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METROPOLITAN WATER DISTRICT OF SOUTHERN CALIFORNIA

9-6

October 18, 1993

*To:* Board of Directors (Special Audit Committee--Information)  
(Finance and Insurance Committee--Information)  
*From:* Auditor  
*Subject:* Audited Comparative Financial Statements as of  
June 30, 1993 and 1992

**Report**

The District's audited comparative Financial Statements as of and for the years ended June 30, 1993 and 1992, together with the Independent Auditors' Report on those statements are attached. The accompanying accrual basis Financial Statements and Independent Auditors' Report are prepared annually pursuant to the District's audit services contract with KPMG Peat Marwick and are consistent with those issued in the prior year.

**Board Committee Assignments**

This letter is referred for information to:

The Special Audit Committee because of its responsibility regarding auditors' periodic and annual reports, pursuant to Administrative Code Section 2561(a)(1); and

The Finance and Insurance Committee because of its interest in the form and content of financial statements and reports, pursuant to Administrative Code Section 2441(k).

**Recommendation**

For information only.

*Michael W. Hondorp*  
Michael W. Hondorp

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Enclosure



Peat Marwick

Certified Public Accountants

**THE METROPOLITAN WATER DISTRICT  
OF SOUTHERN CALIFORNIA**

FINANCIAL STATEMENTS

AS OF AND FOR THE YEARS ENDED  
JUNE 30, 1993 AND 1992

(WITH INDEPENDENT AUDITORS' REPORT THEREON)

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The Metropolitan Water District  
of Southern California  
June 30, 1993 and 1992

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Peat Marwick

Certified Public Accountants

725 South Figueroa Street  
Los Angeles, CA 90017

### INDEPENDENT AUDITORS' REPORT

The Board of Directors  
The Metropolitan Water District of Southern California:

We have audited the accompanying balance sheets of The Metropolitan Water District of Southern California as of June 30, 1993 and 1992 and the related statements of revenues and expenses, changes in equity and cash flows for the years then ended. These financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. 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 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. We believe that 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 the The Metropolitan Water District of Southern California as of June 30, 1993 and 1992 and the results of its operations and its cash flows for the years then ended in conformity with generally accepted accounting principles.

*KPMG Peat Marwick*

September 8, 1993



Member Firm of  
KPMG Peat Marwick Goerdeler

**FINANCIAL STATEMENTS**

## BALANCE SHEETS

The Metropolitan Water District  
of Southern California

June 30,	1993	1992
	(in thousands)	
<b>ASSETS</b>		
<b>Current Assets:</b>		
Cash and investments (Notes 3 and 10)	\$ 364,806	\$ 326,771
Receivables:		
Water sales	97,425	79,693
Annexation charges	7,832	7,525
Interest on investments	16,933	7,956
Other	7,023	12,951
Receivables	129,213	108,125
Inventories (at moving-average cost):		
Water in storage	5,694	7,057
Operating supplies	10,789	10,736
Inventories	16,483	17,793
Total current assets	510,502	452,689
Restricted cash and investments (Notes 3 and 9)	978,031	447,869
<b>Plant and Equipment:</b>		
Plant and equipment (Note 2)	2,565,236	2,358,289
Less accumulated depreciation and amortization	467,316	440,108
Total plant and equipment - net	2,097,920	1,918,181
<b>Participation Rights:</b>		
Participation rights in state water facilities (Note 6a)	2,229,750	2,086,816
Participation rights in other facilities (Note 6b)	79,932	28,750
Participation rights	2,309,682	2,115,566
Less accumulated amortization	1,080,457	999,365
Total participation rights - net	1,229,225	1,116,201
<b>Other Assets:</b>		
Deposits, deferred charges and other (Note 7)	229,499	166,261
Annexation charges—noncurrent portion	31,833	32,001
Assets held for employees' deferred compensation (Notes 3 and 8)	26,352	24,079
Total other assets	287,684	222,341
<b>Total Assets</b>	<b>\$ 5,103,362</b>	<b>\$ 4,157,281</b>

See notes to financial statements.

## BALANCE SHEETS

The Metropolitan Water District  
of Southern California

June 30,	1993	1992
	(in thousands)	
<b>LIABILITIES AND EQUITY</b>		
<b>Current Liabilities:</b>		
<b>Payable from current assets:</b>		
Accounts payable and accrued expenses	\$ 190,448	\$ 220,576
Accrued compensated absences-current portion	9,594	8,546
Other	21,354	23,773
Payable from current assets	221,396	252,895
<b>Payable from restricted assets:</b>		
Commercial paper notes (Note 4)	60,000	60,000
Current portion of long-term debt	29,124	27,475
Accrued bond interest	48,799	29,923
Matured bonds and coupons not presented for payment	2,625	2,250
Customer deposits and trust funds	34,608	11,975
Current portion of obligation for off-aqueduct power facilities	3,124	3,230
Payable from restricted assets	178,280	134,853
Total current liabilities	399,676	387,748
<b>Long-Term Liabilities:</b>		
Long-term debt (Note 4)	2,034,603	1,288,285
Obligation for off-aqueduct power facilities (Note 6d)	147,919	169,935
Deferred compensation obligation (Note 8)	26,352	24,079
Accrued compensated absences	8,684	7,597
Obligation for arbitrage tax rebate (Note 6j)	7,504	5,678
Total long-term liabilities	2,225,062	1,495,574
Total liabilities	2,624,738	1,883,322
<b>Commitments and Contingencies (Notes 6 and 11)</b>		
<b>Equity:</b>		
Contributions in aid of construction	30,518	28,551
<b>Retained earnings:</b>		
Reserved (Note 9)	156,125	141,709
<b>Unreserved:</b>		
Designated (Note 10)	188,056	221,767
Undesignated	2,103,925	1,881,932
Retained earnings	2,448,106	2,245,408
Total equity	2,478,624	2,273,959
<b>Total Liabilities and Equity</b>	<b>\$ 5,103,362</b>	<b>\$ 4,157,281</b>

## STATEMENTS OF REVENUES AND EXPENSES

The Metropolitan Water District  
of Southern California

June 30,	1993	1992
	(in thousands)	
<b>Operating Revenues:</b>		
Water sales	\$ 544,266	\$ 404,477
Water standby charges (Note 1c)	23,661	—
Power recoveries	13,454	13,003
<b>Total operating revenues</b>	<b>581,381</b>	<b>417,480</b>
<b>Operating Expenses:</b>		
Power and water costs	123,270	196,202
Operations and maintenance	189,471	189,227
Other-net	598	1,422
<b>Total operating expenses</b>	<b>313,339</b>	<b>386,851</b>
Operating income before depreciation and amortization	268,042	30,629
Less depreciation and amortization	109,395	106,216
<b>Operating income (loss)</b>	<b>158,647</b>	<b>(75,587)</b>
<b>Other Income (Expense):</b>		
Taxes-net	78,606	75,497
Bond interest, net of \$33,363 and \$22,190 of interest capitalized in fiscal 1993 and 1992, respectively	(79,403)	(60,872)
Interest on investments	44,042	50,825
Other-net	18,041	(11,699)
<b>Total other income - net</b>	<b>61,286</b>	<b>53,751</b>
Income (loss) before extraordinary item	219,933	(21,836)
Extraordinary item - loss on defeasance of bonds (Note 4)	17,235	—
<b>Net Income (Loss)</b>	<b>\$ 202,698</b>	<b>\$ (21,836)</b>

See notes to financial statements.

