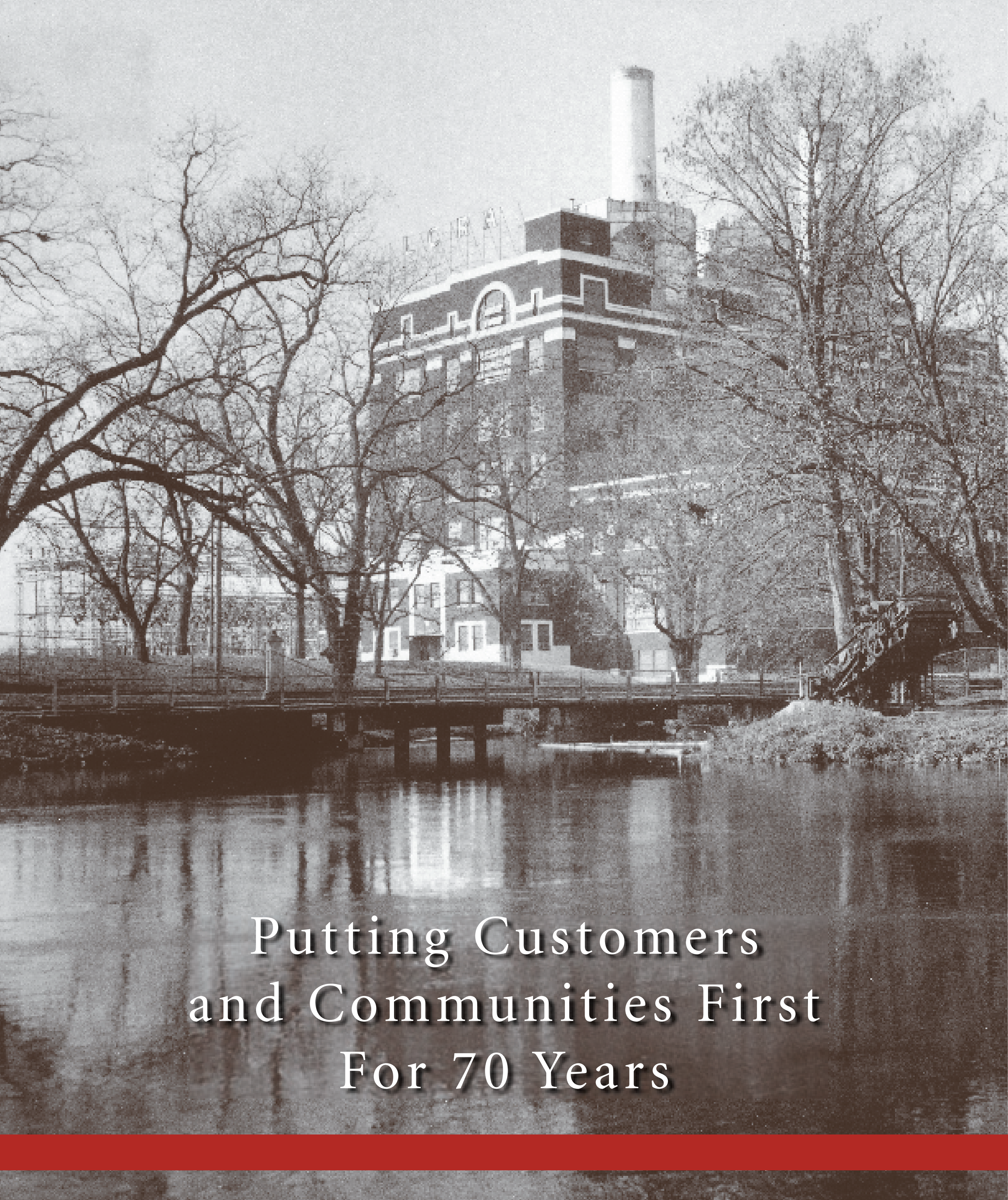
LCRA 2004 ANNUAL REPORT



Putting Customers and Communities First For 70 Years

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A Message From Management

"Putting Customers and Communities First," the theme of LCRA's fiscal year 2004 Annual Report, describes LCRA's approach in providing energy, water and community services.

As this annual report shows, we are continuing to do all of this on a sound financial footing. During fiscal year 2004, LCRA's electric, water and community services operations generated $694.4 million in revenues and $599.4 million in expenses. The financial performance of LCRA and its affiliates was on target, with $183.3 million in net revenues available for debt service, $7.6 million above projections. We finished the fiscal year with a debt service ratio of 1.37, better than the FY 2004 goal of 1.32.

We are pleased with our financial performance for FY 2004 and are confident that we will continue to operate on a sound financial basis in the years to come. But the efficacy of LCRA's operations must be measured in ways that transcend dollars and cents. We are not just providing utility and public services – we are building relationships with the people who depend on our services and investing in the quality of life that makes the region of Texas we serve a great place to live.

LCRA's historic Comal Power Plant, which is featured on the cover, is a good example of putting customers and communities first. At one time, it generated electricity for LCRA until rising operational costs forced LCRA to shut it down more than 30 years ago. That could have been the end of the Comal Plant story. But, as you can read in this report, LCRA gave Comal a new life, transforming it into a community asset that will create jobs and tax revenues.

We believe Comal illustrates an aspect of LCRA that makes us unique to the people and communities we serve. Seventy years ago, the State of Texas created LCRA to provide not just utility services but – more important – a better way of life for people in the lower Colorado River basin and surrounding Central Texas communities. LCRA employees of those days knew exactly why they were building dams and stringing power lines: it was to provide a measure of safety and a living standard that other organizations, public or private, would not or could not provide.

Seventy years later, some of our region's specific needs may have changed – such as issues related to a more urban and rapidly growing population – but the underlying need to maintain and improve the region's quality of life has not. And in that respect, LCRA's mission is still the same – to provide the services and programs needed by communities and people for a better life.

This annual report reflects that unchanging commitment, both in a summary of our 2004 fiscal year and in historical perspectives looking back over LCRA's first 70 years. We look forward to LCRA carrying out that same commitment for many years to come.

Ray A. Wilkerson, Board Chair

Joseph J. Beal, P.E., General Manager

Opposite page:
Joseph J. Beal (left) and Ray A. Wilkerson

Construction crew at Buchanan Dam – LCRA's first major project to dam the Colorado River as the project neared completion in 1937.

Creating LCRA

The Texas Legislature created LCRA in November 1934 to harness the lower basin of the Colorado River of Texas by minimizing the impacts of floods and droughts, generating electricity, and providing other services that would vastly improve the lives of basin residents.

LCRA's first logo – the original seal that was used on official LCRA documents – illustrated those duties and helped tell LCRA's story. One of the original LCRA Board members, Ralph Yarborough (who would go on to serve as a U.S. senator), claimed to have designed the first version when illness prevented him from attending one of the frequent meetings held by the Board to get LCRA organized.

The final version of the seal symbolized LCRA's original areas of responsibility: an electric motor and light bulb for electric generation and power, a tree for reforestation, a plow for soil conservation, and a fish for the waters of the Colorado – all placed around a lone star that reflected LCRA's ties to the State of Texas. Inside the star was a depiction of Buchanan Dam and its power house, the first project tackled by LCRA.

While the design served as LCRA's official seal until 1980, LCRA used a variety of logos through the decades to represent itself, including one with a lightning bolt that was used from the 1940s into the mid-1970s.

The original LCRA seal was designed in the 1930s.

LCRA Today

Many LCRA employees, and perhaps a few customers, were surprised when LCRA unveiled its new logo in the early 1990s: in place of a variation of a state seal, the new logo featured "LCRA" in bold block letters that sported a lightning bolt and water waves.

The new look illustrated the changing environment in which LCRA operated. Its executives believed LCRA's key to success lay in changing the organization's longtime image as a government agency to more of a business that added value to the services it provided customers.

The original version of the logo carried the tagline, "The Power To Make a Difference," which summarized LCRA's history of transforming the lower Colorado River basin and a confidence in continuing that tradition of value. The current version of the logo, modified in 2001, has a simpler tagline that summarizes the value LCRA brings in providing energy, water and community services.

Like the original LCRA logo of 1935, LCRA's current logo reflects its unchanging commitment to serve the people of Texas as a provider of electric and water utility services and a steward of the lower Colorado River's natural resources.

LCRA

ENERGY • WATER • COMMUNITY SERVICES

The LCRA logo of today brands all of LCRA's programs and services.

70 Years of Putting Customers and Communities First

In fiscal year 2004, LCRA focused on carrying out plans to meet growing needs for energy, water and community services in the fast-growing Central Texas and surrounding regions in the coming years, with an emphasis on transmission projects, upgrading power plants to improve operations and lower emissions, completing water and wastewater utilities, and improving public parks.

And while population growth has brought new challenges for LCRA and the communities it serves, the need for efficient, reliable utility and community services is still the same as in 1934, when the Texas Legislature created LCRA to provide those services to people and communities in the lower portion of the Colorado River basin.

In responding to its communities' needs throughout fiscal year 2004, LCRA echoed similar actions it has taken to meet the needs of its service area communities for energy, water and community services over the past 70 years.

In honor of this unchanging commitment, and in recognition of LCRA's 70th anniversary, this year's report features historical vignettes over the past seven decades interspersed among the highlights of the 2004 fiscal year.

The Year and LCRA in Review

Energy: Generation

LCRA produces and sells wholesale electricity to 42 electric cooperatives and city-owned utilities that serve more than 1.1 million people in Central Texas. LCRA's wholesale rates are among the lowest in Texas, and its power plants are among the cleanest in the United States due to a strong commitment to environmental leadership. Communities in LCRA's service area also are eligible to participate in LCRA's community services programs.

Here are some of the things LCRA did during FY 2004 to provide reliable and efficient electric generation to its customers:

- Wholesale electric customers received credits totaling $29.7 million on their electric bills, thanks to lower-than-projected costs by LCRA for fuel and purchased power and better-than-expected performance in operations and maintenance of LCRA's generation facilities.

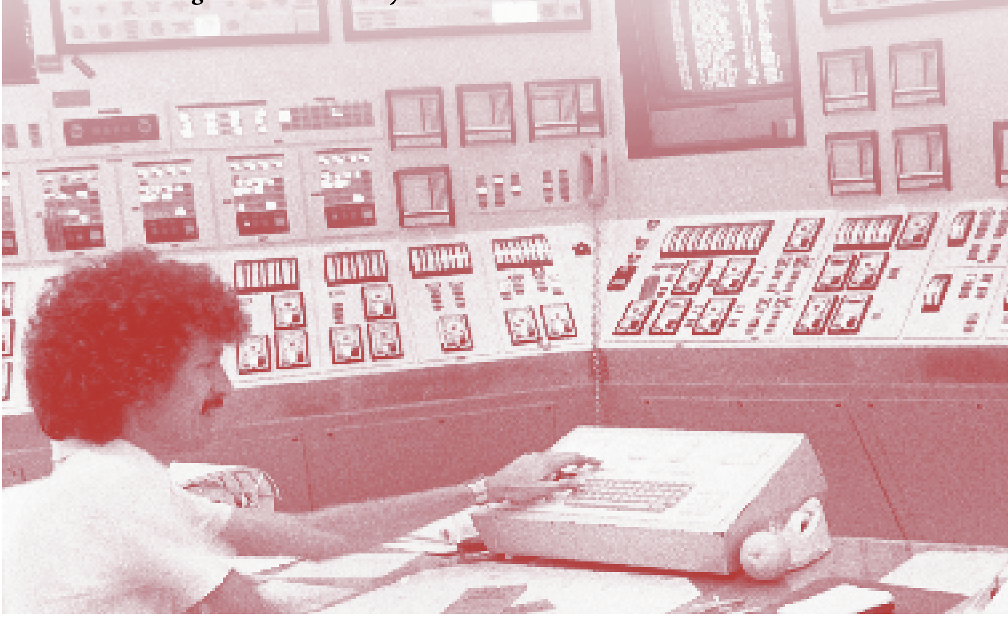
Thomas C. Ferguson, one of LCRA's original directors, in 1974 at the power plant that was named for him.

The Original Clean Energy Source

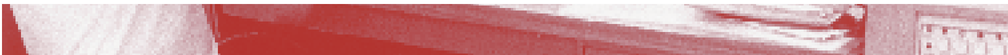
Long before environmental quality was an issue, LCRA was electrifying the rural regions of Central Texas with a renewable energy source. Hydroelectric power stations at dams built in the late 1930s and 1940s by LCRA generated the power that turned on the lights in communities, farms and ranches throughout the Hill Country and other rural areas surrounding Austin.

Low-cost electricity from LCRA transformed rural Central Texas, provided power that contributed to the region's industrial and agricultural output during World War II, and enabled residents to acquire a standard of living comparable to that enjoyed by residents in larger cities. To help rural residents discover the benefits of living better electrically, LCRA and the Rural Electrification Administration in 1940 sponsored "electric fairs," introducing residents to appliances that lightened their workloads and made their homes more comfortable.

LCRA hydroelectricity – created by the force of falling water from the Colorado River – was a major source of the power for Central Texans through the 1950s. As the region continued to grow in the 1940s and '50s, so did the demand for electricity. Because LCRA could not generate more hydroelectric power, it met this additional demand by building power plants, such as the Thomas C. Ferguson Power Plant (opposite page), that burned fossil fuels to generate electricity.



The Fayette Power Project control room in the late 1970s.



A Continuing Commitment to Clean Energy

While most of LCRA's electricity comes from fossil-fueled power plants, LCRA continues to practice environmental leadership in the way it generates and provides electricity.

LCRA has chosen through the years to build and operate its power plants to be as environmentally compatible as possible, in many cases doing far more than is mandated by state and federal governments.

For example, LCRA has reduced nitrogen-oxide emissions by more than half at its power plants in Bastrop County, even with the addition of the 500-megawatt Lost Pines 1 Power Project. LCRA also has worked to reduce nitrogen-oxide emissions at the nearby Fayette Power Project. These reductions contribute to better air quality for the region.

In 1995 LCRA took part in the first wind power project in Texas and today purchases power from three such projects. This wind-generated power, along with hydroelectric generation, makes up about 5 percent of LCRA's total energy resources – making LCRA a leader in providing renewable energy to Texas.

The Fayette Power Project as it appears today. The Unit 3 stack at left is releasing steam.

- LCRA worked to secure a reliable, competitively priced, long-term natural gas supply to enhance fuel reliability for its power plants and keep the cost of fuel steady during market fluctuations. LCRA also provided ancillary services to other utilities and the Electric Reliability Council of Texas. These services produced $14 million in revenues and further offset costs to wholesale electric customers.
- To help meet the future needs of LCRA's wholesale electric customers, GenTex Power Corporation, an LCRA energy affiliate, acquired full ownership of the Lost Pines 1 Power Project in Bastrop County. The purchase adds 272 megawatts of capacity to meet growing customer needs in the next few years.
- As part of an ongoing commitment to safety, LCRA's power plants became chlorine-free by replacing chlorine products with safer alternatives for treating and disinfecting water used in power plant generation processes.

Employees at Sim Gideon Power Plant do maintenance work on the generator shaft of one of the plant's three units.

Energy: Transmission

The success of retail electric competition in Texas depends on the ability of transmission lines to transport large amounts of electricity reliably from one area of the state to another. LCRA has developed and maintained transmission systems for decades to serve its wholesale electric customers in Central Texas. The Texas Legislature in 1999 authorized LCRA to provide transmission services statewide to help improve the grid's reliability and capacity. That law also required utilities in the state to separate electric generation and transmission systems. As a result, LCRA created a nonprofit corporation, LCRA Transmission Services Corporation (LCRA TSC), and transferred its transmission and transformation assets to this corporation.

LCRA provides staff for LCRA TSC. LCRA TSC provides transmission-related services to electric cooperatives and municipal electric systems in Central Texas.

Here are the highlights of LCRA's transmission operations in FY 2004:

- LCRA TSC was a leading constructor of new transmission facilities in the state's largest grid. LCRA TSC completed $196 million in capital additions, including upgrades to 168 substations and 343 miles of transmission line and construction of 30 miles of new line.

LCRA crews, like this one in 1956, built and maintained transmission and distribution lines that delivered LCRA electricity to homes and businesses.

Bringing Power to the People

In 1938, at the urging of Congressman Lyndon Johnson, LCRA determined that it would market the power from its newly completed dams to serve communities and rural areas throughout Central Texas. That decision required a transportation network to deliver the electricity to its customers, and in November 1938 LCRA's transmission network was born, with approval by LCRA directors for the construction of transmission lines from the dams to seven Hill Country towns.

LCRA's transmission network expanded instantly the following year when a private utility sold LCRA a 16-county section of its service area along the Colorado River from Lampasas to Brenham. In 1941 another private utility sold an adjacent portion, forming most of what has been LCRA's traditional electric service area.

By 1948 LCRA's network spanned more than 1,000 miles (less than a third of today's total), carrying power from four Highland Lakes dams and a power plant in New Braunfels to LCRA's wholesale electric customers.

While LCRA's service territory remained about the same, LCRA continued to expand and upgrade its transmission network to respond to the growing need for electricity.

Two LCRA employees inspect a transmission line pole in 1950.

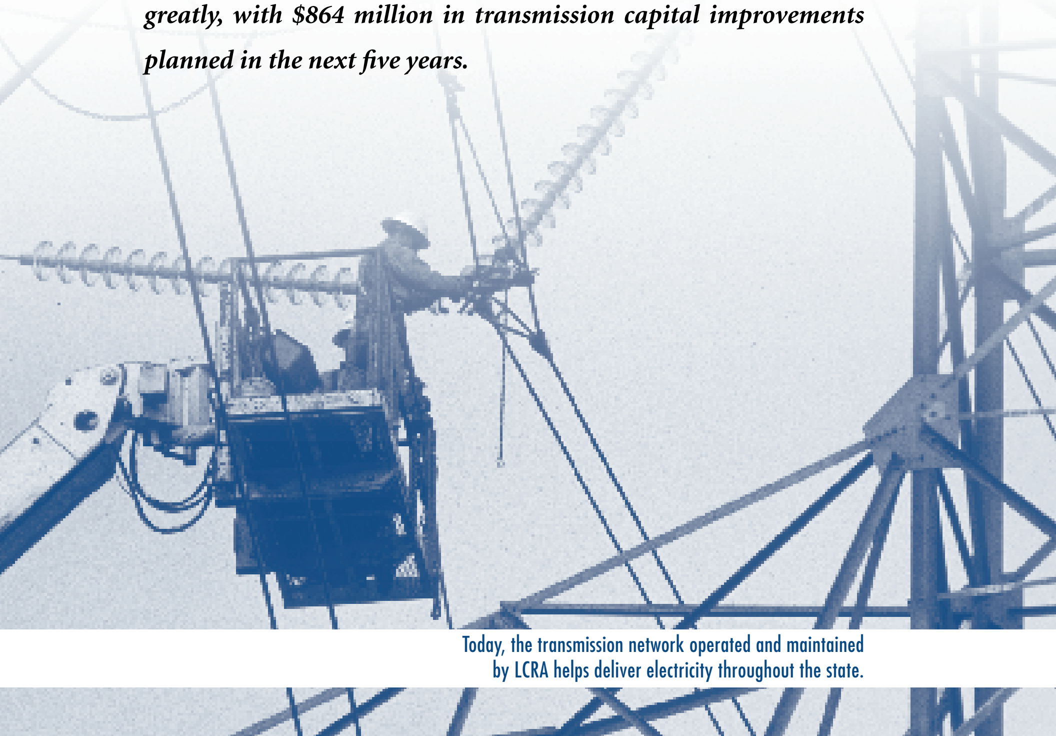
Steadfast Service in Changing Times

An array of large-screen video monitors lines the wall at LCRA's System Operations Control Center, providing instantaneous updates of the transmission network throughout LCRA's electric service area and other parts of Texas. The electronic system long ago replaced analog readouts and a grid of LCRA's transmission system painted on a wall, on which staff tracked the status of lines by moving magnetic markers around the grid.

