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METROPOLITAN WATER DISTRICT OF SOUTHERN CALIFORNIA

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October 17, 1994

To: (Special Audit Committee--Information)
Board of Directors(Finance & Insurance Committee--Information)

From: Auditor

Subject: Audited Comparative Financial Statements as of June 30, 1994 and 1993

Report

The District's audited comparative Financial Statements as of and for the years ended June 30, 1994 and 1993, 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.

Recommendation

For information only.

Michael W. Hondorp
Michael W. Hondorp

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Enclosure

FILED
by the Board of Directors of
The Metropolitan Water District
of Southern California
at its meeting held
NOV - 8 1994
Karen E. Tachiki
EXECUTIVE SECRETARY

Peat Marwick

Certified Public Accountants

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THE METROPOLITAN WATER DISTRICT OF SOUTHERN CALIFORNIA

FINANCIAL STATEMENTS

AS OF AND FOR THE YEARS ENDED
JUNE 30, 1994 AND 1993

(WITH INDEPENDENT AUDITORS' REPORT THEREON)

41176

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The Metropolitan Water District
of Southern California
June 30, 1994 and 1993

KPMG Peat Marwick LLP

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, 1994 and 1993 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, 1994 and 1993 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 LLP

August 26, 1994

FINANCIAL STATEMENTS

Balance Sheets

The Metropolitan Water District
of Southern California

June 30,	1994	1993
	(in thousands)	
ASSETS		
Current Assets:		
Cash and investments (Notes 3 and 10)	$ 490,393	$ 364,806
Receivables:		
Water sales	116,614	97,425
Annexation charges	7,734	7,832
Interest on investments	16,853	16,933
Other	22,094	7,023
Receivables	163,295	129,213
Inventories (at moving-average cost):		
Water in storage	4,674	5,694
Operating supplies	12,004	10,789
Inventories	16,678	16,483
Total current assets	670,366	510,502
Restricted cash and investments (Notes 3 and 9)	787,797	978,031
Plant and Equipment:		
Plant and equipment (Note 2)	2,888,060	2,565,236
Less accumulated depreciation and amortization	499,010	467,316
Total plant and equipment - net	2,389,050	2,097,920
Participation Rights:		
Participation rights in state water facilities (Notes 1 and 6b)	2,361,583	2,229,750
Participation rights in other facilities (Note 6b)	127,029	79,932
Participation rights	2,488,612	2,309,682
Less accumulated amortization	1,165,064	1,080,457
Total participation rights - net	1,323,548	1,229,225
Other Assets:		
Deposits, deferred charges and other (Note 7)	195,796	229,499
Annexation charges—noncurrent portion	26,019	31,833
Assets held for employees' deferred compensation (Notes 3 and 8)	28,332	26,352
Total other assets	250,147	287,684
Total Assets	$ 5,420,908	$ 5,103,362

See accompanying notes to financial statements.

June 30,	1994	1993
	(in thousands)	
LIABILITIES AND EQUITY		
Current Liabilities:		
Payable from current assets:		
Accounts payable and accrued expenses	$ 230,354	$ 190,448
Accrued compensated absences-current portion	11,419	9,594
Other	18,332	21,354
Payable from current assets	260,105	221,396
Payable from restricted assets:		
Commercial paper notes (Note 4)	60,000	60,000
Current portion of long-term debt	32,020	29,124
Accrued bond interest	46,760	48,799
Matured bonds and coupons not presented for payment	668	2,625
Customer deposits and trust funds	19,703	34,608
Current portion of obligation for off-aqueduct power facilities	3,309	3,124
Payable from restricted assets	162,460	178,280
Total current liabilities	422,565	399,676
Long-Term Liabilities:		
Long-term debt (Note 4)	2,006,972	2,034,603
Obligation for off-aqueduct power facilities (Note 6d)	145,355	147,919
Deferred compensation obligation (Note 8)	28,332	26,352
Accrued compensated absences (Note 1k)	8,585	8,684
Obligation for arbitrage tax rebate (Note 6j)	7,504	7,504
Total long-term liabilities	2,196,748	2,225,062
Total liabilities	2,619,313	2,624,738
Commitments and Contingencies (Notes 6 and 11)		
Equity:		
Contributions in aid of construction	32,297	30,518
Retained earnings:		
Reserved (Note 9)	150,883	156,125
Unreserved:		
Designated (Note 10)	313,625	188,056
Undesignated	2,304,790	2,103,925
Retained earnings	2,769,298	2,448,106
Total equity	2,801,595	2,478,624
Total Liabilities and Equity	$ 5,420,908	$ 5,103,362