## STATEMENTS OF CHANGES IN EQUITY

The Metropolitan Water District  
of Southern California

(in thousands)	Contributions in Aid of Construction	Retained Earnings			Total Equity
		Reserved	Unreserved		
			Designated	Undesignated	
<b>Balance at June 30, 1991</b>	\$ 28,551	\$ 102,949	\$ 289,311	\$ 1,874,984	\$ 2,295,795
Decrease in amounts designated for reduction of future water revenue requirements (Note 10)	—	—	(54,389)	54,389	—
Decrease in amounts designated for reduction of future water treatment costs (Note 10)	—	—	(13,155)	13,155	—
Increase in amounts reserved for revenue bond and commercial paper note indenture requirements (Note 9)	—	38,760	—	(38,760)	—
Net loss for fiscal 1992	—	—	—	(21,836)	(21,836)
<b>Balance at June 30, 1992</b>	28,551	141,709	221,767	1,881,932	2,273,959
Fiscal 1993 contributions in aid of construction	1,967	—	—	—	1,967
Decrease in amounts designated for reduction of future water revenue requirements (Note 10)	—	—	(48,708)	48,708	—
Increase in amounts reserved for revenue bonds and commercial paper note indenture requirements (Note 9)	—	14,366	—	(14,366)	—
Increase in amounts reserved for purposes for which the water standby charges are designated (Note 9)	—	50	—	(50)	—
Amounts designated for pay-as-you-go capital expenditures (Note 10)	—	—	14,997	(14,997)	—
Net income for fiscal 1993	—	—	—	202,698	202,698
<b>Balance at June 30, 1993</b>	<b>\$ 30,518</b>	<b>\$ 156,125</b>	<b>\$ 188,056</b>	<b>\$ 2,103,925</b>	<b>\$ 2,478,624</b>

See notes to financial statements.

## STATEMENTS OF CASH FLOWS

The Metropolitan Water District  
of Southern California

Year Ended June 30,	1993	1992
	(in thousands)	
<b>Cash Flows from Operating Activities:</b>		
Operating Income (Loss)	\$ 158,647	\$ (75,587)
Adjustments to reconcile operating income (loss) to net cash provided by operating activities:		
Depreciation and amortization	109,395	106,216
Increase in receivables	(11,583)	(24,839)
Decrease in inventories	1,310	1,581
Increase in prepaid expenses	(3,658)	(1,703)
(Decrease) increase in accounts payable	(5,922)	2,787
Other expense-net	3,560	5,935
<b>Net Cash Provided by Operating Activities</b>	<b>251,749</b>	<b>14,390</b>
<b>Cash Flows from Capital and Related Financing Activities:</b>		
Acquisition and construction of capital assets	(259,395)	(177,236)
Payments for participation rights in state water facilities	(170,078)	(144,731)
Payments for participation rights in other facilities	(28,021)	(20,129)
Proceeds from sale of revenue and general obligation bonds	977,398	289,107
Transfers to escrow trust accounts	(223,222)	—
Proceeds from tax levy	86,426	83,572
Principal and interest paid on bonds and commercial paper notes	(116,740)	(94,712)
Purchase of operating equipment	(2,513)	(3,852)
Other	20,014	5,109
<b>Net Cash Provided by (Used for) Capital and Related Financing Activities</b>	<b>283,869</b>	<b>(62,872)</b>
<b>Cash Flows from Investing Activities:</b>		
Purchase of investment securities	(19,971,968)	(16,004,294)
Proceeds from sales and maturities of investment securities	19,400,823	15,997,341
Interest on investments	35,081	55,116
<b>Net Cash Provided by (Used for) Investing Activities</b>	<b>(536,064)</b>	<b>48,163</b>
Net decrease in cash and cash equivalents	(446)	(319)
Cash and cash equivalents at beginning of year	446	765
<b>Cash and Cash Equivalents at End of Year</b>	<b>\$ —</b>	<b>\$ 446</b>
<b>Reconciliation of Cash and Investments to Cash and Cash Equivalents</b>		
Unrestricted cash and investments	\$ 364,806	\$ 326,771
Restricted cash and investments	978,031	447,869
Employee deferred compensation fund	25,180	23,477
Total cash and investments	1,368,017	798,117
Less carrying value of investments and employee deferred compensation fund	1,368,017	797,671
<b>Total Cash and Cash Equivalents</b>	<b>\$ —</b>	<b>\$ 446</b>

See notes to financial statements.

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## 1. Reporting Entity and Summary of Significant Accounting Policies

(a) **Reporting Entity.** The Metropolitan Water District of Southern California (the "District"), a special district of the State of California, was organized in 1928 by vote of the electorates of several Southern California cities following adoption of the Metropolitan Water District Act (the "Act") by the California Legislature. The District's primary purposes under the Act are to develop, store, and distribute water at wholesale rates for domestic and municipal purposes to its member public agencies. Surplus water is sold for other beneficial uses, including agricultural use. The District's service area comprises 5,139 square miles and includes portions of the six counties of Los Angeles, Orange, Riverside, San Bernardino, San Diego and Ventura. There are 27 independent member agencies of the District, consisting of 14 cities, 12 municipal water districts, and one county water authority. The District has no oversight responsibility over its member agencies and no component units within its reporting entity structure. The District is governed by a 51 member Board of Directors comprised of representatives of the member agencies. Representation and voting rights are based on the relative assessed valuations of property within the member agencies.

(b) **Principles of Presentation.** The District operates as a utility enterprise and the accompanying financial statements reflect the accrual basis of accounting. In order to comply with certain debt covenants and other purposes, the District has segregated its cash and investment accounts to include a water revenue fund, water standby charge fund, operations and maintenance fund, revenue bond reserve fund, revenue remainder fund, general fund, water rate and water treatment surcharge stabilization funds, special tax fund, state contract fund, bond interest and redemption funds, general obligation refunding escrow account, bond excess earnings funds, general obligation and revenue bond construction funds, pay-as-you-go fund, revolving construction fund, commercial paper note construction fund, commercial paper interest and principal payment fund, commercial paper excess earnings fund, several trust funds, and an employee deferred compensation fund.

For purposes of the statements of cash flows, the District defines cash and cash equivalents as cash in demand accounts, cash on hand and non-negotiable time

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

The Metropolitan Water District  
of Southern California  
June 30, 1993 and 1992

deposits. The indirect method is used to present cash flows from operating activities and for the periods presented, non-cash investing, capital and financing activities were not significant.

(c) **Revenue Policies.** The District's principal source of revenue is water sales. Other sources of revenue include taxes, interest income, water standby charges and hydroelectric power sales. Generally, water revenue requirements are determined by the Board after giving consideration to a formula which allocates costs between water users and taxpayers. Water rates are established by the Board of Directors and are not subject to regulation by the Public Utilities Commission of California or by any other local, state, or federal agency. Water is delivered to the member agencies on demand, and revenue is recognized at the time of delivery.

In May 1992 the District's Board imposed a water standby charge for fiscal 1993 of \$5 per year per acre (or per parcel if less than an acre), on non-exempt real property within the District's service area in order to raise approximately \$25 million. Standby charges are established on a year to year basis and the Board by resolution specified that revenues attributable to such charges must only be used for the following purposes:

- Capital payments to the State Water Project (SWP)
- Water storage-Domenigoni Reservoir
- Water Recycling and Conservation
- System Improvements

For these purposes a total of \$23,678,831 of standby charge revenue and interest earnings were expended during fiscal 1993. Of this amount, 55% was used for SWP, 15% for water storage, 9% for system improvements, and 21% for water recycling and conservation.

In May 1993, the Board adopted a water standby charge for fiscal 1994 in order to raise approximately \$50 million from this source during such year. The per acre or smaller parcel rate for fiscal 1994, which may vary by member agency, is a

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

The Metropolitan Water District  
of Southern California  
June 30, 1993 and 1992

composite rate of no more than \$15 consisting of a \$5 uniform component and a variable component, determined according to historic water use by member agency, of no more than \$10.