More than the technology has changed. In the 1990s the Texas Legislature deregulated the state's electric utility industry to increase competition and benefit consumers. As required by state law, LCRA and other utilities have "unbundled" their generation and transmission services and operate them separately. For LCRA, that included moving Transmission Services employees to another work location, as well as transferring its transmission assets to a nonprofit corporation it created. (LCRA staff continues to operate and maintain the assets.)

Deregulation allowed LCRA to expand outside its traditional electric area to work with investor-owned utilities to upgrade the statewide transmission network to improve reliability, relieve congestion and deliver renewable energy from West Texas wind power farms.

Today, LCRA Transmission Services Corporation's network spans nearly 3,500 miles. Transmission services will continue to expand greatly, with $864 million in transmission capital improvements planned in the next five years.



Today, the transmission network operated and maintained by LCRA helps deliver electricity throughout the state.

- In November 2003, LCRA TSC filed a rate case with the Public Utility Commission of Texas to recover significant costs incurred while improving transmission systems in Texas. LCRA TSC's net capital assets have increased by $447 million, or 124 percent, since January 2002, with additional planned investments of $864 million in capital improvement projects through fiscal year 2009. The rate case, which was under way at the end of the fiscal year, was the second in a series to recover LCRA TSC's costs of constructing new assets.
- LCRA TSC continued to improve transmission system reliability, based on the systemwide average number of minutes per customer that "the lights are out" during unplanned outages. The average achieved in FY 2004 was 4.4 minutes, better than the FY 2003 average of 9.8 minutes and the FY 2002 average of 13.8 minutes.
- Maintaining transmission rights of way plays a significant role in ensuring both safety and system reliability. As more people move into rural areas, managing rights of way can become a challenge. LCRA TSC held five community open houses and visited more than 450 landowners and public officials during FY 2004 to seek public input on proposed transmission construction projects.

An LCRA crew erects a transmission tower as part of a substation upgrade to continue providing reliable service to residents in San Saba.

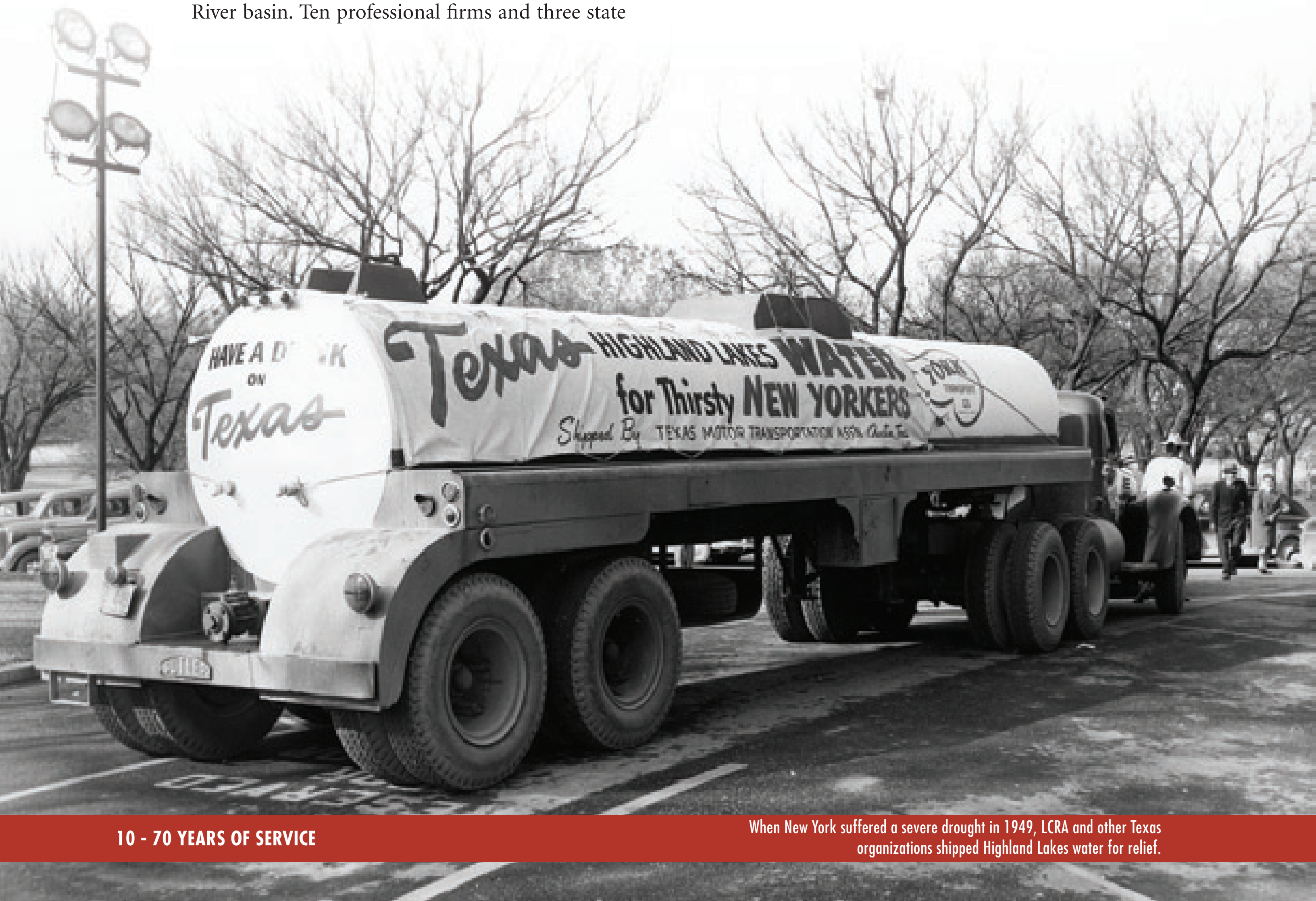
Water Services

River Management

LCRA manages the 600-mile lower segment of the Colorado River and built and operates the dams that form the Highland Lakes above Austin. LCRA stores water supplies for cities, industries, farmers and estuaries in the basin. LCRA also manages floods and works with local and county governments along the river to improve flood controls and help protect lives and property from floods.

Here are highlights of LCRA's river management operations in FY 2004:

- LCRA and the San Antonio Water System (SAWS) continued to study the feasibility of an innovative, long-term, interbasin water supply plan that would provide water to the San Antonio area while developing more water supplies for the lower Colorado River basin. Ten professional firms and three state universities are helping conduct the studies to determine if the plan is technically, environmentally and economically sound before it is implemented. SAWS is funding the studies.
- In partnership with three state agencies, LCRA is updating studies to determine freshwater inflow needs from the Colorado River into Matagorda Bay to support a diverse marine habitat.
- LCRA successfully managed a major flood that hit the lower Colorado River in June 2004 after storms dropped as much as 10 inches of rain in the upper basin. The amount of water released from Mansfield Dam as a result of the flood – almost 114 billion gallons – would have been enough to supply the City of Austin for more than three years.



When New York suffered a severe drought in 1949, LCRA and other Texas organizations shipped Highland Lakes water for relief.

Harnessing "Flash Flood Alley"

LCRA was created in part to deal with the effects of "Flash Flood Alley" – the Hill Country region where a combination of topography and intense storms resulted in massive floods that frequently devastated Austin and downstream cities. (More than 80 such floods have occurred in the basin since the 1840s.)

The key to protecting the downstream communities was to build a reservoir upstream to capture and hold Hill Country floodwaters and release them in a safe manner. In 1937, with Buchanan and Inks dams nearing completion, LCRA broke ground on what would become Mansfield Dam, the massive structure that would serve as a bulwark against the Hill Country floods.

As though to prove the need for an LCRA, the Colorado suffered three major floods during LCRA's first years – in 1935 and 1936, as well as a 1938 flood that almost put LCRA out of business, as many residents and politicians blamed LCRA and its dams for worsening the flood. An investigation by the Texas Legislature determined that LCRA had actually lessened the flood's impact – and that it needed to raise the elevation of Mansfield Dam, still under construction, to be better prepared for the vagaries of Hill Country floods.

Before LCRA built the Highland Lakes chain of dams, scenes like this – where massive floodwaters pour over the Congress Avenue Bridge in Austin in June 1935 – were common.

Preparing for the Next Great Flood

LCRA completed Mansfield Dam in 1941 and the rest of the Highland Lakes chain in 1951. No floodwaters have ever topped the spillway of Mansfield Dam.

But hydrological evidence suggests the basin will once again experience massive flooding as bad or worse as the 1938 flood. And that flood will afflict a more urban population, much of it located along the Colorado, its lakes and tributaries.

In response, LCRA has expanded its flood-readiness operations. Since the late 1980s it has built throughout the basin the Hydromet network of electronic river and weather gauges that supplies real-time data to provide a more comprehensive picture of potential flood conditions.

Partnering with the National Weather Service, LCRA has built a network of transmitters that broadcast local NOAA Weather Radio information to residents throughout the basin, including warnings of severe weather and floods. LCRA also is working with the U.S. Army Corps of Engineers and local communities to update local floodplain information and educate residents on the responsibilities of living in a floodplain.

And LCRA has upgraded the Highland Lakes dams to ensure they will continue to withstand the most severe floods. LCRA completed this upgrade in fall 2004, five years ahead of the original schedule.

Today, floodgate operations at Buchanan and other LCRA dams help protect downstream communities from the worst effects of Hill Country floods.

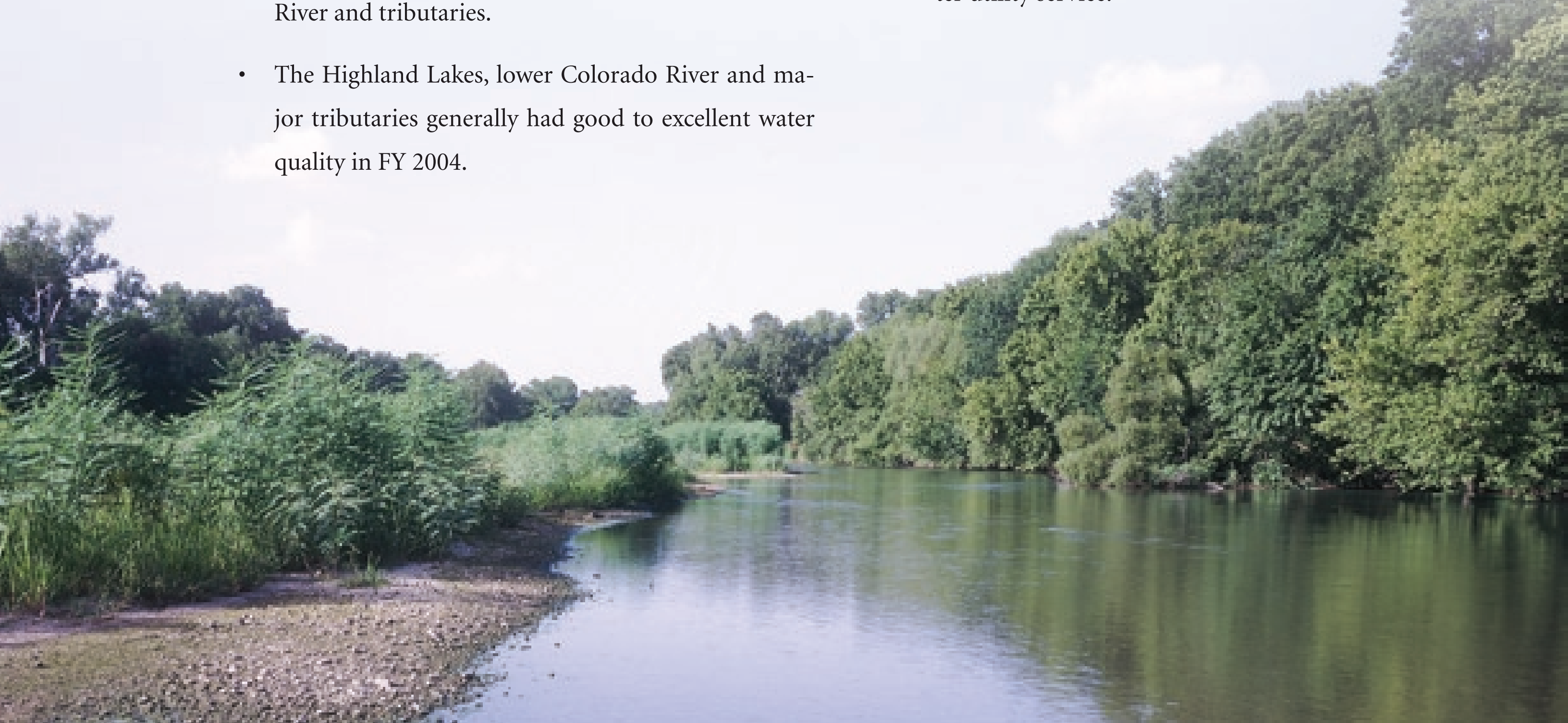
- LCRA continued to expand and upgrade its Hydromet system, a network of sophisticated gauges that provide around-the-clock data on weather conditions, lake levels, streamflows and rainfall in the lower Colorado River basin. The system enables LCRA's River Operations Center in Austin to track fast-changing conditions in the lakes, river and major tributaries during potential flood situations.
- At the end of the fiscal year, LCRA neared completion – five years ahead of its initial schedule – of a $52 million program of structurally reinforcing the Highland Lakes dams to meet current safety standards.
- LCRA helped the Texas Colorado River Floodplain Coalition, whose members include more than 50 city and county government agencies, obtain federal funding commitments of $1.7 million for basinwide flood feasibility studies.
- LCRA began the second step of a 10-year, $8.2 million computer modeling project that will help protect water quality in the Highland Lakes, lower Colorado River and tributaries.
- The Highland Lakes, lower Colorado River and major tributaries generally had good to excellent water quality in FY 2004.

Water and Wastewater Utilities

LCRA offers water and wastewater utility services in rural and suburban communities in the lower Colorado River basin to provide clean, reliable drinking water, protect public health and water quality, and help communities meet growing demands for utility service. LCRA owns or operates 35 water and wastewater systems that serve about 181,300 people in 11 counties.

Here are the highlights of LCRA's water and wastewater utility services in FY 2004:

- LCRA completed construction of eight water utility development projects and four wastewater development projects, and it acquired six water supply systems and one wastewater treatment facility.
- LCRA provided 90 million more gallons of treated drinking water to wholesale and retail customers in FY 2004 than during the previous year, an increase of 5 percent. Many of these customers used unreliable, poor quality groundwater before LCRA provided water utility service.



LCRA works with communities and state agencies to keep the Colorado River downstream of Austin attractive and healthy year-round.

Community Services

LCRA uses 3 percent of its electric and water revenues to provide community services in its 58-county electric and water service area. These services help communities maintain and improve quality of life by supporting tourism, natural science education, recreation and economic and community development.

- Eighty-seven percent of funding for LCRA's community services programs went directly back into the communities in LCRA's service area.
- A policy review of LCRA's community services programs by LCRA's Board of Directors determined that the programs have a solid statutory basis, are needed and wanted by the public, and do not duplicate services provided by others.
- Following a three-year intensive public input process, LCRA adopted safety standards for residential boat docks on the Highland Lakes. The standards were developed to improve dock safety and help protect public access to the popular lakes.
- LCRA helped recruit three new businesses to the area, generating 152 new jobs and $16.3 million in investments. Nearly 1,300 community leaders, elected officials and residents attended economic development training through LCRA's Texas Leadership Institute.
- LCRA completed the sale of land next to its McKinney Roughs Nature Park east of Austin to the Woodbine Development Corporation for a resort hotel, golf course and spa, providing a compatible use to McKinney Roughs. During the two-year construction phase, the project is expected to generate $62 million to the local economy. By 2010 the facility is expected to bring more than $41 million a year to the regional economy.
- Twelve projects totaling 4,830 acres of privately owned ranchland participated in LCRA's Creekside Conservation Program, including 1,541 acres treated for brush management and removal of

Street lights installed by LCRA light up the San Saba courthouse square, 1952.

The Life of a Power Plant

For nearly eight decades, the Comal Power Plant has been a New Braunfels landmark, guarding the entrance to the city's Landa Park.

Comal was built in 1926, almost a full decade before LCRA's creation, by a utility holding company that served San Antonio and other areas of Texas. The plant was built in a pecan grove at the edge of New Braunfels' industrial district to take advantage of the spring-fed waters of the Comal River. Engineers designed the plant to burn lignite for boiler fuel, but by 1929 it was using natural gas and fuel oil.

LCRA acquired the Comal plant in 1947 and operated it for 26 years to help serve the rapidly growing demand for power in its service area. The plant was a training ground for many LCRA employees who went on to run LCRA's newer and larger plants.

Once LCRA's largest single generation source, Comal was all but a museum piece by the early 1970s, with its limited capacity and antiquated equipment. But it could use fuel oil indefinitely (something LCRA's newer plants couldn't do), and it held a contract for some of the lowest-cost natural gas available, which helped offset its rising operational costs.

Then gas costs spiraled out of control in 1973, making the plant uneconomical to operate, and LCRA shut it down. It marked the end of Comal's life as a power plant – but not the end of LCRA's plans for it.

The control room of the Comal Power Plant, late 1940s.

The New Life of a Power Plant

LCRA could have torn down its worn-out Comal plant. Instead it looked for a way to recycle the building and its 37-acre site in a way that would benefit the community.

It wasn't easy. Initial plans to redevelop the site with local organizations fell through, followed by the discovery in 1986 that the plant's insulation contained "friable" asbestos, which can lead to health problems. LCRA began an elaborate remediation process to remove the asbestos as well as lead, PCBs and fuel oil that had been improperly stored in a time when few environmental controls existed. The cleanup took more than a decade.

In April 2004 LCRA sold the site to a development group that will convert the building into the Landmark Loft and Garden Apartments. Developer Larry Peel says he plans to keep the building's distinctive exterior while converting it into 109 loft apartments, along with 186 garden apartments on the campus. It's the first time in Texas for a power plant to be converted to a residential development.

More than 30 years later, the Comal plant's story has a happy ending. Because of LCRA's environmental leadership and commitment to community services, New Braunfels retains its historic landmark while adding $22 million to its tax base.

The interior of the Comal Plant in 1999, after LCRA had completed remediation.

unwanted vegetation such as cedar trees. LCRA's Clean 'n' Green program distributed 12,000 seedlings and 3,750 container trees to schools, local governments and nonprofit entities for planting in 58 communities in the service area.

