



NOTES TO THE BASIC FINANCIAL STATEMENTS

JUNE 30, 2004

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The City of Monterey, California was incorporated in 1850 as a charter city and operates under the Council-Manager form of government. The City provides the following services: public safety (police, fire and building inspection), highways and streets, sewer collection, leisure services, public improvements, planning and zoning, redevelopment and general administration services.

A. Reporting Entity

The financial statements of the City of Monterey include the financial activities of the City as well as separate legal entities which are controlled by and dependent on the City. The City Council serves as the governing board of the Redevelopment Agency of the City of Monterey (the "Agency") and the City of Monterey Joint Powers Financing Authority (the "Authority"), a joint powers authority between the City and the Agency. These financial activities are controlled entirely by the City, which also performs all their administrative and accounting functions. Therefore, the financial activities of these Component Units have been aggregated and merged (termed "blended") with those of the City in the accompanying general purpose financial statements. Financial statements for the Agency and the Authority may be obtained from the City of Monterey, Monterey, California, 93940.

The Agency prepares and implements plans for improvement, rehabilitation, and development of certain areas within the City. The financial activities of the Agency have been included in these financial statements in the Low and Moderate Income Housing Special Revenue Fund, and the Capital Projects Fund, the Debt Service Fund.

The Authority assists with the financing or refinancing of certain public capital facilities in the City. The financial activities of the Authority are not significant and are included in the Enterprise Funds.

B. Basis of Presentation

The City's Basic Financial Statements are prepared in conformity with accounting principles generally accepted in the United States of America. The Government Accounting Standards Board is the acknowledged standard setting body for establishing accounting and financial reporting standards followed by governmental entities in the U.S.A.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Government-wide Statements: The Statement of Net Assets and the Statement of Activities display information about the primary government. These statements include the financial activities of the overall City government, except for fiduciary activities. Eliminations have been made to minimize the double counting of internal activities. These statements distinguish between the *governmental* and *business-type activities* of the City. Governmental activities generally are financed through taxes, intergovernmental revenues, and other nonexchange transactions. Business-type activities are financed in whole or in part by fees charged to external parties.

The Statement of Activities presents a comparison between direct expenses and program revenues for each segment of the business-type activities of the City and for each function of the City's governmental activities. Direct expenses are those that are specifically associated with a program or function and, therefore, are clearly identifiable to a particular function. Program revenues include (a) charges paid by the recipients of goods or services offered by the programs, (b) grants and contributions that are restricted to meeting the operational needs of a particular program and (c) fees, grants and contributions that are restricted to financing the acquisition or construction of capital assets. Revenues that are not classified as program revenues, including all taxes, are presented as general revenues.

Fund Financial Statements: The fund financial statements provide information about the City's funds, including fiduciary funds and blended component units. Separate statements for each fund category—*governmental*, *proprietary*, and *fiduciary*—are presented.

Proprietary fund *operating* revenues, such as charges for services, result from exchange transactions associated with the principal activity of the fund. Exchange transactions are those in which each party receives and gives up essentially equal values. *Nonoperating* revenues, such as subsidies and investment earnings, result from nonexchange transactions or ancillary activities.

C. Major Funds

The emphasis of fund financial statements is on major individual governmental and enterprise funds, each of which is displayed in a separate column. All remaining governmental and enterprise funds are aggregated and reported as nonmajor funds in a single column, regardless of their fund-type.

Government Accounting Standards Board Statements No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments* defines major funds as those that have either assets, liabilities, revenues or expenditures/expenses equal to ten percent of their fund-type total and five percent of the grand total. The General Fund is always a major fund. The City may also select other funds it believes should be presented as major funds. No other funds have been selected.

The City reported the following major governmental funds in the accompanying financial statements:

General Fund – It is the primary operating fund of the City. It is used to account for all financial resources except those required to be accounted for in another fund. The major revenue sources of this fund include transient occupancy tax, property tax, sales tax, business license tax, utility users tax and charges for services. These revenues support the general operations of the City, which

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

include police, fire, street maintenance, parks, recreation, planning and general government. In addition, the General Fund finances many capital improvements each year.

Capital Projects Fund – It is used to account for the financial resources used for the acquisition or construction of major capital facilities (other than those financed by proprietary fund types). The City maintains one Capital Projects Fund, which is shown on the Combined Balance Sheet and the Combined Statement of Revenues, Expenditures and Changes in Fund Balances.

The City reported the following enterprise funds as major funds in the accompanying financial statements:

Marina Fund – This fund was created in 1960 to account for all Marina related revenues and expenditures. All revenues collected in the Marina area are used for operation, maintenance and improvements to the Marina.

Parking Fund – This fund was established to pay for construction, operation, and maintenance of parking facilities and improvements. The revenue sources include parking fees, permits and fines.