Statements of Revenues and Expenses

The Metropolitan Water District
of Southern California

June 30,	1994	1993
	(in thousands)	
Operating Revenues:		
Water sales	$ 630,416	$ 544,266
Water standby charges (Note 1c)	50,000	23,661
Power recoveries	13,785	13,454
Total operating revenues	694,201	581,381
Operating Expenses:		
Power and water costs	94,022	123,270
Operations and maintenance	202,764	189,471
Other-net	590	598
Total operating expenses	297,376	313,339
Operating income before depreciation and amortization	396,825	268,042
Less depreciation and amortization	113,767	109,395
Operating income	283,058	158,647
Other Income (Expense):		
Taxes-net	68,904	78,606
Bond interest, net of $45,364 and $33,363 of interest capitalized in fiscal 1994 and 1993, respectively	(75,916)	(79,403)
Interest on investments	52,711	44,042
Other-net	(4,533)	18,041
Total other income - net	41,166	61,286
Income before extraordinary item	324,224	219,933
Extraordinary item - loss on defeasance of bonds (Note 4)	3,032	17,235
Net Income	$ 321,192	$ 202,698

See accompanying 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: Reserved	Retained Earnings: Unreserved: Designated	Retained Earnings: Unreserved: Undesignated	Total Equity
Balance at July 1, 1992	$ 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
Balance at June 30, 1993	30,518	156,125	188,056	2,103,925	2,478,624
Fiscal 1994 contributions in aid of construction	1,779	—	—	—	1,779
Increase in amounts designated for reduction of future water revenue requirements (Note 10)	—	—	96,928	(96,928)	—
Increase in amounts designated for reduction of future water treatment costs (Note 10)	—	—	4,211	(4,211)	—
Decrease in amounts reserved for revenue bonds and commercial paper note indenture requirements (Note 9)	—	(5,506)	—	5,506	—
Increase in amounts reserved for purposes for which the water standby charges are designated (Note 9)	—	264	—	(264)	—
Amounts designated for pay-as-you-go capital expenditures (Note 10)	—	—	24,430	(24,430)	—
Net income for fiscal 1994	—	—	—	321,192	321,192
Balance at June 30, 1994	$ 32,297	$ 150,883	$ 313,625	$ 2,304,790	$ 2,801,595

See accompanying notes to financial statements.

STATEMENTS OF CASH FLOWS

The Metropolitan Water District
of Southern California

Year Ended June 30,	1994	1993
	(in thousands)	
Cash Flows from Operating Activities:		
Operating Income (Loss)	$ 283,058	$ 158,647
Adjustments to reconcile operating income (loss) to net cash provided by operating activities:		
Depreciation and amortization	113,767	109,395
Increase in receivables	(29,018)	(11,583)
Decrease in inventories	735	1,310
Increase in prepaid expenses	(10,038)	(3,658)
(Decrease) increase in accounts payable	1,779	(5,922)
Other expense-net	(217)	3,560
Net Cash Provided by Operating Activities	360,066	251,749
Cash Flows from Capital and Related Financing Activities:		
Acquisition and construction of capital assets	(237,860)	(259,395)
Payments for participation rights in state water facilities	(149,347)	(170,078)
Payments for participation rights in other facilities	(9,433)	(28,021)
Proceeds from sale of revenue and general obligation bonds	166,294	977,398
Transfers to escrow trust accounts	(166,612)	(223,222)
Proceeds from tax levy	83,362	86,426
Principal and interest paid on bonds and commercial paper notes	(152,331)	(116,740)
Purchase of operating equipment	(4,512)	(2,513)
Other	(9,237)	20,014
Net Cash Provided by (Used for) Capital and Related Financing Activities	(479,676)	283,869
Cash Flows from Investing Activities:		
Purchase of investment securities	(18,455,151)	(19,971,968)
Proceeds from sales and maturities of investment securities	18,521,965	19,400,823
Interest on investments	52,796	35,081
Net Cash Provided by (Used for) Investing Activities	119,610	(536,064)
Net change in cash and cash equivalents	—	(446)
Cash and cash equivalents at beginning of year	—	446
Cash and Cash Equivalents at End of Year	$ —	$ —
Reconciliation of Cash and Investments to Cash and Cash Equivalents		
Unrestricted cash and investments	$ 490,393	$ 364,806
Restricted cash and investments	787,797	978,031
Employee deferred compensation fund	26,263	25,180
Total cash and investments	1,304,453	1,368,017
Less carrying value of investments and employee deferred compensation fund	1,304,453	1,368,017
Total Cash and Cash Equivalents	$ —	$ —

See accompanying notes to financial statements.

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 5,211 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 financial accountability for 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, and no single member agency has a voting majority.

(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 demand account balances, cash on hand and non-negotiable certificates of deposit. The District has elected to utilize the indirect method 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 revenues attributable to such charges must only be used for the following purposes:

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

A total of $23,678,831 of standby charge revenue and interest earnings was expended during fiscal 1993. Of this amount, 55% was used for SWP obligations, 15% for DVR, 9% for water system improvements, and 21% for water recycling and conservation programs.

In May 1993 and May 1994, the Board adopted water standby charges for fiscal 1994 and fiscal 1995, respectively in order to raise approximately $50 million from this source during each year. The per acre or smaller parcel rates for fiscal 1994 and fiscal 1995, which may vary by member agency, are composite rates of no more than $15 consisting of a $5 uniform component and a variable component, based on historic water use by member agency, of no more than $10.