- LCRA completed three major park improvement projects. Sunset Point, at Lake LBJ, includes a boat ramp, swimming area, cabins and recreational vehicle sites. A new public park at Lometa Reservoir offers a fishing pier, fishing jetty and fish habitat structures. Black Rock Park at Lake Buchanan doubled the number of cabins.
- Nearly 10,000 youths attended educational programs and activities at LCRA's natural science centers in FY 2004. More than 66,000 people visited the centers and their adjacent parks.
- The Kids on the Colorado River program, cosponsored by LCRA and the nonprofit Colorado River Foundation, enabled 5,240 youths – 67 percent of whom were low-income and minority children – to experience raft and canoe trips on the lower Colorado River.
- Nearly 1,200 students representing 59 high schools in the service area attended student leadership forums sponsored by LCRA and some of its wholesale electric customers. The forums bring students together with local community leaders for leadership training and activities.
- LCRA's water-safety presentations and classes reached more than 20,000 youths and adults throughout the basin.
- LCRA and its wholesale electric and water customers awarded 84 community development grants totaling nearly $1.6 million to help fund projects of nonprofit and government entities in LCRA's service area, such as volunteer fire departments, emergency medical services, schools and libraries.
- LCRA awarded eight matching grants totaling $1 million for local parks and recreation projects in the service area. Communities raised an additional $5 million for the projects.

A kayaker paddles at the mouth of the Colorado River on the Matagorda Peninsula, where LCRA plans to open a nature center.

The Foundation of Service

LCRA has identified five "Foundation Values" – safety in the work place, environmental leadership, diversity among LCRA's work force and suppliers, customer service and employee focus – that guide LCRA's operations, with a goal of increasing LCRA's value to its customers and attracting and retaining outstanding employees. Here are some highlights of how LCRA put these foundation values into practice in fiscal year 2004:

Safety

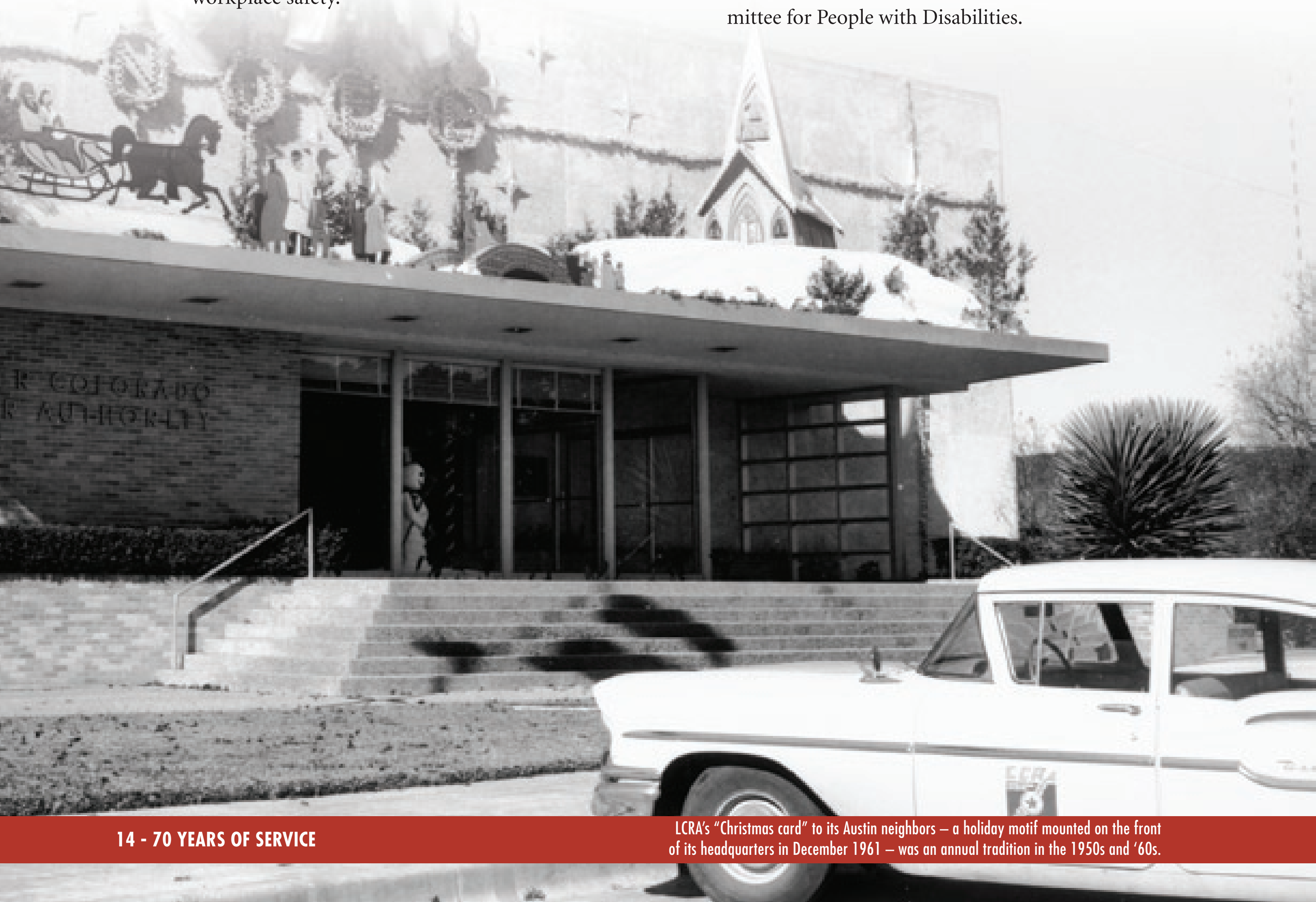
- Work-related injuries and illnesses at LCRA were well under utility industry benchmarking averages. LCRA's frequency rate was 1.97 incidents per 100 full-time employees, well below the national average of 5.00. LCRA has focused on improving workplace safety.

Environmental Leadership

- The coal-fired Fayette Power Project lowered its nitrogen-oxide emissions by 70 percent by adopting innovative combustion techniques and investing in equipment upgrades and modifications. As a result, the plant has one of the lowest emission rates in the nation. LCRA is sharing information about the emission-reduction project with federal agencies and the industry.

Diversity

- LCRA was recognized for its commitment to diversity and for raising awareness about people with disabilities with awards from the Austin Independent School District and the Austin Mayor's Committee for People with Disabilities.



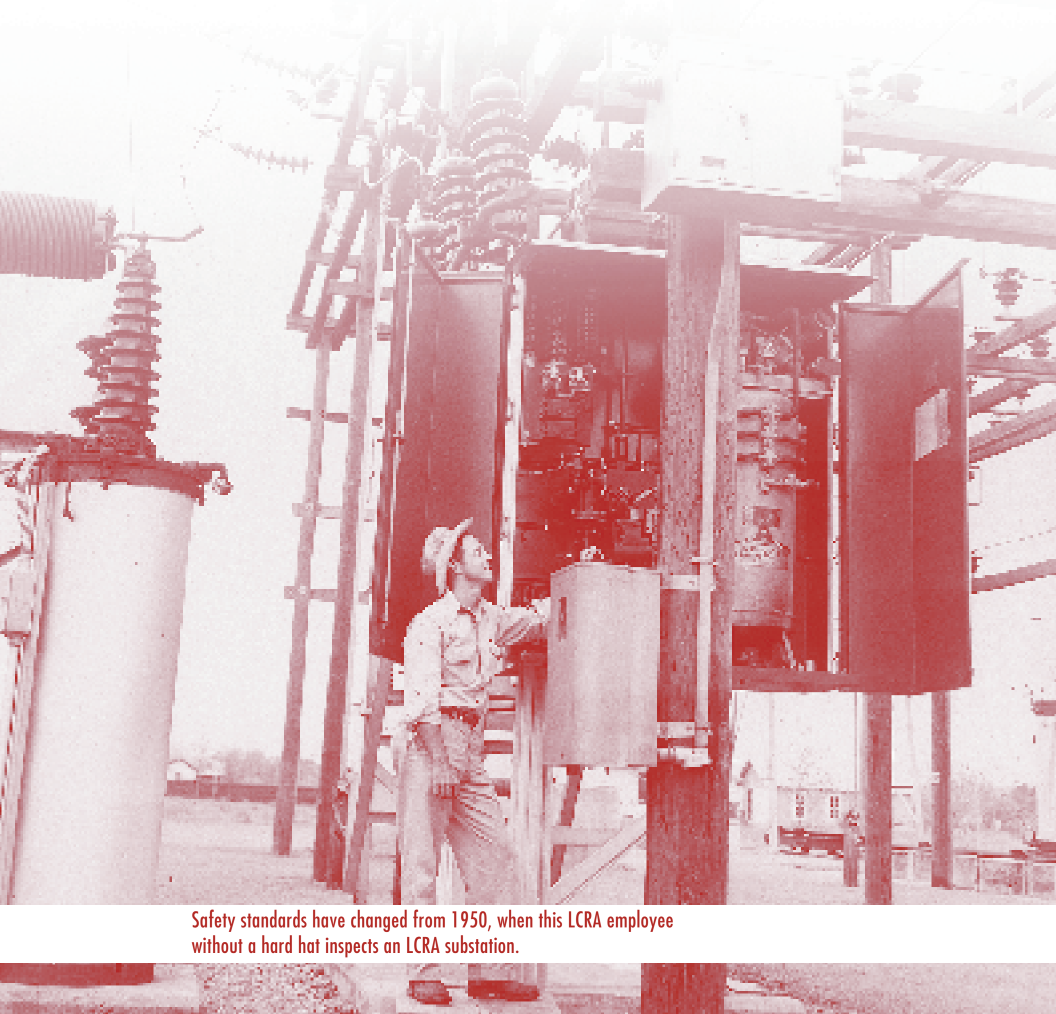
LCRA's "Christmas card" to its Austin neighbors – a holiday motif mounted on the front of its headquarters in December 1961 – was an annual tradition in the 1950s and '60s.

Safety in an Unsafe Environment

The combination of electricity, steel, concrete and high altitude can make for potentially dangerous work situations, and LCRA employees have encountered work-related injuries and deaths in the process of building dams, power plants or transmission facilities. One incident, in which a construction worker at Mansfield Dam was killed in 1939 when a cement bucket fell on him, has resulted in the recurring urban legend that a body lies buried in Mansfield Dam. (In fact the man's family buried him in a nearby cemetery.)

The pages of LCRA's employee magazine reflect LCRA's commitment to safe working conditions and practices through the years. Articles advised readers on such topics as taking salt tablets in summer to avoid heat exhaustion, how to administer mouth-to-mouth resuscitation, and the right way to wear a construction hard hat (this feature was titled, "Wear It Right, Be Alive Tonight!").

LCRA reinforced the safety messages with training, safety manuals, poster contests and awards.



Safety standards have changed from 1950, when this LCRA employee without a hard hat inspects an LCRA substation.

A Foundation Value

LCRA's commitment to safe working conditions and practices has paid off through the years through longstanding records set by plant and construction workers. Employees at the Thomas C. Ferguson Power Plant, for example, celebrated 16 years without a lost-time accident in December 2003, and employees at the Fayette Power Project achieved 3.9 million work-hours without an accident.

In 2002 LCRA developed the five foundation values that guide all its business practices, with safety being one of the five. LCRA management says this is an enlightened approach, because improved workplace safety not only protects the health and well-being of employees but also benefits LCRA customers by increasing employee productivity, ensuring reliability of LCRA's services, and helping keep LCRA's costs as low as possible.

The continued emphasis on safety takes into account that indoor office workplaces, generally thought to be safer environments than those around power plants and dams, pose their own unique safety hazards and in some cases can be more dangerous, if only because office workers tend to take safety issues less seriously.

The attention to safety by LCRA appears to be paying off, as work-related injuries and illnesses during fiscal year 2004 were well under utility industry benchmarking averages.

Today LCRA emphasizes safety for all its employees, including the proper use of hard hats and other equipment, as well as regular training.

- LCRA's strong commitment to supplier diversity has resulted in a 697 percent increase in supplier diversity spending in the past five years, from $3.8 million in FY 1999 to $26.4 million in FY 2004.

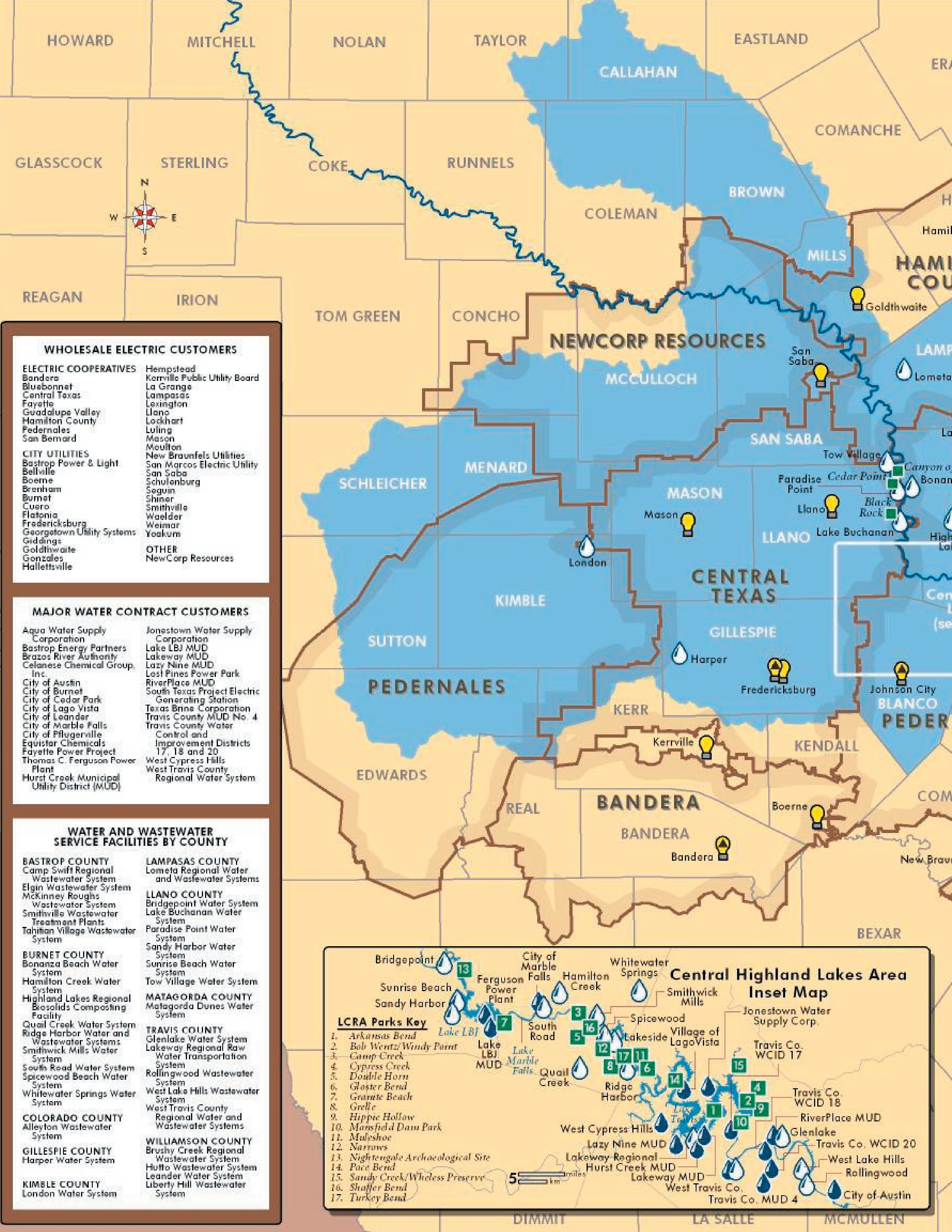
Customer Service

- LCRA's Transmission Services business unit performed $14.4 million in customer service work for utilities in Central Texas. Demand for these services – which include substation and line construction services, protective equipment testing, substation diagnostics and maintenance, engineering and project management – increased by $1.2 million, or 9 percent, from the previous fiscal year.
- LCRA held a series of water town hall meetings in communities along the lower Colorado River to involve the public in discussions on water projects, issues, ideas and concerns. About 250 people attended the meetings.
- LCRA's technology and communications systems provided support to LCRA's wholesale electric and water customers, as well as nonprofit organizations and local governments in its service area.

Employee Focus

- LCRA employees volunteered an estimated 80,000 hours to nonprofit organizations in their communities. LCRA Employees' United Charities, a charitable organization funded and managed by employees, donated $365,000 to about 450 nonprofit organizations.

LCRA encourages networking opportunities to allow employees with similar interests to build skills and relationships.



