

January 17, 2005

To the Board of Directors
Monterey Peninsula Water Management District
Monterey, California

This letter includes comments and suggestions with respect to matters that came to our attention in connection with our audit of the financial statements of the Monterey Peninsula Water Management District for the year ended June 30, 2004. These items are offered as constructive suggestions to be considered part of the ongoing process of modifying and improving the District's practices and procedures.

CURRENT YEAR RECOMMENDATIONS:

Chart of Accounts

For the year ended June 30, 2004, the District implemented GASB Statement No. 34. Pursuant to GASB 34, the statement of activities reports expenses and revenues in a format that focuses on the cost of the District's functions. Currently, the existing chart of accounts does not track revenues and expenses by function. Although it is critical that the District maintain records for each fund as required in the governmental fund statements, it is also necessary for the District to provide information by function.

We recommend that the District review its functions/programs in conjunction with a review of its current chart of accounts and determine a feasible approach to modifying the chart of accounts to accommodate the tracking of revenues and expenses by function as well as by fund.

Compensated Absences

In accordance with GASB Interpretation No. 6, only liabilities for compensated absences that have matured, for example, as a result of employee resignations and retirements are recognized as governmental fund liabilities. The liability for unmatured compensated absences does not constitute an outflow of current financial resources and therefore, is not recognized as a governmental fund liability or expenditure. The District currently records the entire amount for vacation payable as a governmental fund liability.

We recommend that the District record the accrual for unmatured vacation liabilities along with the accrual for sick leave payable in the account group they have established for long-term debt. We further recommend that the District review the total liabilities for compensated absences at year-end to determine if any of the liability should be considered matured and would therefore, be recorded as a governmental fund liability.

January 17, 2005

To the Board of Directors
Monterey Peninsula Water Management District
Monterey, California

This letter is intended to inform the Board of Directors of Monterey Peninsula Water Management District (the District) about significant matters related to the conduct of the annual audit so that it can appropriately discharge its oversight responsibility, and that we comply with our professional responsibilities to the Board of Directors.

In addition to our report on your basic financial statements, we have provided, under separate cover, a letter dated January 17, 2005, concerning constructive suggestions to be considered as part of the ongoing process of modifying and improving the District's practices and procedures. We did not note any matters affecting the internal control conditions during our audit of the District's financial statements for the year ended June 30, 2004.

The following summarizes various matters which must be communicated to you under auditing standards generally accepted in the United States of America.

The Auditors' Responsibility Under Auditing Standards Generally Accepted in the United States of America

Our audit of the financial statements of Monterey Peninsula Water Management District for the year ended June 30, 2004 was conducted in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether caused by error, fraudulent financial reporting or misappropriation of assets. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in 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. Accordingly, the audit was designed to obtain reasonable, rather than absolute, assurance about the financial statements. We believe that our audit accomplished that objective.

Management Judgments and Accounting Estimates

Accounting estimates are an integral part of the preparation of financial statements and are based upon management's current judgment. The process used by management encompasses their knowledge and experience about past and current events and certain assumptions about future events. Management has informed us that they used all the relevant facts available to them at the time to make the best judgments about accounting estimates, and we considered this information in the scope of our audit. Estimates significant to the financial statements include the estimate of depreciation expense. The Board of Directors may wish to monitor throughout the year the process used to compute and record this accounting estimate.

Other Information in Documents Containing Audited Financial Statements

We are not aware of any other documents that contain the audited basic financial statements. If such documents were to be published, we would have a responsibility to determine that such financial information was not materially inconsistent with the audited statements of the District.

Disagreements with Management

We encountered no disagreements with management over the application of significant accounting principles, the basis for management's judgments on any significant matters, the scope of the audit or significant disclosures to be included in the financial statements.

Consultations with Other Accountants

We are not aware of any consultations management had with other accountants about accounting or auditing matters.

Major Issues Discussed with Management Prior to Retention

No major issues were discussed with management prior to our retention to perform the aforementioned audit.

Difficulties Encountered in Performing the Audit

We did not encounter any difficulties in dealing with management relating to the performance of the audit.

Closing

We will be pleased to respond to any questions you have about the foregoing. We appreciate the opportunity to continue to be of service to Monterey Peninsula Water Management District.

This report is intended solely for the information and use of the Board of Directors and management and is not intended to be and should not be used by anyone other than the specified parties.

HAYASHI & WAYLAND
ACCOUNTING & CONSULTING

By _____
Cecil Robbins, C.P.A.

**MONTEREY PENINSULA WATER
MANAGEMENT DISTRICT**

FINANCIAL STATEMENTS

**FOR THE YEAR ENDED
JUNE 30, 2004**

AND INDEPENDENT AUDITORS' REPORT

MONTEREY PENINSULA WATER MANAGEMENT DISTRICT

Board of Directors

June 30, 2004

<u>Member</u>	<u>Office</u>	<u>Representative</u>
Alvin Edwards	Chair	Division 1
Judi Lehman	Director	Division 2
Kristi Markey	Director	Division 3
Michelle Knight	Director	Division 4
Larry Foy	Vice-Chair	Division 5
David Pendergrass	Director	Mayoral
David Potter	Director	Monterey County Board of Supervisors

The Management's Discussion and Analysis on pages 4 through 11 and the Budgetary Comparison Schedules on pages 42 and 45 are not a required part of the basic financial statements, but are 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 supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information listed in the table of contents is presented for purposes of additional analysis and is not a required part of the basic financial statements of the ***Monterey Peninsula Water Management District***. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly we express no opinion on it.