(d) **Taxing Authority.** The District is expressly empowered under the Act to levy and collect taxes on all taxable property within its boundaries for the purpose of carrying on its operations and paying its obligations, subject to certain limitations in the Act, the Revenue and Taxation Code, and the California Constitution. Property taxes are levied annually by the Board of Directors as of July 1, using a lien date of March 1, and are payable by property owners in two equal installments which are due on November 1 and February 1, and become delinquent after December 10 and April 10, respectively. The taxes levied are billed and collected by the counties in the District's service area on behalf of the District and are remitted to the District throughout the year.

Property tax revenue is used to pay the District's general obligation bond debt service and a portion of its obligations under its contract with the State for a water supply (the "State Water Contract"). Special taxes collected pursuant to pre-1978 annexation proceedings are also used for payments under the State Water Contract. In developing the annual tax levy, the District takes into account potential delinquencies, tax allocations to redevelopment agencies and supplemental tax collections.

Effective in fiscal 1991, as a result of legislation enacted in 1984, future tax levies, other than special annexation taxes, were restricted to the amount needed to pay for debt service on District general obligation bonds and the District's proportionate obligation for general obligation bond debt service of the State under the State Water Contract. Under the terms of the 1984 legislation, tax levies may exceed the limitation prescribed therein during periods of financial necessity.

(e) **Annexation Charges.** Charges are collected for areas that annex to the District unless the areas annex to cities which are member agencies, in which case no charge is collected. Since fiscal 1978, such charges are paid in cash before completion of an annexation.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

The Metropolitan Water District

of Southern California

June 30, 1993 and 1992

Prior to fiscal 1978, annexation charges were primarily collected in installments, including interest on unpaid balances, through the levy of special ad valorem taxes. It is the District's policy not to record a receivable on pre-1978 annexations until amortization of the principal and interest thereon can be accomplished within 50 years following the date of annexation through application of a maximum annual tax rate of 0.1875 percent of assessed valuation or less, assuming that the assessed valuation of the annexed area remains constant. Accordingly, at June 30, 1993 and 1992, annexation receivables of \$39,665,000 and \$39,526,000, respectively, including uncollected interest of \$7,400,000 and \$8,714,000, respectively, are not reflected as assets or included in the equity of the District.

(f) **Plant and Equipment.** District plant and equipment are recorded at cost. The cost of constructed assets includes labor, materials, certain general and administrative expenses and interest incurred during construction periods. Depreciation is calculated using the straight-line method based on the estimated average useful lives of the assets, which range from 80 years for storage and distribution facilities, 50 years for treatment plants and hydroelectric power recovery facilities, and 4 to 20 years for vehicles and other operating equipment. The cost of major computer systems software, whether purchased or internally developed, is capitalized if the estimated cost equals or exceeds \$250,000 and useful life is at least 5 years.

(g) **State Water Project Participation Rights.** The District is one of thirty participants contracting with the State of California for a system to provide water throughout much of California. Under the terms of the State Water Contract, as amended, the District is obligated to pay allocable portions of the cost of construction of the system and ongoing operations and maintenance costs through at least the year 2035, regardless of the quantities of water available from the project (see Note 6a). The District and the other contractors may also be responsible to the State for certain obligations of any contractor who defaults on its payments to the State.

Approximately 35 percent of the District's total expenditures during fiscal 1993 pertained to its payment obligations for the state project. The magnitude of these payments is primarily based on contractual water delivery entitlements, the requested and actual deliveries received, and the cost of power required for such deliveries.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

The Metropolitan Water District  
of Southern California  
June 30, 1993 and 1992

Management's present intention is to exercise the District's option to extend the contractual period to at least 2052, under substantially comparable terms. This corresponds to an estimated eighty-year service life for the original facilities. The State is obligated to provide specified quantities of water throughout the life of the contract, subject to certain conditions.

In addition to system "on-aqueduct" power facilities, the State has, either on its own or by joint venture, financed certain off-aqueduct power facilities (OAPF). The power generated is utilized by the system for water transportation purposes. Power generated in excess of system needs is marketed to various utilities. The District is entitled to a proportionate share of the revenues resulting from sales of excess power. The District and the other water contractors are responsible for repaying the capital and operating costs of the OAPF regardless of the amount of power generated (see Note 6d).

The District capitalizes its share of system construction costs as Participation Rights in State Water Facilities, as such costs are billed by the State. Unamortized participation rights essentially represent a prepayment for future water deliveries through the State system. The District's share of system operations and maintenance costs is charged to expense.

The District amortizes a portion of capitalized participation rights each month using a formula that considers the estimated useful life and estimated production capacity of the assets based upon information provided by the State of California. Amortization expense totalled \$81,081,000 and \$75,804,000 in fiscal 1993 and 1992, respectively.

(h) **Participation Rights in Imperial Irrigation District Facilities.** The District has entered into a water conservation agreement with the Imperial Irrigation District (IID) (see Note 6b). As capital projects are completed, the costs contributed by the District to each completed project will be capitalized as participation rights in the District's accounting records. These participation rights are amortized using the straight-line method over the original term of the agreement, which is thirty-five years, plus the number of years remaining in the original five-year construction period. Amortization expense of \$827,000 and \$486,000 was recorded in fiscal 1993 and 1992, respectively.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

The Metropolitan Water District  
of Southern California  
June 30, 1993 and 1992

(i) **Contributions in Aid of Construction.** Amounts received from member agencies for construction of service connections or other facilities are included as part of equity and are combined with retained earnings for purposes of determining the District's borrowing limitations. Contributed service connections or other facilities are recorded as District assets and are depreciated in accordance with established policy for similar capital assets.

(j) **Compensated Absences.** The District accrues its estimated obligations for vacation, sick, and compensatory leave when earned by eligible employees. The allocations to the current and long-term portions of these vested obligations are based on experience.

2. **Plant and Equipment**

At June 30, 1993 and 1992, plant and equipment (at cost) consists of the following (in thousands):

	1993	1992
Land, easements, and rights of way	\$ 180,120	\$ 139,725
Parker Power Plant and Dam	13,009	13,009
Power recovery plants	103,123	103,038
Other dams and reservoirs	103,385	103,359
Water transportation facilities	984,826	936,030
Pumping plants and facilities	71,802	66,871
Treatment plants and facilities	293,934	252,239
Power lines and communication facilities	14,430	14,228
Computer systems software	700	—
Miscellaneous	47,840	44,225
Construction in progress	639,435	582,839
Major equipment	68,037	58,131
Pre-operating interest and other expenses of original aqueduct	44,595	44,595
Plant and equipment	<u>2,565,236</u>	<u>2,358,289</u>
Less accumulated depreciation and amortization	467,316	440,108
Total plant and equipment — net	<u>\$ 2,097,920</u>	<u>\$ 1,918,181</u>

Title to the northerly portion of the First San Diego Aqueduct (included in the asset category of water transportation facilities at a cost of \$19,595,000) is vested in the United States government. It will be transferred to the District in 1995 upon

