business-type activities. These statements distinguish between the *governmental* and *business-type activities* of the City. Governmental activities, which normally are supported by taxes, are reported separately from business-type activities, which rely to a significant extent on fees charged to external parties.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The statement of activities presents a comparison between direct expenses and program revenues for each segment of the business-type activities of the City and for each function of the City's governmental activities. Direct expenses are those that are specifically associated with a program or function; and therefore, are clearly identifiable to a particular function. Expenses by function have been adjusted for any internal service profit/loss existing at fiscal year-end. Program revenues include (i) charges paid by the recipients of goods or services offered by the programs and (ii) grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues that are not classified as program revenues, including all taxes, are presented instead as general revenues.

Fund Financial Statements

The fund financial statements provide information about the City's funds and blended component units. Separate statements for each fund category – *governmental and proprietary* – are presented. The emphasis of fund financial statements is on major governmental and enterprise funds, each displayed in a separate column. All remaining governmental and enterprise funds are separately aggregated and reported as nonmajor funds.

Proprietary funds distinguish *operating* revenues and expenses from *nonoperating* items. Proprietary fund *operating* revenues, such as charges for services, result from exchange transactions associated with the principal activity of the fund. Exchange transactions are those in which each party receives and gives up essentially equal values. *Nonoperating* revenues, such as subsidies and investment earnings, result from nonexchange transactions or ancillary activities. *Operating* expenses include the cost of sales and services, administrative expenses and depreciation on capital assets. All expenses not meeting this definition are reported as nonoperating expenses.

The City reports the following major governmental funds:

The *General Fund* is the City's primary operating fund. It is used to account for all revenues and expenditures necessary to carry out basic governmental activities of the City that are not accounted for through other funds. For the City, the General Fund includes such activities as general government, public safety, health services, and public works.

The *Vernon Redevelopment Agency* was activated September 16, 1986, by action of the Vernon City Council pursuant to the Community Redevelopment Law of California. The Agency has the broad authority to acquire, rehabilitate, develop, administer, and sell or lease property. Additionally, the Agency has the right of eminent domain to facilitate acquisition of property. The principal objectives of the Agency are to improve the commercial environment, provide new public improvements, strengthen the City's economic base, generate added employment opportunities, and expand the City's industrial base.

The *Industrial Development Fund* is utilized to acquire, rehabilitate, develop, administer, and sell or lease property. The principal objectives of the Industrial Development Department are to improve the commercial environment, strengthen the City's economic base, generate added employment opportunities, and expand the City's industrial base.

The City reports the following major enterprise funds:

- The *Light and Power Fund* accounts for the maintenance and operations of the City's electric utility plant. Revenue for this fund is primarily from charges for services.

- The *Gas Fund* accounts for maintenance and operations of the City's gas utility system. Revenue for this fund is primarily from charges for services.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Additionally, the City reports the following fund types:

- The City's *Special Revenue Funds* are used to account for the proceeds of specific revenue sources that are legally restricted to expenditures for specific purposes.

- The City's *Capital Projects Funds* are used to account for financial resources designated for the acquisition or construction of major capital facilities other than those financed by proprietary fund types.

- The City's *Internal Service Funds* are specifically designed to account for goods and services that are provided on a cost-reimbursement basis to other City funds. That is, the goal of an internal service fund should be to measure the full cost of providing goods and services for the purpose of fully recovering that cost through fees or charges. Some examples of the City's services accounted for in the internal service funds are self-insurance activities for worker's compensation, general liability, group medical and dental, and vehicle replacement. The Internal Service Funds are presented in summary form as part of the proprietary fund financial statements. In the government-wide financial statements, the changes in net assets for the fiscal year, as presented in the statements of activities, were allocated to the user functions of the governmental activities, to reflect the entire activity for the year. Since the predominant users of the internal services are the City's governmental activities, the asset and liability balances of the Internal Service Funds are consolidated into the governmental activities column at the government-wide level.

The government-wide and proprietary fund 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 at the time liabilities are incurred, regardless of when the related cash flows take place. Nonexchange transactions, in which the City gives (or receives) value without directly receiving (or giving) equal value in exchange, include property and sales taxes, grants, entitlements and donations. On an accrual basis, revenue from property taxes is recognized in the fiscal year for which the taxes are levied. Revenues from sales taxes are recognized when the underlying transactions take place. Revenues from grants, entitlements and donations are recognized in the fiscal year in which all eligible requirements have been satisfied.

Governmental fund type financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Under this method, revenues and other governmental fund type financial resources are recognized when they become susceptible to accrual – that is, when they become both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. Property, sales, and other taxes are considered available and are accrued when received within 60 days after fiscal year-end. Additionally, all other revenue sources are considered available and are accrued when received within 60 days of year-end. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due. General capital assets acquisitions are reported as expenditures in governmental fund statements.

For the government-wide financial statements and proprietary fund financial statements, under GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the City applies all applicable GASB pronouncements as well as any applicable pronouncements of the Financial Accounting Standards Board, the Accounting Principles Board or any Accounting Research Bulletins issued on or before November 30, 1989 unless those pronouncements conflict with or contradict GASB pronouncements. The City has elected to not apply private-sector accounting standards issued after November 30, 1989.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Because the governmental fund financial statements are presented on a different measurement focus and basis of accounting than the government-wide financial statements for governmental activities, reconciliations are presented which briefly explain the adjustments necessary to reconcile the fund financial statements to the governmental-wide statements.

The City's policy regarding whether to first apply restricted or unrestricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available is to use restricted resources first.

Cash Deposits and Investments

The City follows the practice of pooling cash and investments of all funds to maximize returns for all funds, except for funds held by trustee or fiscal agents.

For purposes of the statement of cash flows, the City considers all highly liquid investments (including restricted cash and investments) with an original maturity of three months or less when purchased to be cash equivalents. Investment transactions are recorded on the trade date. Investments in nonparticipating interest-earning investment contracts are reported at cost, and all other investments are reported at fair value. Fair value is defined as the amount that the City could reasonably expect to receive for an investment in a current sale between a willing buyer and a seller and is generally measured by quoted market prices.

Interfund Receivables/Payables

Short-term interfund receivables and payables are classified as "due from other funds" and "due to other funds", respectively, on the balance sheet/statement of fund net assets. Long-term interfund receivables and payables are classified as "advances to/from other funds," respectively, on the balance sheet/statement of fund net assets.

Inventories

Inventories consist of consumable supplies and fuel stock, which are stated at cost on a first-in, first-out basis. The cost of inventories is recorded as an expenditures/expense when the items are used.

Capital Assets

Capital assets (including infrastructure) are recorded at historical cost or at estimated historical cost if actual historical cost is not available. Contributed capital assets are valued at their estimated fair market value on the date contributed. Capital assets include public domain (infrastructure) general capital assets consisting of certain improvements including roads and bridges, sidewalks, curbs and gutters, and traffic light system. The capitalization threshold for all capital assets is $5,000. Capital assets used in operations are depreciated using the straight-line method over their estimated useful lives in the government-wide statements and proprietary funds.

The estimated useful lives are as follows:

Infrastructure	10 to 50 years
Utility plant and buildings	25 to 50 years
Improvements	10 to 20 years
Machinery and equipment	3 to 35 years

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Maintenance and repairs are charged to operations when incurred. Betterments and major improvements, which significantly increase values, change capacities or extend useful lives, are capitalized. Upon sale or retirement of capital assets, the cost and related accumulated depreciation are removed from the respective accounts and any resulting gain or loss is included in the changes in financial position. For tax-exempt securities, interest income and expense associated with construction of capital assets is capitalized during the construction phase up until the capital asset is substantially complete and ready for its intended use.

Compensated Absences

Accumulated vacation is accrued when incurred in the government-wide and proprietary fund financial statements. A liability for accrued vacation is recorded in the governmental funds only to the extent that such amounts have matured (i.e., as a result of employee resignations and retirements). Upon termination of employment, the City will pay the employee all accumulated vacation leave at 100% of the employee's base hourly rate.

Deferred/Unearned Revenue

Deferred revenue arises when a potential revenue transaction does not meet the "available" criteria for recognition in the current period. Unearned revenue arises when resources are received before the City has a legal claim to them, as when grant monies are received in advance of incurring qualified expenditures.

Long-term Obligations

Certain of the City's governmental fund obligations not currently due and payable at year-end are reported in the government-wide statement of net assets. Long-term debt and other obligations financed by proprietary funds are reported as liabilities in the appropriate proprietary fund and government-wide statement of net assets. Bond issuance costs, discounts and premiums and deferred amounts on refunding are amortized over the life of the bonds using the straight-line method.

Net Assets

The government-wide financial statements and proprietary fund financial statements utilize a net assets presentation. Net assets are categorized as invested in capital assets (net of related debt), restricted and unrestricted.

- Invested In Capital Assets, Net of Related Debt – This category groups all capital assets, including infrastructure, into one component of net assets. Accumulated depreciation and the outstanding balances of debt that are attributable to the acquisition, construction or improvement of these assets reduce the balance in this category.

- Restricted Net Assets – This category presents external restrictions imposed by creditors, grantors, contributors or laws or regulations of other governments and restrictions imposed by law through constitutional provisions or enabling legislation.

- Unrestricted Net Assets – This category represents net assets of the City not restricted for any project or other purpose.

Fund Equity

In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not appropriable or legally restricted for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Use of Estimates

The preparation of basic financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Property Taxes

The County of Los Angeles (County) levies, collects and apportions property taxes for all taxing jurisdictions with the County. Property taxes are determined by applying approved rates to the properties' assessed values. The County remits property taxes applicable to the City less an administrative fee throughout the year.

Article XIIIA of the State of California Constitution limits the property tax levy to support general government services of the various taxing jurisdictions to $1.00 per $100 of assessed value. Taxes levied to service voter-approved debt prior to June 30, 1978 are excluded from this limitation.

Secured property taxes are levied in two installments, November 1 and February 1. They become delinquent with penalties on December 10 and April 10, respectively. The lien date is January 1 of each year for secured and unsecured property taxes and the levy date occurs on the 4th Monday of September of the tax year. Unsecured property taxes on the tax roll as of July 31 become delinquent with penalties on August 31.

GASB Pronouncements

In September 2006, 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 ascertain whether the proceeds received should be reported as revenue or as a liability and provides additional guidance for sales of receivables and future revenues within the same financial reporting entity. This Statement includes a provision that stipulates that governments should not revalue assets that are transferred between financial reporting entity components. This Statement also includes guidance to be used for recognizing other assets and liabilities arising from a sale of specific receivables or future revenues, including residual interests and recourse provisions. The disclosures pertaining to future revenues that have been pledged or sold are intended to provide financial statement users with information about which revenues will be unavailable for other purposes and how long they will continue to be so. The City implemented this Statement during the fiscal year ended June 30, 2008 and it had no effect on financial position, changes in financial position, or cash flows.

In May 2007, GASB issued Statement No. 50, *Pension Disclosures – an Amendment of GASB Statements No. 25 and No. 27.*, which more closely aligns the financial reporting requirements for pensions with those for other postemployment benefits (OPEB) and, in doing so, enhances information disclosed in notes to financial statements or presented as required supplementary information (RSI) by pension plans and by employers that provide pension benefits. The reporting changes required by this Statement amend applicable note disclosure and RSI requirements of Statements No. 25 and No. 27, and to conform to the requirements of Statements No. 43 and No. 45. The City implemented this Statement during the fiscal year ended June 30, 2008. Additional note disclosures are presented in Note 9.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

In June 2008, GASB issued Statement No. 53 – *Accounting and Financial Reporting for Derivative Instruments.* This Statement addresses the recognition, measurement, and disclosure of information regarding derivative instruments entered into by state and local governments. Common types of derivative instruments used by governments include interest rate and commodity swaps, interest rate locks, options (caps, floors, and collars), forward contracts, and futures contracts. Governments enter into derivative instruments as investments; as hedges of identified financial risks associated with assets or liabilities, or expected transactions or to lower the costs of borrowings or with the intention of effectively fixing cash flows or synthetically fixing prices. The guidance in this Statement improves financial reporting by requiring governments to measure derivative instruments, with the exception of certain instruments, at fair value in their economic resources measurement focus financial statements. Although effective for fiscal periods beginning after June 15, 2009, the City has elected to early implement the provisions of this Statement for the fiscal year ended June 30, 2008. See Notes 7 and 16 for further discussion.