A total of $49,377,299 of standby charge revenue and interest earnings was expended during fiscal 1994. Of this amount, 56% was used for SWP obligations, 28% for DVR, 5% for water system improvements and 11% for water recycling and conservation programs.

(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.

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, 1994 and 1993, annexation receivables of $33,753,000 and $39,665,000, respectively, including uncollected interest of $7,646,000 and $7,400,000, respectively, are not reflected as assets or included in the equity of the District.

(f) **Plant and Equipment.** District plant and equipment assets 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 22 percent and 27 percent of the District's total expenditures during fiscal 1994 and 1993, respectively, pertained to its net payment obligations for the state project. These payments are primarily based on contractual water delivery entitlements, the requested and actual deliveries received, and the cost of power required for such deliveries, offset by credits received from the project.

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 $82,712,000 and $81,081,000 in fiscal 1994 and 1993, 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 are 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 $1,235,000 and $827,000 was recorded in fiscal 1994 and 1993, respectively.

(i) **Participation Rights in South County Pipeline.** In 1989, the District entered into an agreement with two member agencies and one of their subagencies to participate in the construction of an upsized version of a 26 mile long pipeline, serving the South Orange County portion of its service area (South County Pipeline). The District paid $40,537,000 prior to June 30, 1994 for its pro-rata share of pipeline construction costs. At such date, the District remains obligated to pay a capacity share, totalling $24,381,000 including interest, by September 1, 1994 for the subagency-owner of the South County Pipeline. These participation rights are amortized using the straight-line method over 80 years. Amortization expense of $651,000 and $562,000 was recorded in fiscal 1994 and 1993, respectively.

(j) **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.

(k) **Compensated Absences.** The District's employees earn vacation, sick and compensatory leave in varying amounts depending primarily on length of service. Upon termination from District service, employees are entitled to full payment for accrued vacation and compensatory leave at their final pay rates, and are entitled to payment for one half of their accrued sick leave at such rates. The District records its obligations for vacation, sick, and compensatory leave when earned by eligible employees based on current pay rates at the time. The allocations to the current and long-term portions of these vested obligations are based on experience and projections of turnover. Accrued compensated absences current portion $11,419,000 and $9,594,000 and long-term portion of $8,585,000 and $8,684,000 was recorded at June 30, 1994 and 1993, respectively. The increase in the current portion of the fiscal 1994 compensated absences liability over the 1993 balance results primarily from the additional cash payoff expected in late 1994 due to the implementation of an early retirement program. (See Note 5a)

2. Plant and Equipment

At June 30, 1994 and 1993, plant and equipment (at cost) consists of the following (in thousands):

	1994	1993
Land, easements, and rights of way	$ 287,656	$ 180,120
Parker Power Plant and Dam	13,009	13,009
Power recovery plants	125,139	103,123
Other dams and reservoirs	103,385	103,385
Water transportation facilities	979,983	984,826
Pumping plants and facilities	71,779	71,802
Treatment plants and facilities	293,786	293,934
Power lines and communication facilities	14,430	14,430
Computer systems software	700	700
Miscellaneous	48,544	47,840
Construction in progress	824,908	639,435
Major equipment	80,146	68,037
Pre-operating interest and other expenses of original aqueduct	44,595	44,595
	2,888,060	2,565,236
Less accumulated depreciation and amortization	499,010	467,316
Total plant and equipment — net	$ 2,389,050	$ 2,097,920

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 completion of reimbursement to the United States for the cost of the aqueduct. Title to Parker Power Plant and Dam and surrounding land is also vested in the United States government. However, the District is entitled in perpetuity to approximately one-half of the energy generated at the power plant and to certain water diversion rights from the reservoir.

3. Cash and Investments

As a public agency, the District's investment practices are prescribed by various provisions of the California Government Code and the Act, as well as by administrative policies. Cash and investments may or may not be restricted as to use, depending on the specific purposes for which such assets are held (see Notes 9 and 10).

The District's statement of investment policy describes the Treasurer's investment authority, practices and limitations. The basic investment policy has as its objectives, in order of importance: safety of principal, liquidity, and return on investment.

A summary of the District's deposit and investment policies and information on credit or market risks follows:

(a) **Deposits.** The balances per bank of the District's demand deposits and certificates of deposit, as categorized by credit risk, are shown below (in thousands):

June 30,	1994	1993
Amount insured by the FDIC and the NCUA	$ 200	$ 200
Amount collateralized with pooled securities held by the District's bank's trust department	8,453	8,378
Total balance per bank	$ 8,653	$ 8,578

The carrying amounts of the District's cash and demand deposits at June 30, 1994 and 1993 are disclosed in the table of Cash and Investments on page 15.