January 17, 2005

MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

OVERVIEW OF THE FINANCIAL STATEMENTS (CONTINUED)

The District's financial statements are prepared on an accrual basis in conformity with accounting principles generally accepted for the United States of America (GAAP) as applied to government units. Under this basis of accounting, revenues are recognized in the period in which they are earned, expenses are recognized in the period in which they are incurred, and depreciation of assets is recognized in the Statement of Revenues, Expenses and Changes in Fund Balances. All assets and liabilities associated with the operation of the District are included in the Statement of Net Assets.

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

The *statement of net assets* presents information on all of the District's assets and liabilities, with the difference between the two reported as net assets. Over time, increases and decreases in net assets may serve as a useful indicator of whether the financial position of the District is improving or deteriorating. The statement of net assets combines and consolidates governmental funds' current financial resources (short-term spendable resources) with capital assets and long-term obligations.

The *statement of activities* presents information showing how the District's net assets changed during the most recent fiscal year. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes).

The government-wide financial statements include all the governmental activities of the District. The governmental activities of the District include conservation, mitigation and water supply. The business-type activity includes the water reclamation project.

The government-wide financial statements can be found on pages 12 and 13 of this report.

Fund Financial Statements – A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The fund financial statements provide detail information about the most significant funds, not the District as a whole. The District, like other special districts, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. The District's funds are segregated into two categories: governmental funds and proprietary funds. Fund financial statements report essentially the same functions as those reported in the government-wide financial statements. However, unlike the government-wide financial statements, fund financial statements focus on *near-term inflows and outflows of spendable resources*, as well as on *balances of spendable resources* available at the end of the fiscal year.

MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

GOVERNMENT-WIDE FINANCIAL ANALYSIS (CONTINUED)

Net Assets

This Statement of Net Assets, the difference between the District's assets and liabilities, is one way to measure the District's financial health or position. Net assets are reported in two categories: Invested in capital assets, net of related debt and Unrestricted. Unrestricted assets are funds available for future operational and capital expenditures.

Table A-1

Summary of Net Assets
Governmental Activities

	<u>2004</u>
<u>Assets</u>	
Current Assets	\$3,792,249
Prepaid Expenses and Deposits	25,015
Capital Assets - Net	<u>2,800,158</u>
Total Assets	<u>6,617,422</u>
 <u>Liabilities</u>	
Current Liabilities	385,238
Long-Term Liabilities	<u>311,816</u>
Total Liabilities	<u>697,054</u>
 <u>Net Assets</u>	
Invested in Capital Assets, Net of Related Debt	2,800,158
Unrestricted	<u>3,120,210</u>
Total Net Assets	<u>\$5,920,368</u>

The District's assets exceeded its liabilities by approximately \$5.9 million at the end of the current fiscal year. The District's total net assets at June 30, 2004 of approximately \$5.9 million decreased by approximately 15.0% since June 30, 2003.

The activities decreased the District's net assets by \$1.1 million during the current fiscal year, due primarily to expenses exceeding revenues. Charges for services and grants were not adequate to cover the cost of providing services; therefore the District is required to rely heavily on property tax to provide those services.

MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

GOVERNMENT-WIDE FINANCIAL ANALYSIS (CONTINUED)

- The planned use of previously accumulated operating reserves of approximately \$915,000 was the major contributor to the decrease
- Increased user fee revenue of just over \$300,000 mitigated the decrease
- Decreased connection charge revenue of about \$165,000 contributed to the decrease
- Reduced project reimbursement revenue of nearly \$165,000 added to the decrease
- Personnel cost increases of over \$200,000 contributed to the decrease
- Increased project expenditures related to development of long-term water supplies added more than \$100,000 of the decrease

CAPITAL ASSETS

The District's capital assets, net of accumulated depreciation, at June 30, 2004 totaled \$2,800,158 as shown on Table A-3 below. This amount represents a net increase, including additions and disposals, net of depreciation, of approximately \$2,258,500 or 24% over June 30, 2003. Most of the increase is attributable to the capitalization of the District's Santa Margarita aquifer storage and recovery well.

Table A-3

Capital Assets
(Net of Depreciation)

	<u>2004</u>
Office Equipment	\$44,510
Computer Equipment	170,995
Operating Equipment	603
Transportation Equipment	94,966
Project Equipment	8,908
Telephone System	6,578
Building and Improvements	1,680,255
Monitoring Stations	11,123
Injection Wells	678,813
Fish Rearing Facility	<u>103,407</u>
Total	<u>\$2,800,158</u>

MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET AND RATES

In developing the fiscal year 2004-2005 budget, the staff and management had to consider a number of factors that would impact the District's economy and finances. As part of the State budget process, agreements were being considered by the Governor, the Legislature, and the local government representatives that would have a negative impact on the District's revenue from property taxes. Therefore, projected property tax revenues were decreased accordingly resulting in an overall decrease in projected operating revenues. While operating expenditures were also estimated to decrease (project expenditures in particular), they were expected to continue to exceed operating revenues. Rather than to increase the User Fee, which is the District's largest and most fluid revenue source, the Board of Directors opted to continue to use of operating reserves to balance the budget.

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of the District's finances for all those with an interest. Questions concerning any of the information provided in this report or requests for additional financial information should be directed to Rick Dickhaut, Administrative Services Manager/Chief Financial Officer at (831) 658-5614.