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

The Metropolitan Water District

of Southern California

June 30, 1993 and 1992

Cash and Investments							
(in thousands)							
	June 30, 1993					June 30, 1992	
	Category			Carrying Amount	Market Value	Carrying Amount	Market Value
	1	2	3				
U.S. Treasury securities	\$ 388,886	\$ —	\$ —	\$ 388,886	\$ 397,259	\$ 275,065	\$ 278,781
U.S. Treasury securities held for crossover refunding bonds	228,632	—	—	228,632	228,632	—	—
U.S. Guarantees - GNMA's	6,299	—	—	6,299	6,907	9,119	9,829
Federal agency securities	195,248	—	—	195,248	195,800	110,713	113,260
State agency securities	35	—	—	35	35	34	34
Bankers' acceptances	70,908	—	—	70,908	71,037	51,412	51,521
Prime commercial paper	177,031	—	—	177,031	177,132	129,973	129,973
Negotiable certificates of deposit	53,522	—	—	53,522	53,522	40,794	40,794
Repurchase agreements	232,456	—	—	232,456	231,086	165,561	166,812
Total	<u>\$ 1,353,017</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 1,353,017</u>	<u>1,361,410</u>	<u>782,671</u>	<u>791,004</u>
Local agency investment fund - State of California				15,000	15,000	15,000	15,000
Total investments				<u>1,368,017</u>	<u>\$ 1,376,410</u>	<u>797,671</u>	<u>\$ 806,004</u>
Add:							
Cash/demand deposits				(100)		346	
Non-negotiable certificate of deposit				100		100	
Total cash				<u>—</u>		<u>446</u>	
Total cash and investments				<u>1,368,017</u>		<u>798,117</u>	
Less:							
Restricted cash and investments				978,031		447,869	
Employee deferred compensation fund (Note 8)				25,180		23,477	
Unrestricted cash and investments				<u>\$ 364,806</u>		<u>\$ 326,771</u>	

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

The Metropolitan Water District  
of Southern California

June 30, 1993 and 1992

(c) **Reverse Repurchase Agreements.** The District is permitted to sell securities owned under written agreements to buy back the securities on or before a specified date for a specified amount. No such reverse repurchase agreements were entered into during the fiscal years ended June 30, 1993 and 1992.

(d) **Investments in Escrow Trust Deposits.** At June 30, 1993 and 1992, U.S. Treasury securities costing \$294,445,000 and \$234,583,000, respectively, were held in irrevocable escrow trust accounts for the redemption of various refunded bond issues or partial issues (see Note 4). The refundings resulted in the defeasance of these bond issues; accordingly, the bond obligations and related investments in the escrow trust accounts are excluded for financial reporting purposes.

#### 4. Short-Term and Long-Term Debt

The District's enabling Act specifies that its indebtedness shall be limited to 15 percent of the assessed value of all taxable property within the District. Existing outstanding long-term debt of \$2.063 billion represents only a fraction of one percent of the 1993-94 taxable assessed valuation of \$881 billion.

The District's long-term debt consists of general obligation and revenue bond issues as well as other obligations. The various revenue bond obligations are special limited obligations of the District and are secured by a pledge of the District's net operating revenues. Such obligations contain certain restrictive covenants, with which the District has complied. The general obligation bonds are secured by the District's authority to levy property taxes in an unlimited amount for such purposes. All of the bond issues contain call provisions. Substantially all of the debt proceeds have been, and will continue to be, utilized to fund new facilities, improvements and betterments and to refund outstanding bonds.

(a) **Short-term Debt.** The Board authorized the issuance of \$200 million in commercial paper notes, and \$60 million were sold and were outstanding at June 30, 1993 and 1992. These notes are intended to be redeemed by net operating revenues and are subordinate to all other District debt. It is the intent of the District to renew these notes as they become due, at the option of the District.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

The Metropolitan Water District  
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(b) **General Obligation Bonds.** In 1966, voter authorization was obtained to incur \$850,000,000 of general obligation bonded indebtedness to finance a portion of the District's capital improvement program. The original amounts issued as Series A through G under the 1966 authorization totalled \$800,000,000 at June 30, 1993. The District has advance refunded some of these general obligation bond issues through the issuance of refunding bonds. At June 30, 1993, a total of \$889,605,000 in general obligation bonds and refunding general obligation bonds was outstanding.

Each general obligation bond issue consists of both serial and term bonds which mature in varying amounts through 2022 at interest rates ranging from 2.25 percent to 8.5 percent. The term bonds are subject to mandatory redemption prior to maturity. All general obligation bonds maturing on or after certain interest payment dates are subject to call and redemption prior to maturity at the option of the District, as a whole or in part (by lot within each maturity) on any interest payment date on or after the earliest call date applicable to such general obligation bonds. Early redemptions made on certain interest payment dates are subject to an early redemption premium.

(c) **Revenue Bonds.** Pursuant to a 1974 voter authorization, additional funds, primarily for the capital improvement program, were obtained through sales of Waterworks Revenue or Water Revenue Refunding Bonds since 1975. Revenue bonds may be issued subject to certain provisions, including a requirement that the total of revenue bonds outstanding does not exceed the equity of the District as of the fiscal year-end prior to such issuance. At June 30, 1993, a total of \$1,689,805,000 of revenue bonds and revenue refunding bonds had been issued under the 1974 authorization, of which \$1,207,400 remain outstanding.

Each revenue bond issue consists of both serial and term bonds which mature in varying amounts through 2023 at interest rates ranging from 3.0 percent to 8.50 percent. The term bonds are subject to mandatory redemption prior to maturity. All revenue bonds maturing on or after certain interest payment dates are subject to call and redemption prior to maturity at the option of the District, as a whole or in part (by lot within each maturity) on any interest payment date on or after the earliest call date applicable to such revenue bonds. Early redemptions made on certain interest payment dates are subject to an early redemption premium.

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(d) **Fiscal 1993 Bond Issues, Refundings and Defeasances.** In August 1992, the District sold \$550,000,000 of Water Revenue Bonds at an average interest cost of 5.94 percent, to finance construction of improvements and works of the District. These bonds have varying interest rates. Their maturities extend to July 2022 and are subject to mandatory and optional redemption provisions.

On February 12, 1993, the District also issued \$279,735,000 of Waterworks General Obligation Refunding Bonds consisting of \$138,085,000, 1993 Series A1 Bonds, \$87,315,000, 1993 Series A2 Bonds and \$54,335,000, 1993 Series A3 Bonds. The Series A1 and A2 Bonds (Crossover Bonds) were issued to advance refund on March 1, 1999, \$136,940,000 of outstanding Waterworks Bonds, Election 1966, Series G and on March 1, 1996, \$86,705,000 of outstanding Waterworks Refunding General Obligation Bonds, Issue of 1986 (Crossover Prior Bonds). The Series A3 Bonds were issued to advance refund \$12,075,000 of outstanding Waterworks General Obligation Bonds, Election of 1966 Series D, and \$42,000,000 of outstanding Waterworks Refunding General Obligation Bonds, Issue of 1976 (A3 Prior Bonds). The net proceeds from these sales totaled \$283,318,000 (after receipt of \$5,364,000 of original issue premium and payment of \$1,781,000 in underwriters fees and other issuance costs) were used to purchase U.S. Treasury Securities totalling \$283,318,000.

Securities with a cost basis of \$228,632,000 were deposited in an irrevocable escrow trust account with a bank acting as an independent fiscal agent (Crossover Trust Account) to provide for all debt service on the Series A1 Bonds through March 1, 1999 and the Series A2 Bonds through March 1, 1996. At the Crossover Dates, the funds available in the Crossover Trust Account will be used to advance refund the Crossover Prior Bonds being refunded. At the Crossover Dates, the Crossover Prior Bonds will be considered defeased. Prior to the Crossover Dates, the Crossover Bonds will be special obligations of the District payable from the Crossover Trust Accounts. After the Crossover Dates, the Crossover Bonds will become general obligations of the District.

Securities with a cost basis of \$54,686,000 were deposited in an irrevocable trust account with a bank acting as an independent fiscal agent (A3 Trust Account) to provide for all future debt service payments of the A3 Prior Bonds being refunded.

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As a result, the A3 Prior bonds are considered defeased; accordingly, the liability for those bonds, as well as the related investments in the A3 Trust Account, have been excluded from the District's financial statements.

