



BLENDING TRADITION WITH INNOVATION

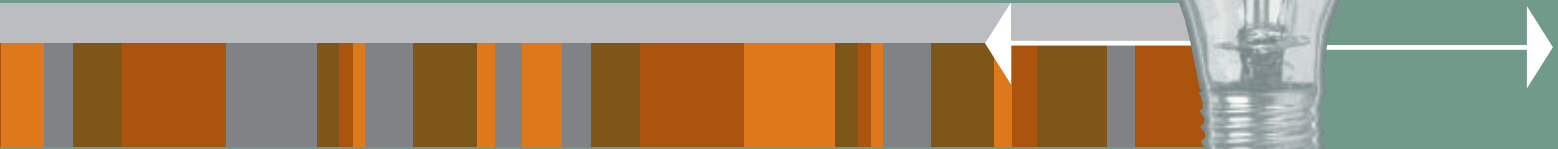




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LETTER TO THE GOVERNOR

December 1, 2003

The Honorable
Janet A. Napolitano
Governor of Arizona
State Capitol
Ninth Floor, West Wing
Phoenix, AZ 85007



Dear Governor:

This 45th Annual Report of the Arizona Power Authority details the Authority's operational and financial activities for the fiscal year ending June 30, 2003. This Annual Report highlights the Authority's efforts in blending its traditional stewardship of the state's power entitlement from federal generation with the encouragement of new technologies. The Authority remains a forward-looking power participant in the Southwest.

The Authority continues to assure reliable energy to its customers at one of the lowest rates in the nation, through its active role in Hoover Dam's engineering and operating functions. In addition, the Authority is helping to define the role of public power within the new deregulated utility environment in Arizona.

As Arizona's power needs and capabilities continue to evolve, the Authority remains focused on its original mandate—to provide the greatest public service through the best use of all power resources available.

Sincerely,

A handwritten signature in cursive script that reads "Michael C. Francis".

Michael C. Francis
Chairman

REPORT OF THE EXECUTIVE DIRECTOR

JOE MULHOLLAND



EMPOWERING EXPANSION. SUSTAINING GROWTH

In an era of economic uncertainty and rapid statewide growth, the Arizona Power Authority's mandate of providing low cost reliable power to our customers is more critical than ever. Keeping this fundamental purpose clearly in sight, the Authority is actively pursuing ways to enhance its ability to serve its customers and ensure against disruption in pricing or service.

As always, maintenance at Hoover Dam is an extremely high priority. The Authority is working to ensure maintenance procedures are well planned and performed in a cost-effective manner.

Currently, the construction of a nearby bridge has required the movement of major transmission facilities. Some lines have been relocated and certain plant units are being shut down during the building process. The Authority is working closely with the Western Area Power Administration and the Bureau of Reclamation to minimize outages resulting from these developments, and thereby keep our pricing and supply stable.

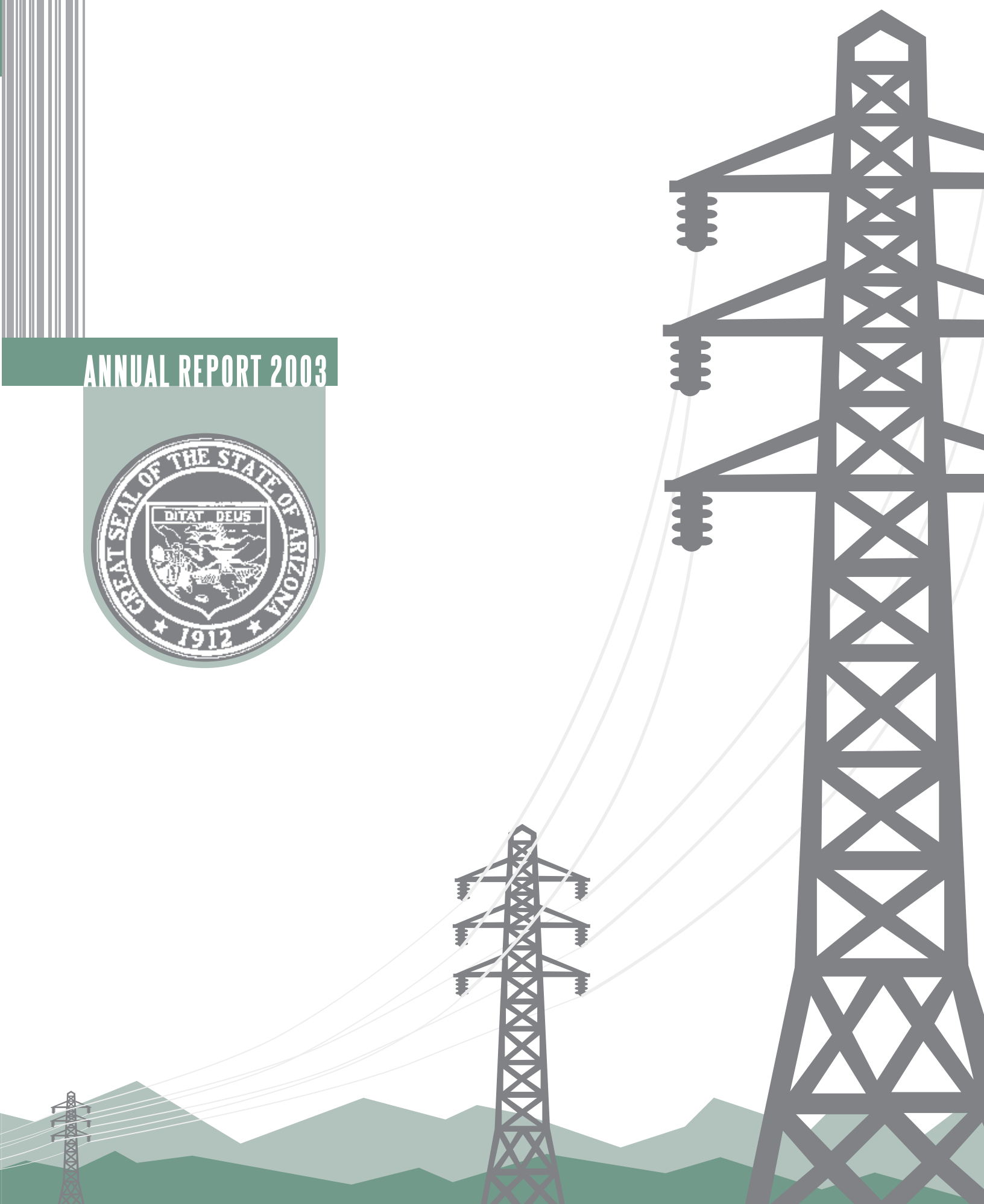
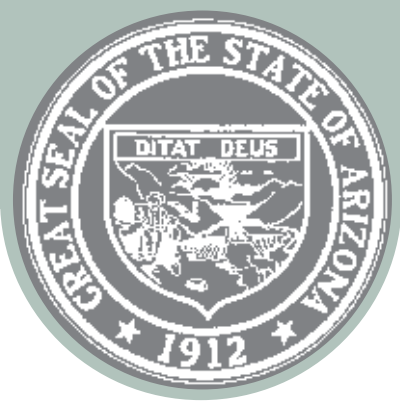
In addition to planning, the Authority has stepped in to help directly finance the maintenance of transmission facilities used to transmit Hoover Power. This action protects against outages and the attendant risk of being forced to purchase power from more expensive sources.

Drought conditions on the Colorado River remain a concern. In response to this, optimum water use planning is being implemented to limit the effect of to our customers. While drought challenges Hoover's generating ability, it presents an important opportunity for much needed maintenance work on the Hoover facility, which is currently being conducted.

In addition to securing the reliability of our current resources, the Authority is also examining the possibility of tapping alternative energy sources. This is in keeping with a trend throughout the country to explore renewable energy in order to make the United States less dependent on fossil fuels. As the state agency empowered to consider such options, the Authority is investigating the opportunities offered by wind and as well as solar power.

The Authority also continues to monitor issues involving the deregulation of power in Arizona. As these issues evolve, the Authority is staying abreast of the most current concepts and proposals under discussion. As it prepares for a future of on-going growth in Arizona, the Authority is above all committed to ensuring the stability and affordability of the power it provides.

ANNUAL REPORT 2003





REPORT OF THE COMMISSION

Since the Arizona Power Authority was established in 1944, it has been primarily responsible for the stewardship of the State of Arizona's allocation of federal power from Hoover Dam and Power Plant. This stewardship was reaffirmed with the enactment of the Hoover Power Plant Act of 1984 and subsequent renewal of Arizona's original Hoover power allocation and an additional allocation of new Hoover power resulting from the uprating of the power plant equipment. While the Authority continues to administer this valuable federal resource, it is also mindful of the growth within the state resulting in increased demands for additional electrical power. The Authority is actively researching and reviewing new technologies within the electric utility industry to provide our customers with the most efficient and cost effective electrical power to meet their future needs while maintaining a reliable and stable electrical system.