MONTEREY PENINSULA WATER MANAGEMENT DISTRICT
STATEMENT OF NET ASSETS
JUNE 30, 2004

	<u>Governmental Activities</u>	<u>Business-Type Activities</u>	<u>Total</u>
ASSETS:			
Cash and cash equivalents	\$ 11,439	\$ 825,273	\$ 836,712
Investments	3,420,233	—	3,420,233
Receivables, net	360,577	347,248	707,825
Prepaid expenses and deposits	25,015	—	25,015
Restricted reserves:			
Cash	—	51,259	51,259
Investments	—	514,199	514,199
Capital assets, net:			
Water resale rights	—	21,150,205	21,150,205
Nondepreciable	—	725,149	725,149
Depreciable	<u>2,800,158</u>	<u>—</u>	<u>2,800,158</u>
Total assets	<u>6,617,422</u>	<u>23,613,333</u>	<u>30,230,755</u>
LIABILITIES:			
Accounts payable	113,133	580,202	693,335
Accrued liabilities	87,460	—	87,460
Interest payable	—	28,992	28,992
Long-term debt:			
Due within one year	184,645	1,000,000	1,184,645
Due in more than one year	<u>311,816</u>	<u>31,500,000</u>	<u>31,811,816</u>
Total liabilities	<u>697,054</u>	<u>33,109,194</u>	<u>33,806,248</u>
NET ASSETS:			
Invested in capital assets, net of related debt	2,800,158	(4,769,797)	(1,969,639)
Restricted for debt service	—	31,224	31,224
Unrestricted (deficit)	<u>3,120,210</u>	<u>(4,757,288)</u>	<u>(1,637,078)</u>
Total net assets (deficit)	<u>\$ 5,920,368</u>	<u>\$ (9,495,861)</u>	<u>\$ (3,575,493)</u>

See Notes to Basic Financial Statements.

MONTEREY PENINSULA WATER MANAGEMENT DISTRICT
BALANCE SHEET – GOVERNMENTAL FUNDS
JUNE 30, 2004

	<u>Capital Projects</u>	<u>Conservation</u>	<u>Mitigation</u>	<u>Total</u>
ASSETS:				
Cash and cash equivalents	\$ 11,439	\$ –	\$ –	\$ 11,439
Investments	3,420,233	–	–	3,420,233
Receivables, net	65,363	46,201	249,013	360,577
Prepaid expenses and deposits	24,205	–	810	25,015
Due from other funds	–	394,313	2,484,137	2,878,450
	<u>3,521,240</u>	<u>440,514</u>	<u>2,733,960</u>	<u>6,695,714</u>
Total assets				
LIABILITIES AND FUND BALANCES:				
Liabilities:				
Accounts payable	63,058	22,428	27,647	113,133
Accrued liabilities	43,207	5,934	38,319	87,460
Due to other funds	2,878,450	–	–	2,878,450
Deferred revenue	3,625	477	364	4,466
	<u>2,988,340</u>	<u>28,839</u>	<u>66,330</u>	<u>3,083,509</u>
Total liabilities				
Fund balances:				
Reserved for prepaid expenses	22,539	–	360	22,899
Unreserved, designated:				
Insurance/litigation	171,354	11,906	66,740	250,000
Capital equipment	30,553	21,750	63,280	115,583
Flood/drought emergencies	–	–	613,944	613,944
Unreserved, undesignated	308,454	378,019	1,923,306	2,609,779
	<u>532,900</u>	<u>411,675</u>	<u>2,667,630</u>	<u>3,612,205</u>
Total fund balances				
Total liabilities and fund balances	<u>\$ 3,521,240</u>	<u>\$ 440,514</u>	<u>\$ 2,733,960</u>	

Amounts reported in the statement of net assets are different because:

Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds	2,800,158
Other assets are not available to pay for current-period expenditures and therefore are deferred in the funds	4,466
Long-term liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds	<u>(496,461)</u>
NET ASSETS OF GOVERNMENTAL ACTIVITIES	<u>\$ 5,920,368</u>

See Notes to Basic Financial Statements.

**MONTEREY PENINSULA WATER MANAGEMENT DISTRICT
RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS TO
THE STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2004**

NET CHANGE IN FUND BALANCES	\$ (913,239)
Amounts reported in the statement of activities are different because:	
Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount by which depreciation exceeded capital outlays in the current period.	(146,652)
The net effect of other miscellaneous transactions involving capital assets (i.e., sales, trade-ins, and donations) is to decrease net assets.	(16,150)
Revenues in the statement of activities that do not provide current financial resources are not reported as revenue in the funds.	4,466
Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds.	<u>(38,879)</u>
CHANGE IN NET ASSETS	<u>\$ (1,110,454)</u>

See Notes to Basic Financial Statements.

MONTEREY PENINSULA WATER MANAGEMENT DISTRICT
STATEMENT OF REVENUES, EXPENSES
AND CHANGES IN NET ASSETS – PROPRIETARY FUND
FOR THE YEAR ENDED JUNE 30, 2004

	Water
OPERATING REVENUES –	
Water sales	\$ 2,158,691
Total operating revenues	2,158,691
OPERATING EXPENSES:	
Plant costs	432,773
Distribution costs	76,850
General and administration	73,666
Potable water	776,286
Total operating expenses	1,359,575
Operating income before amortization	799,116
Less amortization	691,726
Operating income	107,390
NON-OPERATING REVENUES	
(EXPENSES):	
Investment earnings	3,873
Interest expense on certificates of participation	(326,588)
Certificates of participation carrying costs	(476,842)
Subsidy – Pebble Beach Company	1,495,851
Total non-operating revenues (expenses)	696,294
CHANGE IN NET ASSETS	803,684
NET ASSETS (DEFICIT) –	
BEGINNING OF YEAR	(10,299,545)
NET ASSETS (DEFICIT) –	
END OF YEAR	\$ (9,495,861)

See Notes to Financial Statements.