On February 12, 1993, the District issued \$168,760,000 of Water Revenue Refunding Bonds, 1993 Series A, to advance refund \$43,850,000 of outstanding Waterworks Revenue Refunding Bonds, Issue of 1986, and \$110,930,000 of outstanding Water Revenue Bonds, Issue of 1991. The net proceeds of \$165,338,000 (after payment of \$2,922,000 in underwriters fees, original issue discount and other issuance costs) plus an additional \$2,699,000 of debt service and reserve funds of the Prior Bonds were used to purchase U.S. Treasury Securities. These securities, with an initial cost basis of \$168,537,000, were deposited in an irrevocable escrow trust account with a bank acting as an independent fiscal agent to provide for all future debt service payments of the Prior Bonds being refunded. As a result, the Prior Bonds are considered defeased; accordingly, the liability for those bonds, as well as the related investments in the irrevocable trust account, have been excluded from the District's financial statements.

As described in the preceding paragraphs, the District sold Waterworks General Obligation Refunding Bonds, Series A3, and Water Revenue Refunding Bonds, 1993 Series A, to refund certain issues of the District's outstanding debt. Such refundings were accomplished to take advantage of the current lower interest rates available to tax exempt bond issuers. However, in accordance with generally accepted accounting principles, the District recognized accounting losses of \$671,000 and \$16,564,000 from these General Obligation Refunding and Revenue Refunding bond issues, respectively. The losses recognized, which total \$17,235,000, represent the differences between the present value of the reacquisition prices and the net carrying amounts of the old debt on the dates of defeasance. It is estimated that such refundings will result in a net reduction in the District's aggregate debt service payments of \$35,590,000 over the life of the new issues and resulted in an economic gain of \$17,888,000 (difference between the present values of the old and new debt service payments).

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(e) **Prior Years' Defeasance of Debt.** In prior years, the District issued various refunding general obligation and refunding revenue bonds. The proceeds of such refunding bonds were placed in irrevocable escrow trust accounts with independent fiscal agent banks to be used to provide for the future debt service payments of various issues of the District's general obligation and revenue bonds. As a result of the refundings, the original bonds were considered defeased and, accordingly, are excluded from the District's financial statements. At June 30, 1993, \$81,220,000 of such defeased bonds are still outstanding.

(f) **Long-term Debt Obligation Summary.** Interest rates on all outstanding bond obligations range from 2.25 percent to 9.2 percent. Future principal and interest obligations on the currently outstanding issues are (in thousands):

Due in fiscal year ending June 30,	Principal	Interest	Total
1994	\$ 29,659	\$ 105,774	\$ 135,433
1995	31,305	105,142	136,447
1996	41,645	103,182	144,827
1997	44,160	100,026	144,186
1998	46,580	97,656	144,236
Later years	1,680,365	1,303,683	2,984,048
	\$ 1,873,714	\$ 1,815,463	\$ 3,689,177
Crossover Refunding Bonds	223,645		
Less unamortized bond discount, net	33,632		
Total long-term debt	\$ 2,063,727		
Less current portion	29,124		
Long-term portion of debt	\$ 2,034,603		

In July 1993, the District sold \$89,595,000 of Water Revenue Refunding Bonds and \$78,290,000 of General Obligation Refunding Bonds at an average interest cost of 5.39 and 5.49 percent, respectively, to refund certain of the District's outstanding water revenue and general obligation bonds. These bonds have varying interest rates and are subject to mandatory and optional redemption provisions. The maturities of the revenue and general obligation refunding bonds extend to July 2010 and March 2020, respectively. These obligations are not reflected in the preceding table.

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The changes in components of total long-term debt are listed below (in thousands):

	Maturity Dates	Range of Interest Rates
General obligation bonds and refunding general obligation bonds:		
Colorado river waterworks bonds—1931	9/1/92—4/1/94	2.25%—3.00%
Waterworks bonds—1966 — series A-G	3/1/93—3/1/22	4.00%—8.50%
Waterworks refunding general obligation bonds, issue of 1976	3/1/93—3/1/00	4.90%—5.25%
Waterworks refunding general obligation bonds, issue of 1986	3/1/93—3/1/95	5.60%—6.0%
Waterworks general obligation refunding bonds series A1-A3—1993	3/1/94—3/1/12	4.00%—8.00%
Total general obligation and refunding general obligation bonds		
Revenue and refunding revenue bonds:		
Waterworks refunding revenue bonds, issue of 1978	1/1/93—1/1/20	5.00%—5.60%
Waterworks revenue bonds—1979	7/1/92—7/1/20	5.40%—6.10%
Waterworks revenue bonds—1983	6/1/93	7.75%
Waterworks refunding revenue bonds, issue of 1986	6/1/93—6/1/23	5.80%—6.75%
Water revenue bonds—1991	7/1/92—7/1/21	4.75%—6.75%
Water revenue Bonds—1992	7/1/95—8/5/22	3.90%—8.00%
Water revenue refunding bonds, 1993 series A	7/1/93—7/1/21	3.00%—5.75%
Total revenue and refunding revenue bonds		
Payable to San Diego County Water Authority	6/1/92—6/1/95	2.519%
Unamortized bond discount, net		
Total long-term debt		

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June 30, 1992	Additions	Less Maturities, Defeasances and (Amortization)	June 30, 1993
\$ 750	\$ —	\$ 500	\$ 250
541,885	—	24,460	517,425
46,900	—	46,900	—
93,000	—	805	92,195
<u>—</u>	<u>279,735</u>	<u>—</u>	<u>279,735</u>
<u>682,535</u>	<u>279,735</u>	<u>72,665</u>	<u>889,605</u>
122,900	—	2,450	120,450
67,825	—	850	66,975
1,055	—	1,055	—
160,315	—	44,515	115,800
300,000	—	114,585	185,415
—	550,000	—	550,000
<u>—</u>	<u>168,760</u>	<u>—</u>	<u>168,760</u>
<u>652,095</u>	<u>718,760</u>	<u>163,455</u>	<u>1,207,400</u>
564	—	210	354
<u>(19,434)</u>	<u>(20,798)</u>	<u>(6,600)</u>	<u>(33,632)</u>
<u><u>\$ 1,315,760</u></u>	<u><u>\$ 977,697</u></u>	<u><u>\$ 229,730</u></u>	<u><u>\$ 2,063,727</u></u>

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**5. Pension Plan**

(a) **Plan Description.** The District is a member of the California Public Employees' Retirement System (PERS), an agent multiple-employer pension system which provides a contributory defined-benefit pension for substantially all District employees. PERS functions as an investment and administrative agent for its members.

All full-time District employees are required to participate in PERS. The pension plan provides for service and disability retirement, survivor, and death benefits. Vesting occurs after 5 years of credited service. Vested employees who retire at or after age 50 are entitled to a service retirement allowance, payable monthly for the remainder of their lives. Several survivor benefit options are available which reduce a retiree's unmodified allowance.

The District makes biweekly contributions to PERS based on actuarially determined employer contribution rates which, together with employee contributions, will provide sufficient assets to pay benefits when due. Employees are required to contribute 7 percent of their gross earnings (excluding premium pay) to PERS, except that employees hired prior to January 1, 1981, contribute 4.5 percent of their compensation and the District contributes the remaining 2.5 percent.

The District's payroll covered by PERS totalled approximately \$109.7 million and \$97 million, respectively, for the years ended June 30, 1993 and 1992. Total payrolls for the same two periods were \$120.7 million and \$106.5 million, respectively.

(b) **Funding Status and Progress.** The amount shown below as the "pension benefit obligation" is a standardized disclosure measure of the present value of pension benefits, adjusted for the effects of projected salary increases, estimated to be payable in the future as a result of employee service to date. The measure is intended to help users assess the funding status of the system on a going-concern basis, assess progress made in accumulating sufficient assets to pay benefits when due, and make comparisons among employers. The measure is the actuarial present value of credited projected benefits, and is independent of the funding method used to determine contributions to PERS by its members.