NOTE 2 – CASH AND INVESTMENTS

Cash and Investments

Cash and investments as of June 30, 2008 are classified in the accompanying financial statements as follows:

Statement of net assets:	
Cash and investments	$ 180,436,132
Restricted cash and investments	61,327,915
Total cash and investments	$ 241,764,047

Cash and investments as of June 30, 2008 consist of the following:

Cash on hand	$ 1,300
Deposits with financial institutions	37,165,416
Investments	204,597,331
Total cash and investments	$ 241,764,047

The City's Investment Policy

The City's Investment Policy sets forth the investment guidelines for all funds of the City. The Investment Policy conforms to the California Government Code Section 53600 et. seq. The authority to manage the City’s investment program is derived from the City Council. Pursuant to Section 53607 of the California Government Code, the City Council annually appoints the City Treasurer and approves the City’s investment policy. The Treasurer is authorized to delegate this authority as deemed appropriate. No person may engage in investment transactions except as provided under the terms of the Investment Policy and the procedures established by the Treasurer.

This Policy requires that the investments be made with the prudent person standard, that is, when investing, reinvesting, purchasing, acquiring, exchanging, selling or managing public funds, the trustee (Treasurer and staff) will act with care, skill, prudence, and diligence under the circumstances then prevailing, including but not limited to, the general economic conditions and the anticipated needs of the City.

NOTE 2 – CASH AND INVESTMENTS (CONTINUED)

The Investment Policy also requires that when following the investing actions cited above, the primary objective of the trustee be to safeguard the principal, secondarily meet the liquidity needs of depositors, and then achieve a return on the funds under the trustee's control. Further, the intent of the Investment Policy is to minimize risk of loss on the City's held investments from:

A. Credit risk
B. Custodial credit risk
C. Concentration of credit risk
D. Interest rate risk

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

Authorized Investment Type	Maximum Maturity	Maximum Percentage of *Portfolio	Maximum Investment in One Issuer
Securities of the U.S. Government, or it agencies	None	None	None
Certain Asset-Backed Securities	None	None	None
Certificates of Deposit	None	30%	None
Bankers' Acceptances	180 days	40%	30%
Commercial Paper	270 days	25%	10%
Repurchase Agreements	1 year	None	None
Reverse Repurchase Agreements	92 days	20%	None
Medium-Term Notes	None	30%	None
Mutual Funds	N/A	20%	10%
Money Market Mutual Funds	N/A	20%	10%
Mortgage Pass-Through Securities	5 years	20%	None
State Administered Pool Investment	N/A	None	None

* Excluding amounts held by bond trustee that are not subject to California Government Code restrictions.

NOTE 2 – CASH AND INVESTMENTS (CONTINUED)

Investments Authorized by Debt Agreements

Investments of debt proceeds held by bond trustee are governed by provisions of the debt agreements, rather than the general provisions of the California Government Code or the City's Investment Policy. The table below identifies the investment types that are authorized for investments held by bond trustee. The table also identifies certain provisions of these debt agreements that address interest rate risk, credit risk, and concentration of credit risk.

Authorized Investment Type	Maximum Maturity	Maximum Percentage of Portfolio	Maximum Investment in One Issuer
Securities of the U.S. Government, or it agencies	None	None	None
Certain Asset-Backed Securities	None	None	None
Certificates of Deposit	None	None	None
Bankers' Acceptances	1 year	None	None
Commercial Paper	None	None	None
Money Market Mutual Funds	N/A	None	None
State Administered Pool Investment	N/A	None	None
Investment Contracts	None	None	None

Disclosure 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 close to maturity evenly over time as necessary to provide the cash flow and liquidity needed for operations. The City monitors the interest rate risk inherent in its portfolio by measuring the weighted average maturity of its portfolio. The City has no specific limitations with respect to this metric.

Investment Type	Amount	Weighted Average Maturity (in years)	% of Total
Federal Home Loan Discount Notes	$ 27,600,000	-	13.49%
Federal Home Loan Bank	10,114,063	1.21	4.94%
Federal Home Loan Mortgage Corporation	5,101,563	0.71	2.49%
Federal National Mortgage Association	3,622,500	4.47	1.77%
Investment Contracts	20,931,095	13.10	10.23%
Local Agency Investment Fund	529,974	0.58	0.26%
Money Market Mutual Fund	126,225,436	-	61.69%
United States Treasury Notes	10,472,700	2.55	5.13%
	$ 204,597,331	0.65	100.00%

NOTE 2 – CASH AND INVESTMENTS (CONTINUED)

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, or debt agreements, and the actual rating as of the year end for each investment type.

	Minimum Required Rating	Actual Credit Rating Moody's / S&P	Fair Value as of June 30, 2008	% of Total
In custody of Treasurer:				
Cash on hand	Not Rated	Not Rated	$ 1,300	0.00%
Deposits with financial institutions	Not Rated	Not Rated	37,165,416	15.37%
Investments held by Treasurer:				
Federal Home Loan Discount Notes	Not Rated	Not Rated	27,600,000	11.42%
Local Agency Investment Fund	Not Rated	Not Rated	529,974	0.22%
Total in custody of Treasurer			65,296,690	27.01%
In custody of Trustee:				
Investments held by Trustee:				
Federal Home Loan Bank	Aaa / AAA	Aaa / AAA	10,114,063	4.18%
Federal Home Loan Mortgage Corporation	Aaa / AAA	Aaa / AAA	5,101,563	2.11%
Federal National Mortgage Association	Aaa / AAA	Aaa / AAA	3,622,500	1.50%
Investment Contracts	Aa3 / AA	Aa3 / AA	20,931,095	8.66%
Money Market Mutual Fund	Aaa / AAA	Aaa / AAA	126,225,436	52.21%
United States Treasury Notes	Not Rated	Not Rated	10,472,700	4.33%
Total in custody of Trustee			176,467,357	72.99%
Total cash and investments held by Treasurer and Trustee			$ 241,764,047	100.00%

NOTE 2 – CASH AND INVESTMENTS (CONTINUED)

Concentration of Credit Risk

The City's Investment Policy places no limit on the amount the City may invest in any one issuer excluding a 10% limitation on commercial paper, mutual funds, and money market mutual funds. The City’s Investment Policy also places no limit on the amount of debt proceeds held by bond trustee that the trustee may invest in one issuer that are governed by the provisions of debt agreements of the City, rather than the general provisions of the California Government Code or the City's Investment Policy. As of June 30, 2008, the City’s investments in any one issuer exceeding 5% were as follows:

	Issuer	In Custody of	Minimum Required Rating	Actual Credit Rating Moody's / S&P		Fair Value as of June 30, 2008	% of Total
Federal Home Loan Discount Notes	Federal Home Loan Bank	Treasurer	Not Rated	Not Rated	$	27,600,000	11.42%
Investment Contracts	AEGON Institutional Markets	Trustee	Aa3 / AA	Aa3 / AA	$	20,931,095	8.66%
Money Market Mutual Fund	Invesco Aim	Trustee	Aaa / AAA	Aaa / AAA	$	126,225,436	52.21%

Custodial Credit Risk

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The California Government Code and the City's Investment Policy do not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits or investments.

At year-end, the carrying amount of the City’s deposits was $37,165,416 and the bank balance was $37,320,639. The difference between the bank balance and the carrying amount represents outstanding checks and deposits in transit. Of the bank balance, $200,000 was covered by federal depository insurance and $37,120,639 was collateralized by the pledging financial institution as required by Section 53652 of the California Government Code. Under the California Government Code, a financial institution is required to secure deposits in excess of $100,000 made by state or local governmental units by pledging government securities held in the form of an undivided collateral pool. The market value of the pledged securities in the collateral pool must equal at least 110% of the total amount deposited by the public agencies. California law also allows financial institutions to secure City deposits by pledging first trust deed mortgage notes having a value of 150% of the secured public deposits. Such collateral is held by the pledging financial institution’s trust department or agent in the City’s name.

Local Agency Investment Fund (LAIF)

The Agency also maintained cash balances with the State of California Local Agency Investment Fund (LAIF) amounting to $529,974 at June 30, 2008. LAIF is an external investment pool sponsored by the State of California. These pooled funds approximate fair value. The administration of LAIF is provided by the California State Treasurer and regulatory oversight is provided by the Pooled Money Investment Board and the Local Investment Advisory Board. The value of the pool shares in LAIF, which may be withdrawn, is determined on an amortized cost basis, which is different than the fair value of the Agency’s position in the pool.

NOTE 2 – CASH AND INVESTMENTS (CONTINUED)

The total amount invested by all public agencies in LAIF at June 30, 2008 was $25,160,913,446. LAIF is part of the State of California Pooled Money Investment Account (PMIA) whose balance was $70,154,701,610 at June 30, 2008. Of this amount, 11.12% was invested in structures notes and asset-backed securities. PMIA is not SEC-registered, but is required to invest according to California State Code. The average maturity of PMIA investments was 0.58 years as of June 30, 2008. LAIF does not maintain a credit rating.

NOTE 3 - RECEIVABLES

The City's receivables at June 30, 2008 are as follows:

Receivables - Governmental Activities:	General Fund	Redevelopment Agency Fund	Industrial Development Fund	Other Governmental Funds	Total Governmental Activities
Accounts	$ 319,570	$ -	$ 100,000	$ -	$ 419,570
Taxes	77,652	201,230	-	163,504	442,386
Notes or loans	72,276	-	-	-	72,276
Other	1,491,988	-	-	-	1,491,988
Total receivables	$ 1,961,486	$ 201,230	$ 100,000	$ 163,504	$ 2,426,220

Receivables - Business-type Activities:	Light and Power Fund	Gas Fund	Other Enterprise Funds	Total Business-type Activities
Accounts	$ 8,721,157	$ 824,978	$ 358,117	$ 9,904,252
Allowances	(50,000)	-	-	(50,000)
Total receivables	$ 8,671,157	$ 824,978	$ 358,117	$ 9,854,252

NOTE 4 – INTERFUND TRANSACTIONS

The following tables summarize the City's interfund balances and transactions at June 30, 2008:

Due To/From Other Funds

Receivable Fund	Payable Fund	Amount
General Fund	Industrial Development Fund	$ 3,363,528
		$ 3,363,528
General Fund	Light and Power Fund	$ 12,225,254
		$ 12,225,254
Redevelopment Agency Fund	Light and Power Fund	$ 862,611
		$ 862,611
Other Governmental Funds	Light and Power Fund	$ 24,041,683
		$ 24,041,683
Gas Fund	Light and Power Fund	$ 4,022,107
		$ 4,022,107
Other Enterprise Funds	Light and Power Fund	$ 7,551,011
		$ 7,551,011
Internal Service Funds	Light and Power Fund	$ 9,552,340
		$ 9,552,340

The above balances represent interfund borrowings payable due within one year.

Advances to/from other funds

Receivable Fund	**Payable Fund**	**Amount**
Light and Power Fund	General Fund	$ 14,774,667
	Other Governmental Funds	5,979
	Gas Fund	25,238,575
	Other Enterprise Funds	5,301,857
		$ 45,321,078

The above balances represent interfund borrowings payable beyond one year.

NOTE 4 – INTERFUND TRANSACTIONS (CONTINUED)

Transfers

Transfers In	Transfer Out	Amount
General Fund	Light and Power Fund	$ 3,178,597
	Other Enterprise Funds	223,054
		$ 3,401,651
Internal Service Funds	General Fund	$ 685,000
		$ 685,000
Light and Power Fund	Redevelopment Agency Fund	$ 27,754
		$ 27,754
Other Governmental Funds	General Fund	$ 15,824,727
	Industrial Development Fund	1,748,917
		$ 17,573,644

Transfers are used to move revenues from the fund that statute or budget requires to collect them to the fund that statute or budget requires to expend them, or move revenues collected in certain enterprise funds to the General Fund to cover overhead costs provided by the General Fund and for the payment of in-lieu franchise taxes.

For the current year, the Light and Power Fund and the Other Enterprise Funds transferred a total of $3,401,651 for in-lieu franchise taxes.

For the current year, the General Fund transferred $685,000 to the Internal Service Funds for the payment of claims.

For the current year, the Redevelopment Agency Fund transferred $27,754 to the Light and Power Fund for interest rate swap payment made by the Light and Power Fund on behalf of the Redevelopment Agency Fund.

For the current year, the General Fund transferred $15,824,727 and the Industrial Development Fund transferred $1,748,917 to the Other Governmental Funds to close out two inactive Capital Project Funds with deficit balances.