MONTEREY PENINSULA WATER MANAGEMENT DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2004

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Abbreviations Used:

Cal-Am	California-American Water Company
CAWD	Carmel Area Wastewater District
COP	Certificates of participation
O&M	Operations and maintenance
PBCo.	Pebble Beach Company
PBCSD	Pebble Beach Community Services District
Project	CAWD/PBCSD Wastewater Reclamation Project

Description of the Reporting Entity:

Accounting principles generally accepted in the United States of America require that the reporting entity include (1) the primary government, (2) organizations for which the primary government is financially accountable and (3) other organizations for which the nature and significance of their relationship with the primary government are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete. The criteria provided in Government Accounting Standards Board Statement No. 14 have been considered and there are no agencies or entities which should be presented with the District.

The Monterey Peninsula Water Management District was created by Chapter 527, Statutes of 1977 (Assembly Bill No. 1329) of the California Legislature, on September 2, 1977. The District was created to provide integrated management of ground and surface water supplies, and to exercise regulatory control over the collection, storage, distribution, and delivery of water and wastewater within its jurisdiction including, but not limited to, such functions as management and regulation of the use, reuse, reclamation and conservation of water, and bond financing of public works projects. Water service is principally supplied by other entities, but the District has the power to acquire public or private water systems. The District also has the power to levy and collect real estate taxes. Operations were commenced during the fiscal year beginning July 1, 1978.

The District has a seven-member board of directors. Five directors are elected every four years on a staggered basis. Of the other two directors, one must be a member of the Monterey County Board of Supervisors and the other must be a chief executive officer, mayor, or member of the governing body of a city member unit. The Board of Directors has continuing oversight responsibility for the District.

The geographic jurisdiction of the District approximates the Monterey Peninsula and the Carmel River watershed including all of the cities (except Marina) and the unincorporated communities therein.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Statement No. 37 – The District adopted the provisions of GASB Statement No. 37, *Basic Financial Statements and Management's Discussion and Analysis – for State and Local Governments: Omnibus*. This statement clarifies certain provisions of Statement No. 34, for more consistent application and modifies others to meet changing requirements.

Statement No. 38 – The District adopted the provisions of GASB No. 38, *Certain Financial Statement Note Disclosures*. This statement modifies, establishes and rescinds certain financial statement disclosure requirements. Accordingly, certain footnote disclosures have been revised to conform to the provisions of GASB Statement No. 38.

Statement No. 40 – The District adopted the provisions of GASB No. 40, *Deposit and Investment Risk Disclosures*, an amendment of GASB Statement No. 3, *Deposits with Financial Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements*. The Board reconsidered the disclosures required by Statement No. 3 and have modified or eliminated portions of that Statement.

Interpretation No. 6 – The District adopted the provisions of GASB Interpretation No. 6, *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements*. This interpretation clarifies the application of standards for modified accrual recognition of certain liabilities and expenditures in areas where differences have arisen, or potentially could arise, in interpretation and practice. The interpretation impacts the fund level financial statements required by GASB Statement No. 34, but has no direct impact on the government-wide financial statements. Accordingly, the District has not recognized the current portion of certain liabilities and related expenditures in the governmental fund financial statements for amounts not considered to be due and payable as of June 30, 2004.

The adoption of the aforementioned GASB Statements required the District to restate, for purposes of preparing a statement of revenues, expenses, and changes in fund balances and statement of activities, balances previously reported as fund balances in its financial statements for the year ended June 30 2003. The effect of these restatements on net asset balances as of July 1, 2003 is presented below:

- The District has historically capitalized all capital assets, excluding infrastructure. The District also has not recorded annual depreciation expense or the related accumulated depreciation. As of July 1, 2003, the District recorded infrastructure assets of \$768,316 and recognized \$1,838,851 in accumulated depreciation on all governmental activity assets that had not previously been recognized.
- Certain liabilities related to compensated absences had previously been recognized within the District's governmental funds. Upon implementation of GASB Interpretation No.6 these items do not meet the definition of a governmental fund liability. Therefore, the amount accrued of \$172,711 for compensated absences has been removed from fund liabilities and has been added to the beginning fund balance.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

The government-wide focus is more on the sustainability of the District as an entity and the change in aggregate financial position resulting from the activities of the fiscal period. The focus of the fund financial statements is on the major individual funds. Each presentation provides valuable information that can be analyzed and compared to enhance the usefulness of the information.

Measurement Focus and Basis of Accounting – The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements have been met.

Government fund level financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collected within the current period or soon enough thereafter to pay liabilities of the current period.

Property taxes that have been levied and are due on or before year-end are recognized as revenue if they have been collected within ninety days after year-end. User fees due for the current year are considered available and are, therefore, recognized as revenues even though a portion of the user fees may be collected in the subsequent year. Connection charges and permit fees are considered to be measurable when they have been collected and are recognized as revenue at that time. Investment earnings are recorded as earned since they are measurable and available.

Expenditures are recorded when the liability is incurred, except for interest on long-term debt and compensated absences, which are recorded when paid.