The District's demand and time deposits are fully insured or collateralized. Such deposits are covered by federal depository insurance up to a maximum of $100,000 per financial institution; deposits in excess of this limit are collateralized by pooled securities held by the financial institution on behalf of the District and other public agencies, as required by State law. State law requires public agency deposits, including time deposits, in excess of insured levels to be collateralized by the depository institutions with pooled government securities having market values of at least 110 percent of the deposits. To ensure compliance with the 110 percent

Cash and Investments
(in thousands)

	June 30, 1994					June 30, 1993	
	Category			Carrying	Market	Carrying	Market
	1	2	3	Amount	Value	Amount	Value
U.S. Treasury securities	$ 394,071	$ —	$ —	$ 394,071	$ 392,579	$ 388,886	$ 397,259
U.S. Treasury securities held for crossover refunding bonds	227,938	—	—	227,938	227,938	228,632	228,632
U.S. Guarantees - GNMAs	2,990	—	—	2,990	3,153	6,299	6,907
Federal agency securities	150,635	—	—	150,635	148,940	195,248	195,800
State agency securities	35	—	—	35	37	35	35
Bankers' acceptances	1,972	—	—	1,972	1,976	70,908	71,037
Prime commercial paper	166,200	—	—	166,200	166,209	177,031	177,132
Negotiable certificates of deposit	25,821	—	—	25,821	25,821	53,522	53,522
Repurchase agreements	247,791	—	—	247,791	251,876	232,456	231,086
Total	$ 1,217,453	$ —	$ —	1,217,453	1,218,529	1,353,017	1,361,410
Local agency investment fund - State of California				87,000	87,000	15,000	15,000
Total investments				1,304,453	$ 1,305,529	1,368,017	$ 1,376,410
Add:							
Cash/demand deposits				(100)		(100)	
Time certificate of deposit				100		100	
Total cash				—		—	
Total cash and investments				1,304,453		1,368,017	
Less:							
Restricted cash and investments				787,797		978,031	
Employee deferred compensation fund (Note 8)				26,263		25,180	
Unrestricted cash and investments				$ 490,393		$ 364,806	

requirement, the collateral must be marked to market at least monthly by the bank. The District's investment policy does not permit real estate mortgages or mortgage-backed securities to qualify as acceptable collateral in these pools.

(b) **Investments, including Repurchase Agreements.** The District is permitted by State law and Board policy to invest in a variety of instruments including U.S. Treasury, federal agencies, repurchase agreements, and other securities (including negotiable certificates of deposit, bankers' acceptances, and prime commercial paper). All investments are subject to various limitations and restrictions. In the case of money market instruments issued by private entities, risk is controlled by strict eligibility requirements and duration limitations. All securities purchased are delivered against payment and are held in safekeeping on the District's behalf by the trust department of the bank used by the District.

In accordance with Governmental Accounting Standards Board Statement No. 3 (GASB 3) criteria, the District's credit risk on investments is categorized in the table of Cash and Investments on page 15 as follows: Category 1 consists of investments that are insured or registered, or for which the securities are held by the District or its agent in the District's name. Category 2 would consist of securities that are uninsured and unregistered and held by the counter-party's trust department or by its agent in the District's name. Category 3 would consist of securities that are uninsured and unregistered and held by the counter-party, its trust department, or its agent, but not held in the District's name. Deposits in investment pools managed by other governments, such as the District's investments in the State Treasury Local Agency Investment Fund, are not subject to categorization under GASB 3 guidelines.

(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, 1994 and 1993.

(d) **Investments in Escrow Trust Deposits.** At June 30, 1994 and 1993, U.S. Treasury securities costing $248,240,000 and $294,445,000, 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.

In addition, at June 30, 1994 and 1993, U.S. Treasury Securities costing \$227,938,000 and \$228,632,000 respectively, were held in irrevocable trust accounts for debt service on the Waterworks General Obligation Refunding Bonds of 1993, Series A1 and A2, through the Crossover Dates and thereafter to refund the Crossover Prior Bonds (see Note 4).

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 \$2.039 billion represents only a fraction of one percent of the 1994-95 taxable assessed valuation of \$887.4 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 are expected to 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, of which \$60 million were sold and outstanding at June 30, 1994 and 1993. 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.

(b) **General Obligation Bonds.** In 1966 voters authorized the District to incur up to \$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, 1994 and 1993. The District has advance refunded some of these general obligation bond issues through the issuance of refunding bonds. A total of $871,395,000 and $889,605,000 in general obligation bonds and refunding general obligation bonds was outstanding at June 30, 1994 and 1993, respectively.

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 the earliest applicable call date are subject to optional redemption prior to maturity, callable on interest payments dates and subject to early redemption premiums.

No general obligation bonds were issued during the years ended June 30, 1994 and 1993 to finance construction of improvements and works of the District.

(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. A total of $1,779,400,000 and $1,689,805,000 of revenue bonds and revenue refunding bonds had been issued under the 1974 authorization, of which $1,200,350,000 and $1,207,400,000 remain outstanding at June 30, 1994 and 1993, respectively.