NOTE 5 – CAPITAL ASSETS

Capital asset activity of governmental activities for the fiscal year ended June 30, 2008 was as follows:

	Balance June 30, 2007	Additions	Deletions	Transfers & Adjustments	Balance June 30, 2008
Governmental activities:					
Capital assets, not being depreciated:					
Land - General Fund	$ 28,552,138	$ 1,095	$ (5,794,543)	$ (11,101,848)	$ 11,656,842
Land - Redevelopment Agency Fund (RDA)	12,359,401	26,204,318	-	(11,589,424)	26,974,295
Land - Ind. Dev. Fund	-	23,912	(22,715,184)	22,691,272	-
Total land	40,911,539	26,229,325	(28,509,727)	-	38,631,137
Construction in progress - General Fund	3,424,180	332,250	-	(3,184,074)	572,356
Construction in progress - Ind. Dev. Fund	-	739,314	-	-	739,314
Construction in progress - RDA	962,883	5,764,259	-	(195,896)	6,531,246
Total construction in progress	4,387,063	6,835,823	-	(3,379,970)	7,842,916
Total capital assets, not being depreciated	45,298,602	33,065,148	(28,509,727)	(3,379,970)	46,474,053
Capital assets, being depreciated					
Infrastructure - General Fund	24,385,059	-	-	927,405	25,312,464
Infrastructure - RDA	6,035,517	-	-	195,896	6,231,413
Building and Improvements - General Fund	10,700,246	819,612	-	2,118,624	13,638,482
Improvements O/T Buildings - General Fund	9,432,589	584,074	-	138,045	10,154,708
Improvements O/T Buildings - RDA	12,523	-	-	-	12,523
Machinery and Equipment - General Fund	14,049,438	1,439,362	-	-	15,488,800
Machinery and Equipment - Other Gov't Fund	955,613	67,655	-	-	1,023,268
Total capital assets, being depreciated	65,570,985	2,910,703	-	3,379,970	71,861,658
Less accumulated depreciation for:					
Infrastructure - General Fund	(18,886,273)	(551,002)	-	-	(19,437,275)
Infrastructure - RDA	(98,642)	(134,182)	-	-	(232,824)
Building and Improvements - General Fund	(4,062,674)	(296,661)	-	-	(4,359,335)
Improvements O/T Building - General Fund	(2,256,319)	(242,480)	-	-	(2,498,799)
Improvements O/T Building - RDA	(469)	(313)	-	-	(782)
Machinery and Equipment - General Fund	(8,016,371)	(1,251,256)	-	-	(9,267,627)
Machinery and Equipment - Other Gov't Fund	(284,472)	(79,432)	-	-	(363,904)
Total accumulated depreciation	(33,605,220)	(2,555,326)	-	-	(36,160,546)
Total capital assets, being depreciated, net					
Infrastructure - General Fund	5,498,786	(551,002)	-	927,405	5,875,189
Infrastructure - RDA	5,936,875	(134,182)	-	195,896	5,998,589
Building and Improvements - General Fund	6,637,572	522,951	-	2,118,624	9,279,147
Improvements O/T Building - General Fund	7,176,270	341,594	-	138,045	7,655,909
Improvements O/T Building - RDA	12,054	(313)	-	-	11,741
Machinery and Equipment - General Fund	6,033,067	188,106	-	-	6,221,173
Machinery and Equipment - Other Gov't Fund	671,141	(11,777)	-	-	659,364
Total	31,965,765	355,377	-	3,379,970	35,701,112
Governmental activities capital assets, net	$ 77,264,367	$ 33,420,525	$ (28,509,727)	$ -	$ 82,175,165

In the current year, the General Fund sold one parcel of land which originally cost $5,794,543 for $7,530,785 for a net gain of $1,736,242. In the current year, the Industrial Development Fund purchased a total of $22,691,272 of land from the General Fund and Redevelopment Agency Fund as land held for resale. Additionally, the Industrial Development Fund sold one subdivided parcel of land held for resale which originally cost $1,655,015 for $2,709,586 for a net gain of $1,054,571.

NOTE 5 – CAPITAL ASSETS (CONTINUED)

Depreciation

Depreciation expense was charged to governmental functions as follows:

General government	$ 912,681
Public safety	1,265,165
Public works	289,491
Health services	87,989
Total depreciation expense - governmental functions	$ 2,555,326

NOTE 5 – CAPITAL ASSETS (CONTINUED)

Capital asset activity of business-type activities for the fiscal year ended June 30, 2008 was as follows:

	Balance June 30, 2007	Additions	Deletions	Transfers & Adjustments	Balance June 30, 2008
Business-type activities:					
Capital assets, not being depreciated:					
Land - Water	$ 45,000	$ -	$ -	$ -	$ 45,000
Construction in progress - Light and Power	18,826,527	7,501,849	(4,948,448)	(1,317,292)	20,062,636
Construction in progress - Water	837,262	-	-	(837,262)	-
Construction in progress - Gas	27,193	-	-	(27,193)	-
Construction in progress - Fiber Optic	2,280,221	-	-	(2,280,221)	-
Total capital assets, not being depreciated	22,016,203	7,501,849	(4,948,448)	(4,461,968)	20,107,636
Capital assets, being depreciated					
Production plant - Light and Power	10,852,803	27,211	-	-	10,880,014
Transmission plant - Light and Power	65,815,772	134,798	(65,950,570)	-	-
Distribution plant - Light and Power	110,418,047	9,805,859	-	1,047,756	121,271,662
General plant - Light and Power	5,066,154	352,381	-	269,536	5,688,071
Malburg Generating Station plant - Light and Power	176,143,236	-	(176,143,236)	-	-
Buildings - Light and Power	481,800	-	-	-	481,800
Water utility plant	15,680,761	244,917	-	837,262	16,762,940
Gas utility plant	23,636,903	662,596	-	27,193	24,326,692
Fiber Optic utility plant	753,280	162,029	-	2,280,221	3,195,530
Total capital assets, being depreciated	408,848,756	11,389,791	(242,093,806)	4,461,968	182,606,709
Less accumulated depreciation for:					
Production plant - Light and Power	(7,791,436)	(412,832)	-	-	(8,204,268)
Transmission plant - Light and Power	(32,206,594)	(1,720,559)	33,927,153	-	-
Distribution plant - Light and Power	(27,255,388)	(4,428,892)	-	-	(31,684,280)
General plant - Light and Power	(3,699,382)	(185,852)	-	-	(3,885,234)
Malburg Generating Station plant - Light and Power	(6,605,371)	(3,302,686)	9,908,057	-	-
Buildings - Light and Power	(295,752)	(16,464)	-	-	(312,216)
Water utility plant	(10,908,292)	(392,725)	-	-	(11,301,017)
Gas utility plant	(884,945)	(671,185)	-	-	(1,556,130)
Fiber Optic utility plant	(56,496)	(150,799)	-	-	(207,295)
Total accumulated depreciation	(89,703,656)	(11,281,994)	43,835,210	-	(57,150,440)
Total capital assets, being depreciated, net					
Production plant - Light and Power	3,061,367	(385,621)	-	-	2,675,746
Transmission plant - Light and Power	33,609,178	(1,585,761)	(32,023,417)	-	-
Distribution plant - Light and Power	83,162,659	5,376,967	-	1,047,756	89,587,382
General plant - Light and Power	1,366,772	166,529	-	269,536	1,802,837
Malburg Generating Station plant - Light and Power	169,537,865	(3,302,686)	(166,235,179)	-	-
Buildings - Light and Power	186,048	(16,464)	-	-	169,584
Water utility plant	4,772,469	(147,808)	-	837,262	5,461,923
Gas utility plant	22,751,958	(8,589)	-	27,193	22,770,562
Fiber Optic utility plant	696,784	11,230	-	2,280,221	2,988,235
Total	319,145,100	107,797	(198,258,596)	4,461,968	125,456,269
Business-type activities capital assets, net	$ 341,161,303	$ 7,609,646	$ (203,207,044)	$ -	$ 145,563,905

Transmission plant and Malburg Generating Station plant were sold during the current fiscal year (See further discussion in Note 11).

NOTE 5 – CAPITAL ASSETS (CONTINUED)

Depreciation

Depreciation expense was charged to the business-type functions as follows:

Light and Power depreciation	$	10,067,286
Gas Fund depreciation		671,185
Other Enterprise Fund depreciation		543,523
Total depreciation expense - business-type functions	$	11,281,994

NOTE 6 – LONG-TERM OBLIGATIONS

During the fiscal year 2006, a total of $480,265,000 in long-term obligations were issued consisting of the following:

- $49,420,000 Redevelopment Agency of the City of Vernon Industrial Redevelopment Project Tax Allocation Bonds, Series 2005
- $200,000,000 Vernon Natural Gas Financing Authority Variable Rate Revenue Bonds (Vernon Gas Project), 2006 Series A
- $115,440,000 Vernon Gas Project Variable Rate Revenue Bonds, 2006 Series B
- $115,405,000 Vernon Gas Project Variable Rate Revenue Bonds, 2006 Series C

The Industrial Redevelopment Project Tax Allocation Bonds, Series 2005 were issued to provide funds to (i) finance various redevelopment projects in or benefiting the Agency's Industrial Redevelopment Project area, (ii) fund the reserve requirement for the Series 2005 Bonds, and (iii) pay the costs of issuance related to the Series 2005 Bonds.

The Vernon Gas Project 2006 Variable Rate Revenue Bonds were issued to provide funds to (i) finance a portion of the purchase by the City of a fifteen-year, prepaid supply of natural gas from Citigroup Energy Inc. pursuant to an Agreement for Purchase and Sale of Natural Gas, between the City and Citigroup Energy Inc.; and (ii) pay the costs of issuing the 2006 Bonds.

In September 2007, the City entered into a $50,000,000 revolving line of credit agreement with a bank for the purpose of financing the City's industrial development programs. The termination date of the agreement is September 26, 2009 extendable to September 26, 2010. The interest rate on the loan is Libor Rate plus 2.00%. As of June 30, 2008, $30,273,750 of the line of credit was used for the purposes of acquiring land held for resale.

NOTE 6 – LONG-TERM OBLIGATIONS (CONTINUED)

A summary of bonds payable for governmental and business-type activities is as follows:

Bonds	Maturity	Interest Rates*	Annual Principal Installments	Original Issue Amount	Outstanding at June 30, 2008
RDA Industrial Redevelopment Project Tax Allocation Bonds, 2005 Series	09/01/35	Fixed	To begin 09/01/09: $1,160,000 - $3,460,000	$ 49,420,000	$ 49,420,000
Variable Rate Revenue Bonds (Vernon Gas Project), 2006 Series A	08/01/21	Variable	To begin 08/01/07: $9,950,000 - $17,300,000	200,000,000	190,050,000
Variable Rate Revenue Bonds (Vernon Gas Project), 2006 Series B	08/01/21	Variable	To begin 08/01/07: $5,710,000 - $10,070,000	115,440,000	109,730,000
Variable Rate Revenue Bonds (Vernon Gas Project), 2006 Series C	08/01/21	Variable	To begin 08/01/07: $5,710,000 - $10,070,000	115,405,000	109,695,000
Premium					813,356
Total Revenue Bonds				$ 480,265,000	$ 459,708,356

* Rates on the Series 2005 Bonds are fixed rates ranging from 3.25% to 5.25%. Rates on the 2006A Bonds are based on 5% fixed through August 2009 and Weekly Interest Rate thereafter. Rates on the 2006B and 2006C Bonds are based on a Weekly Interest Rate determined by Citigroup Global Markets, Inc. utilizing best efforts to remarket the 2006B and 2006C Bonds, which are subject to optional and mandatory tender. The City expects to convert the 2006 Series B and C Gas Bonds from Weekly Interest Rate to Fixed Rate to maturity prior to March 1, 2009.

NOTE 6 – LONG-TERM OBLIGATIONS

As of June 30, 2008, annual debt service requirements of business-type activities to maturity are as follows:

	Industrial Redevelopment Project Tax Allocation Bonds Payable	
Year ending June 30:	Principal	Interest*
2009	-	2,275,306
2010	1,160,000	2,256,456
2011	1,285,000	2,216,725
2012	1,380,000	2,171,694
2013	1,160,000	2,127,244
2014-2018	7,150,000	9,796,919
2019-2023	7,665,000	8,078,725
2024-2028	7,850,000	6,283,213
2029-2033	11,960,000	4,011,684
2034-2036	9,810,000	756,000
Total requirements	$ 49,420,000	$ 39,973,966

*As of June 30, 2008, debt service was calculated based upon the fixed coupon rates of the bonds ranging from 3.25% to 5.25%. For additional disclosure on basis swap see Note 7.