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

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from producing and delivering water. Operating expenses include the cost of sales, general and administrative expenses, and amortization of capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Under GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*, the District has elected to apply all applicable GASB pronouncements as well as Financial Accounting Standards Board (FASB) pronouncements and Accounting Principles Board (APB) opinions issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements. Investment earnings are accrued. Earned but unbilled revenues are accrued and reported in the financial statements.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Pooled Cash – Cash accounts (Reclamation) which essentially operate as demand deposit accounts are maintained by the Monterey County Treasurer’s Office. Available cash balances are controlled and invested by the County Treasurer in pooled investment funds in order to provide safety, liquidity and high investment returns for all funds. Interest earnings from these funds are generally credited to the District’s account on a quarterly basis.

The Monterey County Treasurer’s Investment policy is in compliance with Section 53635 of the Government Code of the State of California which permits investments in certain securities and participation in certain investment trading techniques or strategies.

Resolution 83–17, adopted September 12, 1983, authorized investment of the District’s monies with the State Treasurer for deposit in the Local District Investment Fund (LAIF). Money in the fund is invested by the State Treasurer to realize the maximum return consistent with prudent treasury management. All earnings of the fund, less a reimbursement of management costs incurred not to exceed one quarter of one percent of earnings, are distributed to the contributing agencies in their relative shares each quarter. The balances of funds in LAIF are stated at market value.

Investments – The District Board has also authorized the investment of District monies in an asset management account at Wells Fargo Bank. The investment at Wells Fargo Bank is recorded at market value.

The types of investments the District may purchase are not limited by legal or contractual provisions, but the Board has established policies on investments and has so directed their investment managers.

Receivables – Receivables are accounted for using the allowance method. The allowance for doubtful accounts is zero at June 30, 2004.

Prepaid Expenses – Prepaid expenses are capitalized and amortized ratably over the period of benefit.

Capital Assets – Property, facilities, and equipment purchased or acquired is carried at historical cost or estimated historical cost. Contributed fixed assets are recorded at estimated fair market value at the time received. Capital assets are defined by the District as assets with an initial, individual cost of more than \$500 and an estimated useful life in excess of one year.

Property, facilities, and equipment of the District is depreciated using the straight–line method over the following estimated useful lives:

Equipment	3 to 20 Years
Building and improvements	5 to 39 Years
Monitoring stations	5 to 10 Years
Wells	30 to 40 Years
Fish rearing facility	5 to 40 Years
Leasehold improvements	10 to 40 Years

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Permit Fees – Permit fee revenue is recorded as permits are issued. The District is required to refund permit fees if the permit is not used or to grant an extension of time upon a reasonable request. If a refund is issued, the refunded party also relinquishes any water rights associated with the permit. It is the District’s policy to record such refunds as they become payable.

Use of Restricted Resources – When both restricted and unrestricted resources are available for use, it is the District’s policy to use restricted resources first, then unrestricted resources, as they are needed.

Use of Estimates – The preparation of the financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported. Actual results are not expected to differ from those estimates.

Reconciliation of Government-Wide and Fund Financial Statements – Explanation of Certain Differences Between the Governmental Fund Balance Sheet and the Government-Wide Statement of Net Assets – The governmental fund balance sheet includes a reconciliation between fund balance – total governmental funds and net assets – governmental activities as reported in the government-wide statement of net assets. One element of that reconciliation explains the “long-term liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds.” The details of this \$496,461 difference are as follows:

Compensated absences	\$ 496,461
Net adjustment to reduce fund balance – total governmental funds to arrive at net assets – governmental activities	<u>\$ 496,461</u>

Explanation of Certain Differences Between the Governmental Fund Statement of Revenues, Expenditures, and Changes in Fund Balances and the Government-Wide Statement of Activities – The governmental fund statement of revenues, expenditures, and changes in fund balances include a reconciliation between net changes in fund balances – total governmental funds and changes in net assets of governmental activities as reported in the government-wide statement of activities. One element of that reconciliation explains, “Governmental funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is capitalized and allocated over their estimated useful lives and reported as depreciation expense.” The details of the \$(146,652) difference are as follows:

Capital outlay	\$ 110,848
Depreciation expense	<u>(257,500)</u>
Net adjustment to increase net changes in fund balances total governmental funds to arrive at changes in net assets of governmental activities	<u>\$ (146,652)</u>

NOTE 2. THE CAWD/PBCSD WASTEWATER RECLAMATION PROJECT (Continued)

The activities of the Project are overseen by a five-member management committee containing two representatives from the CAWD board, two from the PBCSD board and one from PBCo.

The Reclamation Management Committee has proposed a plan to improve and expand current Project facilities. The planned improvements are intended to improve the quality of the reclaimed water by reducing the amount of sodium that remains after treatment. The expansion will utilize the Forest Lake reservoir in Pebble Beach, which will provide approximately 420 acre-feet (AF) of reclaimed water storage. The additional storage is expected to improve the performance of the Project, by meeting peak water demand in the summer months. The cost of the Phase II improvements and expansion is estimated to be \$22 million. The management committee is currently working with the District on arranging financing to pay for the work.

NOTE 3. CASH AND INVESTMENTS

Cash and Cash Equivalents – Balances in cash and cash equivalents consist of bank accounts insured by the Federal Depository Insurance Corporation (FDIC), Securities Investment Protection Corporation (SIPC), and other insurance and unsecured and uncollateralized deposits in the California State Treasurer's Investment Pool, known as the Local District Investment Fund.

Restricted Reserves - The remaining proceeds of the \$33,900,000 in Certificates of Participation issued for the Project were deposited in various restricted trust and reserve accounts as required by the terms of the issuance.