Each revenue bond issue consists of both serial and term bonds which mature in varying amounts through 2023 at interest rates ranging from 2.63 percent to 8.00 percent. The term bonds are subject to mandatory redemption prior to maturity. All revenue bonds maturing on or after the earliest applicable call date are subject to optional redemption prior to maturity, callable on interest payments dates and subject to early redemption premiums.

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 and maturities, with final maturity in July 2022. No revenue bonds were issued during the year ended June 30, 1994 to finance construction of improvements and works of the District.

(d) **Bond Refundings and Defeasances.** During the years ended June 30, 1994 and 1993, as well as in prior years, the District issued Waterworks General Obligation Refunding Bonds and Water Revenue Refunding Bonds to advance refund various issues of Waterworks General Obligation Bonds, Water Revenue Bonds and Water Revenue Refunding Bonds Previously issued. The net proceeds from these sales, after payment of underwriters fees, original issue discount (premium) and other issuance costs, together with certain amounts of debt service and reserve funds of the bonds being refunded, were used to purchase U.S. Treasury securities which were deposited in irrevocable escrow trust accounts with a bank acting as an independent fiscal agent to provide for all future debt service on the bonds being refunded. As a result, those bonds are considered defeased; accordingly, the liability for those bonds, as well as the related investments in the irrevocable trust accounts, have been excluded from the District's financial statements.

These refundings were accomplished to take advantage of the current lower interest rates available to tax exempt issuers. However, in accordance with generally accepted accounting principles, the District recognized accounting losses, which represent the differences between the present value of the reacquisition prices and the net carrying amount of the old debt on the date of defeasance. It is estimated that such refundings will result in a net reduction in the District's aggregate debt service payments over the life of the refunding issues and will result in an economic gain (difference between the present value of the old and new debt service payments).

Refunding transactions during the years ended June 30, 1994 and 1993 were as follows:

Year ended June 30, 1994

- On July 22, 1993, the District issued $78,290,000 of Waterworks General Obligation Refunding Bonds, 1993 Series B, at a true interest cost of 5.49 percent, to advance refund $75,000,000 of outstanding General Obligation Bonds, Election of 1966 Series D. The net proceeds of $77,563,000 (net of $724,000 in underwriters fees, original issue discounts and other issuance costs) was used to purchase escrow securities. Although the transaction resulted in an accounting loss of $1,042,000, the estimated economic gain from the transaction was $2,671,000 resulting from an estimated net reduction in aggregate debt service over the life of the issue of $4,887,000.

- On July 22, 1993, the District issued $89,595,000 of Water Revenue Refunding Bonds, 1993 Series B, at a true interest cost of 5.39 percent, to advance refund $21,170,000 of outstanding Water Revenue Refunding Bonds, Series 1978 and $66,075,000 of outstanding Water Revenue Bonds, Series 1979. The net proceeds of $89,048,000 (net of $887,000 of underwriters fees, original issue discounts and other issuance costs) was used to purchase escrow securities. Although the transaction resulted in an accounting loss of $1,990,000, the estimated economic gain from the transaction was $3,219,000 resulting from an estimated net reduction in aggregate debt service over the life of the issue of $6,373,000.

Year ended June 30, 1993

- On February 12, 1993, the District issued $279,735,000 of Waterworks General Obligation Refunding Bonds, consisting of $138,085,000 of 1993 Series A1 Bonds, $87,315,000 of 1993 A2 Bond and $54,335,000 of 1993 Series A3 Bonds, at a true interest cost of 5.37 percent. 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 estimated economic gain from the transaction was $10,288,000 resulting from an estimated net reduction in aggregate debt service over the life of the issue of $17,201,000. Also as a result of transaction an accounting loss of $671,000 was recognized for the Series A3 Bonds. The net proceeds of $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) was used to purchase escrow securities.

The escrow securities purchased from proceeds of the Crossover Bonds (Crossover Trust Account) will be used to pay all debt service of 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.

- On February 12, 1993, the District issued $168,760,000 of Water Revenue Refunding Bonds, 1993 Series A, at a true interest cost of 5.85 percent, to advance refund $42,850,000 of outstanding Waterworks Refunding Revenue Bonds, Issue of 1986, and $110,930,000 of outstanding Water Revenue Bonds, Issue of 1991. The net proceeds of $165,338,000 (net of $2,922,000 in underwriters fees, original issue discounts and other issuance costs) plus an additional $2,699,000 of debt service and reserve funds of the bonds being refunded was used to purchase escrow securities. Although the transaction resulted in an accounting loss of $16,564,000, the estimated economic gain from the transaction was $7,600,000 resulting from an estimated net reduction in aggregate debt service over the life of the issue of $18,389,000.

The total of all original bonds considered defeased and, accordingly, excluded from the the District's financial statements, which remain outstanding at June 30, 1994 and 1993, is $236,000,000 and $278,000,000, respectively. The related investments in irrevocable trust accounts total $248,240,000 and $294,445,000 at June 30, 1994 and 1993, respectively.