MICHAEL C. FRANCIS

Michael Francis began his tenure on the Commission in 1999, and his current term extends until 2008. Mr. Francis assumed the Chair in April with the passing of Jewell Lewis. He was elected to the Chair in May. He is also a partner in Santa Lucia Farms, which produces more than 3.7-million garden rose bushes annually. In addition to farming, Francis owns and operates Francis Insurance Agency, which writes insurance for Arizona and California farmers. A member of the American Rose Society, Mr. Francis is a member of the M&I Thunderbird Bank Board of Directors Arizona Region.



LT GEN JOHN I. HUDSON

Vice Chairman John Hudson was first appointed to the Arizona Power Authority Commission in March 2000. Gen. Hudson was elected to the Vice Chair in May 2003 with his current term expiring in 2006. John Hudson is a member of the Board of Directors of the Yuma Regional Medical Center, member and past chairman of the Greater Yuma Port Authority Board of Directors, a founding Director of the Foothills Bank of Yuma, a member of the Foothills Rotary Club of Yuma and past president of Yuma's 78-CRIME Board of Directors. General Hudson served in the U.S. Marine Corps for 37 years.



RICHARD S. WALDEN

Richard (Dick) Walden was appointed to the Commission in 1984 and re-appointed through his present term expiring in 2010. He is also a member of the Advisory Council on Small Business and Agriculture for the Federal Reserve Bank of San Francisco. Mr. Walden is the President and CEO of Farmers Investment Co., a family-owned, pecan growing and processing company headquartered in Sahuarita, Arizona. He is a member of the board of International Tree Nut Council and in that capacity serves as the chairman of the Committee for Nutrition and Education associated with the Nutrition and Education Foundation. Dick is also a member of the Board of National Pecan Shellers Association.



DALTON H. COLE

Dalton Cole was appointed to the Commission in January 2002. His term will expire in 2008. Mr. Cole is a retired businessman and farmer. He has served as a member of the Central Arizona Water Conservation District Board. He co-founded and chaired the HoHoKam Irrigation District. He served on the board of Electrical District No. 2 in Pinal County for 18 years and is a past chairman. He is a past president of the State Board of Directors for Community Colleges. He has served on the Ground Water Management Committee for Pinal County and on advisory committees to the Arizona Legislature regarding water and power issues.



DELBERT R. LEWIS

Commissioner Lewis was appointed to the Arizona Power Commission in April 2003 to complete the term of his wife, the late Dr. Jewell Lewis. He has been reappointed for a six-year term ending in January 2010. Commissioner Lewis is one of the founders of KTVK Channel 3 and the CEO of MAC America Communications, Inc. His past and present civic affiliations include the Arizona Broadcasters Association, Metropolitan Phoenix Broadcasters, Phoenix Chamber of Commerce, Samaritan Health Services, Greater Phoenix Leadership, the National Conference, Maricopa County Sports Authority and Orpheum Theatre Foundation. Mr. Lewis and his late wife have been nationally recognized for their financial support and commitment to education and community service.

NEW PERSPECTIVES



ROBERT J. LINSSSEN

Robert J. (Bob) Linssen is Director of Engineering and Operations. Bob has a Bachelor of Electrical Engineering degree and a Master of Science degree in Business Management. He comes to the Arizona Power Authority with over thirty-six years of utility industry experience, as well as four years of experience in small business management and financial consulting. Bob has always been active in the community and is past president of the North Phoenix Chamber of Commerce and past president of the Paradise Valley Rotary Club. He also served four years on the Phoenix Planning Committee for the Paradise Village Area. Bob is a Registered Professional Engineer in Arizona and Wisconsin.



MARCIA KENNEDY

Marcia Kennedy is the APA's Principal Analyst. With over 25 years of professional experience in such industries as advertising, law, financial management and computer software administration, Marcia brings a depth of business knowledge and expertise to the Authority. In addition, Marcia is an adjunct business professor at Southwestern College, specializing in economics, marketing and computer courses. She holds a Bachelor of Arts degree in Music Education. In 2000, Marcia completed an M.B.A. degree in Finance and International Management with a study trip to China. Marcia sings and performs with the Arizona Opera Chorus.





OPERATIONS & THE ENVIRONMENT

The past year saw significant events occur with respect to the Bureau of Reclamation's administration of the Colorado River, particularly in the lower basin. Drier than average hydrologic conditions continued along the Colorado River drainage and storage system. Inflows into Lake Powell was 49 percent of the 30 year average. Water year 2003 was the fourth consecutive year with below average inflow into the Colorado River reservoirs. Lake Mead storage decreased by 1.48 million acre-feet. At the beginning of the water year the Colorado River system storage capacity was 64 percent of capacity and it dropped to 57 percent by year's end.

Projected deliveries for water year 2004 are expected to be sufficient to satisfy downstream delivery requirements. This takes into account the existing water storage conditions in the lower basin, the most probable near-term water supply conditions in the basin, and the Interim Surplus Guidelines. We expect that there will be a Partial Domestic Surplus condition declared and this criterion will govern

the operation of Lake Mead during calendar year 2004. The previous suspension of interim surplus determination was reinstated by the Secretary of the Interior on October 10, 2003. Reclamation does not anticipate any unused apportionment for calendar year 2004.

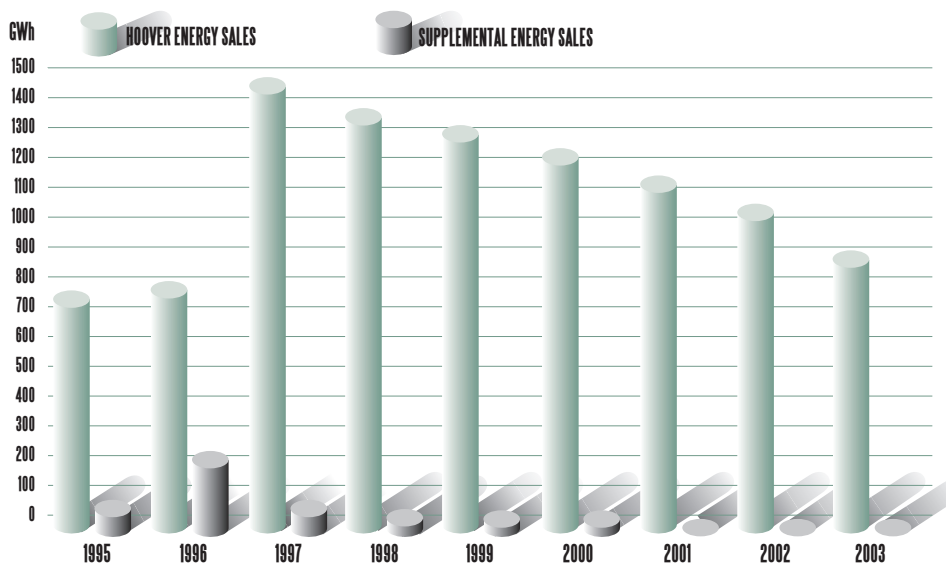
As with last year, the water diversions and power production in the lower basin continues to be monitored for their impact on endangered and threatened species under the Multi-Species Conservation Program (MSCP). Discussions among all interested parties continue in the development of a final MSCP that will be acceptable by all impacted parties and the federal government. Major activities during the past year focused on the amount and allocation of the cost for the MSCP and the development of legislation providing authorization and funding for the long-term program. Concurrent with these processes, strategies are being formulated to assist the participants' successful efforts leading to passage of the legislation.

HISTORICAL ENERGY SALES

The following graph illustrates the Authority's historical energy sales (GWh) since 1995 for power obtained from the Hoover Powerplant and for supplemental sales.

Supplemental power is obtained by the Authority for sale to customers on an "as requested" basis. This energy augments the customers' allocation from the Authority.