	Variable Rate Revenue Bonds Payable	
Fiscal year ending June 30:	Principal	Interest*
2009	$ 22,330,000	$ 22,252,992
2010	23,135,000	20,622,232
2011	24,055,000	15,293,017
2012	24,925,000	14,186,223
2013	26,210,000	13,020,172
2014-2018	147,450,000	45,923,185
2019-2022	141,370,000	10,344,833
Total requirements	$ 409,475,000	$ 141,642,654

*As of June 30, 2008, debt service for 2006 Series A, B, and C was calculated assuming 5.00% for Series 2006A through August 2009 and BMA rate of 1.55% thereafter and 7.00% rate for 2006B and C over the remaining life of the bonds. Does not include net interest rate swaps payment/receipts. For additional disclosure on interest rate swaps see Note 7.

NOTE 6 – LONG-TERM OBLIGATIONS

Changes in long-term liabilities

The following is a summary of long-term liabilities transactions for the fiscal year ended June 30, 2008:

	Balance July 1, 2007	Additions	Reductions	Balance June 30, 2008	Amounts Due Within One Year
Governmental activities:					
Bonds payable	$ 49,420,000	$ -	$ -	$ 49,420,000	$ -
Bond premium	857,701	-	(44,345)	813,356	44,345
Notes payable	-	30,273,750	-	30,273,750	30,273,750
Claims payable	4,552,035	1,605,396	(894,034)	5,263,397	1,754,466
Compensated absences	2,109,353	1,837,061	(2,109,353)	1,837,061	1,837,061
	$ 56,939,089	$ 33,716,207	$ (3,047,732)	$ 87,607,564	$ 33,909,622
Business-type activities:					
Bonds payable	$ 702,295,000	$ -	$ (292,820,000)	$ 409,475,000	$ 22,330,000
Bond discount	(1,485,254)	-	1,485,254	-	-
Deferred amount on refunding	(7,387,000)	-	7,387,000	-	-
Compensated absences	394,736	320,755	(394,736)	320,755	320,755
	$ 693,817,482	$ 320,755	$ (284,342,482)	$ 409,795,755	$ 22,650,755

NOTE 7 – DERIVATIVE INSTRUMENTS

As of June 30, 2008, the City has the following derivative instruments outstanding:

Item	Type	Objective	Notional Amount	Effective Date	Maturity Date	Term	Fair Value
A	Variable to Fixed Swap	Reduce overall exposure to interest rate risk and achieve lower cost of capital for the 2004 Series A Bonds	$ 90,150,000	December 2004	April 2037	Receive 62.87% of LIBOR one-month index plus 0.119%, pay 3.607%	$ (5,429,668)
B	Variable to Fixed Swap	Reduce overall exposure to interest rate risk and achieve lower cost of capital for the 2004 Series B Bonds	83,575,000	December 2004	April 2029	Receive 62.87% of LIBOR one-month index plus 0.119%, pay 3.542%	(3,909,031)
C	Variable to Fixed Swap	Reduce overall exposure to interest rate risk and achieve lower cost of capital for the 2004 Series D Bonds	61,825,000	March 2006	April 2018	Receive 100.00% of LIBOR three-month index, pay 5.227%	(2,295,998)
D	Basis Swap	Reduce interest cost on 2005 Series Bonds	49,420,000	March 2007	September 2035	Receive 67.073% of USD-ISDA ten year swap rate index, pay weekly average BMA	(189,261)
E	Variable to Fixed Swap	Reduce overall exposure to interest rate risk for the 2006 Series A Bonds	200,000,000	June 2006	August 2021	Receive 62.6% of LIBOR one-month index, pay 3.683%	(10,296,283)
F	Variable to Fixed Swap	Reduce overall exposure to interest rate risk for the 2006 Series B and C Bonds	230,845,000	June 2006	August 2021	Receive 64.8% of LIBOR one-month index, pay 3.753%	(11,525,586)
G	Natural Gas Commodity Swap	To adjust the cost of gas from fixed prices to market prices	92,181,397	July 2006	August 2021	Receive fixed natural gas price for notional quantity equal to 25% of monthly quantity deliverable under the gas supply contract with Citigroup Energy, Inc.; pay floating natural gas price	(59,903,859)
H	Derivative Contracts / Futures and Options	To hedge variable price risk associated with the purchase and sale of commodities.	3,549,338	Various	Various	Various	2,922,058

NOTE 7 – DERIVATIVE INSTRUMENTS (CONTINUED)

A - Variable to Fixed Swap – 2004 Series A Bonds

Objective of the interest rate swap: As a means to reducing its overall exposure to interest rate risk and achieving a lower cost of capital relative to long term fixed rate bonds, the City elected to issue its $90,150,000 2004 Series A Electric System revenue bonds (the "2004 Series A Bonds") in a variable rate mode and enter to a fixed payer swap to achieve synthetic fixed debt.

Terms: In December 2004, the City entered into a pay-fixed, receive-variable interest rate swap for the term of the 2004 Series A Bonds. The notional amount of the swap is $90,150,000. Under the original terms of the swap, the City pays the counterparty a fixed rate of 3.637% and receives from the counterparty variable-rate payments equal to 62.87% of the London Interbank Offered Rate (LIBOR) one-month index plus 0.119%. On March 16, 2006, the City amended its fixed payment to 3.607% to the counterparty. In April 2008, the City defeased its 2004 Series A Bonds. The City expects to terminate the swap prior to March 1, 2009.

Fair value: As of June 30, 2008, the swap had a negative fair value of $5,429,668. The fair value was estimated using the zero-coupon method. This method calculates the future net settlement payments required by the swap, assuming that the current forward rates implied by the yield curve correctly anticipate future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for hypothetical zero-coupon bonds due on the date of each future net settlement on the swap.

Credit risk: As the swap's fair value as of June 30, 2008 is negative, the City does not have credit exposure to the counterparty. Should the City's fair value become positive, the City would have credit exposure to the counterparty equal to the fair value amount. As of June 30, 2008, the swap counterparty, Morgan Stanley was rated A+ by Standard & Poor's and Aa3 by Moody's Investors Service. To mitigate the potential for credit risk, if the counterparty's credit quality falls below (BBB/Baa2), the fair value of the swap will be fully collateralized by the counterparty with U.S. government securities. Collateral would be posted with a third-party custodian.

Interest rate risk: The swap increases the City's exposure to interest rate risk. As LIBOR decreases, the City's net payments in the swap increases.

Termination risk: The City or the counterparty may terminate the swap if the other party fails to perform under the terms of the contract. In addition, the City may optionally terminate the agreement on any date. If at the time of termination the swap has a negative fair value, the City would be liable to the counterparty for an amount equal to the negative fair value.

Rollover risk. The City is not exposed to rollover risk on the swap since the term of the swap matched the term of the 2004 Series A Bonds at the time of issuance and the 2004 Series A Bonds were defeased in April 2008.

Swap payments and associated debt: The debt associated with the swap, the 2004 Series A Bonds, has been defeased. The City expects to terminate the swap prior to March 1, 2009.

B - Variable to Fixed Swap – 2004 Series B Bonds

Objective of the interest rate swap: As a means to reducing its overall exposure to interest rate risk and achieving a lower cost of capital relative to long term fixed rate bonds, the City elected to issue its $83,575,000 2004 Series B Electric System revenue bonds (the "2004 Series B Bonds") in a variable rate mode and enter to a fixed payer swap to achieve synthetic fixed debt.

NOTE 7 – DERIVATIVE INSTRUMENTS (CONTINUED)

Terms: In December 2004, the City entered into a pay-fixed, receive-variable interest rate swap for the term of its 2004 Series B Bonds. The notional amount of the swap is $83,575,000. Under the original terms of the swap, the City pays a fixed rate of 3.572% and receives variable-rate payments equal to 62.87% of the London Interbank Offered Rate (LIBOR) one-month index plus .119%. On March 16, 2006, the City revised its fixed payment to 3.542% to the counterparty. In April 2008, the City defeased its 2004 Series B Bonds. The City expects to terminate the swap prior to March 1, 2009.

Fair value: As of June 30, 2008, the swap had a negative fair value of $3,909,031. The fair value was estimated using the zero-coupon method. This method calculates the future net settlement payments required by the swap, assuming that the current forward rates implied by the yield curve correctly anticipate future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for hypothetical zero-coupon bonds due on the date of each future net settlement on the swap.

Credit risk: As the swap's fair value as of June 30, 2008 is negative, the City does not have credit exposure to the counterparty. Should the City's fair value become positive, the City would have credit exposure to the counterparty equal to the fair value amount. As of June 30, 2008, the swap counterparty, Morgan Stanley was rated A+ by Standard & Poor's and Aa3 by Moody's Investors Service. To mitigate the potential for credit risk, if the counterparty's credit quality falls below (BBB/Baa2), the fair value of the swap will be fully collateralized by the counterparty with U.S. government securities. Collateral would be posted with a third-party custodian.

Interest rate risk: The swap increases the City's exposure to interest rate risk. As LIBOR decreases, the City's net payments in the swap increases.

Termination risk: The City or the counterparty may terminate the swap if the other party fails to perform under the terms of the contract. In addition, the City may optionally terminate the agreement on any date. If at the time of termination the swap has a negative fair value, the City would be liable to the counterparty for an amount equal to the negative fair value.

Rollover risk. The City is not exposed to rollover risk on the swap since the term of the swap matched the term of the 2004 Series B Bonds at the time of issuance and the 2004 Series B Bonds were defeased in April 2008.

Swap payments and associated debt: The debt associated with the swap, the 2004 Series B Bonds, has been defeased. The City expects to terminate the swap prior to March 1, 2009.

C - Variable to Fixed Swap – 2004 Taxable Series D Bonds

Objective of the interest rate swap: As a means to reducing its overall exposure to interest rate risk, the City elected to enter into a fixed payer swap to achieve synthetic fixed debt with respect to its $69,100,000 2004 Taxable Series D Electric System revenue bonds (the "2004 Taxable Series D Bonds") issued in a variable rate mode.

Terms: On March 16, 2006, the City entered into a pay-fixed, receive-variable interest rate swap for the term of its 2004 Taxable Series D Bonds. The notional amount of the swap is $61,825,000. Under the terms of the swap, the City pays a fixed rate of 5.227% and receives variable-rate payments equal to 100.00% of the London Interbank Offered Rate (LIBOR) three-month index. In April 2008, the City defeased its 2004 Taxable Series D Bonds. The City expects to terminate the swap prior to March 1, 2009.

Fair value: As of June 30, 2008, the swap had a negative fair value of $2,295,998. The fair value was estimated using the zero-coupon method. This method calculates the future net settlement payments required by the swap, assuming that the current forward rates implied by the yield curve correctly anticipate future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for hypothetical zero-coupon bonds due on the date of each future net settlement on the swap.

NOTE 7 – DERIVATIVE INSTRUMENTS (CONTINUED)

Credit risk: As the swap's fair value as of June 30, 2008 is negative, the City does not have credit exposure to the counterparty. Should the City's fair value become positive, the City would have credit exposure to the counterparty equal to the fair value amount. As of June 30, 2008, the swap counterparty, Morgan Stanley was rated A+ by Standard & Poor's and Aa3 by Moody's Investors Service. To mitigate the potential for credit risk, if the counterparty's credit quality falls below (BBB/Baa2), the fair value of the swap will be fully collateralized by the counterparty with U.S. government securities. Collateral would be posted with a third-party custodian.

Interest rate risk: The swap increases the City's exposure to interest rate risk. As LIBOR decreases, the City's net payments in the swap increases.

Termination risk: The City or the counterparty may terminate the swap if the other party fails to perform under the terms of the contract. In addition, the City may optionally terminate the agreement on any date. If at the time of termination the swap has a negative fair value, the City would be liable to the counterparty for an amount equal to the negative fair value.

Rollover risk. The City is not exposed to rollover risk on the swap since the term of the swap matched the term of the 2004 Taxable Series D Bonds at the time of issuance and the 2004 Taxable Series D Bonds were defeased in April 2008.

Swap payments and associated debt: The debt associated with the swap. 2004 Taxable Series D Bonds, has been defeased. The City expects to terminate the swap prior to March 1, 2009.