(e) **Forward Interest Swap Commitment.** On January 24, 1994, the District entered into a forward interest rate (swap) commitment to refund up to $109,930,000 of Waterworks Refunding Revenue Bonds, Issue of 1986, on the call date of June 1, 1996. The District has agreed to issue $108,375,000 of Water Revenue Refunding Bonds, 1996 Series A, as variable rate bonds in 1996 and has agreed to pay a fixed rate, starting when the bonds are issued, to a third party under the forward swap over the life of the bonds, which are scheduled to mature in 2023. Financial Products Corp., a wholly owned subsidiary of AAA-rated American International Group, Inc., will assume the variable rate exposure on the District's refunding bonds. The forward interest rate commitment was accomplished to take advantage of lower interest rates then available to tax exempt bond issuers. At current rates the gross savings over the life of the bond issue would be approximately $16,464,000 (net of $537,000 in underwriters fees, liquidity and bond insurance guarantees, original issue discount (premium) and other bond issuance costs), but will vary according to day-to-day forward swap quotes which will reflect the duration of the transaction, the level of tax exempt rates, and their relationship to taxable rates.

(f) **Long-term Debt Obligation Summary.** Interest rates on all outstanding bond obligations range from 2.25 percent to 8.5 percent. Future principal and interest obligations on the currently outstanding issues are (in thousands):

Due in fiscal year ending June 30,	Principal	Interest	Total
1995	$ 32,020	$ 104,085	$ 136,105
1996	42,210	102,224	144,434
1997	33,619	99,070	132,689
1998	47,110	96,734	143,844
1999	49,460	94,399	143,859
Later years	1,642,126	1,198,120	2,840,246
	$ 1,846,545	$ 1,694,632	$ 3,541,177
Crossover Refunding Bonds	225,400		
Less unamortized bond discount, net	(32,953)		
Total long-term debt	$ 2,038,992		
Less current portion	32,020		
Long-term portion of debt	$ 2,006,972		

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 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%
Waterworks general obligation refunding bonds series B-1993	3/1/95—3/1/20	3.20%—5.55%
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 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%
Water revenue refunding bonds 1993 series B	7/1/94—10/30/20	2.625%—5.55%
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		

June 30, 1993	Additions	Less Maturities, Defeasances and (Amortization)	June 30, 1994
$ 250	$ —	$ 250	$ —
517,425	—	86,765	430,660
92,195	—	850	91,345
279,735	—	6,910	272,825
—	78,290	1,725	76,565
889,605	78,290	96,500	871,395
120,450	—	21,170	99,280
66,975	—	66,975	—
115,800	—	1,840	113,960
185,415	—	3,830	181,585
550,000	—	—	550,000
168,760	—	535	168,225
—	89,595	2,295	87,300
1,207,400	89,595	96,645	1,200,350
354	—	154	200
(33,632)	(1,592)	(2,271)	(32,953)
$ 2,063,727	$ 166,293	$191,028	$ 2,038,992

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. Effective July 3, 1994, the District will begin contributing a 3 percent portion of the compensation of all Management and Professional Employees Association employees.

The District's payroll covered by PERS totalled approximately $115.0 million and $109.7 million, respectively, for the years ended June 30, 1994 and 1993. Total payrolls for the same two periods were $124.9 million and $120.7 million, respectively.

On July 12, 1994 the District's Board of Directors approved an early retirement program for eligible employees which provided two years additional service credit in PERS and a cash component, payable in three annual installments, equivalent to approximately the value of an additional two years of service credit in PERS. Of the District's 2,050 full-time emloyees, about 8 percent, or 166 employees, have elected to take advantage of the program. The projected cost for the additional PERS service credit component is approximately $4.3 million, and the projected cost to provide the cash payments component is approximately $5.7 million. Implementation of the early retirement program is expected to reduce salaries and benefits by approximately $14 million over the next 18 months, thereby providing the district with a net savings of about $4 million over the estimated cost of $10.0 million.

(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.

The latest pension benefit obligation information available is as of June 30, 1992 and was computed as part of actuarial valuations performed as of that date, but which reflect all plan amendments adopted through June 30, 1993. 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
Pension benefit obligation:	
Retirees and beneficiaries receiving benefits and terminated employees not receiving benefits	$ 124,408
Current employees:	
Accumulated employee contributions, including allocated investment earnings	78,780
Employer-financed vested	116,501
Employer-financed nonvested	4,640
Total pension benefit obligation	324,329
Less: Net assets available for benefits—at cost or amortized cost (market values of $374,154 at June 30, 1992)	331,697
Unfunded (assets in excess of) pension benefit obligation	$ (7,368)

(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.