FISCAL YEAR	1995	1996	1997	1998	1999	2000	2001	2002	2003
HOOVER	773	792	1,485	1,389	1,318	1,205	1,103	1,098	899
SUPPLEMENTAL	65	224	79	3	2	4	0	0	0
TOTAL	838	1,016	1,564	1,392	1,320	1,209	1,103	1,098	899



SCHEDULE OF CAPACITY AND ENERGY SALES

FOR PERIOD OF JULY 1, 2002 THROUGH JUNE 30, 2003

SALE OF HYDRO POWER Customers	AVERAGE BILLING DEMAND (KW)	ENERGY DELIVERED (KWH)	SALES (\$)	MILLS PER KWH	PRIOR YEAR ADJ. (\$)
Aguila Irrigation District	5,157	9,319,000	154,491	16.58	10,469
Avra Valley Irrigation & Drainage District	516	3,355,000	40,976	12.21	2,410
Buckeye Water Conservation District	2,443	8,383,000	122,918	14.66	9,185
Central Arizona Water Conservation District	132,480	237,296,000	3,728,913	15.71	350,265
Chandler Heights Citrus Irrigation District	762	3,718,000	43,411	11.68	2,732
Cortaro-Marana Irrigation District	5,280	18,824,000	241,828	12.85	17,002
Electrical District No. 1, Pinal	0	0	0	0.00	0
Electrical District No. 2, Pinal	15,946	71,047,000	920,268	12.95	67,771
Electrical District No. 3, Pinal	13,036	58,790,000	799,107	13.59	53,271
Electrical District No. 4, Pinal	15,945	77,045,000	970,094	12.59	52,667
Electrical District No. 5, Pinal	12,108	46,965,000	592,353	12.61	27,009
Electrical District No. 5, Maricopa	287	1,705,000	19,933	11.69	104
Electrical District No. 6, Pinal	6,567	20,185,000	246,323	12.20	10,038
Electrical District No. 7, Maricopa	8,607	13,511,000	248,852	18.42	15,505
Electrical District No. 8, Maricopa	19,840	55,906,000	830,673	14.86	61,707
Harquahala Valley Power District	2,041	8,156,000	115,268	14.13	10,903
Maricopa County Municipal Water District #1	7,247	15,167,000	255,118	16.82	19,523
McMullen Valley Water Conservation & Drainage District	7,453	13,909,000	227,249	16.34	7,772
Ocotillo Water Conservation District	1,960	10,285,000	119,390	11.61	(2,518)
Queen Creek Irrigation District	1,451	1,954,000	24,944	12.77	14,640
Roosevelt Irrigation District	2,641	14,160,000	187,669	13.25	34,598
Roosevelt Water Conservation District	5,542	28,164,000	346,365	12.30	124,736
Salt River Project	31,799	135,962,000	1,737,327	12.78	3,002
San Tan Irrigation District	427	3,308,000	37,979	11.48	3,507
Silverbell Irrigation & Drainage District	583	3,768,000	43,950	11.66	5,969
Tonopah Irrigation District	1,271	5,364,000	74,946	13.97	8,397
Wellton-Mohawk Irrigation & Drainage District	2,386	9,620,000	126,882	13.19	2,246
City of Page	853	1,927,000	27,585	14.31	8,965
City of Safford	1,706	7,194,000	90,984	12.65	3,643
Town of Thatcher	861	3,395,000	42,054	12.39	9,863
Town of Wickenburg	1,877	10,774,000	127,691	11.85	0
Ak-Chin Indian Community	0	0	0	0.00	0
Arizona Electric Power Cooperative	0	0	0	0.00	0
Arizona Public Service Company	0	0	0	0.00	0
Citizens Utilities Company	0	0	0	0.00	0
City of Mesa	0	0	0	0.00	0
Tohono O'odham Utilities Authority	0	0	0	0.00	0
San Carlos Project	0	0	0	0.00	0
Tucson Electric Power Company	0	0	0	0.00	0
TOTAL HYDRO POWER SALES	309,072	899,156,000	\$12,545,539	13.95	
TOTAL NET PRIOR YEAR ADJUSTMENT					\$950,625
TOTAL SUPPLEMENTAL POWER SALES	606,932	0	\$3,076,952		
OTHER ELECTRIC SERVICES INCOME**			\$8,441,932		
TOTAL POWER INCOME			\$25,015,047*		

*Difference between Total Electric Sales and Operating Revenue is due to post-closing reconciliation of estimate to actuals between the Authority and Western Area Power Administration.

**Includes Administrative fees, facilities charges, late charges, and Scheduling Entity revenue.



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REPORT OF INDEPENDENT ACCOUNTANTS

To the Arizona Power Authority Commission

In our opinion, the accompanying statements of net assets and the related statements of revenues, expenses, and changes in net assets, and statements of cash flows present fairly, in all material respects, the financial position of the Arizona Power Authority (A Body, Corporate and Politic, of the State of Arizona) at June 30, 2003 and 2002, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As described in Note 1, the Authority adopted the provisions of the Governmental Accounting Standards Board ("GASB") Statement No. 34, Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments, as amended by GASB Statement No. 37, Basic Financial Statements and Management's Discussion and Analysis - for State and Local Governments: Omnibus - an Amendment of GASB Statements No. 21 and No. 34 and GASB Statement No. 38, Certain Financial Statement Note Disclosures, as of July 1, 2001. The management's discussion and analysis is not a required part of the financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

PricewaterhouseCoopers LLP

August 7, 2003, except as to the
last paragraph of Note 6 which is
as of October 1, 2003



MANAGEMENT'S DISCUSSION AND ANALYSIS

The following is a discussion and analysis of the Arizona Power Authority's (the "Authority") financial performance for the fiscal year ended June 30, 2003 and is designed to (a) assist the reader in focusing on significant financial issues, (b) provide an overview of the Authority's financial activity and (c) identify changes in the Authority's financial position. Since the Management's Discussion and Analysis ("MD&A") is designed to focus on the current year's activities, resulting changes and currently known facts, please read it in conjunction with the Authority's financial statements beginning on page 17.

HIGHLIGHTS

FINANCIAL HIGHLIGHTS

- The Authority's net assets decreased by \$193,259 or 6 percent due to a write-off of invested funds associated with investments made by the Arizona State Treasurer ("Treasurer"). See Authority Highlights below.
- The Authority's revenue increased by \$1,994,987 or 9 percent primarily due to an increase in the sale of supplemental power. The sale and concomitant purchase of additional supplemental power resulted from additional customer energy requirements brought on by reduced Hoover power generation, which in turn was caused by the sustained drought currently being experienced throughout the Colorado River Basin. The Authority's purchased power costs increased by \$1,972,328 or 12 percent due to the increase in supplemental power purchases to support additional supplemental power sales. Operating income increased by \$519,188 or 131 percent largely due to a reduction in other operating expenses.

AUTHORITY HIGHLIGHTS

Revised Scheduling Entity Agreement - The Authority and Salt River Project are parties to a Scheduling Entity Agreement which expires on September 30, 2004. This Agreement provides for Salt River Project to pay the Authority \$8.4 million each year in return for allowing Salt River Project to be the Scheduling Entity of the Hoover generation in Arizona. Negotiations are currently underway to extend this Agreement.

Transmission Agreement - On January 24, 2003, the Authority and the Western Area Power Administration ("Western") entered into an agreement for the Advancement of Funds for Transmission Services. The Authority had an existing agreement with Western that provided for the delivery of power and energy. The new agreement provides for the Authority to advance funds to Western on a monthly basis to fund operations, maintenance and replacement costs associated with Western's transmission services. As of June 30, 2003, the Authority recorded a prepaid deposit of \$182,360, which is included in the Statements of Net Assets.

Arizona State Treasurer Investment Write-Off - The Authority is statutorily required to invest certain funds through the Treasurer who has sole investment decision-making authority. In November 2002, the Authority was advised that one of the Treasurer's chosen investments managed by National Century Financial Enterprises was under investigation for fraud. In December 2002, the Authority was informed that the Treasurer was vitiating the investment in question, thereby reducing the value to zero. Since that time, litigation was initiated and continues. There is no guarantee that the litigation will result in the recovery of the Authority's funds, which total \$227,224. Therefore, the Authority has written-off the lost investment amount as of June 30, 2003.

Effects of Drought on Hoover Energy - The Colorado River Basin has been experiencing severe drought conditions for the past four years. As a result, reservoirs have been reduced and power production at Hoover Dam has decreased, since it is dependent on water flows on the Colorado River. Several Authority customers requested that the Authority purchase supplemental power to offset the reduced energy production at Hoover. The supplemental power costs are significantly higher and are passed directly to the customers at cost. These supplemental revenues and costs are reflected on the Authority's books, resulting in much higher revenue and purchased power costs.

Other Changes That Will Improve or Provide Future Benefit to the Arizona Power Authority - No other agreements or new customers were added during the current period. However, the Authority added new staff members during the year bringing substantial experience and knowledge regarding the operations of power systems in the Southwest.

USING THIS ANNUAL REPORT

This annual report consists of a series of financial statements. The Statements of Net Assets, the Statements of Revenues, Expenses and Changes in Net Assets and the Statements of Cash Flows (on pages 17 - 20 respectively) provide information about the activities of the Authority as a whole and present a longer-term view of the Authority's finances. The Authority is a body, corporate and politic of the State of Arizona and is a special-purpose government engaged only in business-type activities. Accordingly, the financial statements presented in this Annual Report are the required basic financial statements in accordance with the provisions of Governmental Accounting Standards Board Statement No. 34, Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments. There are six basic or normal transactions that will affect the comparability of the Statements of Net Assets summary presentation:

Net Results of Activities - which will impact (increase/decrease) current assets and undesignated net assets.