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The latest pension benefit obligation information available is as of June 30, 1992 and 1991 and was computed as part of actuarial valuations performed as of those dates, but which reflect all plan amendments adopted through June 30, 1993 and 1992, respectively. Significant actuarial assumptions used in the valuation include: (a) a rate of return on the investment of present and future assets of 8.75 percent a year compounded annually, and (b) projected salary increases of 7 percent a year compounded annually, attributable to inflation, merit and other increases. Mortality rates and other economic projections are also utilized in the valuation process.

The pension benefit obligation and funded position applicable to the District's employees is as follows, based on the latest information provided by PERS (in thousands):

June 30,	1992	1991
Pension benefit obligation:		
Retirees and beneficiaries receiving benefits and terminated employees not receiving benefits	\$ 124,408	\$ 117,786
Current employees:		
Accumulated employee contributions, including allocated investment earnings	78,780	70,465
Employer-financed vested	116,501	107,875
Employer-financed nonvested	4,640	3,631
Total pension benefit obligation	<u>324,329</u>	<u>299,757</u>
Less: Net assets available for benefits—at cost or amortized cost (market values of \$374,154 and \$331,038 at June 30, 1992 and 1991, respectively)	<u>331,697</u>	<u>298,501</u>
Unfunded (assets in excess of) pension benefit obligation	<u>\$ (7,368)</u>	<u>\$ 1,256</u>

(c) **Actuarially Determined Contribution Requirements and Contributions Made.** The District's annual contribution rate is recalculated effective each July 1 as part of an annual actuarial valuation. The purpose of an actuarial cost method is to assign to each year the cost of the benefit accrued in that year. The actuarial cost of the benefits assigned to a particular year is called the normal cost. PERS uses the Entry Age Normal Actuarial Cost Method which is a projected benefit cost method. That is, PERS takes into account those benefits that are expected to be earned in the future as well as those already accrued.

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The current normal cost would be sufficient to fund the current benefit structure if it had been paid since the members' dates of employment and the emerging experience through the years had been identical to the current actuarial assumptions. However, because of changes through the years in the benefit structure and the actuarial assumptions, and because actuarial gains and losses caused by experience are different from such assumptions, these conditions normally will not be satisfied and, therefore, an unfunded actuarial liability may develop.

The present value of projected benefits is funded by the normal cost paid over the future working lifetime of the plan participants, assets accumulated to date, and the unfunded actuarial liability, if any, which will be funded by the District over a fixed period of time, generally through the year 2000.

The significant actuarial assumptions used to compute the District's contribution requirement are the same as those used to compute the pension benefit obligation. The District's contributions to PERS for fiscal 1993 and 1992 were made in accordance with requirements determined as part of actuarial valuations performed as of June 30, 1992 and 1991, respectively, as follows (in thousands):

Actuarially determined contributions required to cover:	1993		1992	
	Amount	Percentage of Covered Payroll	Amount	Percentage of Covered Payroll
Normal cost	\$ 8,759	8.0%	\$ 8,480	8.75%
Contributions on behalf of employees hired before 1/1/81	1,015	.9	1,001	1.03
Total contributions	<u>\$ 9,774</u>	<u>8.9%</u>	<u>\$ 9,481</u>	<u>9.78%</u>

District employees contributed \$7,685,000 (representing 7 percent of covered payroll) and \$5,835,000 (representing 6.017 percent of covered payroll) during fiscal 1993 and 1992, respectively.

(d) **Trend Information.** Trend information gives an indication of the progress made in accumulating sufficient assets to pay benefits when due. Trend information required by Statement No. 5 of the Government Accounting Standards Board

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is presented below to the extent available from PERS for disclosure purposes (in thousands):

Fiscal Year Ending June 30	Net Assets Available for Benefits (at cost)	Pension Benefit Obligation	Percentage Funded	Unfunded (assets in excess of) Pension Benefit Obligation	Annual Covered Payroll	Unfunded (assets in excess of) Pension Benefit Obligation as a percentage of Covered Payroll
1987	\$ 206,268	\$ 209,913	98.26%	\$ 3,645	\$ 54,100	6.74%
1988	228,871	226,198	101.18	(2,673)	59,200	(4.52)
1989	259,523	247,941	104.67	(11,582)	64,200	(18.04)
1990	282,594	279,216	101.21	(3,378)	72,800	(4.64)
1991	298,501	299,757	99.58	1,256	82,200	1.53
1992	331,697	324,329	102.27	(7,368)	97,000	(7.60)

Analysis of the dollar amounts of net assets available for benefits, pension benefit obligation, and unfunded or assets in excess of pension benefit obligation in isolation can be misleading. Expressing the net assets available for benefits as a percentage of the pension benefit obligation provides one indication of the District's funding status in PERS on a going-concern basis. Analysis of this percentage over time indicates whether the District's funding position is becoming financially stronger or weaker. Generally, the greater this percentage, the stronger the position. Trends in the funded status of the pension benefit obligation and annual covered payroll are both affected by inflation. Expressing the unfunded or assets in excess of pension benefit obligation as a percentage of annual covered payroll approximately adjusts for the effects of inflation and aids analysis of the District's progress made in accumulating sufficient assets in PERS to pay benefits when due. Generally, the smaller this percentage, the stronger the fund.

For fiscal 1993, 1992, and 1991, the District's contributions to the system, all made in accordance with actuarially determined requirements, were 8.9 percent, 9.8 percent and 8.3 percent, respectively, of annual covered payroll.

## 6. Commitments and Contingencies

(a) **State Water Contract.** Estimates of the District's share of the projected fixed costs of the State Water Project are provided annually by the State. The estimates

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are subject to future increases or decreases resulting from changes in planned facilities, refinements in cost estimates, and inflation.

During the next five years payments under the State Water Contract, exclusive of variable power costs, are currently estimated by the State to be as follows (in thousands):

Fiscal year ending June 30,

1994	\$ 315,653
1995	320,316
1996	321,902
1997	324,656
1998	323,173

According to the State's latest estimates, the District's long-term obligations under the contract, for capital and minimum operations and maintenance costs, including interest from 1993 to year 2035, are as follows (in thousands):

Conservation facilities	\$ 1,837,567
Transportation facilities	5,095,530
Off-aqueduct power facilities (See Note 1g)	1,574,764
Revenue bond surcharge	445,712
East Branch enlargement	852,103
Total long-term SWP contract obligations	<u>\$ 9,805,676</u>

The amounts shown above do not contain any escalation for inflation, are based upon a number of assumptions, are contingent upon future events, and are subject to significant variation over time. Accordingly, virtually none of the estimated obligations, other than the \$151 million obligation related to loss accruals on certain off-aqueduct power facilities (see Note 6d), are recorded as liabilities in the accompanying financial statements.

(b) **Participation Rights in Imperial Irrigation District Facilities.** In December 1988 the District and the Imperial Irrigation District (IID) entered into a water conservation agreement which became effective through a subsequent approval

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agreement in December 1989. IID is a California agency which has contracted for the delivery of Colorado River water.

Under the terms of the IID/MWD Agreement the District will pay for capital and annual direct costs, and certain indirect costs of specific conservation projects within IID. The District will then receive an estimated 106,000 acre-feet of conserved water annually, except under certain limited circumstances, upon completion of construction of the conservation projects.

All conserved water must be used by the District in the calendar year the water is conserved, unless stored in a reservoir pursuant to a separate banking agreement. The initial term of the agreement is 35 years after completion of the last project or initial operation of that project, whichever is later.