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 1994 and 1993 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:	1994 Amount	1994 Percentage of Covered Payroll	1993 Amount	1993 Percentage of Covered Payroll
Normal cost	$ 8,239	7.0%	$ 8,759	8.0%
Contributions on behalf of employees hired before 1/1/81	997	0.9	1,015	0.9
Total contributions	$ 9,236	7.9%	$ 9,774	8.9%

District employees contributed $8,050,000 (representing 7 percent of covered payroll) and $7,685,000 (representing 7 percent of covered payroll) during fiscal 1994 and 1993, 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 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)
1993	N/A	N/A	N/A	N/A	109,700	N/A
1994	N/A	N/A	N/A	N/A	115,000	N/A

N/A = Information is not available as of June 30, 1994.

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 1994, 1993, and 1992, the District's contributions to the system, all made in accordance with actuarially determined requirements, were 7.9 percent, 8.9 percent and 9.8 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 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,	
1995	$ 311,489
1996	323,222
1997	333,304
1998	330,860
1999	326,629

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	$ 1,826,744
Transportation facilities	5,154,331
Off-aqueduct power facilities (See Note 1g)	1,252,691
Revenue bond surcharge	505,783
East Branch enlargement	908,946
Total long-term SWP contract obligations	$ 9,648,495

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 $149 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 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, 1994, the District had advanced to IID a total of $116.3 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 $26.5 million for construction, and approximately $7.0 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 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, 1994, 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
1995	$ 3,309	$ 9,901	$ 13,210
1996	3,560	9,681	13,241
1997	3,844	9,444	13,288
1998	4,107	9,187	13,294
1999	4,427	8,914	13,341
Later years	129,417	90,679	220,096
Total long-term obligation	148,664	$ 137,806	$ 286,470
Less current portion	3,309		
Long-term portion of obligation	$ 145,355		

(e) **Construction Programs and Contracts.** At June 30, 1994, the estimated cost of the District's planned construction program through fiscal year 2002 totalled approximately $5.6 billion, including escalations for inflation of 5.5 percent per year. The program includes the estimated costs of facilities which may be required to meet 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, 1994 and 1993, totalling approximately $73,701,000 and $56,931,000, respectively, for rehabilitation of its aqueduct system and expansion of its distribution and storage system.

Major projects in design and/or construction during fiscal year 1994 included the Domenigoni Reservoir, Inland Feeder, San Diego Pipeline No. 6, Central Pool Augmentation Tunnel, and Pipeline, replacement of Type "M" flowmeters, Jensen Plant Expansion No. 1, Mills Filtration Plant Expansion No. 2, chemical spill containment, replacement of area control systems, Etiwanda Power plant, and the desalination demonstration project.

(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.

In April 1994, the Board of Directors selected Union Station as the preferred site for the development of the District's long-term administrative headquarters. The Board also authorized management to enter into a letter of intent with Catellus Development Corporation pertaining to the final development agreement for the headquarters project which was signed on May 9, 1994. The board's action clears the way for final negotiations to begin on project costs, building design, construction timelines and other development matters. Preliminary plans call for construction of a building of approximately 500,000 square feet to begin in the first quarter of 1997, with move-in anticipated sometime in early 1999.

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 $8,121,000 and $2,287,000 for fiscal 1994 and 1993, respectively. Rent expense for fiscal 1994 was significantly higher than 1993 due to the move of the administrative headquarters from a District-owned facility to leased office space in downtown Los Angeles pending construction of the new headquarters. The former headquarters site will be offered for sale.

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, 1994 (in thousands).

Fiscal year ending June 30	
1995	$ 11,444
1996	11,678
1997	11,642
1998	11,778
1999	11,918
Later Years	7,669
Total Minimum Payments Required	$ 66,129

(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 762 and 733 retired District employees at June 30, 1994 and 1993, respectively, and are paid from operating revenues on a current basis. During fiscal years 1994 and 1993, the District paid $2,402,000 and $2,184,000, 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 and will be lowered again in a second stage in the early 2000s. 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, ozone or PEROXONE technology will be phased in at each of the District's treatment plants by 2003 to meet the deadline for complying with the second stage of the DBP standards. 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, 1994 and 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, 1994 and 1993, the District has recorded arbitrage rebate liabilities presently estimated at $7,504,000. 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. In August 1994, in accordance with U.S. Treasury regulations, the District paid $5,753,900 to the IRS.

(k) **Landfill.** In compliance with the State of California law as an operator of a solid waste landfill facility at its Iron Mountain Pumping Plant, the District is subject to the regulatory requirements of Section 66796.22 of the Government Code, adopted in 1987, as amended in 1988. This statute requires landfill operators to evidence their financial ability to pay the costs of closure and postclosure maintenance of their respective facilities.

In August 1989, the California Integrated Waste Management Board issued amended regulations. Accordingly, the District was required to establish a separate funding mechanism to insure that sufficient monies would be available to pay the estimated costs of closure and postclosure maintenance of its solid waste site. The engineering estimate of the costs (in 1990 dollars) for the closure in the year 2030 and for the postclosure period ending in the year 2045 was $3.4 million

In 1990 the District established a trust fund, the Iron Mountain Landfill Closure/Postclosure Maintenance Fund, in the amount of $3.4 million which is adjusted annually for inflation for closure and postclosure maintenance of the facility. At June 30, 1994 and 1993 the balances of this fund were 4,093,000 and 4,000,000, respectively.