Borrowing for Capital - which will increase assets and long-term debt.

Spending Borrowed Proceeds on New Capital - which will reduce current assets and increase capital assets. There is a second impact, an increase in invested capital assets and an increase in related net debt which will not change the investment in capital assets, net of debt.

Spending of Nonborrowed Current Assets on New Capital - which will (a) reduce current assets and increase capital assets and (b) will reduce undesignated net assets and increase investment in capital assets, net of debt.

Principal Payment on Debt - which will reduce current assets and reduce long-term debt.

Reduction of Capital Assets through Depreciation - which will reduce capital assets and investment in capital assets, net of debt.

OVERVIEW OF THE FINANCIAL STATEMENTS

This Discussion and Analysis is an introduction to the Authority's basic financial statements, which are comprised of two components:

- (1) Fund Financial Statements.
- (2) Notes to the Financial Statements.

Fund Financial Statements (Reporting on all of the Authority's Funds.)

The Fund Financial Statements begin on page 17 and provide detailed information about the individual funds. A fund is a fiscal and accounting entity with a self-balancing set of accounts that the Authority uses to keep track of specific sources of revenues and disbursements for specific purposes. The Authority's funds are treated as proprietary and are enterprise in nature. Most of the Authority's financial dealings are with contracts outside of state government. A separate fund is not maintained for government activities. The Authority does not act as a fiduciary.

**CONDENSED STATEMENTS OF NET ASSETS
BUSINESS TYPE ACTIVITIES**

	June 30, 2003	June 30, 2002	Diff \$	Diff %
Current assets	\$ 12,360,167	\$ 13,102,938	\$ (742,771)	(6)%
Long-term assets	49,519,365	51,832,754	(2,313,389)	(4)%
Capital assets	160,664	181,499	(20,835)	(11)%
	62,040,196	65,117,191	(3,076,995)	(5)%
Current liabilities	4,854,228	5,476,945	(622,717)	(11)%
Long-term(Bonds pay, net)	54,255,067	56,516,086	(2,261,019)	(4)%
	59,109,295	61,993,031	(2,883,736)	(5)%
Net Assets:				
Capital Assets	160,664	181,499	(20,835)	(11)%
Unrestricted	2,770,237	2,942,661	(172,424)	(6)%
Net Assets, End of Year	\$ 2,930,901	\$ 3,124,160	\$ (193,259)	(6)%

The largest component of the Authority's net assets is unrestricted reserves (property replacement, designated and undesignated).

CONDENSED STATEMENTS OF NET ASSETS DISCUSSION

Current Assets changed because of increased expenditures from the APA General Fund partially offset by increased accounts receivable from Hoover Upgrading Fund power sales and a reduced prepaid purchased power balance.

Long Term Assets changed because of the reduction in the cost of the current year Upgrading Program and an increase in amortization of prior year charges. Property, plant and equipment was also reduced due to depreciation.

Current Liabilities changed primarily due to an increase in bonds expected to be repaid next year and decreased power contracts payable due to less Hoover energy being available for sale.

Long Term Liabilities changed due to a reclassification of bonds payable from long term to current liabilities and a change in the investments held by the Trustee that is attributable to an increased accrual for the payment of bond principal.

Net Assets changed because of decreases in capital assets, property replacement and undesignated assets.

There are six basic or normal transactions that will affect the comparability of the Statements of Changes in Net Assets summary presentation.

REVENUES:

Economic Drought Condition - The sustained drought condition in the Colorado River Basin results in a decline in power production from Hoover Dam and this has a substantial impact on Hoover generated power, supplemental power consumption and rates for power sold.

Increase/Decrease in Commission Approved Power Rates - State statute requires rates to be set at levels to recover the cost of supplying service. In addition, contracts between the Authority and its customers provide specific details regarding rate determination. Consequently, the Arizona Power Authority's Commission is solely responsible for periodically modifying rates, as appropriate.

Market Impacts on Investment Income - Market conditions cause investment income to fluctuate more in the long-term than alternative shorter-term options.

EXPENSES:

Introduction of New Programs - Individual programs may be added or deleted to meet changing Authority needs.

Increase/Decrease in Authorized Personnel - Changes in the Authority's services may result in an increase/decrease in authorized staffing. Staffing costs (salary and related benefits) represent 2.5 percent of the Authority's operating costs.

Salary Increases (cost of living, merit and market adjustment) - The ability to attract and retain competent personnel requires the Authority to provide a competitive salary structure.



The following condensed financial information was derived from the Statements of Revenues, Expenses and Changes in Net Assets and reflects how the Authority's net assets changed during the fiscal year.

**STATEMENTS OF REVENUES, EXPENSES,
AND CHANGES IN NET ASSETS
BUSINESS TYPE ACTIVITIES**

	June 30, 2003	June 30, 2002	Diff \$	Diff %
Operating Revenues	\$ 25,013,450	\$ 23,018,463	\$ 1,994,987	9 %
Operating Expenses:				
Purchased Power	18,048,125	16,075,797	1,972,328	12 %
Western Credits	(5,325,522)	(4,623,123)	(702,399)	15 %
Amortization of Hoover Uprating Program Costs	5,325,522	4,623,123	702,399	15 %
Transmission and Distribution	5,229,802	5,205,863	23,939	0 %
Administrative and general	1,427,504	1,215,200	212,304	17 %
Depreciation	30,711	28,855	1,856	6 %
Other	155,357	889,985	(734,628)	(83)%
Total operating expenses	24,891,499	23,415,700	1,475,799	6 %
Operating Income (loss)	121,951	(397,237)	519,188	(131)%
Other (deductions) income:				
Interest Expense	(3,675,878)	(3,729,166)	53,288	(1)%
Deferred Interest Expense	2,958,718	2,977,031	(18,313)	(1)%
Interest Income	627,332	746,533	(119,201)	(16)%
Other, Net	(225,382)	2,323	(227,705)	(9,802)%
Total other income (loss)	(315,210)	(3,279)	(311,931)	9,513 %
Change in Net Assets	(193,259)	(400,516)	207,257	(52)%
Net Assets, Beginning of Year	3,124,160	3,524,676	(400,516)	(11)%
Net Assets, End of Year	\$ 2,930,901	\$ 3,124,160	\$ (193,259)	(6)%

CHANGES IN NET ASSETS DISCUSSION

Operating revenues changed because of increased supplemental power sales and correspondingly, operating expenses changed because of increased supplemental purchased power costs; Uprating credits increased because of increased principal payments and other costs related to the Uprating Program; amortization of the Uprating Program increased because of additional credits received; Administrative and general increased due to additional staff, increased legal costs and increased audit costs; depreciation increased because additional capital assets were acquired; and other costs increased because of the investment loss write-off.

CAPITAL ASSETS

As of fiscal year end, the Authority had \$160,664 invested in a variety of capital assets, as reflected in the following schedule, which represents a net decrease (additions less retirements and depreciation) of \$20,835 or 11 percent from the end of last year.

	June 30, 2003	June 30, 2002
Distribution Plant	\$ 32,273	\$ 40,341
General Plant - Office	128,391	141,158
	<u>\$ 160,664</u>	<u>\$ 181,499</u>

The following reconciliation summarizes the change in Capital Assets, which is presented in detail on page 24 of the Notes to the Financial Statements

	June 30, 2003
Beginning Balance	\$ 181,499
Additions	9,876
Depreciation	(30,711)
Ending Balance	<u>\$ 160,664</u>

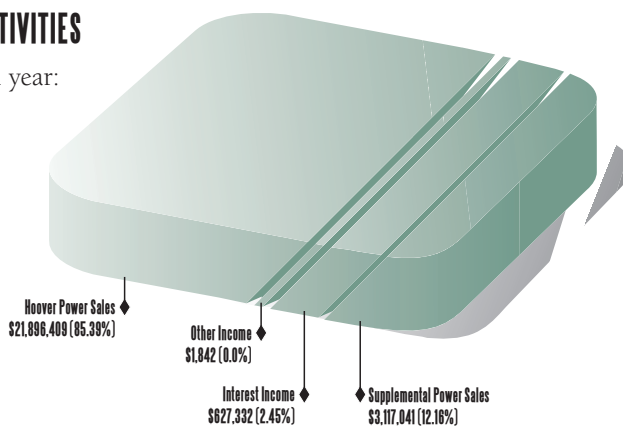
DEBT OUTSTANDING

As of fiscal year-end, the Authority had \$67,495,000 in debt outstanding, compared to \$68,945,000 last year as a result of a \$1,450,000 principal payment during the fiscal year. Also see page 25 of the Notes to the Financial Statements for a detailed summary of debt activity during the year.