D - Basis Swap – Series 2005

Objective of the interest rate swap: As a means to reduce its bond interest cost, the Agency entered into an interest basis swap in connection with its $49,420,000 Industrial Redevelopment Project Tax Allocation Bonds, Series 2005 (the "Series 2005 Bonds").

Terms: As structured, the Series 2005 Bonds and the related swap agreement mature on September 1, 2035, and the swap's aggregate notional amount of $49,420,000 million matches the par amount of the Series 2005 Bonds. The swap was entered into on March 1, 2007. Under the swap, the Agency pays the counterparty payments equal to the average of the weekly Bond Market Association (BMA) variable rate index and receives payments equal to 67.073% of the USD-ISDA (ISDA) ten-year swap rate index.

Fair value: Because the differential between the BMA index and ISDA index has decreased since execution of the swap, the swap has an aggregate negative fair value of $189,261 as of June 30, 2008. The fair value was estimated using the zero-coupon method. This method calculates the future net settlement payments required by the swap, assuming that the current forward rates implied by the yield curve correctly anticipate future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for hypothetical zero-coupon bonds due on the date of each future net settlement on the swap.

Credit risk: As the swap's fair value as of June 30, 2008 was negative, the Agency does not have credit exposure to the counterparty. Should the swap's fair value become positive, the Agency would have credit exposure to the counterparty equal to the fair value amount. The swap counterparty, Lehman Brothers, was rated A+ by Fitch Ratings and A1 by Moody's Investors Service as of June 30, 2008. To mitigate the potential for credit risk, if the counterparty's credit quality falls below "A-" or "A3", the fair value of the swap will be fully collateralized by the counterparty with U.S. government securities. Collateral would be posted with a third-party custodian.

Basis risk: The swap exposes the Agency to basis risk should the relationship between ISDA index and BMA index diverge to a ratio lower than that stated in the swap. If such a change occurs, the swap may not provide the expected interest cost savings.

NOTE 7 – DERIVATIVE INSTRUMENTS (CONTINUED)

Termination risk: The Agency or its counterparty may terminate the swap if the other party fails to perform under the terms of the contract. The swap may be terminated by the Agency at any time. If at the time of termination, the swap has a negative fair value, the Agency would be liable to the counterparty for a payment equal to the swap's fair value.

Rollover risk. The Agency is not exposed to rollover risk since the term of the swap matches the term of the Series 2005 Bonds at the time of issuance.

The following summarizes the expected net debt service if BMA remains constant 1.55% and 10 Year ISDA remains constant at 4.75% (actual rates as of June 30, 2008).

Year Ending June 30	Principal Amount	Interest	Basis Swap, Net	Total Debt Service
2009	$ -	$ 2,275,306	$ (808,495)	$ 1,466,811
2010	1,160,000	2,256,456	(799,007)	2,617,449
2011	1,285,000	2,216,725	(779,007)	2,722,718
2012	1,380,000	2,171,694	(757,208)	2,794,486
2013	1,160,000	2,127,244	(736,431)	2,550,813
2014-2018	7,150,000	9,796,919	(3,348,498)	13,598,421
2019-2023	7,665,000	8,078,725	(2,729,734)	13,013,991
2024-2028	7,850,000	6,283,213	(2,121,604)	12,011,609
2029-2033	11,960,000	4,011,684	(1,325,134)	14,646,550
2034-2036	9,810,000	756,000	(247,358)	10,318,642
	$ 49,420,000	$ 39,973,966	$ (13,652,476)	$ 75,741,490

E - Variable to Fixed Swap – 2006 Series A Gas Bonds

Objective of the interest rate swap: As a means to reducing its overall exposure to interest rate risk, the Vernon Natural Gas Financing Authority elected to enter into a fixed payer swap to achieve synthetic fixed debt with respect to its $200,000,000 Variable Rate Revenue Bonds (Vernon Gas Project), 2006 Series A (the "2006 Series A Gas Bonds") issued in a variable rate mode.

Terms: The City entered into four (4) pay-fixed, receive-variable interest rate swaps for the term of its 2006 Series A Gas Bonds. The notional amounts of each of the four (4) swaps is $50,000,000. Under the terms of the swaps, the City pays a fixed rate of 3.683% and receives variable-rate payments equal to 62.6% of the London Interbank Offered Rate (LIBOR) one month index. The City expects that the variable-rate payments from the swaps will approximate the interest payments on the 2006 Series A Gas Bonds. The notional amount of the swaps and the amortization of the principal of the 2006 Series A Gas Bonds are exactly matched.

Fair value: As of June 30, 2008, the swaps had a negative fair value of $10,296,283. The fair value was estimated using the zero-coupon method. This method calculates the future net settlement payments required by the swap, assuming that the current forward rates implied by the yield curve correctly anticipate future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for hypothetical zero-coupon bonds due on the date of each future net settlement on the swap.

NOTE 7 – DERIVATIVE INSTRUMENTS (CONTINUED)

Credit risk: As the swap's fair value as of June 30, 2008 is negative, the City does not have credit exposure to the counterparty. Should the City's fair value become positive, the City would have credit exposure to the counterparty equal to the fair value amount. As of June 30, 2008, the swap counterparty, Citibank, N.A. was rated AA by Standard & Poor's and Aa1 by Moody's Investors Service. To mitigate the potential for credit risk, if the counterparty's credit quality falls below (A-/A3), the fair value of the swap will be fully collateralized by the counterparty with U.S. government securities. Collateral would be posted with a third-party custodian.

Interest rate risk: The swap is structured to reduce the City's exposure to interest rate risk.

Basis risk: The swap exposes the City to basis risk should the relationship between LIBOR and BMA converge to a ratio higher than variable leg of the swap.

Termination risk: The City or the counterparty may terminate the swap if the other party fails to perform under the terms of the contract. In addition, the City may optionally terminate the agreement on any date. If at the time of termination the swap has a negative fair value, the City would be liable to the counterparty for an amount equal to the negative fair value.

Rollover risk. The City is not exposed to rollover risk on the swap since the term of the swap matched the term of the 2006 Series A Gas Bonds.

Swap payments and associated debt: It is expected that the variable payments received by the City on the swap will approximate the variable interest payments on the 2006 Series A Gas Bonds, resulting in the City's net interest exposure being equaled to the fixed payment on the swap to the counterparty. Because the variable payments on the 2006 Series A Gas Bonds and the swap are on different bases, some basis differential is expected from time to time.

The following summarizes the expected net debt service if BMA remains constant 1.55% and 1 Month LIBOR remains constant at 2.4625% (actual rates as of June 30, 2008). In addition, interest is assumed to be 5.00% for Series 2006 A through August 2009 and BMA rate of 1.55% thereafter.

June 30	Amount	Interest	Swap, Net	Debt Service
2009	$ 10,400,000	$ 7,658,750	$ 3,865,719	$ 21,924,469
2010	10,775,000	6,890,682	3,635,645	21,301,327
2011	11,200,000	2,458,429	3,396,558	17,054,987
2012	11,650,000	2,278,435	3,147,879	17,076,314
2013	12,175,000	2,090,401	2,888,091	17,153,492
2014-2018	68,450,000	7,364,502	10,174,772	85,989,274
2019-2022	65,400,000	1,654,625	2,286,025	69,340,650
	$ 190,050,000	$ 30,395,824	$ 29,394,689	$ 249,840,513

F - Variable to Fixed Swap – 2006 Series B and C Gas Bonds

Objective of the interest rate swap: As a means to reducing its overall exposure to interest rate risk, the Vernon Natural Gas Financing Authority elected to enter into a fixed payer swap to achieve synthetic fixed debt with respect to its $115,440,000 Variable Rate Revenue Bonds (Vernon Gas Project), 2006 Series B and $115,405,000 Variable Rate Revenue Bonds (Vernon Gas Project), 2006 Series C (the "2006 Series B and C Gas Bonds") issued in a variable rate mode.

NOTE 7 – DERIVATIVE INSTRUMENTS (CONTINUED)

Terms: The City entered into a pay-fixed, receive-variable interest rate swap for the term of its 2006 Series B and Series C Gas Bonds. The notional amount for the swap is $230,845,000. Under the terms of the swap, the City pays a fixed rate of 3.753% and receives variable-rate payments equal to 64.8% of the London Interbank Offered Rate (LIBOR) one month index. The notional amount of the swaps and the amortization of the principal of the 2006 Series B and Series C Gas Bonds are exactly matched. The City expects to convert the 2006 Series B and C Gas Bonds from Weekly Interest Rate to Fixed Rate to maturity prior to March 1, 2009. Upon such conversion to Fixed Rate bonds, the City will terminate the 2006 Series B and C Gas Bonds interest rate swap.

Fair value: As of June 30, 2008, the swaps had a negative fair value of $11,525,586. The fair value was estimated using the zero-coupon method. This method calculates the future net settlement payments required by the swap, assuming that the current forward rates implied by the yield curve correctly anticipate future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for hypothetical zero-coupon bonds due on the date of each future net settlement on the swap.

Credit risk: As the swap's fair value as of June 30, 2008 is negative, the City does not have credit exposure to the counterparty. Should the City's fair market value become positive, the City would have credit exposure to the counterparty equal to the fair value amount. As of June 30, 2008, the swap counterparty, Citibank, N.A. was rated AA by Standard & Poor's and Aa1 by Moody's Investors Service. To mitigate the potential for credit risk, if the counterparty's credit quality falls below (A-/A3), the fair value of the swap will be fully collateralized by the counterparty with U.S. government securities. Collateral would be posted with a third-party custodian.

Interest rate risk: The swap is structured to reduce the City's exposure to interest rate risk.

Basis risk: The swap exposes the City to basis risk should the relationship between LIBOR and BMA converge to a ratio higher than variable leg of the swap.

Termination risk: The City or the counterparty may terminate the swap if the other party fails to perform under the terms of the contract. In addition, the City may optionally terminate the agreement on any date. If at the time of termination the swap has a negative fair value, the City would be liable to the counterparty for an amount equal to the negative fair value.

Rollover risk. The City is not exposed to rollover risk on the swap since the term of the swap matched the term of the 2006 Series B and C Gas Bonds.

Swap payments and associated debt: It is expected that the variable payments received by the City on the swap will approximate the variable interest payments on the 2006 Series B and Series C Gas Bonds, resulting in the City's net interest exposure being equaled to the fixed payment on the swap to the counterparty. Because the variable payments on the 2006 Series B and C Gas Bonds and the swap are on different bases, some basis differential is expected from time to time.

NOTE 7 – DERIVATIVE INSTRUMENTS (CONTINUED)

The following summarizes the expected net debt service if BMA remains constant 1.55% and 1 Month LIBOR remains constant at 2.4625% (actual rates as of June 30, 2008). In addition, interest is assumed to be 7.00% over the remaining life of the bonds.

June 30	Amount	Interest	Swap, Net	Debt Service
2009	$ 11,930,000	$ 14,594,242	$ 4,497,737	$ 31,021,979
2010	12,360,000	13,731,550	4,231,868	30,323,418
2011	12,855,000	12,834,588	3,955,437	29,645,025
2012	13,275,000	11,907,788	3,669,810	28,852,598
2013	14,035,000	10,929,771	3,368,399	28,333,170
2014-2018	79,000,000	38,558,683	11,883,235	129,441,918
2019-2022	75,970,000	8,690,208	2,678,198	87,338,406
	$ 219,425,000	$ 111,246,830	$ 34,284,684	$ 364,956,514

G - Natural Gas Commodity Swap

The Vernon Natural Gas Financing Authority issued its Revenue Bonds (Vernon Gas Project) 2006 Series A, B and C to finance the cost of acquiring a fixed quantity of natural gas to be delivered over a fifteen year period by Citigroup Energy, Inc. under an Agreement for Purchase and Sale of Natural Gas, the gas supply contract. In connection with the gas supply contract, the City entered into a natural gas commodity swap agreement with a counterparty Societe Generale' to adjust the cost of gas from fixed prices to market prices. The counterparty under such natural gas commodity swap was rated "Aa2" by Moody's and "AA-" by S&P as of June 30, 2008.

Under the terms of the natural gas commodity swap, the City will pay a floating natural gas price over fifteen years and receive a fixed natural gas price for a notional quantity equal to 25% of the monthly quantity of natural gas supplied under the gas supply contract with Citigroup Energy, Inc. The natural gas commodity swap was entered into in July 2006.

The natural gas commodity swap addresses the termination payments received or payable by the City in the event the termination of the natural gas commodity swap apart from or in connection with the termination of the gas supply contract. In the event of termination, the natural gas commodity swap has provisions whereby the City may have to make a termination payment to the counterparty.