Custodial Credit Risk—Deposits – Custodial credit risk is the risk that in the event of a bank failure, the District's deposits may not be returned to it. The District has a deposit policy that complies with California Government Code Section 53638 (Public Deposit Act). As of June 30, 2004, \$563,441 of the District's bank balances of \$1,200,622 was exposed to custodial credit risk as uninsured and collateralized by the pledging bank's trust department not in the District's name.

The difference between bank balances and the carrying amounts (book value) represents outstanding checks and deposits in transit.

NOTE 3. CASH AND INVESTMENTS (Continued)

Governmental activities:	
US Government obligations	\$ 2,922,085
Liquid assets	95,640
Local Agency Investment Fund	<u>402,508</u>
Subtotal Governmental activities	<u>3,420,233</u>
Business-type activities:	
US Government obligations	283,394
Corporate obligations	198,070
Liquid assets	<u>32,735</u>
	514,199
Less restricted reserves	<u>514,199</u>
Subtotal Business-type activities	<u>—</u>
Total Investments	<u>\$ 3,420,233</u>

NOTE 4. RECEIVABLES

Receivables, net of allowances for uncollectibles (estimated to be \$—), consist of the following at June 30, 2004:

	<u>Capital Projects</u>	<u>Conservation</u>	<u>Mitigation</u>	<u>Total</u>
Governmental activities:				
Project reimbursements (Cal – Am)	\$ 18,908	\$ —	\$ 9,700	\$ 28,608
User fees	—	43,829	237,505	281,334
Taxes	18,022	2,372	1,808	22,202
Interest	24,782	—	—	24,782
Other	<u>3,651</u>	<u>—</u>	<u>—</u>	<u>3,651</u>
Total Governmental activities	<u>\$ 65,363</u>	<u>\$ 46,201</u>	<u>\$ 249,013</u>	<u>360,577</u>
Business-type activities:				
Water sales				180,797
Interest				843
Affiliates (Reclamation)				149,983
Other				<u>15,625</u>
Total Business-type activities				<u>347,248</u>
TOTAL				<u>\$ 707,825</u>

NOTE 5. CHANGES IN CAPITAL ASSETS (Continued)

	<u>BALANCE BEGINNING OF YEAR</u>	<u>CURRENT ADDITIONS</u>	<u>DELETIONS</u>	<u>BALANCE END OF YEAR</u>
Business-type activities:				
Nondepreciable assets:				
Construction in progress	\$ 146,541	\$ 578,608	\$ —	\$ 725,149
Water resale rights	27,804,708	20,524	—	27,825,232
Less accumulated amortization for:				
Water resale rights	<u>5,983,301</u>	<u>691,726</u>	<u>—</u>	<u>6,675,027</u>
Total water resale rights, net	<u>21,821,407</u>	<u>(671,202)</u>	<u>—</u>	<u>21,150,205</u>
Total business type activities capital assets, net	<u>21,967,948</u>	<u>(92,594)</u>	<u>—</u>	<u>21,875,354</u>
Total capital assets, net	<u>\$ 24,930,909</u>	<u>\$ (239,246)</u>	<u>\$ 16,151</u>	<u>\$ 24,675,512</u>

Depreciation expense was charged to functions/programs of the District as follows:

Conservation	\$ 40,995
Mitigation	144,304
Water supply	<u>72,201</u>
Total depreciation expense	<u>\$ 257,500</u>

NOTE 6. INTERFUND RECEIVABLES AND PAYABLES

At June 30, 2004 interfund receivables and payables consist of :

<u>Fund</u>	<u>Interfund Receivable</u>	<u>Interfund Payable</u>
Capital projects	\$ —	\$ 2,878,450
Conservation	394,313	—
Mitigation	<u>2,484,137</u>	<u>—</u>
	<u>\$ 2,878,450</u>	<u>\$ 2,878,450</u>

Interfund payables and receivables arise primarily from the Capital Projects Fund cash accounts receiving all revenue and paying all expenditures. The Proprietary Fund also collects user fees which are remitted to the other funds periodically. Any fund transfers made between accounts are reflected in the above balances as well as in the respective fund balances.

NOTE 8. LONG-TERM DEBT

The Variable Rate Demand Certificates of Participation – Wastewater Reclamation Project Series 1992 (COPs) were issued in December 1992 in the amount of \$33,900,000 by the District, and will mature on July 1, 2022. The COPs are in the minimum denomination of \$100,000 or any integral multiple thereof or, during any reset period or on or after the conversion date, in the minimum denomination of \$5,000 or any integral multiple thereof. The COPs bear interest at a variable rate unless the interest rate is converted to a reset rate for a reset period or to a fixed rate to the maturity of the COPs. The variable rate is the rate necessary to produce a par bid if the COPs were sold on the day the rate is computed. The COPs accrued interest at an initial rate of 2.30% per annum at issuance and, thereafter, accrue at a variable rate determined as provided in the Official Statement of the COPs issuance.