WHOLESALE ELECTRIC CUSTOMERS

ELECTRIC COOPERATIVES
Bandera
Bluebonnet
Central Texas
Fayette
Guadalupe Valley
Hamilton County
Pedernales
San Bernard

CITY UTILITIES
Bastrop Power & Light
Bellville
Boerne
Brenham
Burnet
Cuero
Flatonia
Fredericksburg
Georgetown Utility Systems
Giddings
Goldthwaite
Gonzales
Hallettsville
Hempstead
Kerrville Public Utility Board
La Grange
Lampasas
Lexington
Llano
Lockhart
Luling
Mason
Moulton
New Braunfels Utilities
San Marcos Electric Utility
San Saba
Schulenburg
Seguin
Shiner
Smithville
Waelder
Weimar
Yoakum

OTHER
NewCorp Resources

MAJOR WATER CONTRACT CUSTOMERS

Aqua Water Supply Corporation
Bastrop Energy Partners
Brazos River Authority
Celanese Chemical Group, Inc.
City of Austin
City of Burnet
City of Cedar Park
City of Lago Vista
City of Leander
City of Marble Falls
City of Pflugerville
Equistar Chemicals
Fayette Power Project
Thomas C. Ferguson Power Plant
Hurst Creek Municipal Utility District (MUD)
Jonestown Water Supply Corporation
Lake LBJ MUD
Lakeway MUD
Lazy Nine MUD
Lost Pines Power Park
RiverPlace MUD
South Texas Project Electric Generating Station
Texas Brine Corporation
Travis County MUD No. 4
Travis County Water Control and Improvement Districts 17, 18 and 20
West Cypress Hills
West Travis County Regional Water System

WATER AND WASTEWATER SERVICE FACILITIES BY COUNTY

BASTROP COUNTY
Camp Swift Regional Wastewater System
Elgin Wastewater System
McKinney Roughs Wastewater System
Smithville Wastewater Treatment Plants
Tahitian Village Wastewater System

BURNET COUNTY
Bonanza Beach Water System
Hamilton Creek Water System
Highland Lakes Regional Biosolids Composting Facility
Quail Creek Water System
Ridge Harbor Water and Wastewater Systems
Smithwick Mills Water System
South Road Water System
Spicewood Beach Water System
Whitewater Springs Water System

COLORADO COUNTY
Alleyton Wastewater System

GILLESPIE COUNTY
Harper Water System

KIMBLE COUNTY
London Water System

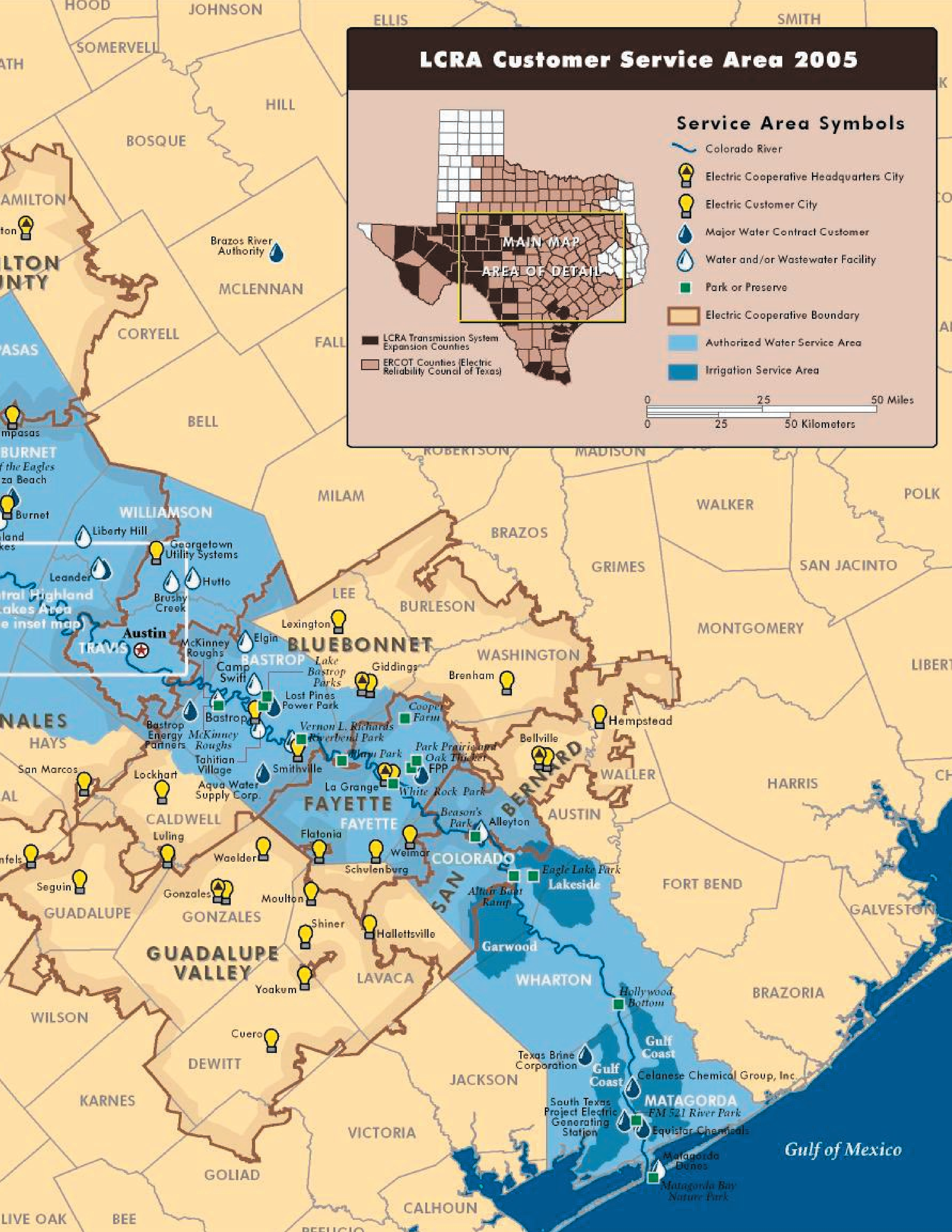
LAMPASAS COUNTY
Lometa Regional Water and Wastewater Systems

LLANO COUNTY
Bridgepoint Water System
Lake Buchanan Water System
Paradise Point Water System
Sandy Harbor Water System
Sunrise Beach Water System
Tow Village Water System

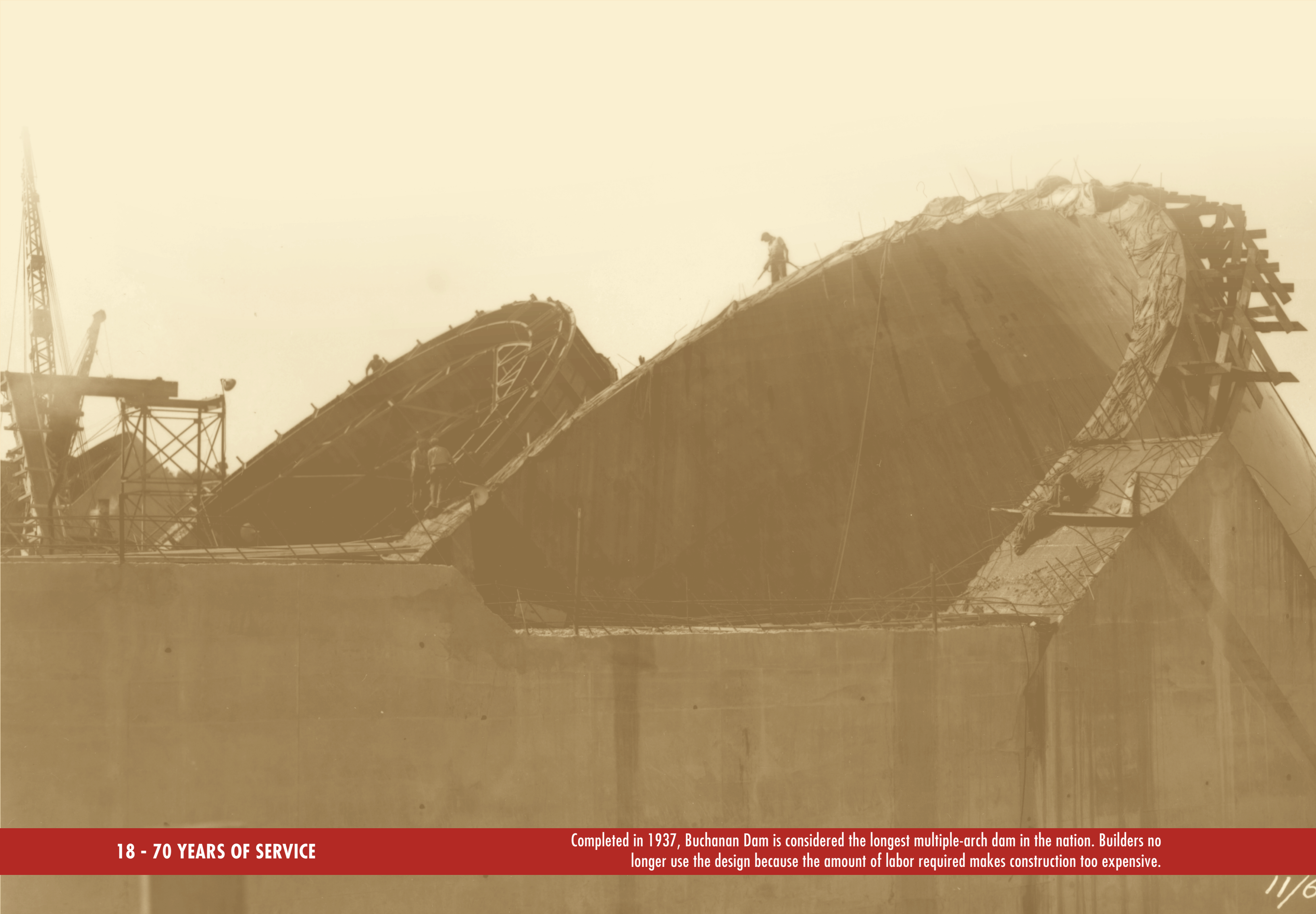
MATAGORDA COUNTY
Matagorda Dunes Water System

TRAVIS COUNTY
Glenlake Water System
Lakeway Regional Raw Water Transportation System
Rollingwood Wastewater System
West Lake Hills Wastewater System
West Travis County Regional Water and Wastewater Systems

WILLIAMSON COUNTY
Brushy Creek Regional Wastewater System
Hutto Wastewater System
Leander Water System
Liberty Hill Wastewater System


LCRA Customer Service Area 2005
Service Area Symbols
Colorado River
Electric Cooperative Headquarters City
Electric Customer City
Major Water Contract Customer
Water and/or Wastewater Facility
Park or Preserve
Electric Cooperative Boundary
Authorized Water Service Area
Irrigation Service Area
0 25 50 Miles
0 25 50 Kilometers
MAIN MAP AREA OF DETAIL
LCRA Transmission System Expansion Counties
ERCOT Counties (Electric Reliability Council of Texas)
HOOD
JOHNSON
ELLIS
SMITH
SOMERVELL
HILL
BOSQUE
Brazos River Authority
MCLENNAN
CORYELL
FALLS
BELL
ROBERTSON
MADISON
MILAM
WALKER
POLK
BRAZOS
GRIMES
SAN JACINTO
WILLIAMSON
Liberty Hill
Georgetown Utility Systems
Leander
Hutto
Brushy Creek
Burnet
LEE
BURLESON
MONTGOMERY
Lexington
Austin
TRAVIS
McKinney Roughs
Elgin
BLUEBONNET
BASTROP
Lake Bastrop Parks
Camp Swift
Giddings
WASHINGTON
Brenham
LIBERTY
Lost Pines Power Park
Cooper Farm
Bastrop
Hempstead
Bastrop Energy Partners
McKinney Roughs
Vernon L. Richards Riverbend Park
HAYS
Tahitian Village
Park Prairie and Oak Thicket
Bellville
San Marcos
Lockhart
Smithville
Allan Park
FPP
WALLER
Aqua Water Supply Corp.
La Grange
White Rock Park
SAN BERNARD
HARRIS
FAYETTE
CALDWELL
Beason's Park
Alleyton
AUSTIN
FAYETTE
Luling
Flatonia
Weimar
COLORADO
Waelder
Schulenburg
Eagle Lake Park
Lakeside
Seguin
FORT BEND
Gonzales
Moulton
Altair Boat Ramp
GUADALUPE
GONZALES
GALVESTON
Shiner
Hallettsville
Garwood
GUADALUPE VALLEY
LAVACA
Yoakum
WHARTON
Hollywood Bottom
BRAZORIA
WILSON
Gulf Coast
Cuero
Texas Brine Corporation
Gulf Coast
DEWITT
JACKSON
Celanese Chemical Group, Inc.
KARNES
MATAGORDA
South Texas Project Electric Generating Station
FM 521 River Park
Equistar Chemicals
VICTORIA
Gulf of Mexico
Matagorda Dunes
GOLIAD
Matagorda Bay Nature Park
LIVE OAK
BEE
CALHOUN

Financial Information



Completed in 1937, Buchanan Dam is considered the longest multiple-arch dam in the nation. Builders no longer use the design because the amount of labor required makes construction too expensive.

Five-Year Financial Summary

Comparative Financial Information

(Dollars in Thousands)

	Fiscal Year ended June 30, 2004	2003[4]	2002	2001[2]	2000
Operating revenues					
Electric[1]	$ 627,424	$ 581,266	$ 511,655	$ 635,231	$ 483,131
Other	22,542	24,041	16,695	17,765	12,981
Water, wastewater and irrigation	44,745	38,113	35,068	29,601	26,460
Total operating revenues	694,711	643,420	563,418	682,597	522,572
Interest and other income available for debt service	5,833	9,399	6,839	10,770	13,048
Total	700,544	652,819	570,257	693,367	535,620
Operating expenses as adjusted[1][3]	517,250	480,648	400,660	498,041	341,000
Net Revenues Available for Debt Service	$ 183,294	$ 172,171	$ 169,597	$ 195,326	$ 194,620
Debt Service Requirement	$ 134,205	$ 120,438	$ 91,615	$ 79,707	$ 82,774
Debt Service Coverage Ratio	1.37x	1.43x	1.85x	2.45x	2.35x
Utility plant	$ 3,089,615	$ 2,657,942	$ 2,346,050	$ 2,141,434	$ 2,041,473
Accumulated depreciation	$ 984,209	$ 905,487	$ 834,490	$ 775,909	$ 695,984
Long-term debt	$ 1,695,413	$ 1,393,810	$ 1,407,020	$ 925,747	$ 1,086,706
Equity ratio	22%	25%	25%	28%	30%
Statistics					
MWH Sales					
Wholesale	12,890,547	13,193,923	12,971,239	12,606,527	11,598,517
Retail	-	-	7,871	57,784	65,230
Total MWH Sales	12,890,547	13,193,923	12,979,110	12,664,311	11,663,747
MWH Generation and Purchased Power					
Hydraulic	287,601	367,766	233,318	342,748	167,487
Fossil	11,633,444	11,922,306	11,530,871	11,118,742	10,966,833
Purchased power	1,408,290	1,262,661	1,392,680	1,709,241	1,057,220
Total MWH Generation and Purchased Power	13,329,335	13,552,733	13,156,869	13,170,731	12,191,540
Net Peak Demand (MW) (Summer/Winter)	2,887(S)	2,747(W)	2,838(S)	2,692(S)	2,454(S)
Electric Customers:					
Wholesale	42	42	42	43	43
Other		-	-	2	3
Total Electric Customers	42	42	42	45	46

(1) Excludes GenTex Power Corporation's revenues and expenses (see Note 2 of Notes to Financial Statements). Net revenues of nonobligated affiliates, such as GenTex Power Corporation, are not available for debt service.

(2) Reflects restatements for the effects of the adoption of Governmental Accounting Standards Board Statement No. 34, "Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments" (fiscal years 2002, 2003 and 2004 reflect the application of Statement No. 34).

(3) Operating expenses have been adjusted to include other interest and exclude depreciation, depletion, amortization, and other noncash miscellaneous expenses.

(4) As disclosed in Footnote 10, the financial statements for June 30, 2003, and year then ended were restated to reflect adjustments related to the depreciation of certain completed capital projects. In addition, certain amounts have been reclassified to conform to current year presentation.

Report of Management

The management's discussion and analysis, the financial statements and related footnotes included herein are the responsibility of LCRA's management as is other information contained in this annual report. The financial statements are prepared in conformity with generally accepted accounting principals applied on a consistent basis and, in some cases, reflect amounts based on the best estimates and judgments of management, giving due consideration to materiality. Financial information contained elsewhere in this annual report is consistent with that in the financial statements.

Management has developed and maintains a system of accounting and controls, including an internal audit program, designed to provide reasonable assurance that LCRA's assets are protected from improper use and that accounting records provide a reliable basis for the preparation of financial statements. This system is continually reviewed, improved and modified in response to changing business conditions and operations and to recommendations made by the independent auditors and the internal auditors. Due to the inherent limitations of the effectiveness of internal controls, no internal control system can provide absolute assurance that errors and irregularities will not occur. However, management strives to maintain a balance, recognizing that the cost of such a system should not exceed the benefits derived.

LCRA's Board of Directors, appointed by the governor of Texas, oversees LCRA's financial reporting activities through the Audit Committee and Finance and Administration Committee, which are comprised wholly of Board members. The duties of these committees include keeping informed of the financial condition of the LCRA and reviewing its financial policies and procedures, its internal accounting controls, and the objectivity of its financial reporting. Both LCRA's independent and internal auditors may meet directly with the Audit Committee without management concurrence.

The Independent Auditor's Report, included herein, does not limit the responsibility of management for information in the financial statements and elsewhere in the annual report.

John M. Meismer
Deputy General Manager
Chief Financial Officer

James D. Travis
Controller

Joseph J. Beal, P.E.
General Manager

Management's Discussion and Analysis

Condensed Balance Sheets

(Dollars in Thousands)

	June 30, 2004	June 30, 2003 (As restated, see note 10)
Current assets	$ 319,204	$ 247,464
Capital assets, net	2,147,019	1,781,725
Other long-term assets	476,068	449,370
Total Assets	$ 2,942,291	$ 2,478,559
Current liabilities	$ 398,237	$ 316,576
Long-term liabilities	1,887,402	1,539,686
Total Liabilities	2,285,639	1,856,262
Equity - Invested in capital assets, net of related debt	501,613	479,168
Equity - Restricted other	25,315	11,388
Equity - Unrestricted	129,724	131,741
Total Equity	656,652	622,297
Total Liabilities and Equity	$ 2,942,291	$ 2,478,559

Condensed Statements of Revenues, Expenses and Changes in Equity

(Dollars in Thousands)

	Year Ended June 30, 2004	2003 (As restated, see note 10)
Operating revenues	$ 694,404	$ 644,949
Operating expenses	(599,442)	(549,966)
Operating income	94,962	94,983
Interest and other income	4,858	9,478
Interest and other expenses	(99,969)	(90,157)
Costs to be recovered from revenues	29,715	1,707
Income before capital contributions	29,566	16,011
Capital contributions	4,789	5,397
Change in equity	34,355	21,408
Equity, Beginning of Year	622,297	600,889
Equity, End of Year	$ 656,652	$ 622,297

Financial Highlights

Current assets increased by $72 million, primarily due to a $30 million increase in receivables from higher transmission and water rates and an increase in demand for electricity, and a $39 million increase in investments with shorter term maturities. Net capital assets increased by $365 million or 20 percent for fiscal year (FY) 2004. The majority of the increase is due to the acquisition of a generating unit and construction of transmission and water and wastewater facilities to meet increasing demand for these services. Current liabilities increased $81 million or 26 percent due to an increase in tax exempt commercial paper and the over-recovery of fuel costs.

Long-term liabilities for FY 2004 increased by $348 million or 23 percent primarily due to issuance of LCRA 2003 and 2004 and LCRA Transmission Services Corporation Series 2003C revenue bonds. Equity-Restricted Other increased by $14 million for funds set aside by the LCRA Board for construction and park development.

Operating revenues for FY 2004 increased by $49 million or 8 percent due to higher fuel revenues of $34 million resulting from passing on increases in the cost of fuel to customers and higher transmission revenues of $15 million due to rate increases.

Operating expenses for FY 2004 increased by $49 million or 9 percent due primarily to higher fuel and purchased power and depreciation and amortization expenses.

Interest and other income decreased by $5 million or 49 percent primarily due to an unfavorable change in the fair value of investments and lower average investment balances in FY 2004. Interest and other expenses increased by $10 million or 11 percent primarily due to an increase in the amortization of loss on refundings of $6 million and the retirement of assets of $3 million.

Costs to be recovered from revenues for FY 2004 increased by $28 million due to an increase in depreciation expense to be recovered in future rates.

As disclosed in footnote 10, the financial statements for June 30, 2003 and year then ended, were restated to reflect adjustments related to the depreciation of certain completed capital projects. The resulting impact reduced FY 2003 beginning equity by $7.1 million and reduced FY 2003 income before capital contributions by $1.2 million. These adjustments do not impact LCRA's rates or ability to service debt requirements due to their noncash nature.

Overview of the Financial Statements

In accordance with the Governmental Accounting Standards Board issued Statement No. 34, "Basic Financial Statements – Management's Discussion and Analysis – for State and Local Governments," LCRA is considered a special-purpose government engaged only in business-type activities. Statement No. 34 requires the following components in a governmental entity's annual report:

Management's Discussion and Analysis

The purpose is to provide an objective and easily readable analysis of the government's financial activities based on currently known facts, decisions or conditions.

Balance Sheet

Assets and liabilities of proprietary funds should be presented to distinguish between current and long-term assets and liabilities.

Statement of Revenues, Expenses and Changes in Equity

This statement provides the operating results broken into the categories of operating revenues and expenses, nonoperating revenues and expenses, and capital contributions.