Presidio of Monterey Public Works Fund – This fund was created in fiscal year 1998-99 to account for costs and revenues pertaining to the Presidio of Monterey maintenance contract.

The City also reports the following fund types:

Internal Service Funds. These funds are established to finance and account for services and commodities furnished by designated department or agency to other departments and agencies within a single governmental unit, or to other governmental units, all of which are provided to other departments on a cost-reimbursement basis. These funds account for automotive services, automotive replacement, data processing and other information services, worker's compensation, and general liability.

Fiduciary Funds. Private-Purpose Trust Funds, Pension Trust Funds and Agency Funds are used to account for assets held by the City as an agent for individuals, private organizations, and other governments. The City contains only Agency fund transactions, whose financial activities are excluded from the Government-wide financial statement, but are presented in separate Fiduciary Fund financial statements.

D. *Basis of Accounting*

The government-wide, proprietary, and fiduciary fund financial statements are reported using the *economic resources measurement focus* and the full *accrual basis* of accounting. Revenues are recorded when *earned* and expenses are recorded at the time liabilities are *incurred*, regardless of when the related cash flows take place.

Governmental funds are reported using the *current financial resources* measurement focus and the *modified accrual* basis of accounting. Under this method, revenues are recognized when *measurable* and *available*.

The City considers all revenues reported in the governmental funds to be available if the revenues are collected within sixty days after year-end. Expenditures are recorded when the related fund liability is incurred, except for claims and judgments, compensated absences, which are recognized as expenditures to the extent they have matured, and principal and interest on general

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

long-term debt. Financial resources usually are appropriated in other funds for transfer to the debt service fund in the period in which maturing debt principal and interest must be paid. Such amounts are not current liabilities of the debt service funds as their settlement will not require expenditure of existing fund assets.

Governmental capital asset acquisitions are reported as *expenditures* in governmental funds. Proceeds of governmental long-term debt and acquisitions under capital leases are reported as *other financing sources*.

Those revenues susceptible to accrual are property and franchise taxes, licenses, certain other intergovernmental revenues, certain charges for services and interest revenue. Sales taxes collected and held by the State at year end on behalf of the City also are recognized as revenue.

Non-exchange transactions, in which the City gives or receives value without directly receiving or giving equal value in exchange, include taxes, grants, entitlements, and donations. On the accrual basis, revenue from taxes is recognized in the fiscal year for which the taxes are levied or assessed. Revenue from grants, entitlements, and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied.

The City may fund programs with a combination of cost-reimbursement grants, categorical block grants, and general revenues. Thus, both restricted and unrestricted net assets may be available to finance program expenditures. The City's policy is to first apply restricted grant resources to such programs, followed by general revenues if necessary.

Certain indirect costs are included in program expenses reported for individual functions and activities.

The City follows Statements and interpretations of the Financial Accounting Standards Board and its predecessors that were issued on or before November 30, 1989, in accounting for its business-type activities, unless they conflict with Government Accounting Standards Board pronouncements.

E. Budgets and Budgetary Accounting

The City follows these procedures in establishing the operating budgetary data reflected in the financial statements:

1. Prior to June 30, the City Manager submits to the City Council a proposed operating budget for the fiscal year commencing the following July 1. The operating budget includes proposed expenditures and the means of financing them. Public hearings are conducted to obtain taxpayer comments.
2. The budget is legally enacted through passage of a resolution during the second City Council meeting in the month of June.
3. The City Manager may transfer budgeted amounts among accounts within a fund; however, any revisions that alter the total expenditures of any fund must be approved by the City Council.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

4. Formal budgetary integration is employed as a management control device during the year for the General Fund, Special Revenue Funds, Debt Service Fund, Enterprise Funds and the Capital Projects Fund. These are the only Funds with legally adopted budgets
5. Budgets are adopted on a basis consistent with generally accepted accounting principles (GAAP), except for Capital Projects Fund capital expenditures which are budgeted on a project length basis. Budget versus actual comparisons for these expenditures have therefore not been presented in these financial statements.
6. Budgeted amounts are as originally adopted or as amended by City Council. Individual amendments were not material in relation to the original appropriations.

F. Encumbrances

Encumbrance accounting is employed as an extension of formal budgetary integration in the governmental fund types. Under encumbrance accounting, purchase orders, contracts and other commitments for the expenditure of monies are recorded in order to reserve that portion of the applicable appropriation. Encumbrances outstanding at year end are reported as reservations of fund balance since they do not constitute expenditures or liabilities. Outstanding encumbrances at year-end are automatically reappropriated the following year.

Unexpended appropriations lapse at year-end unless budgeted on a project basis.