Restricted Reserves - As a requirement of this issuance two reserve funds were established. A Renewal and Replacement Reserve was established to pay for future major repairs and an Operations and Maintenance Reserve was established to cover future operating deficits. Each of these reserves is held in a segregated account restricted for its intended purposes. At June 30, 2004 the balances in these funds were as follows:

Renewal and Replacement Reserve	\$ 224,274
Operations and Maintenance Reserve	<u>289,925</u>
Total	<u>\$ 514,199</u>

Security for Repayment – The Project assets have not been pledged to secure payment of the COPs, nor have any other assets of the District. However, pursuant to the Water Purchase Agreement, all net operating revenues from the operations of the Project are irrevocably pledged by the District to the payment of COPs. This pledge constitutes a first lien on the net operating revenues and, subject to application of amounts on deposit therein as permitted in the Water Purchase Agreement, for the payment of the COPs in accordance with the terms of the Water Purchase Agreement and of the Trust Agreement. Notwithstanding the foregoing, the District may at any time issue obligations or execute contracts which are secured by a lien subordinate to the pledge of net operating revenues created under the Water Purchase Agreement. The Bond Letter of Credit also guarantees the COPs.

Long-term debt activity for the year ended June 30, 2004 is as follows:

	<u>2003</u>	<u>Additions</u>	<u>Reductions</u>	<u>2004</u>	<u>Due Within One Year</u>
COPs	\$ 33,500,000	\$ -	\$ 1,000,000	\$ 32,500,000	\$ 1,000,000
Compensated absences	<u>457,582</u>	<u>38,879</u>	<u>-</u>	<u>496,461</u>	<u>184,645</u>
	<u>\$ 33,957,582</u>	<u>\$ 38,879</u>	<u>\$ 1,000,000</u>	<u>\$ 32,996,461</u>	<u>\$ 1,184,645</u>

In prior years, the capital projects, conservation and mitigation funds have been used to liquidate compensated absences.

NOTE 10. JOINT POWERS AGREEMENT (Continued)

Condensed financial information of the SDRMA as of and for the year ended June 30, 2003 (the most current information available) is as follows:

Total assets	\$ 13,896,021
Total liabilities	<u>3,738,586</u>
Risk margin (SDRMA equity)	<u>\$ 10,157,435</u>
Total revenues	\$ 4,983,267
Total expenses	<u>4,324,400</u>
Net income	<u>\$ 658,867</u>

The SDRMA did not have long-term debt outstanding at June 30, 2003, other than claims liabilities and capital lease obligations. The District's share of year-end assets, liabilities and risk margin has not been calculated by the SDRMA.

NOTE 11. DEFERRED COMPENSATION PLAN

The District has a deferred compensation plan for its eligible employees wherein amounts earned by the employees are paid at a future date. This plan meets the requirements of Internal Revenue Code Section 457. All full-time, regular employees are permitted to participate in the plan beginning on the day of hire.

The employee may elect to make tax deferred contributions up to the limits established by the Internal Revenue Service for this type of plan. The employee is 100% vested in his contributions from the first date of participation. The plan does not provide for district contributions. The participant has a choice of investment options.

The plan is administered by ICMA Retirement Corporation (International City Management Association). The assets of the plan are held in trust, with the District serving as trustee. The plan assets held in the ICMA Retirement Trust are held for the exclusive benefit of the plan participants and their beneficiaries. The assets shall not be diverted to any other purpose. The plan does not permit loans.

Government Accounting Standards Board Statement (GASB) 32 states that if a fiduciary relationship does not exist between the governmental entity and the Section 457 Deferred compensation plan, the governmental entity should not report the assets of the plan in its financial statements.

The District believes, and the auditors concur, that, since it does not provide investment advice or administer the plan, it does not maintain a fiduciary relationship with the plan. Therefore, the District does not report the plan assets in its financial statements.

NOTE 14. COMMITMENTS

Pipeline Cathodic Protection – The Project awarded a contract on May 28, 2004, in the amount of \$50,000, for engineering, and another contract on May 28, 2004, in the amount of \$103,000, for construction of a project to reduce corrosion potential and extend the useful life of the steel reclaimed water pipeline. Work should be completed on both contracts in December 2004. The amount outstanding on the engineering project is \$5,210 and the full contract amount is outstanding on the construction project as of June 30, 2004.

NOTE 15. BUILDING ACQUISITION

The District purchased a building at 5 Harris Court in Ryan Ranch Office Park for approximately \$1.6 million. The total costs to purchase the land, building, tenant improvements, interior design fee, furnishings and equipment were approximately \$1.9 million. The District purchased the building from monies available in the Mitigation and Capital Projects Funds. The District plans to repay the funds over a term of fifteen years, with interest at 5.35%.

**MONTEREY PENINSULA WATER MANAGEMENT DISTRICT
PENSION FUNDING INFORMATION
FOR THE YEAR ENDED JUNE 30, 2004**

The funded status of the Plan for the actuarial valuations performed as of June 30, 2000 through June 30, 2002 are as follows:

Required Supplementary Information

Actuarial Valuation Date	(A) Actuarial Asset Value	(B) Entry Age Actuarial Accrued Liability	(C) Unfunded Actuarial Accrued Liability/ (Excess Assets) [(B)-(A)]	(D) Funded Ratio [(A)/(B)]	(E) Covered Payroll	(F) Unfunded Actuarial Liability/ (Excess Assets) Percentage of Covered Payroll {[(B)-(A)/(E)]}
06/30/00	\$ 4,052,165	\$ 3,043,909	\$ (1,008,256)	133.1%	\$ 1,357,454	(74.3)%
06/30/01	\$ 4,319,526	\$ 3,470,469	\$ (849,057)	124.5%	\$ 1,447,376	(58.7)%
06/30/02	\$ 4,225,552	\$ 4,000,876	\$ (224,676)	105.6%	\$ 1,627,374	(13.8)%