As of June 30, 1993, the District paid IID a total of \$102.7 million for construction costs, operations and maintenance costs and indirect costs for conservation projects. During the remainder of the construction program the District is obligated to pay IID an estimated \$37.9 million for construction, and approximately \$14 million for indirect and operations and maintenance costs. In addition, the District will pay IID approximately \$3 million per year for operation and maintenance costs during the 35 year term of this agreement.

(c) **Land Fallowing Program.** In May 1992, the Board authorized the General Manager to execute agreements for the Palo Verde Irrigation District (PVID) land fallowing program. This two year test program will develop approximately 186,000 acre feet of water for the District's use at an estimated cost of \$25 million.

The District executed agreements with lessees and/or landowners in PVID to fallow agreed upon amounts of farmland. This means that they are not using Colorado River water to irrigate the fallowed farmland between August 1, 1992 and July 31, 1994. The U.S. Bureau of Reclamation is storing this unused water in Lake Mead under a separate agreement and it will be available to the District until January 1, 2000. The program costs will be recorded as intangible water rights, in keeping with the District's policy of recording water owned by the District that is stored in another

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agency's facilities. Also, it is management's intent that this water will be retained in this storage facility and will be used in future years, prior to January 1, 2000.

(d) **Off-Aqueduct Power Facilities.** As described in Note 1g, the State Department of Water Resources (DWR) has financed the construction of certain off-aqueduct power facilities (OAPF) in order to provide power for water transportation purposes for the State Water Project system. Construction of one such facility, the South Geysers Geothermal Power Plant, was suspended in 1987 due to a lack of a steam supply sufficient to operate the plant at planned capacity. During the year ended June 30, 1989, DWR officials decided to dispose of the plant assets, if possible, by leasing the steam field and plant site and selling the power plant equipment. A second OAPF project, the Bottle Rock Geothermal Power Plant, was shut down (mothballed) in 1990. This shutdown was necessary because the declining steam supply made continued operation of the plant uneconomical.

As a result of these actions by DWR, management recorded losses of \$76.5 million and \$127.6 million in fiscal years 1989 and 1990, respectively. The District's estimated remaining long-term obligations for debt service on the Bottle Rock and South Geysers facilities as of June 30, 1993, which are based on the State's latest estimates, including imputed interest at 6.66 percent through the year 2024, are as follows (in thousands):

Due in fiscal year ending June 30,	Principal	Interest	Total
1994	\$ 3,124	\$ 10,059	\$ 13,183
1995	3,335	9,851	13,186
1996	3,561	9,629	13,190
1997	3,814	9,392	13,206
1998	4,039	9,138	13,177
Later years	133,170	99,173	232,343
Total long-term obligation	<u>151,043</u>	<u>\$ 147,242</u>	<u>\$ 298,285</u>
Less current portion	<u>3,124</u>		
Long-term portion of obligation	<u>\$ 147,919</u>		

(e) **Construction Programs and Contracts.** At June 30, 1993, the estimated cost of the District's planned construction program through fiscal year 2002 totalled approximately \$5.9 billion, including escalations for inflation of 5 percent per year. The program includes the estimated costs of facilities which may be required to meet

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future water quality standards (see Note 6i). Planning studies are in progress to revise and update the construction program based upon estimates of increasing population and water demand in the District's service area, and the need to enhance the water treatment process.

The District had commitments under construction contracts in force at June 30, 1993 and 1992, totalling approximately \$56,931,000 and \$108,774,000, respectively, for rehabilitation of its aqueduct system and expansion of its distribution and storage system.

(f) **Claims and Litigation.** A number of suits and claims arising in the normal course of business are pending against the District. In the opinion of the District's General Counsel, the adverse results, if any, of such legal actions will not have a material effect on the District's financial position.

(g) **Lease and Purchase Commitments.** Commitments under installment purchases are not material.

The District is obligated under certain leases for office and warehouse space which are accounted for as operating leases. Rent expense for these leases was approximately \$2,287,000 and \$1,623,000 for fiscal 1993 and 1992, respectively.

A lease previously executed by the District which was to commence during fiscal 1992 was deemed rejected by the lessor by order of the United States Bankruptcy Court and accordingly has been eliminated from future lease obligations. In order to replace the lost space and obtain additional needed space, the District entered into a six year lease for 344,000 square feet of office space located in downtown Los Angeles beginning in fiscal 1993.

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The following is a schedule, by year, of future minimum rental payments required under operating leases that have initial or remaining noncancellable lease terms in excess of one year, as of June 30, 1993 (in thousands).

Fiscal year ending June 30

1994	\$ 8,675
1995	11,117
1996	10,292
1997	10,390
1998	10,496
Later Years	4,874
Total Minimum Payments Required	<u>\$ 55,844</u>

Subsequent to June 30, 1993, the Board of Directors authorized an amendment to the building lease for an additional 50,000 square feet of office space in an amount not to exceed \$7.5 million plus expenses. This obligation is not included in the preceding schedule.

(h) **Post-Retirement Benefits.** The District pays a basic premium to the California Public Employees' Retirement System to provide health care benefits to its retirees. These benefits are provided to all retired District employees and are paid on a pay-as-you-go basis. During fiscal years 1993 and 1992, the District paid \$2,184,000 and \$2,135,000, respectively, for health care benefits for its retirees.

(i) **Drinking Water Quality Standards.** Under the Safe Drinking Water Act (SDWA) Amendments of 1986, the United States Environmental Protection Agency (EPA) has been mandated by Congress to set new drinking water quality standards. New standards for disinfection by-products (DBPs), such as trihalomethanes (THMs), will be set in the mid to late 1990s. The 1986 SDWA amendments identified granular activated carbon (GAC) as the best method to control synthetic organic chemicals, which could be interpreted to include THMs. District studies, however, have concluded that GAC is not a cost-effective means of reducing THMs for the District.

Further studies by the District have explored the use of ozone and a new technology, ozone/hydrogen peroxide (PEROXONE), to minimize the production of DBPs. Subject to completion of the studies and approval by the Board of Directors,

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ozone or PEROXONE technology will be phased in at each of the District's treatment plants by 2003. These treatment methods are anticipated to be compatible with EPA's goals and objectives. Current estimates of the cost to implement ozone or PEROXONE treatment, including escalations for inflation of 5 percent per year, range as high as \$501 million. This amount is included in the District's Capital Improvement Program (see Note 6e).

(j) **Arbitrage Rebate Obligation.** At June 30, 1993, the District had general obligation and revenue bonds and commercial paper notes outstanding which are subject to arbitrage limitations. The term arbitrage rebate refers to the required payment to the U.S. Treasury of excess earnings received on applicable tax-exempt bond proceeds that are invested at a higher yield than the yield of the tax-exempt bond issue. The District's ultimate rebate of arbitrage earnings on these issues is contingent on various factors, including future yields on invested proceeds.

As of June 30, 1993 and 1992, the District has recorded arbitrage rebate liabilities presently valued at \$7,504,000 and \$5,678,000, respectively. The rebate obligations are computed and adjusted, as applicable, on an annual basis in accordance with regulations promulgated by the U.S. Treasury Department. Required rebates are generally due and payable in five-year intervals during the life of debt issues, with final rebates due upon the retirement of the debt issues.

## 7. Deferred Water Rights

The District has entered into several water exchange, storage, and reclamation project agreements with other agencies. These agreements provide the District with additional reliable water supplies to supplement deliveries of Colorado River and State project water. The District is also actively pursuing other agreements, both within and outside its service area, to provide additional water supplies.

The exchange and storage agreements generally provide for advance delivery of water during periods when water is available. The reclamation project agreements effectively provide for District funding to local agencies for the construction of reclamation facilities that produce subpotable water for irrigational and industrial uses.