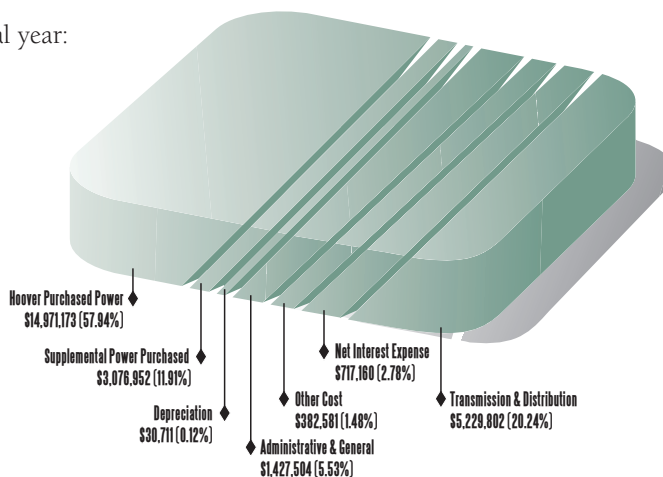
BUSINESS TYPE ACTIVITIES

The following chart depicts the sources of revenues for the fiscal year:

The Authority's revenues may decrease in the coming year(s) due to drought conditions. Insufficient rain and snow pack results in less water to be processed through the turbines at Hoover Dam thereby, producing less hydroelectric power available for sale. Additional wet years, and other factors, could help stabilize revenues.



The following chart depicts the types of expenses for the fiscal year:



For further information and/or questions on this report, please call the Power Authority Office at 602-542-4263.

FINANCIAL STATEMENTS



STATEMENT OF NET ASSETS

June 30, 2003 and 2002

	APA General Fund		Hoover Uprating Fund		Total	
	2003	2002	2003	2002	2003	2002
ASSETS						
Current assets:						
Cash and cash equivalents	\$ 3,894,085	\$ 4,329,510	\$ 2,098,840	\$ 2,532,576	\$ 5,992,925	\$ 6,862,086
Cash with fiscal agent		-	2,694,576	2,694,576	2,694,576	2,694,576
Accounts receivable, customers					-	-
power purchases	235,854	215,369	1,950,056	1,648,972	2,185,910	1,864,341
Interest receivable	10,802	17,768	130,383	134,857	141,185	152,625
Prepaid purchased power	-	-	1,345,571	1,529,310	1,345,571	1,529,310
Total current assets	4,140,741	4,562,647	8,219,426	8,540,291	12,360,167	13,102,938
Property, plant and equipment, net	160,664	181,499	-	-	160,664	181,499
Advances for Hoover Uprating Program, net	-	-	49,337,005	51,832,754	49,337,005	51,832,754
Prepaid transmission	182,360	-	-	-	182,360	-
Total assets	\$ 4,483,765	\$ 4,744,146	\$ 57,556,431	\$ 60,373,045	\$ 62,040,196	\$ 65,117,191
LIABILITIES						
Current liabilities:						
Accounts payable and other	\$ 3,830	\$ 7,688	\$ 107,768	\$ 86,653	\$ 111,598	\$ 94,341
Power contracts payable	232,500	212,743	1,296,311	2,808,280	1,528,811	3,021,023
Accrued interest payable	-	-	893,819	911,581	893,819	911,581
Bonds payable	-	-	2,320,000	1,450,000	2,320,000	1,450,000
Total current liabilities	236,330	220,431	4,617,898	5,256,514	4,854,228	5,476,945
Bonds payable	-	-	65,175,000	67,495,000	65,175,000	67,495,000
Discounts on bonds payable	-	-	(1,180,499)	(1,263,341)	(1,180,499)	(1,263,341)
Less investments held by trustee, including unamortized net discount on investments of \$0 and \$3,566	-	-	(9,739,434)	(9,715,573)	(9,739,434)	(9,715,573)
Bonds payable, net	-	-	54,255,067	56,516,086	54,255,067	56,516,086
Total liabilities	\$ 236,330	\$ 220,431	\$ 58,872,965	\$ 61,772,600	\$ 59,109,295	\$ 61,993,031
NET ASSETS						
Net assets:						
Invested in capital assets	\$ 160,664	\$ 181,499	\$ -	\$ -	\$ 160,664	\$ 181,499
Unrestricted						
Property placement	1,017,785	1,030,150	-	-	1,017,785	1,030,150
Designated	4,000,000	4,000,000	-	-	4,000,000	4,000,000
Undesignated	(931,014)	(687,934)	(1,316,534)	(1,399,555)	(2,247,548)	(2,087,489)
Total net assets	\$ 4,247,435	\$ 4,523,715	\$ (1,316,534)	\$ (1,399,555)	\$ 2,930,901	\$ 3,124,160

The accompanying notes are an integral part of these financial statements.

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS

June 30, 2003 and 2002

	APA General Fund		Hoover Upgrading Fund		Total	
	2003	2002	2003	2002	2003	2002
OPERATING REVENUES	\$ 3,117,041	\$ 761,942	\$ 21,896,409	\$ 22,256,521	\$ 25,013,450	\$ 23,018,463
Operating expenses:						
Purchased power	3,076,952	731,432	14,971,173	15,344,365	18,048,125	16,075,797
Western credits (Note 5)	-	-	(5,325,522)	(4,623,123)	(5,325,522)	(4,623,123)
Amortization of Hoover Upgrading Project costs	-	-	5,325,522	4,623,123	5,325,522	4,623,123
Transmission and distribution	11,996	1,715	5,217,806	5,204,148	5,229,802	5,205,863
Administrative and general	68,552	116,602	1,358,952	1,098,598	1,427,504	1,215,200
Depreciation	30,711	28,855	-	-	30,711	28,855
Other	133,846	871,843	21,511	18,142	155,357	889,985
Total operating expenses	3,322,057	1,750,447	21,569,442	21,665,253	24,891,499	23,415,700
Operating income (loss)	(205,016)	(988,505)	326,967	591,268	121,951	(397,237)
Other (deductions) income:						
Interest expense	-	-	(3,675,878)	(3,729,166)	(3,675,878)	(3,729,166)
Deferred interest expense	-	-	2,958,718	2,977,031	2,958,718	2,977,031
Interest income	66,177	114,455	561,155	632,078	627,332	746,533
Other, net	(137,441)	-	(87,941)	2,323	(225,382)	2,323
Total other income (loss)	(71,264)	114,455	(243,946)	(117,734)	(315,210)	(3,279)
Increase (decrease) in net assets	(276,280)	(874,050)	83,021	473,534	(193,259)	(400,516)
Net assets, beginning of the year	4,523,715	5,397,765	(1,399,555)	(1,873,089)	3,124,160	3,524,676
Net assets, end of the year	\$ 4,247,435	\$ 4,523,715	\$ (1,316,534)	\$ (1,399,555)	\$ 2,930,901	\$ 3,124,160

The accompanying notes are an integral part of these financial statements.



STATEMENT OF CASH FLOWS

June 30, 2003 and 2002

	APA General Fund		Hoover Uprating Fund		Total	
	2003	2002	2003	2002	2003	2002
Cash flows from operating activities:						
Cash received from customers	\$ 3,096,556	\$ 548,602	\$ 21,595,325	\$ 22,928,051	\$ 24,691,881	\$ 23,476,653
Cash payments to suppliers for goods or services	(3,457,807)	(884,184)	(22,264,987)	(21,366,600)	(25,722,794)	(22,250,784)
Cash payments to employees for services	-	-	(611,569)	(521,521)	(611,569)	(521,521)
Net cash provided by (used in) operating activities	(361,251)	(335,582)	(1,281,231)	1,039,930	(1,642,482)	704,348
Cash flows from capital and related financing activities:						
Interest payments on obligations	-	-	(3,610,797)	(3,646,323)	(3,610,797)	(3,646,323)
Principle payments on obligations	-	-	(1,450,000)	-	(1,450,000)	-
Acquisition of capital assets	(9,877)	(19,367)	-	-	(9,877)	(19,367)
Advances for Hoover Uprating Program	-	-	5,456,308	4,094,782	5,456,308	4,094,782
Net cash provided by (used in) capital and related financing activities	(9,877)	(19,367)	395,511	448,459	385,634	429,092
Cash flows from investing activities:						
Interest on investments	73,144	132,970	565,628	669,860	638,772	802,830
Loss on investments	(137,441)	-	(89,783)	-	(227,224)	-
Purchase of investment securities	-	-	(7,355,125)	(10,176,793)	(7,355,125)	(10,176,793)
Proceeds from sale and maturities of investment securities	-	-	7,331,264	8,394,596	7,331,264	8,394,596
Transfer to fiscal agent	-	-	-	(2,694,576)	-	(2,694,576)
Net cash provided by (used in) investing activities	(64,297)	132,970	451,984	(3,806,913)	387,687	(3,673,943)
Net decrease in cash and cash equivalents	(435,425)	(221,979)	(433,736)	(2,318,524)	(869,161)	(2,540,503)
Cash and cash equivalents, beginning of year	4,329,510	4,551,489	2,532,576	4,851,100	6,862,086	9,402,589
Cash and cash equivalents, end of year	\$ 3,894,085	\$ 4,329,510	\$ 2,098,840	\$ 2,532,576	\$ 5,992,925	\$ 6,862,086
Reconciliation of operating income (loss) to net cash provided by (used in) operating activities						
Operating income (loss)	\$ (205,016)	\$ (988,505)	\$ 326,967	\$ 591,268	\$ 121,951	\$ (397,237)
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities						
Depreciation	30,711	28,855	-	-	30,711	28,855
Changes in assets and liabilities						
(Increase) decrease in accounts receivable	(20,485)	(213,340)	(301,084)	671,530	(321,569)	458,190
(Increase) in prepaid transmission	(182,360)	-	-	-	(182,360)	-
Decrease in prepaid purchased power	-	624,954	183,739	585,614	183,739	1,210,568
(Decrease) in accounts payable and other	(3,858)	(289)	21,115	32,931	17,257	32,642
Increase (decrease) in power contracts payable	19,757	212,743	(1,511,968)	(591,413)	(1,492,211)	(378,670)
Decrease in accounts payable customer credits	-	-	-	(250,000)	-	(250,000)
Total adjustments	(156,235)	652,923	(1,608,198)	448,662	(1,764,433)	1,101,585
Net cash provided by (used in) operating activities	\$ (361,251)	\$ (335,582)	\$ (1,281,231)	\$ 1,039,930	\$ (1,642,482)	\$ 704,348
Supplemental schedule of noncash capital and related financing activities						
Deferred interest on obligations	\$ -	\$ -	\$ 2,958,718	\$ 2,977,031	\$ 2,958,718	\$ 2,977,031
Supplemental schedule of cash paid for interest	\$ -	\$ -	\$ 3,593,036	\$ 3,646,323	\$ 3,593,036	\$ 3,646,323