G. Compensated Absences

Compensated absences comprise unused vacation leave and compensated time off, which are accrued as earned, and become "due" upon the occurrence of relevant events such as resignations, retirements, and uses of leave balances by covered employees. Unused sick leave does not vest. The liability for compensated absences is determined annually.

For Governmental funds, a liability for these amounts is reported only if they have matured, for example, as a result of employee resignations and retirements. No such liabilities existed at fiscal year end. Therefore, the entire liability is only recorded in the Statement of Net Assets.

The changes in compensated absence balances were as follows:

	Governmental Activities	Business-Type Activities	Total
Beginning Balance	\$ 1,898,897	\$ 248,206	\$ 2,147,103
Additions	1,742,158	230,194	\$ 1,972,352
Payments	(1,817,932)	(232,786)	\$ (2,050,718)
Ending Balance	<u>\$ 1,823,123</u>	<u>\$ 245,614</u>	<u>\$ 2,068,737</u>
Current Portion	<u>\$ 1,818,840</u>	<u>\$ 245,037</u>	<u>\$ 2,063,877</u>

The current portion (i.e., due within one year) is estimated based on historical earnings and usage trends.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**H. Property Tax**

Monterey County assesses properties and bills, collects, and distributes the City's portion of actual property taxes collected to the City. Secured and unsecured property taxes are levied on January 1. Property taxes levied are recorded as revenue and receivables in the fiscal year of levy, provided they are collected during the fiscal year or within 30 days of the fiscal year end.

Secured property tax is due in two installments, on November 1 and March 1, and becomes a lien on those dates. It becomes delinquent on December 10 and April 10, respectively. Unsecured property tax is due on July 1, and becomes delinquent on August 31. The term "unsecured" refers to taxes on personal property, which is property other than real estate, land and buildings. These taxes are secured by liens on the property being taxed.

I. Property Held for Resale

As part of its Low & Moderate Income Housing Program, the Redevelopment Agency purchases and sells affordable homes in the City to low/moderate income homebuyers in accordance with the affordable housing program. Homes are sold at below-market prices, but purchasers must resell these homes only to the Agency at approximately the same price and in the same condition. Homes owned by the Agency are accounted for at cost, which is below market.

NOTE 2 - CASH AND INVESTMENTS**A. Categorization of Credit Risk of Securities Instruments**

The City and its fiscal agents invest in individual investments and in investment pools. Individual investments are evidenced by specific identifiable pieces of paper called *securities instruments*, or by an electronic entry registering the owner in the records of the institution issuing the security, called the *book entry* system.

The City categorizes its individual securities instruments in ascending order to reflect the relative risk of loss of these instruments. This risk is called Credit Risk; the lower the number, the lower the risk. The three levels of risk prescribed by generally accepted accounting principles are described as follows:

Category 1 – This is the lowest degree of Credit Risk. Securities instruments in this category are in the City's name and are in the possession of the Trust Department of the bank employed by the City solely for this purpose. The City is the registered owner of securities held in book entry form by the bank's Trust Department.

Category 2 - Securities instruments and book entry form securities in this category are in the bank's name but are held by its Trust Department in a separate account in the City's name.

Category 3 - None of the City's investments are in this category, which would include only City-owned securities instruments or book entry form securities which were not in the City's name or which were not held by the bank's Trust Department.

Pooled Investments - Pooled investments are not categorized because of their pooled, rather than individual, nature

CITY OF MONTEREY

Notes to Basic Financial Statements

June 30, 2004

NOTE 2 - CASH AND INVESTMENTS (Continued)

Investments are carried at fair value, which is the same as market value, and are categorized as follows at June 30, 2004:

	Total Fair Value
Category 1 investments:	
U.S. Government Securities:	
Federal National Mortgage Assoc.	\$ 5,893,440
Federal Home Loan Mortgage Corp.	7,867,130
Federal Farm Credit Bank	2,909,390
Federal Home Loan Bank	26,536,910
Corporate Stocks	1,401,366
Category 2 investments:	
Repurchase Agreement	1,904,500
U.S. Government Securities:	
Federal Home Loan Bank	2,629,606
Non-categorized investments:	
Local Agency Investment Fund	11,221,838
Mutual Funds	1,302,403
Investment Agreement	1,037,175
	62,703,758
Total Investments	62,703,758
Cash (overdraft) in bank and on hand	299,602
Total cash and investments	\$ 63,003,360

The total cash and investments above include those amounts held by the City in its Fiduciary funds (\$46,886). However, the entity-wide presentation excludes Fiduciary funds totals, as the City is merely acting as an agent for other parties (assessment and promotion districts).

B. Cash Deposits

California Law requires banks and savings and loan institutions to pledge government securities with a market value of 110% of the City's cash on deposit or first trust deed mortgage notes with a value of 150% of the deposit as collateral for these deposits. Under California Law, this collateral is held in the City's name and places the City ahead of general creditors of the institution. The City has waived collateral requirements for the portion of deposits covered by federal deposit insurance.