For the fiscal year ended June 30, 2008, the City was a net payor under the natural gas commodity swap in the amount of $354,434. As of June 30, 2008, the fair value of the natural gas commodity swap was negative $59,903,859. The fair value was based on the estimated forward curve for natural gas at the delivery points set forth in the gas supply contract.

H - Derivative Contracts / Futures and Options

The City’s Light and Power Fund (Fund), which accounts for the maintenance and operations of the City’s electric utility plant, enters into contracts for electricity and natural gas to meet the expected needs of its retail customers. The Fund also sells excess electricity capacity during periods when it is not needed to meet its retail requirements. Derivative contracts (futures and options) designated as cash flow hedges are entered into by the Fund to hedge variable price risk associated with the purchase and sale of commodities. At June 30, 2008, the Fund’s derivative contracts cost totaled $3,549,338. The fair value of the derivative instruments at June 30, 2008 totaled $2,922,058.

NOTE 7 – DERIVATIVE INSTRUMENTS (CONTINUED)

I - Change in Fair Value of Derivative Instruments

The fair value balances and notional amounts of derivative instruments outstanding at June 30, 2008, classified by type, and the change in fair value of such derivative instruments for the year then ended as reported in the current financial statements are as follows:

	Change in Fair Value		Fair Value at June 30, 2008		
	Classification	Amount	Classification	Amount	Notional
Governmental activities					
Hedging derivative instrument					
Cash flow hedge					
Basis Swap - Series 2005	Increase in fair value	$ 66,480	Derivative liability	$ (189,261)	$ 49,420,000
Business-type activities					
Hedging derivative instruments					
Cash flow hedge					
Variable to Fixed Swaps					
2004 Series A Bonds	Decrease in fair value	(6,725,916)	Derivative liability	(5,429,668)	90,150,000
2004 Series B Bonds	Decrease in fair value	(5,158,989)	Derivative liability	(3,909,031)	83,575,000
2004 Series D Bonds	Decrease in fair value	(3,134,471)	Derivative liability	(2,295,998)	61,825,000
2006 Series A Gas Bonds	Decrease in fair value	(7,362,396)	Derivative liability	(10,296,283)	200,000,000
2006 Series B and C Gas Bonds	Decrease in fair value	(9,412,856)	Derivative liability	(11,525,586)	230,845,000
Natural Gas Commodity Swap	Deferred outflow	59,903,859	Derivative liability	(59,903,859)	92,181,397
Investing derivative instruments					
Derivative Contracts /					
Futures and Options	Increase in fair value	1,424,920	Derivative asset	2,922,058	3,549,338

The change in fair value adjusted to beginning net assets is discussed in Note 16. The change in fair value subsequent to June 30, 2008 is discussed in Note 15.

NOTE 8 – RISK MANAGEMENT

The City is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; natural disasters; unemployment coverage, and providing health benefits to employees, retirees, and their dependents. The City is self-insured for its general liability, workers' compensation, and property liability. The City has chosen to establish risk financing Internal Service Funds, whereby assets are set aside for claim settlements associated with the above risks of loss up to certain limits.

The City has obtained various insurance policies that provide coverage for "Special Form Perils" against direct physical loss or damage, including earthquake and flood, to all real and personal property of the City, including equipment, business and revenue interruption, errors and omissions, boiler and machinery and pollution legal liability. The flood portion of the policies have a 5% deductible of the total insurable values per building, structure or covered item at the time and place of loss. In the most recent "Statement of Values" for the City, real and personal property total insured values equaled $154,419,000.

Property insurance has been distinguished by "Utility" and "Non-utility" assets. Excess utility insurance is provided by the Commonwealth Insurance Company and Liberty International. The total value of insured utility assets is $55,189,000. Non-utility insurance is provided by the Lexington Insurance Company and Landmark American Insurance Company. The total value of insured non-utility assets is $99,230,000.

Crime (Employee Theft and, Depositors Forgery and Alteration, and Computer and Funds Transfer Fraud) coverage in also in force with a limit $100,000 for each line of coverage.

NOTE 8 – RISK MANAGEMENT (CONTINUED)

The City is self insured for the first $1,000,000 of workers' compensation claims and for the first $2,000,000 of its general liability coverage. Southern California Risk Managers Association (SCRMA) is the Third Party Administrator for the City's workers compensation claims. The City self administers its general liability claims. Loss run reports for workers compensation and general liability are provided by SCRMA.

Excess liability coverage is provided by a stand alone policy purchased by the City. Excess coverage is provided by the Insurance Company of Pennsylvania. Excess workers compensation coverage is provided by a stand alone policy purchased through ACE American Insurance Company. The insurance limits are as follows:

		Excess	
Type of Coverage	Self-Insured Retention	Limit	Carrier
General Liability	$2,000,000	Up to $20,000,000	Insurance Co. of the State of PA
Excess Workers' Compensation	$1,000,000	Up to $50,000,000	ACE American Insurance Co.
Property:	$500,000 (Deductible)		
Blanket Building & Contents		Up to $200,000,000	Lloyds of London, Commonwealth, Liberty Mutual, and Allianz
Flood Sublimit – Annual		Up to $50,000,000	Lloyds of London
Electronic Data Processing		Up to $5,000,000	Lloyds of London
Equipment:			
Unscheduled Locations		Up to $1,000,000	Lloyds of London
Machinery Breakdown		Included	Lloyds of London

Amounts in excess of these limits are self-insured. There have been no significant reductions of coverage from the prior year. There have been no settlements exceeding insurance coverage for each of the past three fiscal years.

The unpaid claims liabilities included in each of the self-insurance Internal Service Funds are based on the results of actuarial studies and third-party administrator claim reports and include amounts for claims incurred but not reported, including loss adjustment expenses. Claims liabilities are calculated considering the effects of inflation and recent claim settlement trends, including frequency and amount of payouts and other economic and social factors.

Changes in the balances of claims liabilities during the past two fiscal years for all self-insurance funds combined are as follows:

	Fiscal Year Ended June 30	
	2008	2007
Claims payable, beginning of fiscal year	$ 4,552,035	$ 7,358,573
Incurred claims	1,605,396	992,028
Claims payments and adjustments	(894,034)	(3,798,566)
Claims payable, end of fiscal year	$ 5,263,397	$ 4,552,035

NOTE 9 – PENSION PLAN

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

NOTE 9 – PENSION PLAN (CONTINUED)

All full-time safety (police and fire personnel) and miscellaneous personnel and temporary or part-time employees who have worked 1,000 hours in a fiscal year are eligible to participate in the PERS. Benefits vest after five years of service. Employees who retire at age 50 with five years of credited service are entitled to retirement benefits. Monthly retirement benefits are based on an employee's average compensation for his or her single highest year of compensation for each year of credited service.

Miscellaneous members with five years of credited service may retire at age 55 with full benefits based on a benefit factor derived from the "2.7% at 55 Miscellaneous Factor" benefit factor table and between age 50 and 54 with reduced retirement benefits. Safety members may retire at age 50 with full benefits based on a benefit factor derived from the "3% at 50 Safety Factor" for Police Department Employees and "3% at 50 Safety Factor" for Fire Department Employees benefit factor table with five years of credited service. The PERS also provides death and disability benefits. These benefit provisions and all other requirements are established by State statute and City ordinance.

The City's plan does not issue a stand-alone financial report but is included in the PERS report, which can be obtained from PERS at Lincoln Plaza, 400 P Street, Sacramento, California 95814.

The State-required City employee salary contributions of 8% for miscellaneous employees and 9% for safety members are subsidized by the City. The City is required to contribute the remaining amounts necessary to fund the benefits for its members, using the actuarial basis adopted by the PERS Board of Administration.

The City's total contribution to the PERS for the year ended June 30, 2008 was $6,007,916. City contribution rates as a percentage of covered payroll were 7.086% for miscellaneous plan members and 17.958% for safety plan members.

The City's contribution was made in accordance with actuarially determined requirements based on an actuarial valuation performed as of June 30, 2006.

The PERS uses the entry age normal actuarial cost method, which is a projected benefit cost method that takes into account those benefits expected to be earned in the future as well as those already accrued. According to this cost method, the normal cost for an employee is the level amount that would fund the projected benefit if it were paid annually from the date of employment until retirement. The PERS uses a modification of the entry age normal cost method whereby the employer's total normal cost is expressed as a level percentage of payroll. Unfunded liabilities are amortized over a closed, 20-year period.

Significant actuarial assumptions used in the valuation included (a) a rate of return on the investment of present and future assets of 7.75% a year, compounded annually; (b) overall payroll growth of 3.25%, compounded annually; and (c) a merit scale varying by duration of employment coupled with an assumed annual inflation growth of 3.00% and an annual production growth of 0.25%.

The actuarial value of assets was determined using techniques that smooth the effects of short-term volatility in the market value of investments over a 15 year period.

NOTE 9 – PENSION PLAN (CONTINUED)

Trend information for the current and two preceding fiscal years is as follows:

Fiscal Year Ended June 30	Annual Pension Cost (APC)	Amount Contributed	Percentage of APC Contributed	Net Pension Obligation
2008	$ 6,007,916	$ 6,007,916	100%	-
2007	4,919,700	4,919,700	100%	-
2006	5,792,468	5,792,468	100%	-

The following schedules present the funded status as of June 30, 2006, the most recent actuarial valuation date (dollar amounts in millions).

Safety Plan Schedule of Funding Progress

Valuation Date	Actuarial Accrued Liability (AAL) (a)	Actuarial Value of Assets (b)	Unfunded (Overfunded) UAAL (OAAL) (a)–(b)	Funded Ratio (b)/(a)	Annual Covered Payroll (c)	UAAL (OAAL) as a % of Covered Payroll [(a)–(b)]/(c)
6/30/2006	$130,796,720	$117,846,016	$12,950,704	90.1%	$11,081,334	116.9%

Miscellaneous Plan Schedule of Funding Progress

Valuation Date	Actuarial Accrued Liability (AAL) (a)	Actuarial Value of Assets (b)	Unfunded (Overfunded) UAAL (OAAL) (a)–(b)	Funded Ratio (b)/(a)	Annual Covered Payroll (c)	UAAL (OAAL) as a % of Covered Payroll [(a)–(b)]/(c)
6/30/2006	$72,037,986	$73,178,437	($1,140,451)	101.6%	$10,818,668	(10.5%)

The schedules of funding progress, presented as required supplemental information following the notes to the financial statements, provides multi-year trend information based on the three most recent actuarial valuations and shows information about progress made in accumulating sufficient assets to pay benefits when due.

NOTE 10 – DEFICITS IN FUND EQUITY

The Community Development Block Grant Fund has a deficit of $20,853 at June 30, 2008, which will be recovered from future grants or future transfers from the General Fund.

The Gas Enterprise Fund has a deficit of $4,275,037 at June 30, 2008, which will be recovered from future operating revenues from customers.

The Fiber Optic Other Enterprise fund has a deficit of $175,229 at June 30, 2008, which will be recovered from future operating revenues from customers.

The Group Medical Insurance Fund has a deficit of $483,206 at June 30, 2008. To the extent such deficit is attributed to shortfalls in charges to other funds, such deficit will be recovered through future rate increases and transfers from the General Fund.

NOTE 10 – DEFICITS IN FUND EQUITY (CONTINUED)

The Group Dental Insurance Internal Service Fund has a deficit of $268,487 at June 30, 2008. To the extent such deficit is attributed to shortfalls in charges to other funds, such deficit will be recovered through future rate increases and transfers from the General Fund.

NOTE 11 – LIGHT AND POWER OPERATIONS AND COMMITMENTS

Asset Sale and Bond Redemption – Special Items

On December 13, 2007, the City entered into an Amended and Restated Purchase and Sale Agreement (the "Bicent Agreement"), with Bicent (California) Power LLC ("Bicent"), which is an affiliate of Bicent Holdings and Natural Gas Partners, to sell to Bicent the Malburg Generating Station ("MGS") and the economic burdens and benefits of the City's interests in 22 MW from the Hoover Dam Uprating Project for $287,500,000. This transaction closed on April 10, 2008.