The accompanying notes are an integral part of these financial statements.



NOTES TO FINANCIAL STATEMENTS

1. DESCRIPTION OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Description of Business

The Arizona Power Authority (the "Authority") is a body, corporate and politic, without taxing power, established by the Arizona Legislature on May 27, 1944 by the Power Authority Act. Under the Power Authority Act, the Authority is directed to obtain electric power developed from the mainstream of the Colorado River and sell such power to certain qualified purchasers. The Power Authority Act provides that the Authority must be a self-supporting agency and prohibits the Authority from incurring any obligation, which would be binding upon the State of Arizona.

The Authority supplies capacity and energy on a wholesale basis to certain power purchasers in the State of Arizona. The Authority's primary source of power and energy is the Hoover Power Plant at Hoover Dam, located approximately 25 miles from Las Vegas, Nevada. Hoover power is produced by the Boulder Canyon Project hydropower plant owned by the Bureau of Reclamation. Hoover Dam is the highest and third largest concrete dam in the United States of America. Hoover Dam was dedicated in 1935 and the first generator of the Hoover Power Plant was in full operation in October 1936 and has been in continuous operation since. Power and energy from the Hoover Power Plant is transmitted to load centers in Arizona, California and Nevada. The Authority first contracted for Arizona's share of Hoover power in 1952 and has continuously provided power and energy to its customers since that time.

The Authority is governed by a commission of five members appointed by the Governor (the "Commission"). The term of office for each member is six years and the members select a chairman and vice-chairman from among its membership for two-year terms.

Pursuant to Arizona law, the Commission serves as the Authority's regulatory body with the exclusive authority to establish electric prices. The Authority is required to follow certain procedures, pertaining to public notice requirements and special meetings, before implementing changes in electric price schedules.

Change in Accounting Policy

Effective July 1, 2001, the Authority adopted Governmental Accounting Standards Board ("GASB") Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, as amended by GASB Statement No. 37, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments: Omnibus* - an Amendment of GASB Statements No. 21 and No. 34 and GASB Statement No. 38, *Certain Financial Statement Note Disclosures*. These statements established a new financial reporting model for state and local governments consisting of both the governmentwide and fund financial statements (within the basic financial statements) and primary activities are categorized as either governmental or business type. The Authority is only engaged in business activities. In accordance with the provisions of paragraph 138 of GASB No. 34, this report presents the required basic financial statements for special-purpose governments engaged only in business-type activities. Accordingly, no significant change or impact resulted from the adoption of GASB No. 34, as amended by GASB No. 37 and No. 38.

1. DESCRIPTION OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Measurement Focus

The Authority's funds are accounted for on a flow of economic resources measurement focus. All assets and liabilities (whether current or noncurrent) associated with their activity are included in the Statements of Net Assets. The Statements of Revenues, Expenses, and Changes in Net Assets present increases (revenues) and decreases (expenses) in total net assets. The Authority's reported total net assets are segregated into invested capital assets and unrestricted components.

Basis of Accounting

Basis of Accounting refers to the time at which revenues and expenses are recognized in the accounts and reported in the financial statements, regardless of the measurement focus applied. The accrual basis of accounting is used by the Authority whereby revenues are recognized in the accounting period in which they are earned and become measurable, and expenses are recognized when incurred.

Basis of Presentation

GASB No. 20, Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting, requires that governments' proprietary activities apply all GASB pronouncements as well as the following pronouncements issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements, Financial Accounting Standards Board ("FASB") Statements and Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins. Governments are given the option whether or not to apply all FASB Statements and Interpretations issued after November 30, 1989, except for those that conflict with or contradict GASB pronouncements. The Authority has elected not to implement FASB Statements and Interpretations issued after November 30, 1989.

Revenue Recognition

The Authority recognizes revenue when power is delivered and billed to the customers.

Cash and Cash Equivalents

The Authority treats short-term temporary cash investments with original maturities when purchased, of three months or less as cash equivalents.

Property, Plant, Equipment and Depreciation

Property, plant and equipment are stated at original cost. The costs of additions and replacements are capitalized. Replacements of minor items of property are charged to expense as incurred. Costs of property retired are eliminated from accounts, likewise such costs plus removal expense less salvage are charged to accumulated depreciation.

Advances for Hoover Upgrading Program

Proceeds from bonds payable were advanced by the Authority for upgrading the Hoover Power Plant and are recorded as advances. Such advances, including debt issue costs, plus net interest expense incurred by the Authority are reimbursed in the form of credits on the monthly power bills rendered by the Western Area Power Administration of the Department of Energy ("Western"). These credits are issued over the 30-year life of the bonds. Substantially all advances, net interest expense and other related costs on the bonds are charged to the Upgrading Program as amounts to be recovered from future credits.

1. DESCRIPTION OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Investments

The Authority has classified its marketable securities as held-to-maturity. Held-to-maturity securities represent those securities that the Authority has both the intent and ability to hold to maturity and are carried at amortized cost.

Schedule C Energy

Under its Electric Service Contract with Western, the Authority has preferential rights to excess energy ("Schedule C energy") generated at the Hoover Power Plant. The Authority buys Schedule C energy when available from Western during an operating year (October 1 to September 30). The Authority's financial statements are prepared on a fiscal year (July 1 to June 30) basis. When excess energy is available, the Authority bills its customers as Schedule C energy is delivered and receives payment during a given operating year, but Western does not bill for the cost of such Schedule C energy until the following operating year. An estimate of such amounts is accrued for at the end of the fiscal year. The Statement of Net Assets as of June 30, 2003 does not include an accrual for Schedule C energy as no Schedule C energy was available during the operating year.

Operating and Nonoperating Revenues

Operating revenues are revenues derived from the sale of power to customers or from other contractual agreements. Operating revenues include \$8,400,000 and \$6,300,000 received from Salt River Project for scheduling entity services during the years ended June 30, 2003 and 2002, respectively. The revenue is the result of an agreement between the Authority and the Salt River Project which will yield \$8,400,000 annual revenues to the Authority thereby reducing the overall revenue requirements to be paid by the Authority's customers through power rates. The agreement expires September 30, 2004 unless renewed. Nonoperating revenues are from sources other than the sale of power to customers and primarily consist of income earned on investments.

Application of Net Assets to Expenses Incurred

The Authority applies unrestricted, undesignated net assets to expenses incurred. To the extent undesignated net assets are unavailable, unrestricted, designated net assets will be applied to expenses incurred.

Customer Credits

The Authority operates on a nonprofit basis and reduces charges to its customers, through credits on power bills, for any revenues in excess of expenses after the close of the operating year. Likewise, the Authority bills its customers for any deficit in revenues versus expenses incurred during the operating year.

As of June 30, 2003, there were no accrued credits to be applied to customers' power bills based upon rates from Western's operating year ending September 30, 2003.

Income Taxes

The Authority is exempt from federal and Arizona state income taxes. Accordingly, no provision for income taxes has been recorded for the Authority in the accompanying financial statements.