## NOTES TO FINANCIAL STATEMENTS (CONTINUED)

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Expenditures associated with these agreements have been recorded as deferred charges and are amortized to the cost of water as the rights are exercised. At June 30, 1993 and 1992, deferred water rights totalled approximately \$14,989,000 and \$20,654,000, respectively, based on volumes of 469,000 and 538,000 acre-feet, as of such dates. The reductions in amounts since June 30, 1992 resulted primarily from the termination of agreements with two member agencies.

### 8. Deferred Compensation and Savings Plans

For the benefit of its employees, the District has adopted and administers a deferred compensation plan in accordance with Section 457 of the Internal Revenue Code. Generally, eligible employees may defer receipt of a portion of their salary until termination, retirement, death or unforeseeable emergency. Until the funds are paid or otherwise made available to the employee, the employee is not obligated to report the deferred salary for income tax purposes.

All amounts of compensation deferred under the plan, all assets purchased with these amounts, and all income attributable to these amounts or assets (until paid or made available to the employee or other beneficiary) are solely the property of the District, subject to the claims of the District's general creditors. Participants' rights to deferred amounts under the plan are equivalent to those of the general creditors of the District. The District has no liability for losses under the plan, but does have the duty of due care that would be required of an ordinary prudent investor. The District believes it is highly unlikely that it will ever become necessary to use these assets to satisfy the claims of general creditors.

Deferred amounts under the plan are invested by the District's Treasurer. The monies are invested primarily in U.S. Treasury securities or guarantees and Federal Agency securities. Monies are also invested in the State Treasury Local Agency Investment Fund. At June 30, 1993 and 1992, such assets totalled approximately \$26,352,000 and \$24,079,000, respectively, including accrued interest of \$1,172,000 and \$602,000. Differences between the costs and market values of deferred compensation fund assets were not material at such dates.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

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The District also has adopted two compensation deferral arrangements in accordance with Section 401(k) of the Internal Revenue Code. Savings Plan I is available to management, confidential, and supervisory employees. Savings Plan II is available to employees represented by the MWD Employees Association. Taken together, the savings plans are available to substantially all employees. At June 30, 1993, 331 and 785 employees were participants in Plan I and Plan II, respectively. Amounts deferred by participants, District matching contributions, and accumulated earnings thereon are fully vested. Deferred amounts and matching contributions are transferred by the District each pay period to a third-party broker who invests such proceeds in a variety of investment vehicles in accordance with the instructions of each participant. An Assistant Director of Finance serves as Trustee for each plan. The District is not liable to its employees for any losses that may be incurred in connection with their participation in such plans.

Effective January 1, 1990, the District initiated a matching contribution program on behalf of each participating employee in Savings Plan I. This contribution amounts to 50 cents for each dollar contributed by the employee. The District's contribution is currently subject to a maximum of 3 percent of the total of the employee's total cash compensation.

Effective January 1, 1992, the District began a matching contribution program for each participating employee in Savings Plan II. This contribution amounts to 20 cents for each dollar contributed by the employee (to be increased to 25 cents in 1993), subject to a maximum of 2 and 3 percent of the employee's total cash compensation for the years beginning January 1992 and 1993 respectively.

Contributions to the Savings Plans by employees totalled \$4,018,000 and \$2,297,000 for fiscal 1993 and 1992, respectively. Matching contributions by the District totalled \$1,266,000 and \$650,000 for fiscal 1993 and 1992, respectively. Employee contributions represented 3.6 and 2.2 percent of the District's eligible payrolls of \$112,595,000 and \$104,143,000 for fiscal 1993 and 1992, respectively.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

The Metropolitan Water District  
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**9. Restricted Assets and Reserved Retained Earnings.**

The District has established a number of separate accounts (funds) to provide for specific activities in accordance with special regulations, bond covenants, trust arrangements, or Board policy. The funds are classified as either "restricted" or "unrestricted." Most restricted funds have minimum cash and investment balance requirements and all are nondiscretionary in terms of the use of fund assets. Among other things, the restricted funds provide for: payments of debt service on District bonds and commercial paper notes; reserves for principal and interest on outstanding bonds; payments for arbitrage tax rebate; construction of capital assets; payments of capital costs under the State Water Contract; payment of District operations and maintenance expenses; and payment of the costs related to the closure and post closure maintenance of the District's solid waste landfill facility at Iron Mountain. The cash and investments in the respective restricted funds are, in total, reflected as restricted assets for financial reporting purposes.

A portion of restricted assets relates to reserved retained earnings, which represent funds legally restricted for specific purposes. These balances are not available for appropriation for other purposes. As of June 30, 1993 and 1992, reserved retained earnings consists of the following amounts (in thousands):

	1993	1992
Reserved for revenue bond operations and maintenance	\$ 84,427	\$ 87,666
Reserved for revenue bond current debt service	53,129	23,642
Contingency reserve for revenue bonds	17,508	29,900
Reserved for payment of commercial paper notes	1,011	501
Reserved for purposes for which water standby charges are designated	50	—
Total reserved retained earnings	<u>\$ 156,125</u>	<u>\$ 141,709</u>

**10. Unrestricted Funds and Designated Unreserved Retained Earnings**

Unlike the restricted accounts (funds) (see Note 9), the Board of Directors has complete discretion in establishing the minimum cash and investment balance requirements in the various unrestricted accounts (funds) and in the uses of such

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

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assets. Cash and investments available for working capital purposes, exclusive of amounts on hand for pay-as-you-go construction and water rate and water treatment surcharge stabilization, totalled \$200,190,000 and \$130,004,000, at June 30, 1993 and 1992, respectively. Such amounts, which reflect the combined cash and investments in the revenue remainder and general funds, net of trust account balances, meet the minimum levels required at such dates as established by Board policy. At June 30, 1993, the minimum requirements for working capital purposes consisted of \$25 million for emergency repairs, casualty losses and claims, and \$150 million for general purposes in the event that revenues are insufficient to pay expenses. At June 30, 1992, minimum working capital requirements totalled \$130 million.

The District utilizes a water rate stabilization fund for the purpose of identifying amounts available, at the end of each fiscal year, to mitigate future water rate increases. The District also utilizes a water treatment surcharge stabilization fund for the purpose of identifying any treatment surcharge revenues in excess of water treatment costs, at the end of each fiscal year, to mitigate increases in future treatment charges. In fiscal 1989, the District established a pay-as-you-go fund to pay for certain capital expenditures on a current basis in lieu of using bond funds. As of June 30, 1993 and 1992, the cash and investments in these three funds totalled approximately \$163 million and \$197 million, respectively.

The Board retains the option to adjust or eliminate the amounts set aside as retained earnings designated for specific purposes. At June 30, 1993 and 1992, the following amounts, which represent the Board's tentative plans for future use of the assets of certain of the unrestricted funds, have been reflected as designated unreserved retained earnings for financial reporting purposes (in thousands):

	1993	1992
Designated for emergency repairs, casualty losses, and claims (see Note 11)	\$ 25,000	\$ 25,000
Designated for reduction of future water revenue requirements	98,056	146,764
Designated for reduction of future water treatment surcharges	—	—
Designated for pay-as-you-go capital expenditures	65,000	50,003
Total designated retained earnings	<u>\$ 188,056</u>	<u>\$ 221,767</u>

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

The Metropolitan Water District

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**11. Risk Management**

It is the District's policy to self-insure for District property loss and damage risks. Third-party liability coverage is maintained in excess of a self-insured retention. During the years ended June 30, 1992 and 1991, excess liability coverage of \$75 million was maintained in excess of a self-insured retention of \$25 million for each year. The third-party liability insurance program was renewed for fiscal 1993 at the same coverage and retention levels.

Workers' compensation insurance is maintained at \$10 million in excess of a self-insured retention of \$400,000. Other District insurance coverages include a comprehensive bond, aircraft liability, and other specialty coverage.