Notes to the Financial Statements

The notes explain information in the financial statements and provide additional detailed information.

Competition

Senate Bill 7 (SB 7) provided for retail electric competition to open Jan. 1, 2002. Retail customers of investor-owned utilities and retail customers of municipality owned utilities and electric cooperatives that elect to participate in retail competition now can choose their electric provider. LCRA's strategy is to help its wholesale electric customers succeed regardless of how they position themselves. As part of this strategy, LCRA will work aggressively to reduce generation costs as well as to support wholesale electric customers in their opt-in decisions.

Regulatory Matters

LCRA Transmission Services Corporation

In order to promote electric competition, SB 7 requires all transmission system owners to make their transmission system available for use by others at prices and terms comparable to each respective owner's use of its system for its own wholesale transactions. Pursuant to the requirements of SB 7, in January 2002, LCRA transferred its existing electric transmission and transformation facilities to LCRA Transmission Services Corporation (LCRA TSC), a component unit of LCRA for accounting purposes. LCRA TSC owns and operates all of LCRA's regulated electric transmission and transformation assets. In accordance with accounting and financial reporting requirements, the assets, liabilities and transactions of LCRA TSC are included in the financial statements of LCRA.

Transmission Cost of Service Rates

In February 2003, LCRA TSC received approval from the Public Utility Commission of Texas (PUC) for a new Transmission Cost of Service (TCOS) rate. This new rate represented a 20 percent increase over the interim rate initially put into effect May 31, 2002. The increase in revenues attributable to the new TCOS rate was $15.3 million for FY 2003.

In May 2003, LCRA TSC received PUC approval for new transformation and metering services tariffs. Although the transformation tariff increased by 14 percent, the revenues to be collected, effective prospectively from May 2003, will decrease on an annual basis because of lower cost of service and billing demand.

In July 2003, LCRA TSC filed an annual interim update to its wholesale transmission rate. The updated transmission rate was approved and implemented Sept. 26, 2003. The increase in revenues of $13.4 million, attributable to the new transmission rate since Sept. 26, 2003, is included in the FY ended June 30, 2004.

In November 2003, LCRA TSC filed a rate case with the PUC seeking a new TCOS rate. In January 2004, the administrative law judge approved an interim rate of $3 per kilowatt (kW) to be effective June 1, 2004. However, LCRA TSC recognized revenue for June 2004 activity based on a rate of $2.33 per kW since the final rate case outcome is unknown. As a result, LCRA TSC recorded $13.3 million of deferred revenue related to the $3 per kW interim rate. The rate case administrative hearings phase was concluded in June 2004, with PUC commissioners' approval of a final TCOS rate anticipated for December 2004.

Capital Expansion and Improvement Program

LCRA's capital improvement program for FY 2005 through FY 2009 is $1.47 billion, with $1 billion or 70 percent to be debt funded. The majority of capital expenditures are for expansion of transmission services, water and wastewater services and generation improvements, as well as additional corporate infrastructure and facilities. LCRA TSC continues to increase its transmission system investment due to the need for additional electric transmission capability statewide. LCRA will continue its water and wastewater services capital expansion due to the region's growing population.

The capital budget is expected to be applied as follows:

(1) $864 million for transmission projects, including $351 million for transmission projects in South and West Texas under a joint development agreement with a private entity.

(2) $249 million for dam improvements and modernization, and acquisition and construction of water and wastewater utilities and facilities.

(3) $202 million for generation and system improvements.

(4) $153 million for park and corporate facilities.

The cost of the capital program will be provided from internally generated funds of LCRA long-term bonds (including LCRA bonds and LCRA bonds issued on behalf of LCRA TSC) and commercial paper notes.

Capital Asset Activity

- $463 million was expended for construction activities in FY 2004. The majority of these expenditures were for acquisition and construction of generation, transmission, and water and wastewater facilities to meet increasing demand for these services.
- $98 million of depreciation expense and asset retirements were recorded in FY 2004 on plant in service.
- For additional detail, see Capital Asset Activity table in Note 8 of the Notes to the Financial Statements.

Debt Activity

- On Oct. 16, 2003, LCRA issued $105 million of Refunding and Improvement Bonds, Series 2003. The proceeds were used to refund $104.6 million of tax-exempt commercial paper and to provide $4 million for capital project funding. In addition, LCRA on behalf of LCRA TSC issued $135.4 million of Transmission Contract Auction Rate Refunding Revenue Bonds, Series 2003C. The proceeds were used to refund $135 million of tax exempt commercial paper.
- On Nov. 17, 2003, LCRA refunded $16.2 million of the Series 2000 Refunding Revenue Bonds, Series D with tax-exempt commercial paper.
- On April 27, 2004, LCRA issued $105.6 million of tax-exempt Revenue Bonds, Series 2004. The proceeds from the bond issue were used to refund $20 million of taxable commercial paper and $89 million of tax-exempt commercial paper.
- On June 18, 2004, LCRA issued $0.2 million and $0.04 million of tax-exempt Revenue Bonds, Series 2004A and 2004B respectively. In addition, LCRA issued $0.05 million of taxable Revenue Bonds, Series 2004C. The proceeds from each of these fundings were used for capital project funding.
- During FY 2004, LCRA issued $380.5 million of tax-exempt commercial paper, of which $169.3 million was on behalf of LCRA TSC. In addition, LCRA issued $30.6 million of taxable commercial paper to fund various capital projects.
- For additional detail, see Note 4 to the Financial Statements.

Independent Auditors' Report

Deloitte.

Deloitte & Touche LLP
JPMorgan Chase Tower
2200 Ross Avenue, Suite 1600
Dallas, TX 75201-6778
USA

Tel: +1 214 840 7000
www.deloitte.com

INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Lower Colorado River Authority
Austin, Texas

We have audited the accompanying balance sheets of the Lower Colorado River Authority ("LCRA") as of June 30, 2004 and 2003 and the related statements of revenues, expenses and changes in equity, and of cash flows for the years then ended. These financial statements are the responsibility of LCRA's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in the Government Auditing Standards issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes, examining, on a test basis, evidence supporting the amounts and disclosures of the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of LCRA as of June 30, 2004 and 2003 and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 10, the accompanying financial statements as of June 30, 2003 and for the year then ended have been restated.

Management's Discussion and Analysis is not a required part of the basic financial statements but is supplementary information required by the GASB. 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.

Deloitte & Touche LLP

October 11, 2004

Member of
Deloitte Touche Tohmatsu

Lower Colorado River Authority
Balance Sheets
(Dollars in Thousands)

	June 30, 2004	June 30, 2003 (As restated, see note 10)
Assets		
Current Assets:		
Cash and cash equivalents	$ 56,950	$ 57,935
Investments	56,857	17,643
Receivables, net	123,459	93,248
Accrued interest receivable	696	962
Inventories	73,339	74,128
Other	7,903	3,548
Total current assets	319,204	247,464
Long-term Assets:		
Restricted cash and cash equivalents	7,520	9,992
Restricted investments	41,644	22,270
Unrestricted investments	70,902	101,481
Capital assets:		
Utility plant in service	2,778,083	2,407,544
Construction work in progress	283,374	222,240
Oil and gas property	28,158	28,158
Other physical property	41,613	29,270
Less accumulated depreciation	(984,209)	(905,487)
Capital assets, net	2,147,019	1,781,725
Water rights, net	86,381	86,381
Other	10,672	6,211
Deferred charges:		
Costs to be recovered from future revenues	203,316	170,280
Unamortized debt expense	26,907	22,506
Contract extension settlement with major customers	9,681	10,456
Other	19,045	19,793
Deferred charges, net	258,949	223,035
Total long-term assets	2,623,087	2,231,095
Total Assets	$ 2,942,291	$ 2,478,559

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

Lower Colorado River Authority
Balance Sheets
(Dollars in Thousands)

	June 30, 2004	June 30, 2003 (As restated, see note 10)
Liabilities		
Current Liabilities:		
Accounts payable	$ 138,820	$ 114,837
Compensated absences	7,299	7,101
Bonds, notes, and loans payable	252,118	194,638
Total current liabilities	398,237	316,576
Long-term Liabilities:		
Accounts payable from restricted assets	60,179	36,709
Bonds, notes, and loans payable	1,695,413	1,393,810
Deferred credits	131,810	109,167
Total long-term liabilities	1,887,402	1,539,686
Total liabilities	2,285,639	1,856,262
Equity		
Invested in capital assets, net of related debt	501,613	479,168
Restricted other	25,315	11,388
Unrestricted	129,724	131,741
Total equity	656,652	622,297
Total Liabilities and Equity	$ 2,942,291	$ 2,478,559

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

Lower Colorado River Authority
Statements of Revenues, Expenses, and Changes in Equity
(Dollars in Thousands)

	Year Ended June 30, 2004	2003 (As restated, see note 10)
Operating Revenues		
Electric	$ 627,197	$ 582,795
Water, wastewater and irrigation	44,676	38,113
Other	22,531	24,041
Total operating revenues	694,404	644,949
Operating Expenses		
Fuel	248,979	224,760
Purchased power	58,340	42,020
Operations	168,847	180,213
Maintenance	37,957	34,935
Depreciation, depletion and amortization	85,319	68,509
Plant commitment	-	(471)
Total operating expenses	599,442	549,966
Operating income	94,962	94,983
Nonoperating Revenues (Expenses)		
Interest and Other Income	4,858	9,478
Interest and Other Expenses	(99,969)	(90,157)
Nonoperating Revenues (Expenses)	(95,111)	(80,679)
Income before costs to be recovered from revenues and capital contributions	(149)	14,304
Costs To Be Recovered from Revenues	29,715	1,707
Income before capital contributions	29,566	16,011
Capital Contributions	4,789	5,397
Change in Equity	34,355	21,408
Total Equity, Beginning of Year	622,297	600,889
Total Equity, End of Year	$ 656,652	$ 622,297

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

Lower Colorado River Authority
Statements of Cash Flows
(Dollars in Thousands)

	Year Ended June 30, 2004	2003 (As restated, see note 10)
Cash Flows From Operating Activities		
Received from customers	$ 697,785	$ 660,104
Payments for goods and services	(379,899)	(374,220)
Payments to employees	(135,184)	(121,764)
Other revenues and (expenses), net	3,879	(4,252)
Net cash provided by operating activities	186,581	159,868
Cash Flows From Noncapital Financing Activities		
Grant proceeds received	4,625	1,855
Other expenses	(1,597)	(3,711)
Net cash provided by (used in) noncapital financing activities	3,028	(1,856)
Cash Flows From Capital and Related Financing Activities		
Expenditures for property, plant and equipment	(439,107)	(316,434)
Proceeds from sale of capital assets	3,244	2,533
Contributed capital received for capital expenditures	4,775	2,636
Proceeds from refundings and new debt issues	775,265	701,936
Debt principal payments	(74,307)	(42,915)
Interest paid	(82,486)	(78,614)
Payments to refund debt and related issue costs	(355,461)	(660,225)
Net cash used in capital and related financing activities	(168,077)	(391,083)
Cash Flows From Investing Activities		
Sale and maturity of investment securities	160,351	602,395
Purchase of investment securities	(193,907)	(393,935)
Interest received	8,603	13,130
Infrastructure financial assistance activity	(36)	(242)
Net cash provided by (used in) investing activities	(24,989)	221,348
Net Decrease in Cash and Cash Equivalents	(3,457)	(11,723)
Cash and Cash Equivalents, Beginning of Year	67,927	79,650
Cash and Cash Equivalents, End of Year	$ 64,470	$ 67,927

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

Lower Colorado River Authority
Statements of Cash Flows
(Dollars in Thousands)

	Year Ended June 30, 2004	2003 (As restated, see note 10)
Reconciliation of Operating Income to Net Cash Provided by Operating Activities		
Operating income	$ 94,962	$ 94,983
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation, depletion and amortization	85,319	68,509
Plant commitment	-	(471)
Changes in assets and liabilities:		
Accounts receivable	(30,299)	(7,506)
Inventories	789	(7,658)
Other current assets	(4,295)	3,191
Current liabilities	21,300	9,384
Other deferred charges	(651)	62
Deferred credits and other long-term liabilities	19,456	(626)
Net cash provided by operating activities	$ 186,581	$ 159,868
Noncash Investing Activities		
Investment market adjustments	$ (5,547)	$ (4,407)
Noncash Financing for Property, Plant and Equipment Expenditures		
Purchase of equipment through short-term trade payables	$ 23,457	$ 8,532
Note receivable received in exchange for asset	$ 4,495	$ -

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

Notes to Financial Statements

1. General

The Lower Colorado River Authority (LCRA) is a conservation and reclamation district created by the Texas Legislature in 1934. It receives no state tax money and cannot levy taxes. It operates on revenues from the sale of wholesale electricity, water and other services. The LCRA Board of Directors (Board) is appointed by the governor of the state, with Senate approval, to serve six-year terms. The financial condition of LCRA is not controlled by or dependent on the State or any other political subdivision. Under the criteria set forth in Governmental Accounting Standards Board Statement (GASB) No. 14, "The Financial Reporting Entity," LCRA considers its relationship to the state to be that of a related organization.

LCRA's basic statutory boundaries include a 10-county district comprising the counties of San Saba, Burnet, Llano, Blanco, Travis, Bastrop, Fayette, Colorado, Wharton and Matagorda. LCRA's service area includes all or part of 58 Central Texas counties in which LCRA provides electric utility services, flood management, water and wastewater services, economic development programs, and other public services. LCRA is responsible for regulating the flow of water within its reservoirs for water supply and irrigation, flood management, hydroelectric generation and other useful purposes. LCRA aids in the prevention of flood damage, conserves and protects the forests within the Colorado River watershed, and operates and maintains electric generating plants and 3,665 miles of transmission lines. LCRA also has a comprehensive water quality program along the Colorado River within its 10-county statutory district and owns 40 parks, recreational areas and wildlife preserves adjacent to the Highland Lakes or the Colorado River. Eighteen of these parks are leased to or operated by other entities.

LCRA has 2,882 megawatts (MW) of net generating capacity and power supply contracts through June 2016 with 42 wholesale customers. Hydroelectric net generating capacity of 281 MW is provided by five dams LCRA owns and one it leases. LCRA owns four gas-fired steam boiler generation units with 1,040 MW of net generation and one 536 MW gas-fired combined cycle generation unit. LCRA has full ownership of one coal-fired generating unit with a 445 net MW capacity and a 50 percent ownership interest with the City of Austin (Austin) in two coal-fired units for a combined net capacity of 1,160 MW.

Sales of electricity to LCRA's two largest electric customers represented approximately 35 percent of total electric revenues for fiscal year (FY) 2004 and 32 percent for FY 2003. Electric revenues represented approximately 90 percent of LCRA's operating revenues for both FY 2004 and 2003.

Senate Bill 7 (SB 7) allows LCRA to own, build and manage transmission infrastructure statewide with the approval of the Public Utility Commission of Texas. The LCRA Board authorized the creation of LCRA Transmission Services Corporation (LCRA TSC), a nonprofit corporation benefiting and accomplishing public purposes of LCRA. LCRA TSC is governed by a board of directors, which is composed in its entirety of the LCRA Board of Directors. LCRA TSC was created under provisions of the Subchapter B of Chapter 152, Texas Water Code and the Texas Non-Profit Corporation Act. Effective Jan. 1, 2002, LCRA TSC began operations subsequent to the transfer of LCRA's transmission and transformation assets to LCRA TSC pursuant to the terms of an Electric Transmission Facilities Contract (the Initial Contractual Commitment) dated Oct. 1, 2001.

LCRA has ownership and operating arrangements for various water and wastewater systems. Some water and wastewater facilities are owned by LCRA and operated by another river authority in connection with an alliance agreement to address immediate and long-term water and wastewater needs in Williamson County and other areas. In addition, LCRA owns three irrigation systems consisting of 791 miles of canal and three low-head dams. The irrigation systems are located in Colorado, Wharton and Matagorda counties.

2. Significant Accounting Policies

Basis of Accounting: The accompanying financial statements of LCRA, a governmental entity, have been prepared utilizing proprietary fund and accrual basis accounting. LCRA implements all applicable GASB pronouncements and all applicable Financial Accounting Standards Board (FASB) pronouncements that do not conflict with or contradict GASB pronouncements. LCRA's accounts are maintained in accordance with the Federal Energy Regulatory Commission's Uniform System of Accounts. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

LCRA considers electric revenues and costs that are directly related to the generation, purchase, transmission and distribution of electricity to be operating revenues and expenses. Water and wastewater revenues and other services related to environmental laboratory operations, licensing and recreation, and the costs directly related to these services, are also considered operating revenues and expenses. Revenues and expenses related to financing and other activities are reflected as nonoperating.

Newly Adopted Standards for FY 2004 and FY 2003: In FY 2004, LCRA implemented GASB Statement No. 42, "Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries." This statement establishes accounting and financial reporting standards for impairment of capital assets. For governmental entities, GASB 42 replaces FASB Statement of Financial Accounting Standard No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." The provisions of GASB 42 are effective for fiscal periods beginning after Dec. 15, 2004. LCRA implemented the Statement prior to the required implementation date. GASB 42 states asset impairment is a significant, unexpected decline in the service utility of a capital asset. The service utility of a capital asset is the usable capacity that at acquisition was expected to be used to provide services. An impairment loss reflects the decline in service utility. The implementation of GASB 42 did not have a material impact on LCRA's financial position or results of operations.

In FY 2003, LCRA implemented a number of FASB pronouncements:

Statement of Financial Accounting Standards No. 143 (SFAS 143): This statement, "Accounting for Asset Retirement Obligations," applies to retirement obligations that result from the acquisitions, construction, development or normal operations of long-lived assets. Effective for fiscal years beginning after June 15, 2002, the fair value of asset retirement obligations must be recognized as a liability in the period in which it is incurred, if a reasonable estimate of fair value can be made. The implementation of SFAS 143 did not have a material impact on LCRA's financial position or results of operations.

Statement of Financial Accounting Standards No. 146 (SFAS 146): This statement, "Accounting for Costs Associated with Exit or Disposal Activities," requires a liability for a cost associated with an exit or disposal activity to be recognized and measured initially at fair value in the period in which the liability is incurred. The most common costs associated with exit or disposal activity are one-time employee termination benefits, contract termination costs, and costs associated with the consolidation or closing of facilities and the relocation of employees. This statement is effective for exit or disposal activities initiated after Dec. 31, 2002. The implementation of SFAS 146 did not have a material impact on LCRA's financial position or results of operations.

Financial Interpretation No. 45 (FIN 45): This statement, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others," requires a company to disclose in its financial statement footnotes many of the guarantees or indemnification agreements it issues. In addition, a company is required to recognize a liability at the time it enters into the guarantees. The initial recognition and initial measurement provisions of this Interpretation are applicable to guarantees issued or modified after Dec. 31, 2002. The disclosure requirements are effective for financial statements with periods ending after Dec. 15, 2002. The implementation of FIN 45 did not have an impact on LCRA's financial position or results of operations.