1. DESCRIPTION OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Use of Estimates

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

Geographic and Product Concentration

The Authority's revenues are derived from the sale of electrical power and services to contracted customers in the state of Arizona. The Hoover Uprating Fund is used to purchase electric power solely from Western. The Authority's General Fund is used to purchase electric power from various providers.

2. FUND ACCOUNTING

Hoover Uprating Fund

The Hoover Power Plant Act of 1984 ("Hoover Act") authorized the U.S. government to increase the capacity i.e., "uprate," of existing generating equipment at the Hoover Dam Power Plant ("Uprating Program"). Instead of appropriating further federal funds for the Uprating Program, Congress implemented an advancement of funds procedure whereby prospective nonfederal purchasers of the uprated Hoover capacity and associated energy contribute to the financing of the Uprating Program. The Uprating Program was determined to be complete in September 1995.

The Authority financed a portion of the total Uprating Program by issuing bonds. The Hoover Uprating Fund accounts for advances by the Authority in connection with the Uprating Program. Effective June 1, 1987, the Authority executed new power contracts with Western and its customers which expire in 2017. The revenues and expenditures applicable to the sale and transmission of power and energy received by the Authority from Western under these contracts are accounted for in the Hoover Uprating Fund.

APA General Fund

The Authority's operations other than those applicable to the Hoover Uprating Fund are accounted for in the APA General Fund. The purchase of supplemental power and the sale and transmission of such power to the Authority's customers comprise the majority of this fund's activity.

3. CASH

All cash balances maintained by the State of Arizona Treasurer are for pooled investment purposes. Statutes require the State Treasurer to invest these pooled funds. The Authority's Commission requires these pooled investments to be invested in obligations of the U.S. government. All investments are carried at cost.

4. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment of the APA General Fund at June 30, 2003 and 2002 were as follows:

	2003	2002
Transmission and distribution plant	\$ 508,683	\$ 508,683
General plant	669,766	702,966
Total	1,178,449	1,211,649
Less: Accumulated depreciation	(1,017,785)	(1,030,150)
Property, plant and equipment, net	<u>\$ 160,664</u>	<u>\$ 181,499</u>

	June 30, 2002	Additions	Disposals	June 30, 2003
Property, plant and equipment				
Transmission plant	\$ 289,049			\$ 289,049
Distribution plant	219,634	-	-	219,634
General plant - office	702,966	9,876	(43,076)	669,766
Total property, plant and equipment	<u>1,211,649</u>	<u>9,876</u>	<u>(43,076)</u>	<u>1,178,449</u>
Accumulated depreciation				
Transmission plant	(289,049)	-	-	(289,049)
Distribution plant	(179,293)	(8,068)	-	(187,361)
General plant - office	(561,808)	(22,643)	43,076	(541,375)
Total accumulated depreciation	<u>(1,030,150)</u>	<u>(30,711)</u>	<u>43,076</u>	<u>(1,017,785)</u>
Property, plant and equipment, net	<u>\$ 181,499</u>	<u>\$ (20,835)</u>		<u>\$ 160,664</u>

The transmission and distribution plant is comprised of a substation and related equipment. Purchased power is delivered over transmission facilities owned by Western. Depreciation is provided on the straight-line composite method based on the estimated useful lives of the property items, which range from five to 44 years.

5. ADVANCES FOR HOOVER UPRATING PROGRAM

Advances for the Hoover Upgrading Program were reimbursed by Western through credits on the Authority's power bills in the amount of \$5,325,522 and \$4,623,123 for the years ended June 30, 2003 and 2002, respectively. Credits were received for the upraters' portion of principal and interest expense on the bonds and other costs associated with the Hoover Upgrading Program. During the year ended June 30, 2003, principal amortization, interest expense and other related costs on the bonds issued to finance the Upgrading Program exceeded interest income by \$5,211,025.



6. BONDS PAYABLE

Bonds payable consists of the following:

	June 30, 2002	Increases	Reductions	Transfers	June 30, 2003
Bond payable current	\$ 1,450,000		\$ (1,450,000)	\$ 2,320,000	\$ 2,320,000
Bond payable long-term	67,495,000	-	-	(2,320,000)	65,175,000
Total bonds payable	\$ 68,945,000		\$ (1,450,000)		\$ 67,495,000

In prior years, the Authority defeased various issues of bonds by purchasing U.S. government securities which were deposited in an irrevocable trust with an escrow agent to provide for future debt service until the call dates. As a result, those bonds are considered to be defeased and the liability for these bonds has been removed from the Hoover Upgrading Fund. Accordingly, these trust account assets and related liabilities are not included in the Authority's financial statements.

The remaining bonds, totaling \$67,495,000, bear interest ranging from 5.0 percent to 5.4 percent, are due from 2004 through 2017, and are secured by the pledged property, as defined by the resolution, which includes the proceeds from the sale of the bonds, rights and interest in various contracts and revenues. The Authority amortizes the bond discount using the straight-line method, which approximates the effective interest method. Principal amounts due over the next five fiscal years ended June 30 and thereafter are as follows: \$2,320,000 in 2004, \$2,545,000 in 2005, \$2,790,000 in 2006, \$3,070,000 in 2007, \$3,385,000 in 2008, \$22,675,000 in 2009 through 2013, and \$30,710,000 in 2014 through 2018. Interest amounts due over the next five fiscal years ended June 30 and thereafter are as follows: \$3,575,274 in 2004, \$3,459,274 in 2005, \$3,329,479 in 2006, \$3,184,399 in 2007, \$3,021,689 in 2008, \$11,958,780 in 2009 through 2013, and \$5,009,369 in 2014 through 2018.

Crossover Refunding

On September 12, 2001 the Authority issued \$57,520,000 of Special Obligation Crossover Refunding Bonds. Proceeds from the sale of the bonds along with a fund contribution by the Authority will be held in an escrow trust account invested in government securities until October 1, 2003 (the "Crossover Date") when, if certain conditions are met, the crossover refunding is scheduled to take place and \$62,630,000 of the 1993 Series Power Resource Revenue Refunding Bonds maturing on and after October 1, 2005 will be called. If these conditions are not met, the assets in the escrow trust account will be used to retire the Special Obligation Crossover Bonds on the Crossover Date. The crossover is subject to the condition that on the Crossover Date balances held in the Debt Service Reserve Account at least equal the Debt Service Reserve Requirement and an appropriate legal opinion regarding the validity of the Authority's 2001 Series Power Resource Revenue Refunding Bonds has been received.

6. BONDS PAYABLE
(CONTINUED)

(Crossover Refunding - Continued)

The proceeds in the government securities escrow trust account, together with the income realized from investment of trust assets, serve as collateral for the Special Obligation Crossover Bonds and are paying the debt service on those bonds until the Crossover Date. The Special Obligation Crossover Bonds are payable solely from the amounts in the escrow trust account and are not payable from any other source. Because they are not payable from revenues derived by the Authority or secured by any assets held by the Authority, neither the Special Obligation Crossover Bonds nor the assets held in the escrow trust account are reflected on the Authority's Statements of Net Assets at June 30, 2003 or 2002. However, in conjunction with the issuance of the Crossover Bonds, the Authority deposited \$2,694,576 with the crossover bond trustee; this amount is reflected as "Cash with fiscal agent" in the Authority's Statements of Net Assets at June 30, 2003 and 2002.

If the crossover occurs on the Crossover Date, the outstanding Special Obligation Crossover Bonds will be exchanged for 2001 Series Power Resource Revenue Refunding Bonds of the same principal amount, maturity date, and interest rate as the crossover bonds. The proceeds in the escrow trust account will be used to call that portion of the 1993 Series Bonds maturing on and after October 1, 2005. The 2001 Series Bonds will be reflected as obligations on the Authority's books, and any gain or loss on extinguishment will be reflected in the Authority's records as of the Crossover Date. On and after the Crossover Date, the called portion of the 1993 Series Bonds will no longer be outstanding and will cease to be entitled to any lien on the revenues pledged to payment of those bonds. Instead, the revenue stream originally pledged to secure the called portion of the 1993 Series Bonds will "cross over" to pay debt service on the 2001 Series Bonds. The Crossover Bonds and 2001 Series Bonds bear interest at a rate of 5 percent and 5.25 percent, payable on April 1 and October 1 of each year, commencing April 1, 2004 and maturing in 2017.

On October 1, 2003, the Authority met the conditions described above to effect the crossover refunding which resulted in \$57,520,000 of Special Obligation Crossover Refunding Bonds being exchanged for 2001 Series Power Resource Revenue Refunding Bonds of the same principal amount, maturity date and interest rates as the crossover bonds. In addition, as part of the crossover, \$62,630,000 of the 1993 Series Power Resource Revenue Refunding Bonds maturing on and after October 1, 2005 were called. As required by regulation, the Authority applied an additional \$600,113 of funds held in the Debt Service Reserve Account to effect the crossover transaction and call the \$62,630,000 obligation. As a result of this transaction, the Authority recognized an economic gain (difference between the present value of the old and new debt service payments) of \$2,095,648. The crossover refunding resulted in the recognition of a deferred amount of \$2,411,956 that will be reflected as a decrease in bonds payable and will be amortized as a component of interest expense over the life of the refunded bonds. The cash flows required to service the new debt are \$4,572,093 less than the cash flows required to service the old debt.