Bicent has agreed to sell the capacity and the energy of the MGS to the City on the terms set forth in a Power Purchase Tolling Agreement, by and between the City and Bicent, dated as of April 10, 2008 (the "PPTA"). In addition, Bicent has acquired the benefits and burdens of the City's interest in the Hoover Uprating Project (described below) on the terms set forth in the Hoover Contract for Differences ("CFD"), between Bicent (California) Hoover LLC, a Delaware limited liability company ("BCH") and the City, dated as of April 10, 2008 (the "Hoover Differences Contract"). Pursuant to the Bicent Agreement, Bicent has assigned its rights and obligations with respect to the MGS to its affiliate, Bicent (California) Malburg LLC, a Delaware limited liability company ("BCM"). Pursuant to the Bicent Agreement, Bicent has assigned its rights and obligations with respect to the economic benefits and burdens of the Hoover Uprating Project to its affiliate, BCH. The City treated the PPTA as an asset lease-back transaction by deferring most of the gain from the sale of MGS to be amortized over the 15 year life of the PPTA. The City also deferred the gain from the CFD to be amortized over the 10 year life of the CFD. As of June 30, 2008, a deferred gain of $81,839,411 remains to be amortized over the life of the PPTA and CFD which will be amortized in proportion to the capacity payments the City will be making under the PPTA and CFD.

In a separate transaction, the City entered into a Purchase and Sale Agreement on September 28, 2007 with the Transmission Agency of Northern California for the purchase of the City's interest in the California Oregon Transmission Project (the "TANC Agreement") for $55,000,000. This transaction closed on April 3, 2008.

Additionally, in a separate transaction, the City sold its interests in the Mead-Adelanto Transmission Project and the Mead-Phoenix Transmission Project pursuant to a Purchase and Sale Agreement dated, as of December 13, 2007, with Starwood Energy Infrastructure Fund, L.P. (the "Starwood Agreement") for $39,500,000. This transaction closed on April 22, 2008.

After netting the sales proceeds with the book basis of the assets sold, selling costs, and deferred gain, the City recognized a $1,488,234 gain from the Bicent Agreement and a $62,603,465 gain from the TANC and the Starwood Agreements for a total of $64,091,699 in the current year.

The City used the proceeds from the sale of the Electric System assets described above, and other available funds, to redeem the 2004 Series A, B, C and D Bonds, provide funds for economic development in the City, and increase the Electric System's cash reserves. Approximately $39,250,000 of such reserves will be used by the City to make a portion of the payments under the PPTA over the first four years of the contract.

NOTE 11 – LIGHT AND POWER OPERATIONS AND COMMITMENTS (CONTINUED)

After the completion of the sale of the City's interests in the California Oregon Transmission Project, Mead-Adelanto Transmission Project and the Mead-Phoenix Transmission Project, the City no longer owns any transmission facilities outside of the City and no longer receives Transmission Revenue Requirements ("TRR") relating to such assets. The City continues to receive TRR associated with existing transmission service contracts with Edison and the Los Angeles Department of Water and Power ("LADWP").

The City's Electric System continues to include ownership interests or capacity rights in other electric facilities and the electric transmission and distribution system within the boundaries of the City. The City currently operates and maintains the Electric System facilities located within the City, except that Petrelli Electric Inc. currently maintains the City's electric distribution system under contract with the City.

Deregulation

Effective April 1, 1998, competition was introduced into California's electricity market, and customers of the state's investor-owned utilities (IOUs) became eligible for direct access. The implementation of competition in accordance with State Assembly Bill 1890 (AB1890) resulted in significant structural changes to the electric power industry, including mandated direct access for IOU customers, energy sales through the California Power Exchange ("CPX"), and management of transmission assets through an Independent System Operator ("ISO"). The original deregulation legislation applied to the State's IOUs and did not compel participation by publicly owned utilities, such as the City's electric utility.

During fiscal year 2001, the City made sales of energy to CPX. CPX made minimal payments on those sales and filed for protection under Chapter 11 of the Federal Bankruptcy Code in January 2001. As of June 30, 2008, the CPX statements show that a total of $3,664,884 was due to the City from CPX. The City wrote-off this receivable as of June 30, 2008 and the basis of the write-off is further discussed Note 13.

Participating Transmission Owner

On August 30, 2000, the City filed a petition for declaratory order with the Federal Energy Regulatory Commission ("FERC") requesting a determination by the FERC that the City's Transmission Revenue Requirement ("TRR"), as approved by its rate setting body, the City Council, is proper for purposes of the City becoming a Participating Transmission Owner ("PTO") in the California ISO. The FERC issued its order accepting the City's petition, with certain modification, on October 20, 2000. Certain aspects of the FERC order were challenged by some of the State's other PTOs. A federal appeals court ruled that the way the FERC arrived at its decision was improper and remanded the case back to the FERC for further proceedings. The City's outcome of these proceedings is discussed at Note 13. As a PTO, the City turned over operational control of its transmission entitlements to the ISO effective January 1, 2001 and shall be reimbursed based upon its TRR by the ISO through the ISO's collection of a transmission access charge ("TAC").

On December 21, 2000, the ISO filed, on behalf of itself and the PTOs, a number of changes to its Transmission Control Agreement ("TCA") to recognize Vernon's application to become a PTO. The ISO also filed revisions to identify the transmission interests that the City will be turning over to the ISO's operational control and the inclusion of an explicit contractual provision to ensure that all PTOs, including an entity such as the City, which is not subject to the rate jurisdiction or refund jurisdiction of FERC under sections 205 and 206 of the Federal Power Act ("FPA"), make appropriate refunds or payment adjustments to implement any relevant FERC order applicable to them.

NOTE 11 – LIGHT AND POWER OPERATIONS AND COMMITMENTS (CONTINUED)

Project Commitments

A. Southern California Public Power Authority

In 1980, the City entered into a joint powers agreement with nine (9) Southern California cities and an irrigation district to form the Southern California Public Power Authority (the "Authority"). The Authority's purpose is the planning, financing, acquiring, constructing and operating of projects that generate or transmit electric energy.

The Authority purchased a 5.91% interest in the Palo Verde Nuclear Generating Station (the "Station"), a nuclear-fired generating station near Phoenix, Arizona, from the Salt River Project Agricultural Improvement and Power District, and a 6.55% share of the right to use certain portions of the Arizona Nuclear Power Project Valley Transmission System. The City has a 4.9% entitlement share of the Authority's interest in the station.

Between 1983 and 2002, the Authority issued $3.166 billion in debt of Power Project Revenue Bonds for the Station to finance the bonds and the purchase of the Authority's share of the Station and related transmission rights. The bonds are not obligations of any member of the Authority or public agency other than the Authority. Under a power sales contract with the Authority, the City is obligated on a "take or pay" basis for its proportionate share of power generated, as well as to make payments for its proportionate share of the operating and maintenance expenses of the Station, debt service on the bonds and any other debt, whether or not the project or any part thereof or its output is suspended, reduced or terminated. The City's proportionate share of costs during fiscal year 2008 was $3,959,830.

B. Hoover Dam Power Plant Upgrade Program

In January 1987, the City entered into a contract with the Federal Bureau of Reclamation to fund part of an upgrading program of the Hoover Dam power plant to increase the plant's generating capacity. In exchange, the City will receive its pro rata share of the additional power produced. Total program costs are estimated to be $155 million.

As of June 30, 2008, the City's total advances were $6,690,998 for the upgrading program. At June 30, 2008, the outstanding note receivable was $3,566,803. The City has no obligation to advance funds in the future. The note is being repaid with interest over a period of 30 years. The City must also make payments for its pro rata share of operating and maintenance costs not recovered by the plant through revenues. The amount paid during the current year for purchased power was reduced by principal and interest amounts totaling $281,317 due the City on the outstanding note receivable. The contract expires in September 2017.

NOTE 11 – LIGHT AND POWER OPERATIONS AND COMMITMENTS (CONTINUED)

Power Purchase Commitments

As of June 30, 2008, the City has entered into long-term commitments to purchase power subject to certain conditions. The following table summarizes the value of the commitments at June 30, 2008:

Fiscal Year		Amount*
2009	$	18,113,862
2010		14,355,862
2011		17,170,648
2012		21,413,703
2013		21,413,703
2014-2018		135,241,445
2019-2023		166,296,412
	$	394,005,635

*Commitments under the PPTA and CFD net of amortization of deferred gain.

Electric Rate Increase

Effective November 1, 2007, the City increased its electric rates 5% charged for electrical energy distributed and supplied by the City within its boundaries.

NOTE 12 – POSTEMPLOYMENT BENEFITS

The City Council approved a post-employment benefit plan for all employees with 20 years of service who retire at 60 or 30 years or more of service to the City. The plan pays for qualified employees' medical and dental insurance premiums and claims from age 60 to 65. Funding of the plan is on a pay-as-you-go basis. During the year ended June 30, 2008, approximately 344 (302 current employees and 42 retired employees) participants were able to receive benefits from the City's health insurance plans. Amounts paid for premiums for the year ended June 30, 2008 totaled $176,395.

NOTE 13– CONTINGENCIES

As of June 30, 2008, a number of lawsuits and claims were pending against the City that arose in the normal course of operations. Management estimates that certain pending lawsuits and claims may result in additional liabilities of approximately $500,000.

The City is currently in proceedings with the FERC and certain other utilities and agencies regarding the appropriate TRR for the City. Background to this dispute is discussed in Note 11. Prior to April, 2008, the City was receiving revenue from the ISO based upon a TRR of approximately $10.6 million. In November, 2007, the ISO made a filing with FERC seeking an order permitting the ISO to collect approximately between $12 million and $16.4 million (depending upon interest calculations) from Vernon related to the amounts paid to Vernon for its TRR since January, 2001. The validity of the ISO's request is subject to ongoing litigation before FERC and the United States Court of Appeals (the "TRR Case"). In addition, the City is involved in litigation over the market price charged by the City for certain electric energy sales made during the period October 2, 2000 through June 20, 2001. FERC has ordered reductions in certain of the market prices for electric energy during that period, and the legitimacy of that order and its impact on entities are being litigated before the United States Court of Appeals and other courts (the "Refund Cases").

NOTE 13– CONTINGENCIES (CONTINUED)

On July 9, 2008, the City entered into a Settlement Agreement with the State's three IOUs, among others, settling all claims related to the City in the TRR Case and the Refund Cases. Pursuant to that settlement, the City will release any claims to the receivable from CPX discussed in Note 11, as well as certain other claims which the City may have against other parties in those proceedings. The settlement has received final approval by the FERC.

NOTE 14 – FUTURE GASB PRONOUNCEMENTS

The City is currently analyzing its accounting practices to determine the potential impact on the financial statements for the following GASB 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 other postemployment 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 cost 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. This statement is effective for the City's fiscal year ending June 30, 2009.

In December 2006, GASB issued Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*. This statement requires state and local governments to provide the public with better information about the financial impact of environmental cleanup and identifies the circumstances under which a governmental entity would be required to report a liability related to pollution remediation and how to measure that liability. The statement also requires governments to disclose information about their pollution obligations associated with clean up efforts in the notes to the financial statements. GASB Statement No. 49 will be effective for financial statements for periods beginning after December 15, 2007, but liabilities will be measured at the beginning of that period so that beginning net assets can be restated.

In June 2007, GASB issued Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*. Governments possess many different types of assets that may be considered intangible assets, including easements, water rights, timber rights, patents, trademarks, and computer software. This Statement requires that all intangible assets not specifically excluded by its scope provisions be classified as capital assets, and also addresses recognition and amortization. The requirements of this Statement are effective for financial statements for periods beginning after June 15, 2009.

The City has not determined the impact on the City's financial statements of the adoption of these statements.

NOTE 15 – SUBSEQUENT EVENTS

Electric Rate Increase

The City's Electric System has experienced volatility in the cost of natural gas since the disruption of the California energy markets in 2001 and 2002, with unusual volatility from 2006 to the present. In response, in 2006, the City entered into an agreement with the Vernon Natural Gas Financing Authority for the purchase of a supply of prepaid natural gas. In addition, the City has established the Fuel Cost Adjustment Billing Factor ("FCABF") in connection with the cost of natural gas related to power generation and purchases. The FCABF went into effect on July 1, 2008 and will be added to all retail customer bills based on electrical consumption. The FCABF, as amended in August 2008, will add an amount to each retail bill to recover the excess over $7.50 per MMBtu the City pays for natural gas and the embedded cost of natural gas in power purchased by the City.

Renewable Energy

On August 12, 2008, the City entered into an agreement to acquire approximately 29,722 acres of land for the potential development of wind renewable resources and an option to acquire approximately 3,840 acres of land for the potential development of solar renewable resources for a total of approximately $42,000,000.