Issued But Not Yet Effective Pronouncements: In March 2003, the GASB issued Statement No. 40, "Deposit and Investment Risk Disclosures - an Amendment of GASB Statement No. 3." This Statement addresses common deposit and investment risks related to credit risk, concentration of credit risk, interest rate risk, and foreign currency risk. As an element of interest rate risk, this Statement requires certain disclosures of investments that have fair values that are highly sensitive to changes in interest rates. Deposit and investment policies related to the risks identified in this Statement must also be disclosed. This Statement is effective for LCRA beginning in FY 2005. The implementation of GASB 40 is not expected to have a material effect on LCRA's financial position or results of operations.

GenTex Power Corporation: The GenTex Power Corporation (GenTex), a nonprofit corporation and wholly owned affiliate of LCRA, is governed by a nine-member board appointed by the LCRA Board. GenTex owns a 536-MW gas-fired combined cycle generating facility which began commercial operation in June 2001.

In FY 2000, LCRA entered into an agreement with a public company for the two entities to construct the generating facility. Each entity owned an undivided 50 percent interest in the generating facility. In FY 2004, GenTex purchased the other entity's 50 percent share for $150 million.

GenTex's share of the initial construction costs of the facility was entirely funded by an LCRA economic development grant. GenTex entered into contracts with LCRA's wholesale customers to sell energy to the customers at a price recovering only operating expenses, excluding depreciation, over the life of the plant. The contracts provide the customers the right of first refusal to purchase GenTex's original 50 percent interest in the facility at a price of $975 per customer. Because the initial cost of the facility was funded by an economic development grant provided by LCRA, there is no debt service to recover and the expected cash flows are intended to recover only the operating costs. The initial construction cost of the plant is effectively committed to serve LCRA's wholesale customers and is included in the Balance Sheets at the contractual value. The recently purchased interest is fully recoverable from customers and thus is included in the balance sheets at the purchase price.

Although it is a separate legal entity, GenTex is reported as part of LCRA because its sole purpose is to provide assistance to LCRA's 42 long-term wholesale customers in meeting their demands and operating in a competitive market.

LCRA Transmission Services Corporation: LCRA TSC is a nonprofit corporation created by LCRA that began operations on Jan. 1, 2002, by engaging in the electric transmission and transformation business activities previously performed by LCRA. Although it is a separate legal entity, LCRA TSC is reported as part of LCRA because it is governed by a board of directors which is composed in its entirety of the LCRA Board of Directors.

Fayette Power Project: LCRA's coal-fired generating units are located at the Fayette Power Project (FPP) and operate pursuant to a participation agreement with Austin. LCRA has an undivided 50 percent interest in units 1 and 2 and wholly owns Unit 3. LCRA's investment is financed with LCRA funds, and its pro-rata share of operations is recorded as if wholly owned. The original cost of LCRA's share of FPP's generation and transmission facilities is recorded in the utility plant accounts of LCRA in accordance with its accounting policies. The equity interest in FPP is calculated pursuant to the participation agreement and is reported in various asset and liability accounts within LCRA's financial statements.

Restricted Funds: Restricted Funds consist of construction funds derived from debt issues and system revenues, which have been designated for specific purposes by the Board.

Utility Plant: Utility plant consists of generating plants, electric transmission and distribution facilities, dams, reservoir land, natural gas production and development, irrigation systems, water and wastewater treatment facilities, telecommunication facilities, and related projects under construction. These assets are recorded at cost, which includes materials, labor, overhead and interest capitalized during construction. The costs of repairs and minor replacements are charged to operating expense as incurred. Costs of asset replacements and betterments are capitalized. The cost of depreciable plant retired, along with removal expense less salvage value, is charged to nonoperating expense on the Statement of Revenues, Expenses and Changes in Equity. Gains and losses upon disposition are recorded in the period incurred.

Water Rights: Water rights are stated at cost, net of accumulated amortization of $7.4 million as of June 30, 2004 and 2003. Beginning in FY 2003, in accordance with accounting and reporting requirements, water rights are no longer being amortized but are evaluated annually to determine whether they are impaired and whether an indefinite life is reasonable.

Inventories: Coal is recorded at cost using the last-in, first-out method. Stored natural gas, fuel oil, and materials and supplies are stated at average cost. All nonfuel inventories are stated at the lower of cost or market.

Investments: Investments are stated at fair value. Any changes, unrealized and realized, in the fair value of financial investments are recorded as investment income.

Refunding and Defeasance of Debt: For debt refundings, the difference between the reacquisition price and the net carrying amount of the old debt is deferred and reported as a deduction from or an addition to the debt liability. For debt defeasances, the difference between the carrying amount of the debt and the amount of funds needed to retire the debt is recognized immediately in the Statements of Revenues, Expenses and Changes in Equity as a special item.

Compensated Absences: Earned vacation leave is recorded as a liability and accrues for certain salary-related expenses associated with the payment of compensated absences.

Rates and Regulations: LCRA's electric, water and wastewater rates are set by LCRA's Board at a level sufficient to recover its operating costs, debt service and debt service coverage requirements. LCRA's bond counsel is of the opinion that a Texas court applying Texas law would ultimately conclude that LCRA's Board has the authority to establish and collect such fees and charges. LCRA's transmission service rates remain regulated by the Public Utility Commission of Texas (PUC). While the LCRA Board has original jurisdiction over its water and wastewater rates, the Texas Commission on Environmental Quality has appellate jurisdiction.

SB 7, passed by the Texas Legislature in 1999, provided for retail electric open competition to begin in January 2002, continued electric transmission open access, and fundamentally redefined and restructured the Texas electric industry. SB 7 directly and indirectly impacts LCRA and its wholesale electric customers. Under SB 7, LCRA has structurally unbundled its electric generation business and assets from its electric transmission business and assets. SB 7 also allows retail customers of investor owned utilities, as well as the retail customers of those municipally owned utilities and electric cooperatives that elect to participate in retail competition, to choose their electric supplier.

Transmission rates within the Electric Reliability Council of Texas (ERCOT) system are determined pursuant to a universal 100 percent "postage stamp" rate that spreads the total annual costs of transmission services among distribution service providers (DSPs) according to their electric loads. The transmission costs are determined pursuant to transmission cost of service (TCOS) rate proceedings required to be filed by all transmission service providers, including LCRA TSC. Every electric end-use consumer in the ERCOT system pays a portion of the total cost of maintaining a reliable statewide transmission system. Transmission charges are calculated by multiplying a DSP's share of the statewide electric load by the statewide "postage stamp" rate. The load shares and rates are determined by the PUC through its TCOS regulatory process. Additionally, pursuant to a tariff approved by the PUC, LCRA TSC collects revenues for transformation services, providing transformers that "step down" voltage from levels appropriate for transmission to lower levels for distribution. A monthly charge for each transformation delivery point is also authorized under the transformation tariff.

The greatest potential impact on LCRA from SB 7 could result from actions of its wholesale electric customers. If LCRA's larger wholesale electric customers open their territories to retail competition, there is a potential that such customers could lose end-user customers to other retail electric providers resulting in a reduced electric load, thus reducing the requirements served by LCRA under the existing wholesale power agreements. On the other hand, if LCRA's wholesale electric customers are successful in retaining existing customers and in growing their customer base, requirements served by LCRA under the existing wholesale power agreements could increase.

Deferred Revenues: In November 2003, LCRA TSC filed a rate case with the PUC seeking a new TCOS rate. In January 2004, the administrative law judge approved an interim rate of $3 per kilowatt (kW) to be effective June 1, 2004. However, LCRA TSC recognized revenue for June 2004 activity only based on a rate of $2.33 per kW because the final rate case outcome is unknown. LCRA TSC recorded $13.3 million of deferred revenue related to the $3 per kW interim rate. As a result, the rate case administrative hearings phase was concluded in June 2004, with PUC commissioners' approval of a final TCOS rate anticipated for December 2004.

Regulatory Assets and Liabilities: LCRA applies the accounting requirements of FASB Statement of Financial Accounting Standards No. 71 (SFAS 71), "Accounting for the Effects of Certain Types of Regulation." Accordingly, certain costs may be capitalized as a regulatory asset that would otherwise be charged to expense. A regulatory asset is recorded when it is probable that future revenue in an amount at least equal to the capitalized costs will result from inclusion of those costs in future rates. In addition, rate actions of the regulator may impose a liability on LCRA. A regulatory liability occurs when a regulator requires refunds to customers or provides current rates intended to recover costs that are expected to be incurred in the future. Any regulatory asset is amortized over the life of LCRA's outstanding long-term debt, while a regulatory liability is recognized and charged to income when the associated costs are incurred. LCRA's regulatory assets amounted to $219 million and $188 million at June 30, 2004 and 2003, respectively. Regulatory liabilities amounted to $2.4 million and $2.9 million at June 30, 2004 and 2003, respectively. The regulatory assets, which are included under deferred charges, consist of depreciation of debt-funded assets and costs related to outstanding debt. Debt-funded costs are deferred pending future recovery through the inclusion of the related debt service in rates. Regulatory liabilities are included in deferred credits and other long-term liabilities.

LCRA has reviewed and will continue to monitor the relevance of SFAS 71 in light of SB 7 and future changes in the Texas electric industry. As of June 30, 2004, and for the foreseeable future, management believes that SFAS 71 will continue to apply and anticipates no material losses from the write-off of regulatory assets.

Capitalized Interest: Interest is capitalized as part of the cost of capital assets and deferred charges if financed by debt proceeds. During FY 2004 and 2003, LCRA capitalized $20.5 million and $20.6 million of interest, respectively.

Gas Price Management: LCRA enters into futures contracts, swaps and options for energy price risk management purposes. Derivative instruments are recorded on the balance sheet at their fair value. Changes in the fair value of derivatives are recorded each period in current earnings. LCRA is using mark-to-market accounting for its derivatives and gains and losses related to the financial contracts are recognized in current earnings as a component of the fixed-fuel factor.

Fixed Fuel Factor: Revenues from the sale of electricity include amounts collected through the fixed-fuel factor. LCRA records over- or under-recoveries of fuel costs, including unrealized gains or losses on financial contracts entered into as part of its gas price management program, as a deferred asset or liability. These costs are periodically reconciled through adjustment of the fixed-fuel factor. Over-recoveries may result in refunds to customers and, correspondingly, under-recoveries may result in additional assessments to customers.

Natural Gas Development and Production: LCRA has adopted the full-cost method of accounting for natural gas development and production. Under this method, all costs directly associated with acquisition and development of oil and gas properties are capitalized and depleted to expense over the life of proved reserves on a units-of-production method. For the years ended June 30, 2004 and 2003, depletion expense totaled approximately $0.4 million and $0.5 million, respectively.

Contract Extension Settlement with Major Customers: According to the terms of a 1987 settlement with two major customers, their wholesale power contracts were extended to 2016, and in return, LCRA reimbursed the customers for their costs incurred in planning generating facilities. These costs are amortized over the period affected by the contract extension.

Impairment: LCRA evaluates the carrying value of its property, plant and equipment, and other long-lived assets when major events or changes in circumstances indicate a decline in an asset's service capacity. In accordance with GASB 42, impairment is measured using methods that isolate the asset's service capacity that has been rendered unusable.

Depreciation and Amortization: LCRA depreciates its utility plant in service on a straight-line basis over the estimated useful lives of the various classes of these assets. Annual depreciation expense, expressed as a percentage of average depreciable utility plant, was approximately 3 percent for FY 2004 and 2003. Depreciation and amortization expense for FY 2004 and 2003 was approximately $85 million and $69 million respectively.

The estimated useful life of property, plant and equipment by major category is as follows:

Hydraulic Production Plant	55 - 100 years
Steam Production Plant	35 - 40 years
Transmission Plant	35 - 65 years
General Plant	4 - 45 years
Irrigation Plant	15 - 100 years
Sewage and Water Treatment Plant	10 - 50 years
Telecommunication Facilities	10 - 25 years

Water rights are not amortized but are evaluated annually to determine whether they are impaired and whether an indefinite life is reasonable. Gains or losses created by refunding transactions are amortized over the shorter of the remaining terms of the new issues or the refunded bonds. Amortization of debt discount and premium is computed using the interest method over the life of the related bond issues. Amortization of debt issue cost is computed on the straight-line method over the life of the related bond issues, which approximates the interest method. Other deferred charges are amortized on a straight-line basis ranging from 20 to 40 years.

Statements of Cash Flows: All highly liquid investments (including investments in restricted funds) with an original maturity of three months or less are considered cash equivalents. Hedge transactions are classified in the same category as the item being hedged.

Reclassifications: Certain amounts in the prior year's financial statements have been reclassified to conform to current year presentation.

3. Financial Instruments

Deposits: Texas law and Board policy require that LCRA deposits be placed in financial institutions located in Texas. Such deposits must be collateralized with securities or surety bonds to the extent not insured by the Federal Deposit Insurance Corporation (FDIC). Securities that may be accepted as collateral are those authorized by the Public Funds Collateral Act. Accordingly, these are limited to obligations of the United States and its agencies and instrumentalities, obligations issued by public agencies with at least a rating of "A" by a nationally recognized rating agency, and any other security in which a public entity may invest under the Public Funds Investment Act.

At June 30, 2004 and 2003, LCRA deposits in excess of the amount insured by the FDIC were collateralized entirely by direct obligations of the United States and its agencies and instrumentalities. This collateral, amounting to approximately $7.1

million for June 30, 2004, and $7.6 million for June 30, 2003, was held at the Federal Reserve Bank in the name of LCRA in an account separate and apart from the pledging banks.

Investments: LCRA's investment activities are governed by state statute (the Public Funds Investment Act), LCRA Board policy, internal operating procedures and applicable bond resolutions. These governing instruments further restrict certain funds from participating in all investment types. At June 30, 2004 and 2003, LCRA investments consisted of securities of the United States and its agencies and instrumentalities, commercial paper, and a money market fund.

At June 30, 2004 and 2003, LCRA's investments, including cash equivalents, are insured or registered or are held by LCRA or by LCRA's agent in LCRA's name.

External Investments Pool: LCRA's investments included a money market fund with TexPool at June 30, 2004. The State Comptroller of Public Accounts oversees TexPool, and the pool seeks to maintain a $1 value per share as required by the Texas Public Funds Investment Act. There are no minimum balance requirements for TexPool participants, and there is no limit on the number of accounts per participant.

Estimation of Fair Values: The carrying amount of all financial instruments is market value. Investment securities are valued at quoted market prices.

Type of Investment	June 30, 2004	June 30, 2003
	(Dollars in Thousands)	
Investments		
U.S. Government Securities	$ 169,403	$ 141,108
Commercial Paper	-	286
Cash Equivalents		
U.S. Government Securities	-	5,996
Commercial Paper	25,500	19,869
Money Market Fund	38,059	43,476
Totals	$ 232,962	$ 210,735

The carrying amount of receivables and certain other liabilities approximates market value due to the short maturity of these instruments. The estimated market value of long-term debt, based on current market yields, was $2.3 billion and $2.0 billion at June 30, 2004 and 2003, respectively.

Hedging Instruments: LCRA's gas activities subject LCRA's earnings to variability based on fluctuations in the market price of natural gas as measured by changes in the delivered price of natural gas at various points in the system's natural gas grid. In an effort to mitigate the financial and market risk associated with these activities for the customers, LCRA routinely enters into natural gas swaps, futures contracts and options for other than trading purposes. This use of these types of transactions for the purpose of reducing exposure to price risk is generally referred to as hedging, with the results matching the financial impact of these transactions with the cash impact resulting from consummation of the transaction being hedged. These contracts are commitments to either purchase or sell designated quantities of a commodity at a specified price and at a specified date. These contracts may be settled in cash or through delivery of the specified commodity; however, in general, LCRA settles futures contracts in cash. LCRA holds highly liquid contracts with terms ranging up to 18 months. Initial margin requirements, which are flat fees per contract, and daily margin calls are met in cash or short-term liquid government securities. The financial impact of these futures contracts, the effects of which were substantially offset by the physical gas purchases, was to recognize a loss of approximately $1.8 million during 2004 and a loss of $1.8 million during 2003. Net income is not affected because this activity is a component of the fuel costs passed through to the customers and is included in the balance sheet fuel over- or under-recovery account.

All derivative instruments are recorded on the balance sheet at their fair value, which generally reflects the estimated amounts that LCRA would receive or pay to terminate the contracts. At June 30, 2004, the fair value of LCRA's hedging assets and liabilities were $2.3 million and $0.3 million, respectively. Changes in the fair value of the derivatives are recorded in current earnings as a component of the fixed-fuel factor. LCRA has not designated any of the derivatives as hedging instruments, as allowed by FASB 133.

Counterparties expose LCRA to credit-related losses in the event of nonperformance, but LCRA does not expect any counterparties to fail to meet their obligations given their high credit ratings.

4. Long-Term Debt

Changes during FY 2004 and balances at June 30, 2004, of long-term debt, including current portions are as follows (in thousands):

Series	Maturity Date May 15, From	To	Balance June 30, 2003	Increases	(Decreases)	Balance June 30, 2004	Amount Due in FY 2005
Series 2003A (Auction Rate) (1)	2030	2032	$ 50,000	$	$	$ 50,000	$
Series 2003B (5.00%-5.375%)	2005	2031	254,985			254,985	3,010
Series 2003C (5.00%-5.25%)	2005	2033	-	135,355	(1,045)	134,310	3,110
2004 (2.00%-5.00%)	2005	2029	-	105,550		105,550	2,400
2004A (3.50%-3.50%) (3)	2006	2007	-	211		211	
2004B (3.50%-3.50%) (3)	2005	2006	-	42		42	39
2004C (3.50%-3.50%) (3)	2005	2005	-	54		54	54
2003 (3.25%-5.25%)	2005	2033	-	104,975	(5,035)	99,940	3,690
2002 (3.50%-5.00%)	2005	2031	120,195		(1,060)	119,135	1,065
2001A (4.00%-5.375%)	2005	2032	154,285		(2,465)	151,820	2,480
2001 (5.00%-8.00%)	2005	2031	97,610		(560)	97,050	620
1999A (5.50%-5.875%)	2014	2020	347,540			347,540	
1999B (5.875%-6.00%)	2007	2014	348,520			348,520	
1999C (6.92%-7.02%)	2005	2006	111,530		(39,260)	72,270	41,950
1999D (6.875%-6.875%) (2)	2003	2003	16,185		(16,185)	-	
1999E (4.75%-5.75%)	2005	2011	24,410		(1,250)	23,160	1,200
1999F (5.50%-5.75%)	2008	2012	97,930			97,930	
1999G (3.60%-4.85%) (3) (4)	2004	2016	43,060		(1,435)	41,625	1,645
1999H (2.85%-3.30%) (3) (5)	2005	2011	7,775		(890)	6,885	1,120
1999I (3.10%-4.15%) (5)	2005	2020	3,720		(80)	3,640	95
TWDB Note Payable (6.05%-6.10%)	2020	2034	10,500			10,500	
TWDB Note Payable (5.63%-5.78%)	2023	2036	7,455			7,455	
Add: Unamortized Net Premium			29,800	17,978	(5,414)	42,364	492
Subtotal			1,725,500	364,165	(74,679)	2,014,986	62,970
Unamortized Net Losses on Refunded Debt			(281,052)		13,297	(267,755)	(11,152)
Taxable Commercial Paper (Variable Rate)			1,500	30,600	(25,100)	7,000	7,000
Tax-Exempt Commercial Paper (Variable Rate)			142,500	380,500	(329,700)	193,300	193,300
Total			$ 1,588,448	$ 775,265	$ (416,182)	$ 1,947,531	$ 252,118

(1) Rate is reset at auction every 28 days (1.24 percent as of June 30, 2004).
(2) Maturity Date is Nov. 15.
(3) Represents yield rate of Capital Appreciation Bonds.
(4) Maturity Date is July 1.
(5) Maturity Date is Jan. 1.