7. INVESTMENTS HELD BY TRUSTEE

As of June 30, 2003 and 2002, investments are collateralized with securities held by the Authority's trustee. The amortized cost, which approximates fair value due to the short-term nature of the held-to-maturity investments, of the investment securities at June 30 is as follows:

	2003	2002
Repurchase agreement	\$ 7,146,663	\$ 7,146,663
U.S. government securities	2,592,771	2,568,910
Total held-to-maturity investments	<u>\$ 9,739,434</u>	<u>\$ 9,715,573</u>

On September 19, 1996, the Authority entered into a repurchase and custody agreement with MBIA Investment Management Corporation ("IMC") wherein the Authority agreed to effect a series of repurchase transactions with IMC, in investments allowable under the bond resolution agreements and state law, with a fixed earnings rate of 6.95 percent. The securities are held in trust by Bank One of Arizona, N.A. If at any time the aggregate market value of all purchased securities is less than the amount required under the repurchase and custody agreement (calculated using a percentage of 104 percent), the Authority may require IMC to transfer additional securities so the aggregate market value of all securities will equal or exceed such requirement.

8. NET ASSETS

Allocations of net assets for specified purposes are authorized and designated by the Commission, under provision of the Arizona Power Authority Act of 1944, as amended. The designated reserves shown on the accompanying statements of net assets are comprised of the following at June 30, 2003 and 2002:

	2003	2002
Resource development	\$ 3,500,000	\$ 3,500,000
Operations fund	200,000	200,000
Power contracts	100,000	100,000
System improvement and repairs	200,000	200,000
Total	<u>\$ 4,000,000</u>	<u>\$ 4,000,000</u>

9. RETIREMENT PLAN

The Authority contributes to the retirement plan described below. Benefits are established by state statute and generally provide retirement, death, long-term disability, survivor, and health insurance premium benefits.

The Arizona State Retirement System (the "Plan" or "ASRS") administers a cost-sharing multiple-employer defined benefit pension plan that covers permanent, full-time employees of the Authority. The ASRS is governed by the Arizona State Retirement System Board according to the provisions of ARS Title 38, Chapter 5, Article 2. The ASRS issues a publicly available financial report that includes its financial statements and required supplementary information. A report may be obtained by writing or calling the Plan at 1020 East Missouri Avenue, Phoenix, Arizona 85014, (602) 255-5575. The Plan was established by the State of Arizona to provide benefits for employees of the state and employees of participating political subdivisions and school districts. The Plan became effective on July 1, 1971. By actuarial computation, employee member and Authority contributions to the Plan were fixed at 2.49 percent (2.00 percent retirement and .49 percent long-term disability) of their compensation for the years ended June 30, 2003 and 2002, with the contributions made through payroll deductions. Employee contributions vest immediately. Total contributions to the Plan for the years ended June 30, 2003 and 2002 by the Authority's covered employees were \$14,854 and \$12,728, respectively.

9. RETIREMENT PLAN (CONTINUED)

Matching employer member contributions were actuarially determined and fixed at the same rate as employee member contributions for the years ended June 30, 2003 and 2002. In the event the Plan's actuary determines that additional contributions are needed in order to amortize an unfunded accrued liability, every employer member will be required to contribute the revised contribution percentage which is established by the Arizona State Legislature.

All full-time employees of the Authority are required to become members of the Plan. The Authority's total payroll for employees covered by this Plan for the years ended June 30, 2003 and 2002 were \$611,569 and \$521,521, respectively. Contributions to the Plan by the Authority for its covered employees vest over five years. All required employer contributions are made to the Plan by the end of each month.

10. ADDITIONAL BENEFITS

In addition to the pension benefits described above, ASRS offers health care benefits to retired and disabled members that are no longer eligible for health care benefits through their former member employer's group health plan. Retired is defined as actively receiving an annuity benefit and disabled is defined as receiving a long-term disability ("LTD") benefit through the LTD program administered by ASRS. The following chart illustrates the maximum amount of the monthly available benefit for eligible members and their dependents:

Years of Credited Service	Percent of Premium Benefit	Member		Member and Dependent(s)	
		Not Medicare Eligible	Medicare Eligible	Not Medicare Eligible	Medicare Eligible
5.0 - 5.9	50%	\$ 75.00	\$ 50.00	\$ 130.00	\$ 85.00
6.0 - 6.9	60%	90.00	60.00	156.00	102.00
7.0 - 7.9	70%	105.00	70.00	182.00	119.00
8.0 - 8.9	80%	120.00	80.00	208.00	136.00
9.0 - 9.9	90%	135.00	90.00	234.00	153.00
10.0+	100%	150.00	100.00	260.00	170.00

11. PURCHASED POWER, SALES AND TRANSMISSION COMMITMENTS

The Authority is party to Firm Electric Service and Transmission Service Contracts with terms expiring September 30, 2017. This requires the Authority to pay approximately 19 percent of Western's revenue requirements each operating year until the contract expires. During the years ended June 30, 2003 and 2002, the Authority paid \$14,971,173 and \$15,344,365, respectively, for purchased power under this contract. The Authority is obligated to pay these costs under the contract even in the unlikely event that no power is supplied.



11. PURCHASED POWER, SALES AND TRANSMISSION COMMITMENTS (CONTINUED)

The Authority also has a contract with Western for transmission services. During the years ended June 30, 2003 and 2002, the Authority paid \$5,217,806 and \$5,204,148, respectively, for transmission costs to Western. On January 24, 2003, the Authority entered into the Advancement of Funds for Transmission Services contract with Western. The contract provides for the Authority to advance funds to Western on a monthly basis to fund operations, maintenance and replacement costs associated with Western's transmission services. The advanced funds are then applied to the subsequent month's transmission invoice. As of June 30, 2003, the Authority recognized a prepaid deposit of \$182,360 that is refundable upon termination of the contract.

The Authority has sales contracts with all customers. Under these contracts, customers are obligated to pay for their percentage allocation if any Hoover power is delivered or made available for delivery. These sales contracts expire September 30, 2017, but some can be terminated by the Authority on June 1, 2007 or thereafter.

The Authority also has contracts with Salt River Project for the purchase and transmission of power to the Authority's customers. Under the transmission contract, the Authority must pay an annual transmission fee of \$63,898 until September 30, 2017.

DEBT SERVICE COVERAGE RATIO

NET INCOME	\$ 83,021
Add:	
Interest Expense (1)	3,593,036
Amortization (1)	82,842
Depreciation (1)	21,511
Western Credits	5,325,528
Credits to Customers for Prior Year	2,894
Total Additions	9,025,811
Deduct:	
Deferred Interest Expense	(2,958,718)
Total Deductions	(2,958,718)
Income available for debt service	\$ 6,150,114
Debt service (2)	\$ 5,333,036
Debt service coverage ratio	1.15

(1) Interest expense, depreciation expense and amortization of Uprating Costs are not expenses under the Bond Resolution.

(2) Debt Service is the total of Principal and Interest Expense accrued between July 1, 2002 and June 30, 2003.

IN MEMORY OF:



DR. JEWELL M. LEWIS
1929 - 2003

Dr. Jewell M. Lewis was originally appointed to the Arizona Power Authority Commission in 1986. The Authority was privileged to have Dr. Lewis as Commission Chair from 1994 to 1996, and for the past 15 months. During her tenure, Dr. Lewis was a strong advocate of protecting the environment and endangered species while ensuring the preservation of the Colorado River as a water and power resource for the State of Arizona. Under Dr. Lewis' guidance, the Authority focused on maintaining close relationships with the Bureau of Reclamation and the Western Area Power Administration. She was instrumental in the Authority's efforts to provide for the operation and maintenance of Hoover Dam and its associated transmission system, thereby assuring the availability of these resources to the citizens of Arizona.

Dr. Lewis was well known for her commitment to public education and her generosity in supporting various community projects. At the time of her passing, Dr. Lewis was a member of the Arizona Prenatal Board of Trustees, the NAU Center for Excellence in Education Advisory Board and the Governor's Advisory Committee on Quality Education. In 2001, Dr. Lewis was named Valley Leadership Woman of the Year.

Jewell was a valued member of our Commission for many years. She was a gracious, intelligent lady, and we will miss her.



ARIZONA POWER AUTHORITY
1810 West Adams Street / Phoenix, Arizona 85007
(602) 542-4263 / Fax (602) 253-7970