As of June 30, 1994, sixty-two percent of the Iron Mountain Landfill capacity (20,000 cubic yard) was filled. The estimated remaining landfill life is about thirty-six years.

(l) **Joint Ventures and Purchases.** The District is completing an agreement with a member agency to purchase a pipeline in Orange County called the Allen-McColloch Pipeline (AMP) to provide additional service to member agencies. Under the terms of the proposed agreement the first payment of principal and interest, to be paid in October, 1994, will be approximately $11,500,000. During Fiscal 1995 the District will commence annual payments of $4.6 million for the next thirteen years, which are equivalent to the remaining debt obligation on AMP. The District will also pay approximately $3.0 million annually for the next twenty-three years for the remaining debt obligation already incurred for the pipeline Flow Augmentation Project that began in 1989.

The District will pay the maintenance costs of the AMP, except for energy costs at Pump Station ST-21. These maintenance costs are estimated at approximately $1.2 million annually through June 30, 2000. Effective July 1, 2000, all operation and maintenance costs will then be assumed by the District. During fiscal 1995, the District will assume control of the AMP and ownership of the pipeline capacity. On July 1, 2016, the District will assume full ownership of the system facilities.

The District entered into a trust agreement effective July 1, 1980 for the San Joaquin Reservoir for a term of 60 years. The purpose of the trust is to provide for the ownership, manner of use, maintenance and operation, and improvement and repairs consisting of certain real property, a water reservoir, and certain pipeline facilities and appurtenances connecting such facility to the facilities of the District and other agencies.

The District's ownership of 9.84% was allocated at no buy-in cost in consideration of the District's agreement to operate and maintain the reservoir. The District though must participate in payments and expenses based on it's percentage of ownership throughout the agreement.

It is anticipated that a floating cover will be constructed to cover the San Joaquin Reservoir at an estimated cost of $18.2 million within the next two years. When the construction is completed the percentage of ownership for the District in the reservoir will increase to more than 50%.

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.

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, 1994 and 1993, deferred water rights totalled approximately $18,020,000 and $14,989,000, respectively, based on volumes of 576,000 and 469,000 acre-feet, as of such dates. The increase in amounts since June 30, 1993 resulted primarily from transfer and exchange programs with Areias Diary Farms from the Central Valley Project, the Semitropic Water Storage District in Kern County and the Central Arizona Water Conservation District with storage in Lake Mead.

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, 1994 and 1993, such assets totalled approximately $28,332,000 and $26,352,000, respectively, including accrued interest of $2,069,000 and $1,172,000. Differences between the costs and market values of deferred compensation fund assets were not material at such dates.

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, 1994 and 1993, respectively, 368 and 331 employees were participants in Plan I and 995 and 785 employees were participants in Plan II for such years. 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. The 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.

The District has established 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.

The District has established a matching contribution program for each participating employee in Savings Plan II. This contribution amounts to 50 and 25 cents for each dollar contributed by the employee for years 1994 and 1993, respectively.

Contributions to the Savings Plans by employees totalled $4,796,000 and $4,018,000 for fiscal 1994 and 1993, respectively. Matching contributions by the District totalled $1,780,000 and $1,266,000 for fiscal 1994 and 1993, respectively. Employee contributions represented 4.1 and 3.6 percent of the District's eligible payrolls of $116,886,000 and $112,595,000 for fiscal 1994 and 1993, respectively.

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 postclosure 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, 1994 and 1993, reserved retained earnings consists of the following amounts (in thousands):

	1994	1993
Reserved for revenue bond operations and maintenance	$ 89,493	$ 84,427
Reserved for revenue bond current debt service	45,589	53,129
Contingency reserve for revenue bonds	14,453	17,508
Reserved for payment of commercial paper notes	1,034	1,011
Reserved for purposes for which water standby charges are designated	314	50
Total reserved retained earnings	$ 150,883	$ 156,125

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 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 $201,636,000 and $200,190,000, at June 30, 1994 and 1993, 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, 1994 and 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.

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. The District has also 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, 1994 and 1993, the cash and investments in these three funds totalled approximately $288,625,000 and $163,000,000, respectively.

The Board retains the option to adjust or eliminate the amounts set aside as retained earnings designated for specific purposes. At June 30, 1994 and 1993, 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):

	1994	1993
Designated for emergency repairs, casualty losses, and claims (see Note 11)	$ 25,000	$ 25,000
Designated for reduction of future water revenue requirements	194,984	98,056
Designated for reduction of future water treatment surcharges	4,211	—
Designated for pay-as-you-go capital expenditures	89,430	65,000
Total designated retained earnings	$ 313,625	$ 188,056

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, 1994 and 1993, 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 1995 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.