LCRA's debt as of June 30, 2004, has been rated by Fitch, Moody's and Standard & Poor's, respectively, as follows:

Fitch, Moody's and Standard & Poor's

Refunding and Improvement Revenue Bonds: A+, A1, and A (Uninsured)

Commercial Paper: F-1+, P-1, A-1

LCRA Transmission Services Corporation Contract Refunding Revenue Bonds Series 2003A, B and C: A, A2, A (Uninsured)

LCRA Transmission Services Corporation Commercial Paper: F-1, P-1, A-1+

Bond and note debt payments, excluding commercial paper, are as follows (in thousands):

Fiscal Year Ending June 30	Principal	Interest	Total
2005	$ 62,478	$ 104,698	$ 167,176
2006	59,160	100,899	160,059
2007	76,864	97,503	174,367
2008	85,300	93,353	178,653
2009	86,675	88,733	175,408
2010-2014	507,445	368,106	875,551
2015-2019	458,885	227,410	686,295
2020-2024	292,700	123,115	415,815
2025-2029	189,000	62,745	251,745
2030-2034	152,640	16,675	169,315
2035-2039	1,475	129	1,604
	1,972,622	1,283,366	3,255,988
Unamortized Net Premium	42,364	-	42,364
Total	$ 2,014,986	$ 1,283,366	$ 3,298,352

New and Refunding Bonds: During FY 2004, LCRA issued $30.6 million of taxable commercial paper and $211.2 million of tax exempt commercial paper. In addition, LCRA on behalf of LCRA TSC issued $169.3 million of tax exempt commercial paper.

On June 18, 2004, LCRA issued $0.2 million and $0.04 million of tax exempt Revenue Bonds, Series 2004A and 2004B respectively. In addition, on June 18, 2004, LCRA issued $0.05 million of taxable Revenue Bonds, Series 2004C. The proceeds from each of these fundings were used for capital project funding.

On April 27, 2004, LCRA issued $105.6 million of tax-exempt Revenue Bonds, Series 2004. The proceeds from the bond issue were used to refund $20 million of taxable commercial paper and $89 million of tax-exempt commercial paper.

On Nov. 17, 2003, LCRA refunded $16.2 million of the Series 2000 Refunding Revenue Bonds, Series D with tax-exempt commercial paper.

On Oct. 16, 2003, LCRA issued $105 million of Refunding and Improvement Revenue Bonds, Series 2003. The proceeds from the bond issue were used to refund $104.6 million of tax-exempt commercial paper and to provide $4 million for capital project funding. In addition, on Oct. 16, 2003, LCRA on behalf of LCRA TSC issued $135.4 million of Transmission Contract Auction Rate Refunding Revenue Bonds, Series 2003C. The proceeds from the bond issue were used to refund $135 million of tax-exempt commercial paper.

On May 7, 2003, LCRA issued $13.2 million of tax-exempt commercial paper to refund $13.2 million of taxable commercial paper. On Oct. 4, 2002, LCRA issued $108 million of tax-exempt commercial paper to refund $108 million of taxable commercial paper.

In March 2003, LCRA on behalf of LCRA TSC issued $50 million of Transmission Contract Auction Rate Refunding Revenue Bonds, Series 2003A and $255 million of Transmission Contract Refunding Revenue Bonds, Series 2003B. The bond proceeds, along with $91.9 million of construction funds and $22 million of Debt Service Reserve funds, were used to call (current refunding) the 2001 LCRA Transmission Services Revenue Construction Bonds. Although the refunding resulted in the recognition of a deferred accounting loss of $56 million, it reduced the future aggregated debt service payment by $231 million over the next 29 years. The deferred loss will be amortized over the life of the refunding issue. The refunding resulted in an economic gain of $40.9 million. The economic gain of the refunding $40.9 million represents the difference between the present value of the old debt service requirements (principal and interest payments) and the present value of the new debt service requirements and adjusted for additional cash paid. The interest rate on the Series 2003A bonds is variable and is reset at auction every 28 days. The Series 2003B bonds have a fixed coupon that pays semiannually. To calculate the economic gain of the transaction, it was necessary to assume a fixed interest rate on the $50 million Series A bonds. For the economic gain calculation, it was assumed that the variable rate bonds had ascending fixed rates of 3.0 percent from May 15, 2004, to May 15, 2005, and 3.5 percent from May 15, 2005, to the final maturity of the bonds. This conservative estimate was based on the 10-year Bond Market Association (BMA) average. The BMA index is a weekly high-grade market index of tax-exempt variable rate demand notes produced by Municipal Market Data Group. Currently the variable rate bonds have a coupon of 1.24 percent, and the BMA index is 1.05 percent. If interest rates remain below the assumed rates in the calculation, the economic gain will be greater than $40.9 million. However, if rates rise above the assumed rates at any time, the economic gain will be less. In order for the LCRA to realize an economic loss on the transaction, rates on the 2003A bonds would have to rise above 7 percent.

On Oct. 15, 2002, LCRA issued $121 million of tax-exempt Revenue Bonds, Series 2002. The proceeds from the bond issue were used to refund $15.9 million of taxable commercial paper and $109.1 of tax-exempt commercial paper.

During FY 2003, LCRA issued $75.6 million of tax exempt commercial paper and $8.5 million of taxable commercial paper to fund various capital projects. In addition, LCRA on behalf of LCRA TSC issued $44.5 million to fund transmission related capital projects.

The principal associated with the bonds that have been previously refunded by LCRA but remain outstanding at June 30, 2004 and 2003, totals $397 million and $510 million, respectively. Proceeds from these refunding bond issues were escrowed to purchase U.S. government obligations that will mature at such time and yield interest as such amounts so that sufficient monies are available for payment of principal, premium, if any, and interest on the refunded bonds when due. None of these refunded bonds are included in LCRA's outstanding long-term debt at June 30, 2004 and 2003.

Optional Redemption: The Series 2004 bonds that mature on and after May 15, 2012, are redeemable at the option of LCRA on May 15, 2011, or on any date thereafter, in whole or in part, in principal amounts of $5,000 or integral multiples thereof (and, if in part, the particular bonds or portions thereof to be redeemed shall be selected by LCRA in its sole discretion) at a redemption price equal to the principal amount of such bonds to be redeemed, plus accrued interest to the redemption date.

The Series 2003 bonds that mature on and after May 15, 2014, are redeemable at the option of LCRA on May 15, 2013, or on any date thereafter, in whole or in part, in principal amounts of $5,000 or integral multiples thereof (and if in part, the particular bonds or portions thereof to be redeemed shall be selected by LCRA in its sole discretion) at a redemption price equal to the principal amount of such bonds to be redeemed, plus accrued interest to the redemption date.

LCRA TSC Series 2003C bonds that mature on and after May 15, 2014, are redeemable at the option of LCRA on May 15, 2013, or on any date thereafter, in whole or in part, in principal amounts of $5,000 or integral multiples thereof (and if in part, the particular bonds or portions thereof to be redeemed shall be selected by LCRA in its sole discretion) at a redemption price equal to the principal amount of such bonds to be redeemed, plus accrued interest to the redemption date.

LCRA TSC Series 2003A bonds are subject to optional redemption by LCRA, upon the written direction of LCRA TSC, in whole or in part, on any interest payment date immediately following an auction period, in authorized denominations at a redemption price equal to the principal amount thereof, plus accrued interest to the redemption date; provided, however, that in the event of a partial redemption of bonds, the aggregate principal amount of bonds that will remain outstanding must equal at least $10 million unless otherwise consented to by the related broker-dealers.

LCRA TSC Series 2003B bonds that mature on and after May 15, 2013, are redeemable at the option of LCRA on May 15, 2012, or on any date thereafter, in whole or in part, in principal amounts of $5,000 or integral multiples thereof (and if in part, the particular bonds or portions thereof to be redeemed shall be selected by LCRA in its sole discretion) at a redemption price equal to the principal amount of such bonds to be redeemed, plus accrued interest to the redemption date.

The Series 2002 bonds that mature on and after May 15, 2014, are redeemable at the option of LCRA on May 15, 2013, or on any date thereafter, in whole or in part, in principal amounts of $5,000 or integral multiples thereof (and if in part, the particular bonds or portions thereof to be redeemed shall be selected by LCRA in its sole discretion) at a redemption price equal to the principal amount of such bonds to be redeemed, plus accrued interest to the redemption date.

The Series 2001A bonds maturing on and after May 15, 2012, are redeemable at the option of LCRA on May 15, 2011, or on any date thereafter, in whole or in part, in principle amounts of $5,000 or integral multiples thereof at a redemption price equal to the principal amount of such bonds to be redeemed, plus accrued interest to the redemption date.

The Series 2001 bonds maturing on or after May 15, 2011, are callable at the option of LCRA for a period of one year beginning on May 15, 2010, at the price of 101 percent plus accrued interest. These bonds are also callable at LCRA's option on May 15, 2011, or on any date thereafter, in whole or in part, in principal amounts of $5,000 or integral multiples thereof at the price of 100 percent plus accrued interest.

The Series 1999A bonds, Series 1999B bonds, Series 1999E bonds and Series 1999F bonds maturing on or after May 15, 2010, are callable at the option of LCRA for a period of one year beginning on May 15, 2009, at the price of 101 percent plus accrued interest. These bonds are also callable at LCRA's option on May 15, 2010, or on any date thereafter, in whole or in part, in principal amounts of $5,000 or integral multiples thereof at the price of 100 percent plus accrued interest.

The LCRA bonds outstanding as of June 30, 2004 and 2003, are parity debt under the Master Resolution and are collateralized by a lien on and pledge of the pledged revenues. Pledged revenues are defined to include all amounts received pursuant to contractual commitments and all lawfully available funds of LCRA. The LCRA Transmission Contract Revenue Bonds Series 2003A and 2003B are solely secured by the obligation of LCRA TSC to make Installment Payments to LCRA from the net revenues of LCRA TSC (subordinate to first lien on gross revenues securing the purchase price payments under the initial contractual commitment). Net revenues are defined as gross revenues less any purchase price payments due to LCRA and less the operating and maintenance expenses during the period.

Commercial Paper: LCRA is authorized to issue up to $350 million in short-term tax-exempt obligations and $350 million in short-term taxable obligations to provide system improvements, acquire fuel reserves and facilities, refund outstanding debt, and pay interest on outstanding debt. Outstanding notes were issued in denominations of $100,000 or more with maturities of 270 days or less from their respective issue dates. The commercial paper program expires May 15, 2020. It is management's intent to renew on a periodic basis outstanding commercial paper upon maturity.

LCRA maintains credit facilities with banks that provide available borrowings sufficient to pay the principal of the notes. LCRA has entered into a revolving credit agreement with a bank that is obligated to lend LCRA amounts of up to $187.5 million for the Tax-Exempt series. Of the $187.5 million, $112.5 million of this agreement expires on Oct. 13, 2004, and the remaining $75 million expires on June 27, 2005. LCRA has an additional revolving credit agreement with a bank that is obligated to lend LCRA aggregate amounts of up to $40 million for the Taxable Series. This agreement expires on Nov. 1, 2005. Failure by LCRA to meet certain restrictive covenants could result in the withdrawal of the banks' commitments for the unused lines of credit. There were no borrowings under any of the agreements as of June 30, 2004.

LCRA TSC is authorized to issue tax exempt commercial paper notes in an aggregate amount of principal and interest not to exceed $150 million in short-term tax-exempt obligations. Outstanding notes were issued in denominations of $100,000 or more with maturities of 270 days or less from their respective issue dates. The commercial paper program expires May 15, 2042. It is management's intent to renew on a periodic basis outstanding commercial paper upon maturity.

LCRA TSC maintains a $150 million credit facility with a bank that provides available borrowings to pay the principal and interest of the commercial paper notes. Of the $150 million total, $137 million is available to pay the principal of the notes and $13 million is available to pay interest on the notes. The credit facility has an expiration date of April 29, 2006. Failure by LCRA or LCRA TSC to meet certain restrictive covenants could result in the withdrawal of the banks' commitments for the unused lines of credit. There were no borrowings under the agreement as of June 30, 2004.

Conduit Debt: At June 30, 2004, there are two series of Pollution Control Revenue Bonds outstanding with an aggregate principal amount payable of $50 million. The bonds mature in April 2027 and 2030, $25 million each year. The bonds were issued to finance the costs of acquiring, constructing and improving certain solid waste and sewage disposal facilities of a private-sector entity. LCRA executed an installment sale agreement with the entity whereby the proceeds of the bonds were used to finance a portion of the project. In turn, the entity agreed to make payments sufficient to pay, when due, the principal and interest on the bonds. The bonds do not constitute a debt or pledge of LCRA, and accordingly have not been reported in the accompanying financial statements.

Mandatory Redemption: The following term bonds will be subject to mandatory redemption prior to maturity on May 15 in each of the following years and in the following amounts at the redemption price equal to the principal amount thereof plus accrued interest to the redemption date, with the particular bonds or portions thereof to be redeemed, to be selected and designated by LCRA (provided that a portion of a bond may be redeemed only in an integral multiple of $5,000):

Series 2004
Term Bond Maturing May 15, 2024

Redemption Date		Amount
May 15, 2023	$	5,120,000
May 15, 2024		5,120,000

Series 2004
Term Bond Maturing May 15, 2026

Redemption Date		Amount
May 15, 2025	$	5,120,000
May 15, 2026		5,120,000

Series 2004
Term Bond Maturing May 15, 2029

Redemption Date		Amount
May 15, 2027	$	5,190,000
May 15, 2028		5,190,000
May 15, 2029		5,200,000

LCRA Transmission Services Corporation Series 2003C
Term Bond Maturing May 15, 2033

Redemption Date		Amount
May 15, 2029	$	4,515,000
May 15, 2030		4,515,000
May 15, 2031		4,515,000
May 15, 2032		4,515,000
May 15, 2033		11,165,000

LCRA Transmission Services Corporation Series 2003C
Term Bond Maturing May 15, 2028

Redemption Date		Amount
May 15, 2026	$	4,515,000
May 15, 2027		4,515,000
May 15, 2028		4,515,000

LCRA Transmission Services Corporation Series 2003B
Term Bond Maturing May 15, 2031

Redemption Date		Amount
May 15, 2026	$	10,985,000
May 15, 2027		10,985,000
May 15, 2028		10,985,000
May 15, 2029		10,985,000
May 15, 2030		7,310,000
May 15, 2031		8,040,000

LCRA Transmission Services Corporation Series 2003A
Term Bond Maturing May 15, 2032

Redemption Date		Amount
May 15, 2030	$	3,675,000
May 15, 2031		12,325,000
May 15, 2032		34,000,000

Series 2003
Term Bond Maturing May 15, 2028

Redemption Date		Amount
May 15, 2026	$	3,795,000
May 15, 2027		3,985,000
May 15, 2028		4,185,000

Series 2003
Term Bond Maturing May 15, 2033

Redemption Date		Amount
May 15, 2029	$	4,395,000
May 15, 2030		4,615,000
May 15, 2031		4,845,000
May 15, 2032		5,090,000
May 15, 2033		5,345,000

Series 2002
Term Bond Maturing May 15, 2031

Redemption Date		Amount
May 15, 2025	$	780,000
May 15, 2026		815,000
May 15, 2027		6,425,000
May 15, 2028		6,460,000
May 15, 2029		6,545,000
May 15, 2030		8,630,000
May 15, 2031		8,665,000

Series 2001A
Term Bond Maturing May 15, 2032

Redemption Date		Amount
May 15, 2029	$	4,500,000
May 15, 2030		4,500,000
May 15, 2031		4,500,000
May 15, 2032		4,505,000

Series 2001A
Term Bond Maturing May 15, 2026

Redemption Date		Amount
May 15, 2022	$	7,380,000
May 15, 2023		6,315,000
May 15, 2024		6,635,000
May 15, 2025		6,975,000
May 15, 2026		7,320,000

Series 2001
Term Bond Maturing May 15, 2026

Redemption Date		Amount
May 15, 2024	$	10,885,000
May 15, 2025		11,210,000
May 15, 2026		3,330,000

Series 2001
Term Bond Maturing May 15, 2031

Redemption Date		Amount
May 15, 2027	$	1,810,000
May 15, 2028		1,900,000
May 15, 2029		2,000,000
May 15, 2030		2,100,000
May 15, 2031		2,210,000

Series 1999A
Term Bond Maturing May 15, 2021

Redemption Date		Amount
May 15, 2020	$	47,535,000
May 15, 2021		27,430,000

5. Retirement and 401(k) Plans, Deferred Compensation and Post-Employment Benefits

Retirement Plan: The Lower Colorado River Authority Retirement Plan (Plan) is a single-employer defined benefit pension plan and is administered by the LCRA Retirement Plan Board of Trustees. The Plan issues a stand-alone financial report that is available from the Board of Trustees. As a result of the amendments and restatements of the Plan during FY 2002, the Plan has submitted an application for a determination concerning the qualification of the Plan to the Internal Revenue Service. The previous Plan had received a favorable determination letter from the Internal Revenue Service and was exempt from federal income taxes, under the appropriate section of the Internal Revenue Code. LCRA anticipates that the restated Plan also will qualify for tax-exempt status.

The Plan provides retirement, death and disability benefits. Employees are not required to contribute to the Plan although the Plan retains employee contributions and associated liabilities for years prior to April 1, 1984, when the plan did require employee contributions. Amendments to the Plan are made only with the authority of the LCRA Board of Directors.

Effective Jan. 1, 2002, the Plan was amended to provide cash balance benefit features. Active employees as of Dec. 31, 2001, were given the opportunity to remain participants under the pension provisions (Retirement Program A) or to elect to become participants under the cash balance provisions (Retirement Program B). Employees hired prior to Jan. 1, 2002, who elected Program A and who worked at least 1,000 hours per annum were eligible plan participants in the plan upon completion of six months of service and become 100 percent vested after three complete years of service. Any employee that was employed by LCRA prior to Jan. 1, 2002, and who elected Program B were eligible to participate in the cash balance benefit plan as of Jan. 1, 2002, and will be 100 percent vested after three complete years of service. Any employee hired after Jan. 1, 2002, who works at least 1,000 hours per annum will automatically be enrolled in Program B, will be eligible to participate in the plan after three consecutive months of service and will be 100 percent vested after three complete years of service.

Under Program A, employees may retire with unreduced accrued benefits at age 65 with five years of service, or when the total of their age and service equals 80. Retirement benefits are based on years of service and salary levels at retirement. Under Program B, the value of the employee's account will be adjusted by increasing the balance by 4 percent of the employee's compensation paid per year. The value of the account earns an annual interest rate of 7 percent. The retirement benefit for an employee who has reached his or her normal retirement date is a single lump sum payment equal to the participant's accrued balance or monthly payments as provided by the Plan.