Bond Financing

On September 17, 2008, the City issued $43,765,000 of 2008 Taxable Series A Electric System Revenue Bonds to provide funds to (i) finance the costs of certain Capital Improvements to the City's Electric System, (ii) fund a deposit to the Debt Service Reserve Fund, and (iii) pay costs of issuance of the 2008 Bonds.

The Capital Improvements to be financed are improvements to the distribution facilities of the Electric System. As the City has paid the costs of these facilities from the Light and Power Fund, the proceeds of the 2008 Bonds will be used to reimburse the Electric System.

A portion of such reimbursement will be used to make the Termination Payments associated with terminating four interest rate swap transactions. Three of the transactions (the "MS Swap Transactions") are between the City and Morgan Stanley Capital Services Inc. ("Morgan Stanley") and related to electric revenue bonds issued by the City in 2004 (the "2004 Bonds"). The 2004 Bonds have been redeemed by the City. The fourth interest rate swap transaction (the "B and C Authority Swap Transaction") is a transaction between the Vernon Natural Gas Financing Authority (the "Authority") and Citibank, N.A., New York. The City is obligated to make payments with respect to the B and C Authority Swap Transaction under the Natural Gas Purchase Agreement (the "Gas Supply Agreement"), dated as of June 1, 2006, between the City and the Authority.

A portion of such reimbursement is expected to be used to pay the conversion costs for the conversion to fixed rate bonds of $207,495,000 aggregate principal amount of variable rate bonds of the Authority (the "2006 B and C Authority Bonds"). The City is obligated to make payments with respect to the 2006 B and C Authority Bonds under the Gas Supply Agreement.

The City anticipated issuing approximately $92,000,000 of the 2008 Bonds and terminating all of the MS Swap Transactions and the B and C Authority Swap Transaction in connection with the issuance of the 2008 Bonds. The City also anticipated converting the 2006 B and C Authority Bonds to fixed rate bonds in conjunction with the issuance of the 2008 Bonds. Due to severe market disruptions existing at the time the 2008 Bonds were sold by the City, the City issued $43,765,000 of 2008 Bonds and has determined to postpone the conversion of the 2006 B and C Authority Bonds and the termination of the B and C Authority Swap Transaction until such conversion can be accomplished on terms similar to the terms that were available prior to the market disruptions.

NOTE 15 – SUBSEQUENT EVENTS (CONTINUED)

The City continues to expect to terminate the MS Swap Transactions in conjunction with the issuance of the 2008 bonds. The City expects to issue approximately $42,160,000 aggregate principal amount of Additional Bonds under the Indenture in fiscal year 2009 if market conditions permit. The City intends to apply the portion of the proceeds of the 2008 Bonds described above, together with other available moneys in the Light and Power Fund to pay any Termination Payments required of the City upon the termination of the MS Swap Transactions and the B and C Authority Swap Transaction, as well as the costs of converting the 2006 B and C Authority Bonds.

Credit Rating

As of June 30, 2008, all bonds issued by the Vernon Redevelopment Agency and Authority had an insured rating of AA by S&P and A2 by Moody's. However, during the Fiscal Year 2008 and subsequently thereafter, S&P and Moody's made numerous rating changes on the Vernon Redevelopment Agency and Authority bonds. Below is a summary of such rating changes.

- In June 2008, S&P downgraded the bond insurer MBIA, the bond insurer for the 2005 Series and 2006 Series, to AA from AAA. As a result of such rating action, the insured rating of the Vernon Redevelopment Agency 2005 Series and the Authority's 2006 Series was lowered to AA from AAA.
- In June 2008, Moody's downgraded the bond insurer MBIA, the bond insurer for the 2005 Series and 2006 Series, to A2 from Aaa. As a result of such rating action, the insured rating of the Vernon Redevelopment Agency 2005 Series and the Authority's 2006 Series was lowered to A2 from Aaa.
- In September 2008, S&P increased the underlying rating of the City's electric system to A- from BBB+.
- In November 2008, Moody's downgraded the bond insurer to MBIA, the bond insurer for the 2005 Series and 2006 Series, to Baa1. As a result of such rating action, the insured rating of the Vernon Redevelopment Agency 2005 Series was lowered to Baa1. However, the insured rating on the Authority's 2006 Series was lowered A3, the underlying rating of the City's electric system by Moody's.

Change in Fair Value of Derivative Instruments

The fair value balances and notional amounts of derivative instruments outstanding at October 31, 2008, classified by type, and the change in fair value of such derivative instruments since June 30, 2008 are as follows:

	Change in Fair Value		Fair Value at October 31, 2008	
	Classification	Amount	Classification	Amount
Governmental activities				
Hedging derivative instrument				
Cash flow hedge				
Basis Swap - Series 2005	Decrease in fair value	$ (1,076,851)	Derivative liability	$ (1,266,112)
Business-type activities				
Hedging derivative instruments				
Cash flow hedge				
Variable to Fixed Swaps				
2004 Series A Bonds	Decrease in fair value	(3,974,359)	Derivative liability	(9,404,027)
2004 Series B Bonds	Decrease in fair value	(1,984,539)	Derivative liability	(5,893,570)
2004 Series D Bonds	Decrease in fair value	(760,491)	Derivative liability	(3,056,489)
2006 Series A Gas Bonds	Decrease in fair value	(1,736,057)	Derivative liability	(12,032,340)
2006 Series B and C Gas Bonds	Decrease in fair value	(2,170,738)	Derivative liability	(13,696,324)
Natural Gas Commodity Swap	Deferred outflow	8,237,274	Derivative liability	(8,237,274)
Investing derivative instruments				
Derivative Contracts /				
Futures and Options	Decrease in fair value	(2,649,851)	Derivative asset	272,207

NOTE 15 – SUBSEQUENT EVENTS (CONTINUED)

On September 29, 2008, Citibank, N.A. was placed on negative watch for possible downgrade with respect to credit rating.

On September 15, 2008, Lehman Brothers Holdings Inc. filed a petition in the United States Bankruptcy Court for the Southern District of New York seeking relief under Chapter 11 of the United States Bankruptcy Code. The City's Redevelopment Agency does not expect Lehman Brothers to be able to post collateral or to continue to perform its obligations under the Basis Swap in the future. The City's Redevelopment Agency is currently reviewing its procedures to terminate the Basis Swap- Series 2005 and determine any claims, if any, to be filed with the bankruptcy court.

NOTE 16 – IMPLEMENTATION OF GASB STATEMENT NO. 53

In the current year, the City adopted an early implementation of GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. In accordance with GASB 53, an evaluation of effectiveness was performed on all derivative instruments as of June 30, 2008 for all derivative instruments existing prior to July 1, 2007. For hedging derivative instruments determined to be effective, the derivative instrument was reported based on hedge accounting as of the end of the current period as if it had been effective from its inception. For hedging derivative instruments determined to be ineffective, the derivative instruments were evaluated as of the end of the previous reporting period and reported as a restatement of beginning net assets.

For the governmental activities, the beginning net assets was restated by reducing beginning net assets by $255,741 which was the fair value of hedging derivative instruments determined to be ineffective as of the end of the previous reporting period.

For business-type activities and enterprise funds, the beginning net assets were restated by reducing beginning net assets by $3,714,145 which was the fair value of the hedging derivative instruments determined to be ineffective as of the end of the previous reporting period.

CITY OF VERNON, CALIFORNIA

Required Supplementary Information
Budgetary Comparison Schedule
General Fund
For the Fiscal Year Ended June 30, 2008

	Budgeted Amounts		Actual	Variance with Final Budget Positive
	Original	Final	Amounts	(Negative)
REVENUES:				
Taxes	$ 9,303,400	$ 9,303,400	$ 10,675,889	$ 1,372,489
Special assessments	-	-	772,086	772,086
Licenses and permits	1,371,000	1,371,000	1,236,622	(134,378)
Fines, forfeitures and penalties	275,000	275,000	249,235	(25,765)
Investement Income	300,000	300,000	159,421	(140,579)
Intergovernmental revenues	201,000	201,000	539,854	338,854
Charges for services	9,000,000	9,000,000	8,861,811	(138,189)
Other revenues	998,805	998,805	1,428,699	429,894
Total revenues	21,449,205	21,449,205	23,923,617	2,474,412
EXPENDITURES:				
General government	17,787,846	17,787,846	16,734,174	1,053,672
Public safety	21,426,562	21,426,562	21,630,258	(203,696)
Public works	5,643,742	5,643,742	4,971,701	672,041
Health services	1,391,889	1,391,889	1,421,492	(29,603)
Capital outlay	3,714,588	3,714,588	3,155,167	559,421
Total expenditures	49,964,627	49,964,627	47,912,792	2,051,835
Deficiency of revenues under expenditures	(28,515,422)	(28,515,422)	(23,989,175)	4,526,247
Other financing sources:				
Proceeds from land	18,000,000	18,000,000	7,530,785	(10,469,215)
Transfers in / (out)	3,200,000	3,200,000	(13,108,076)	(16,308,076)
Net change	$ (7,315,422)	$ (7,315,422)		
Reconciliation of GAAP basis fund balance				
Current year encumbrances			2,814,499	2,814,499
NET CHANGE IN FUND BALANCE			(26,751,967)	(19,436,545)
FUND BALANCE, BEGINNING OF YEAR			28,043,474	29,560,762
FUND BALANCE, END OF YEAR			$ 1,291,507	$ 10,124,217

See accompanying note to the required supplementary information.

CITY OF VERNON, CALIFORNIA
Note to Required Supplementary Information
June 30, 2008

NOTE 1 – BUDGET

The City adheres to the following general procedures in establishing its annual budget, which is reflected in the accompanying General Fund budgetary comparison schedule.

- An annual budget is adopted by the City Council that provides for the general operation of the City. The budget includes authorized expenditures and estimated revenues of the General Fund, Special Revenue Funds and Capital Projects Funds;

- The budget is formally integrated into the accounting system and employed as a management control device during the year;

- Encumbrances, which are commitments related to executory contracts for goods and services, are recorded to assure effective budgetary control and accountability;

- Encumbrances outstanding at year-end do not constitute expenditures or liabilities under GAAP. Encumbrances outstanding at year-end are reported as reservations of fund balance for subsequent year expenditures. Unencumbered appropriations lapse at year-end;

- The budget is adopted on a modified accrual basis, except that encumbrances are treated as budgetary basis expenditures in the year of incurrence of the commitment to purchase;

- Excess expenditures over appropriations are financed by beginning fund balances. The final budgeted amounts used in the accompanying General Fund budgetary comparison schedule include any amendments made during fiscal year 2008. Encumbrances carried forward from the prior year are reflected in the original budget.

For the current year, the City's original and final budget for general fund expenditures was $49,964,627. The General Fund's total positive variance between the final budgeted amount and actual amount for expenditures was $2,051,835. The key reasons for this variance were excess appropriations of $1,053,672 in General Government's legal and contract services expenditures, $672,041 in Public Works' salaries and contract services expenditures, and $559,421 in Capital Outlay.

CITY OF VERNON, CALIFORNIA
Required Supplementary Information
June 30, 2008

Safety Plan Schedule of Funding Progress

Valuation Date	Actuarial Accrued Liability (AAL) (a)	Actuarial Value of Assets (b)	Unfunded (Overfunded) UAAL (OAAL) (a)–(b)	Funded Ratio (b)/(a)	Annual Covered Payroll (c)	UAAL (OAAL) as a % of Covered Payroll [(a)–(b)]/(c)
6/30/2006	$ 130,796,720	$ 117,846,016	$ 12,950,704	90.1%	$ 11,081,334	116.9%
6/30/2005	119,723,715	110,840,144	8,883,571	92.6%	10,839,182	82.0%
6/30/2004	115,366,590	105,789,665	9,576,925	91.7%	10,381,390	92.3%

Miscellaneous Plan Schedule of Funding Progress

Valuation Date	Actuarial Accrued Liability (AAL) (a)	Actuarial Value of Assets (b)	Unfunded (Overfunded) UAAL (OAAL) (a)–(b)	Funded Ratio (b)/(a)	Annual Covered Payroll (c)	UAAL (OAAL) as a % of Covered Payroll [(a)–(b)]/(c)
6/30/2006	$ 72,037,986	$ 73,178,437	$ (1,140,451)	101.6%	$ 10,818,668	(10.5%)
6/30/2005	68,680,220	68,281,654	398,566	99.4%	11,767,928	3.4%
6/30/2004	64,968,438	64,715,108	253,330	99.6%	11,648,187	2.2%