MONTEREY PENINSULA WATER MANAGEMENT DISTRICT
SCHEDULE OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCES, BUDGET AND ACTUAL – CONSERVATION
FOR THE YEAR ENDED JUNE 30, 2004

	Budgeted Amounts		Actual Amounts	Variance With Final Budget
	Original	Final		
REVENUES:				
Property taxes	\$ 104,700	\$ 104,700	\$ 104,792	\$ 92
User fees	299,100	299,100	336,283	37,183
Connection charges, net of refunds \$(86,501)	-	-	-	-
Permit fees	90,000	90,000	106,600	16,600
Project reimbursements	25,000	25,000		(25,000)
Investment income	25,600	25,700	6,407	(19,293)
Legal fee reimbursements	17,000	17,000	18,287	1,287
Recording fees	11,000	11,000	12,177	1,177
Miscellaneous	-	-	-	-
Total revenues	<u>572,400</u>	<u>572,500</u>	<u>584,546</u>	<u>12,046</u>
EXPENDITURES:				
Personnel:				
Salaries	148,200	148,200	142,132	6,068
Employee benefits and other personnel	59,100	59,100	56,089	3,011
Services and supplies:				
Project expenditures	551,800	426,800	122,293	304,507
Operating expenditures	56,700	54,500	48,650	5,850
Professional fees	20,200	20,200	41,255	(21,055)
Capital outlay	10,900	14,500	20,922	(6,422)
Total expenditures	<u>846,900</u>	<u>723,300</u>	<u>431,341</u>	<u>291,959</u>
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	<u>(274,500)</u>	<u>(150,800)</u>	<u>153,205</u>	<u>304,005</u>
OTHER FINANCING SOURCES (USES):				
Proceeds from sale of capital assets	-	-	-	-
Transfers in	-	-	-	-
Transfers out	-	-	(500,000)	(500,000)
Total other financing sources (uses)	<u>-</u>	<u>-</u>	<u>(500,000)</u>	<u>(500,000)</u>
NET CHANGE IN FUND BALANCES	<u>(274,500)</u>	<u>(150,800)</u>	<u>(346,795)</u>	<u>(195,995)</u>
FUND BALANCES – BEGINNING OF YEAR (RESTATED)	<u>615,242</u>	<u>745,204</u>	<u>758,470</u>	<u>13,266</u>
FUND BALANCES – END OF YEAR	<u>\$ 340,742</u>	<u>\$ 594,404</u>	<u>\$ 411,675</u>	<u>\$ (182,729)</u>

See Notes to Required Supplementary Information.

MONTEREY PENINSULA WATER MANAGEMENT DISTRICT
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION
FOR THE YEAR ENDED JUNE 30, 2004

NOTE 1. BUDGETARY DATA

The District adopts an annual legal budget, which covers the Capital Projects Fund (which acts as the District's general fund), Conservation Fund, and Mitigation Fund. All appropriations lapse at fiscal year end and then are rebudgeted for the coming fiscal year. Encumbrance accounting is not used. The budgets are prepared on the modified accrual basis of accounting, which is consistent with generally accepted accounting principles.

A mid-year budget review is performed and the budget is amended and adopted by the board of directors. The District must approve additional appropriations or interfund transfers not included in the amended budget resolution.

Per *GASB Statement No. 34*, only the general fund and major special revenue funds budgets are to be presented in required supplementary information.

**MONTEREY PENINSULA WATER MANAGEMENT DISTRICT
PROJECT EXPENDITURES – BUDGET AND ACTUAL
CAPITAL PROJECTS
FOR THE YEAR ENDED JUNE 30, 2004**

	<u>Budget</u>	<u>Actual</u>	Variance Favorable (Unfavorable)
New wells	\$ 1,127,400	\$ 930,591	\$ 196,809
CEQA	10,000	143,535	(133,535)
District reporting	25,760	19,870	5,890
Operations modeling	6,000	6,000	–
Hydrologic monitoring	17,200	10,967	6,233
Groundwater quality	9,100	7,578	1,522
Groundwater monitoring	54,500	24,379	30,121
Water rights	6,000	10,797	(4,797)
Ordinance enforcement	–	250	(250)
Project reserve	240	–	240
	<u> </u>	<u> </u>	<u> </u>
Total project expenditures	<u>\$ 1,256,200</u>	<u>\$ 1,153,967</u>	<u>\$ 102,233</u>

MONTEREY PENINSULA WATER MANAGEMENT DISTRICT
PROJECT EXPENDITURES – BUDGET AND ACTUAL
MITIGATION
FOR THE YEAR ENDED JUNE 30, 2004

	<u>Budget</u>	<u>Actual</u>	<u>Variance Favorable (Unfavorable)</u>
Fish	\$ 190,900	\$ 142,609	\$ 48,291
Toilet replacement refund program	150,000	22,489	127,511
Riparian projects	72,000	19,390	52,610
District reporting	25,200	15,963	9,237
Erosion control project	12,500	–	12,500
Irrigation	13,500	14,996	(1,496)
Hydrologic monitoring	8,400	2,708	5,692
New wells	–	1,236	(1,236)
Lagoon	1,500	208	1,292
Carmel Valley water quality	1,800	157	1,643
Laguna Seca	4,300	699	3,601
CV large woody debris assessment	–	–	–
Ordinance enforcement	1,800	250	1,550
Project reserve	300	–	300
	<u>\$ 482,200</u>	<u>\$ 220,705</u>	<u>\$ 261,495</u>
Total project expenditures	<u>\$ 482,200</u>	<u>\$ 220,705</u>	<u>\$ 261,495</u>