LCRA makes contributions to the Plan that are determined actuarially as of each of the Plan's valuation dates. The required employer contribution for FY 2004 was 8.34 percent of total employee payroll. The current recommended employer contributions for FY 2005 are 8.15 percent of total employee payroll. The costs of administering the Plan are paid by the Plan and are considered in the determination of the required employer contribution rate.

Changes in plan provisions that impacted funding were an ad hoc cost of living adjustment to retirees effective Jan. 1, 2002, an increase in maximum benefits and compensation limitations imposed under the Internal Revenue Code, and revised assumptions for withdrawal and retirement due to cash balance benefits. Effective April 1, 2004, the amortization period for the recommended contribution amount was increased by one year, from 16 years to 17 years of the unfunded actuarial accrued liability. The prior year's amortization period, effective April 1, 2003, for the contribution amount was increased from 16 years to 17 years of the unfunded actuarial accrued liability.

Schedule of Funding Progress

Actuarial Valuation Date	(1) Actuarial Value of Assets[1]	(2) Actuarial Accrued Liability Entry Age	(3) Funded Ratio (1)/(2)	(4) Unfunded Actuarial Accrued Liability (2)-(1)	(5) Annual Covered Payroll[2]	(6) Unfunded Actuarial Accrued Liability as a Percentage of Covered Payroll (4)/(5)
April 1, 2002	$216,437,489	$279,453,512	77.5	$63,016,023	$107,945,731	58.4
April 1, 2003	225,914,808	303,162,298	74.5	77,247,490	124,210,361	62.2
April 1, 2004	239,289,653	319,622,320	74.9	80,332,667	128,454,336	62.5

[1] Actuarial value recognizes asset gains and losses over a five-year period.

[2] Based on projected payroll as of valuation date.

Three-Year Annual Pension Cost (APC) Trend Information

Fiscal Year Ending	APC	Percentage of APC Contributed	Net Pension Obligation (NPO)[1]
June 30, 2002	$ 9,331,879	100%	$ -
June 30, 2003	10,472,737	100	-
June 30, 2004	10,962,373	100	-

[1] NPO is zero because employer contributions have been equivalent to actuarially determined funding requirements for all fiscal years beginning Dec. 15, 1986.

401(k) Plan: LCRA's Retirement Benefits Board of Trustees administers this single-employer defined contribution plan. The Plan is accounted for on the accrual basis and all assets are recorded at fair value. The Plan has received a favorable determination letter from the Internal Revenue Service and is exempt from federal income taxes, under the appropriate section of the Internal Revenue Code.

Employees are eligible to participate in the Plan following the completion of three months of service. Eligible employees who elect to participate in the Plan may contribute a minimum of 1 percent and a maximum of 100 percent of their annual compensation, not to exceed $13,000 in 2004. Employees age 50 or over may contribute an additional $3,000 in 2004. Effective Jan. 1, 2002, employees under Program A of the Pension Plan receive an LCRA matching contribution equal to 25 percent of the first 4 percent of compensation that the employee had elected to contribute to the plan. Under Program B of the Pension Plan, LCRA provides matching contributions equal to 100 percent of the first 4 percent of compensation and 50 percent of the next 2 percent of compensation that the employee has elected to contribute to the plan. Contributions made by both the employer and employee are vested immediately. Amendments to the Plan are made only with the authority of the LCRA Board. Contributions by the LCRA and the employees for the years ended June 30, 2004 and 2003, are presented below:

	2004	2003
	Dollars in Thousands	
Employer contributions	$1,652	$1,407
Employee contributions	6,968	6,326

Postemployment Benefits: LCRA provides postemployment health care benefits to retirees and to terminated employees eligible for such benefits. LCRA contributes approximately 78 percent of the retirees' health plan premiums but makes no contributions for terminated employees. These contributions are recognized currently as premiums are paid and totaled approximately $4.0 million and $3.6 million for FY 2004 and 2003, respectively. At June 30, 2004, there were 631 retirees and 24 terminated employees eligible for such benefits.

6. Gas Production and Development Activities

LCRA provides a portion of expected annual gas requirements through the ownership of gas reserves. LCRA operates a producing field, Rocky Creek, in Fayette County, Texas, with an average 57 percent ownership interest in 11 producing gas wells. Based on an analysis as of July 1, 2004, by an independent engineering firm, the estimated proved remaining reserves associated with the Rocky Creek program were 5,221 barrels of oil and 2.783 billion cubic feet of gas, net to LCRA's interest. Production for FY 2004 and 2003, for the Rocky Creek program was approximately 1,595 and 2,124 barrels of oil and 0.473 and 0.518 billion cubic feet of gas, respectively. As of June 30, 2004, LCRA had incurred capital costs of approximately $25.8 million for the Rocky Creek program.

7. Commitments and Contingencies

Construction: LCRA's construction budget provides for capital improvement projects with cash requirements through FY 2009 of approximately $1.5 billion, including $386.8 million in FY 2005.

Customer Transmission Leases: LCRA leases and operates certain transmission facilities and equipment owned by 12 customers. The leases are the basis for LCRA to provide the same service to all of its customers and for the cost of such service to be shared by all customers on a consistent basis. Payments for the leased facilities vary from year to year and are based on the original cost of the facilities, adjusted for depreciation, and are updated annually to reflect additions, retirements and depreciation. The terms of the leases are perpetual but may be terminated by LCRA or the lessors upon five years written notice. Lease expenses for FY 2004 and 2003 totaled $10.3 million and $9.7 million, respectively.

Coal and Rail Contracts: For FY 2004, approximately 60 percent of the fuel requirements for the Fayette Power Project units 1 and 2 (FPP 1 & 2) were supplied under two multiyear contracts with mines in Wyoming's Powder River Basin. One contract has a fixed price per year and is for a volume that is subject to LCRA's discretion within a specified range. The second contract has a fixed price for its entire term, and the annual volume is dependent upon railroad performance. In FY 2005, these contracts will supply approximately 60 percent of FPP 1 & 2's coal needs. During FY 2004 and 2003, LCRA's purchases totaled $9.3 million and $6.9 million, respectively, under the multiyear contracts.

For FY 2004 approximately 67 percent of the fuel requirements for Fayette Power Project unit 3 (FPP 3) were supplied under two multiyear contracts with mines in Wyoming's Powder River Basin. One contract had a fixed price for its entire term. The annual volume under this contract is subject to LCRA's discretion, within a specified range. The second contract, that began in the second quarter of FY 2004, is for a fixed volume at a fixed price. In FY 2005, these contracts will supply approximately 76 percent of FPP 3's coal needs. LCRA's purchases under these contracts totaled $5.0 and $6.0 million for FY 2004 and 2003, respectively.

LCRA and Austin Energy have entered into a multiyear transportation agreement with two rail carriers to ship Powder River Basin coal to all three units at FPP. LCRA's share of the costs incurred under these agreements was approximately $48.3 million and $46.8 million in FY 2004 and 2003, respectively.

Natural Gas: LCRA has several long-term contracts to provide a portion of the natural gas requirements to its gas-fired generation units, through April 2014. LCRA is committed to buy a fixed amount of gas annually. LCRA's purchases under this contract totaled $91.6 million for FY 2004 and $83.5 million for FY 2003, based on price indices.

Purchased Power: LCRA has three energy contracts with power marketers to provide 400 MW of firm electric energy for the period June 1 through Sept. 30, 2004, and 100 MW for the period June 1 through Sept. 30, 2005. The total minimum commitment from these contracts is over $8 million plus energy payments.

Wind Power: LCRA is committed to purchase 35 MW of wind power capacity from Texas' first commercial wind power plant, the Texas Wind Power Project. LCRA in turn sells 10 MW of this capacity to Austin Energy. During FY 2004, LCRA purchased 30 MW of wind power capacity from the Delaware Mountain Wind Farm. In FY 2004, LCRA also purchased 51 MW of wind power capacity from the Indian Mesa Wind Farm. Total wind power capacity is 116 MW, of which 106 MW is for LCRA and its customers. LCRA expects to pay approximately $7.9 million in FY 2005 for purchases from all wind power plants, increasing to approximately $10.9 million in FY 2014.

Water Project Study: LCRA has entered into an agreement with the San Antonio Water System (SAWS) to study the feasibility of developing 330,000 acre-feet of water through the development of alternative water supplies and conservation measures. LCRA has committed to sell up to 150,000 acre-feet per year of this additional water to San Antonio, with the remainder used to eliminate water shortages in the lower Colorado basin. The study phase, estimated to be completed by March 2010 at a total cost of approximately $43 million, includes engineering feasibility and environmental studies and costs to obtain necessary permits for development and transfer of water. SAWS funds this study in advance to LCRA in its role as project manager. SAWS has the option to cancel the study phase at any time, with a 100 percent refund of unexpended funds and a 50 percent refund of expended funds due to SAWS when cancelled. As of June 30, 2004, LCRA has received $5.2 million from SAWS and has expended $1.8 million in study costs.

Insurance Self-Funding: In addition to the purchase of commercial insurance, LCRA has established a self-insurance program to finance risk of loss. LCRA is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. LCRA self-funds each worker's compensation claim up to $250,000, and each general liability claim up to a maximum of $2 million dependent on the insurance policy deductible. Self-funding of property damage varies from $100,000 to $2.5 million depending on the insurance deductible. Any claims or damages above self-funded amounts are covered by commercial general insurance. Settled claims have not exceeded commercial insurance coverage in any of the past three fiscal years. Based on an insurance risk analysis, LCRA carries no commercial insurance on transmission lines.

Accrued Liability: The accrued liability presented in the table below is associated with obligations resulting from environmental regulations established by federal, state and local authorities. Although the effect of future environmental regulations upon existing and proposed facilities and operations cannot be determined, LCRA monitors proposed changes and takes actions necessary to mitigate adverse impacts to its operations. At the present, no materially adverse impacts are anticipated.

Changes in the accrued liability amount for FY 2003 and 2004 were as follows:

	Balance Beginning of Year	Changes in Estimates	Payments	Balance End of Year
FY 2003	$3,922,000	-	$1,131,000	$2,791,000
FY 2004	2,791,000	-	368,000	2,423,000

Litigation: There are various lawsuits in which LCRA is involved. LCRA's management, including its general counsel, estimates that the potential claims against LCRA not covered by insurance resulting from such litigation would not materially affect LCRA's financial position, results of operations and cash flows.

8. Capital Activity

Capital asset activity for the year ended June 30, 2004, was as follows:

	Beginning Balance	Additions	Transfers from Construction in Progress	Retirements	Depreciation/ Depletion	Ending Balance
			(Dollars in Thousands)			
Utility plant in service:						
Depreciable assets	$ 2,381,858	$	$ 388,023	$ (18,042)		$ 2,751,839
Nondepreciable assets	25,686		562	(4)		26,244
Total Utility Plant in Service	2,407,544	-	388,585	(18,046)		2,778,083
Construction work in progress:						
Nondepreciable assets	222,240	462,642	(402,121)	613		283,374
Oil and gas property:						
Depletable assets	28,158					28,158
Other physical property:						
Depreciable assets	17,282		4,732	(495)		21,519
Nondepreciable assets	11,988		11,747	(3,641)		20,094
Total Other physical property	29,270	-	16,479	(4,136)		41,613
Less accumulated depreciation	(905,487)	194	(2,943)	6,732	(82,705)	(984,209)
Capital assets, net	$ 1,781,725	$ 462,836	$ -	$ (14,837)	$ (82,705)	$ 2,147,019

9. Segment

Governments that use enterprise fund accounting and reporting standards to report their activities are required to present segment information. A segment is an identifiable activity reported as or within an enterprise fund or another stand-alone entity that has one or more bonds outstanding with a revenue stream pledged in support of that debt. In addition, the activity's revenues, expenses, gains and losses, assets, and liabilities are required to be accounted for separately. An external party should impose the requirements for separate accounting. LCRA TSC qualifies as a segment.

LCRA TSC was created by LCRA to comply with the requirements of SB 7. LCRA transferred all of the assets of its regulated electric transmission and transformation businesses to LCRA TSC effective on Jan. 1, 2002.

Segment information for LCRA TSC:

LCRA Transmission Services Corporation - Segment Information
Balance Sheets
(Dollars in Thousands)

	June 30, 2004	June 30, 2003
Assets		
Current Assets	$ 59,264	$ 42,218
Long-Term Assets		
Restricted cash and cash equivalents	1,528	251
Restricted investments	21	-
Accounts receivable from LCRA - restricted	18,199	12,178
Capital assets:		
Utility plant in service	897,313	705,667
Construction work in progress	75,814	69,886
Less accumulated depreciation	(166,024)	(147,020)
Capital assets, net	807,103	628,533
Deferred charges:		
Costs to be recovered from future revenues	28,720	18,146
Issue costs	12,280	10,214
Deferred charges, net	41,000	28,360
Total long-term assets	867,851	669,322
Total Assets	$ 927,115	$ 711,540
Liabilities		
Current Liabilities	$ 117,278	$ 68,498
Long-Term Liabilities		
Accounts payable to LCRA from Construction Fund	12,880	21,062
Accounts payable from restricted assets	55,409	31,255
Bonds, notes, and loans payable	631,276	506,807
Deferred credits	13,270	-
Total long-term liabilities	712,835	559,124
Total liabilities	830,113	627,622
Equity		
Invested in capital assets, net of related debt	67,968	50,818
Unrestricted	29,034	33,100
Total equity	97,002	83,918
Total Liabilities and Equity	$ 927,115	$ 711,540

LCRA Transmission Services Corporation - Segment Information
Statements of Revenues, Expenses, and Changes in Equity
(Dollars in Thousands)

	Year Ended June 30, 2004	2003
Operating Revenues		
Transmission	$ 110,639	$ 93,322
Transformation	8,581	10,473
Other	42	90
Total operating revenues	119,262	103,885
Operating Expenses		
Operations	52,665	50,192
Maintenance	9,459	9,023
Depreciation and amortization	21,432	14,537
Total operating expenses	83,556	73,752
Operating income	35,706	30,133
Nonoperating Revenues (Expenses)		
Interest and other income	543	4,895
Loss on disposition of property	(3,041)	(2,368)
Interest on debt	(27,934)	(23,328)
Other expenses	(3,570)	(3,150)
Total nonoperating revenues (expenses)	(34,002)	(23,951)
Income before costs to be recovered from revenues and transfers in (out)	1,704	6,182
Cost To Be Recovered from Revenues	10,574	5,771
Income before transfers in (out)	12,278	11,953
Transfers In (Out)	806	(1,345)
Change in Equity	13,084	10,608
Total Equity, Beginning of Year	83,918	73,310
Total Equity, End of Year	$ 97,002	$ 83,918

LCRA Transmission Services Corporation - Segment Information
Statements of Cash Flows
(Dollars in Thousands)

	Year Ended June 30, 2004	Year Ended June 30, 2003
Cash Flows From Operating Activities		
Cash received from customers	$ 100,823	$ 90,953
Cash payments for goods and services	(49,215)	(59,133)
Net cash provided by operating activities	51,608	31,820
Cash Flows From Noncapital Financing Activities		
Other expenses	(3,570)	(3,150)
Net cash used in noncapital financing activities	(3,570)	(3,150)
Cash Flows From Capital and Related Financing Activities		
Expenditures for property, plant and equipment	(187,356)	(192,459)
Issuance costs	(2,653)	-
Proceeds from long-term debt issues	143,330	317,757
Proceeds from commercial paper	169,300	44,500
Principal payments on long-term debt	(32,704)	(29,679)
Interest paid	(6,231)	(1,170)
Cash received on sale of assets	907	2,533
Accounts receivable from LCRA	1,324	14,400
Payment to defease and refund debt and related issue costs	(135,000)	(411,102)
Net cash used in capital and related financing activities	(49,083)	(255,220)
Cash Flows From Investing Activities		
Sale and maturity of investment securities	15,517	405,046
Purchase of investment securities	(19,421)	(207,053)
Interest received	620	3,907
Net cash provided by (used in) investing activities	(3,284)	201,900
Net Decrease in Cash and Cash Equivalents	(4,329)	(24,650)
Cash and Cash Equivalents, Beginning of Year	26,039	50,689
Cash and Cash Equivalents, End of Year	$ 21,710	$ 26,039

LCRA Transmission Services Corporation - Segment Information
Statements of Cash Flows
(Dollars in Thousands)

	Year Ended June 30, 2004	Year Ended June 30, 2003
Reconciliation of Operating Income to Net Cash Flows Provided by Operating Activities:		
Operating income	$ 35,706	$ 30,133
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	21,432	14,537
Changes in assets and liabilities:		
Accounts receivable - trade	(18,439)	(1,197)
Inventories	(401)	-
Current liabilities	86	(1,813)
Other deferred charges and long-term liabilities	13,224	(9,840)
Net cash provided by operating activities	$ 51,608	$ 31,820
Noncash Investing Activities		
Investment market adjustments	$ (21)	$ 410
Noncash Financing for Property, Plant and Equipment Expenditures		
Transfer of net property, plant and equipment and other assets related to the contractual commitment with LCRA	$ 630	$ (3,980)
Capital assets financed through short-term payables	$ 15,579	$ 15,144

10. Restatement of Fiscal Year 2003 Financial Statements

Subsequent to the issuance of the FY 2003 financial statements, LCRA's management identified certain capital projects that had been completed in prior years but had not been depreciated or had been depreciated at an incorrect rate. As a result, the accompanying FY 2003 Balance Sheet has been restated to reflect the proper classification of these assets and an increase in accumulated depreciation and a decrease in the deferred charge, cost to be recovered from future revenues. The FY 2003 Statement of Revenues, Expenses and Changes in Equity has also been restated to reflect a decrease in depreciation expense and cost to be recovered from future revenues.

Balance Sheet
(Dollars in Thousands)

		As Previously Reported		As Restated
Assets				
Capital Assets:				
Utility plant in service	$	2,351,955	$	2,407,544
Construction work in progress	$	277,829	$	222,240
Accumulated depreciation	$	(899,315)	$	(905,487)
Costs to be recovered for future revenues	$	172,438	$	170,280
Equity				
Total Equity	$	630,627	$	622,297
Statement of Revenues, Expenses, and Changes in Equity				
Depreciation, depletion and amortization	$	72,760	$	68,509
Costs to be recovered from future revenues	$	7,202	$	1,707
Income before capital contributions	$	17,255	$	16,011
Total Equity, End of Year	$	630,627	$	622,297

The adjustments for this matter also impacted the beginning equity for FY 2003 as illustrated below:

Equity at Beginning of Period
(Dollars in Thousands)

As previously reported	$	607,975
Prior period adjustments		(7,086)
Beginning equity, as restated	$	600,889

LCRA Mission Statement

The mission of the Lower Colorado River Authority (LCRA) is to provide reliable, low-cost utility and public services in partnership with our customers and communities and to use our leadership role and environmental authority to ensure the protection and constructive use of the area's natural resources.

LCRA is a Texas conservation and reclamation district operating with no taxing authority.

We'd like your comments on LCRA's 2004 Annual Report.
Please let us know what you thought of the information or presentation, or if you need more information about LCRA and its operations.

Write us at ***annual.report@lcra.org.***

LCRA
ENERGY • WATER • COMMUNITY SERVICES

LOWER COLORADO RIVER AUTHORITY
P.O. Box 220
Austin, Texas 78767-0220
1-800-776-5272
(512) 473-3200
www.lcra.org