Cash in banks is entirely insured (Category 1) or collateralized by the institution holding the deposit (Category 2), as discussed above.

The carrying amount of the City's cash deposits was \$299,602 at June 30, 2004. At that date bank balances before reconciling items were \$543,665 of which \$100,000 was insured (Category 1), and \$443,665 was collateralized (Category 2) as discussed previously.

NOTE 2 - CASH AND INVESTMENTS (Continued)**C. Authorized Investments**

The City's investment policy and the California Government Code allow the City to invest in the following:

- Securities of the U.S. Government or its Agencies
- Certificates of Deposit (or Time Deposits) placed with commercial banks and/or savings and loan companies
- Negotiable Certificates of Deposit
- Bankers' Acceptances
- Commercial Paper rated A-1 by Standard & Poor's Corporation or P-1 by Moody's Commercial Paper Record
- Medium Term Corporate Notes
- California Local Agency Investment Fund
- Repurchase Agreements
- Passbook Savings Accounts
- Reverse Repurchase Agreements
- Shares of beneficial interest issued by diversified management companies holding U.S. Treasury or Government agency obligations

The City's investments are carried at fair value, as required by generally accepted accounting principles. The City adjusts the carrying value of its investments to reflect their fair value at each fiscal year end, and it includes the effects of these adjustments in income for that fiscal year.

D. Local Agency Investment Fund

The City is a voluntary participant in the Local Agency Investment Fund (LAIF) that is regulated by California Government Code Section 16429 under the oversight of the Treasurer of the State of California. The fair value of the City's investment in this pool is reported in the accompanying financial statements at amounts based upon the City's pro-rata share of the fair value provided by LAIF for the entire LAIF portfolio (in relation to the amortized cost of that portfolio). The City reports its investment in LAIF at the fair value amount provided by LAIF, which at June 30, 2004 was \$18,162 less than the City's cost. The balance available for withdrawal is based on the accounting records maintained by LAIF, which are on an amortized cost basis. Included in LAIF's investment portfolio are collateralized mortgage obligations, mortgage-backed securities, other asset-backed securities, loans to certain state funds, and floating rate securities issued by federal agencies, government-sponsored enterprises, and corporations.

E. Cash Equivalents

For purposes of the statement of cash flows, the City considers all highly liquid investments with maturity of three months or less when purchased to be cash equivalents. Proprietary fund types' cash and investments balances classified as Available for Operations are considered cash equivalents for purposes of the statement of cash flows. Restricted cash is excluded because it is not liquid and may not be used to liquidate liabilities in the ordinary course of business.

CITY OF MONTEREY

Notes to Basic Financial Statements

June 30, 2004

NOTE 3 – INTERFUND TRANSACTIONS

A. Transfers Among City Funds

With Council approval, resources may be transferred from one City fund to another. The purpose of the majority of transfers is to reimburse a fund that has made an expenditure on behalf of another fund. Less often, a transfer may be made to open or close a fund.

Transfers between funds during the fiscal year ended June 30, 2004 were as follows:

	Transfer In:							TOTAL
	Governmental Funds			Marina	Parking	Non-Major Ent.	Internal Service Funds	
	General Fund	Capital Projects	Non-Major Gov.					
Transfer Out from:								
Governmental Funds:								
General Fund	\$ -	\$ 1,101,719	\$ 1,960,717	\$ -	\$ 16,770	\$ 60,397	\$ 114,636	\$ 3,254,239
Capital Projects fund	275,270	-	2,772	-	-	-	-	278,042
Non-major governmental	135,751	1,595,323	-	-	-	-	-	1,731,075
Enterprise Funds:								
Marina	150,000	-	-	-	163,846	-	-	313,846
Parking	138,649	-	451,537	-	-	-	-	590,186
Presidio of Monterey	-	-	-	-	-	-	49,712	49,712
Non-major enterprise	-	-	-	3,884	-	-	-	3,884
Total transfers out	<u>\$ 699,670</u>	<u>\$ 2,697,043</u>	<u>\$ 2,415,027</u>	<u>\$ 3,884</u>	<u>\$ 180,616</u>	<u>\$ 60,397</u>	<u>\$ 164,348</u>	<u>\$ 6,220,983</u>

B. Current Interfund Balances

Current interfund balances arise in the normal course of business and are expected to be repaid shortly after the end of the fiscal year. At June 30, 2004 interfund balances comprised the following:

	<u>Due From / To Other Funds</u>	
	<u>Receivable</u>	<u>Payable</u>
Governmental Funds		
General Fund	\$ 2,458,619	\$ -
Capital Projects Fund	-	1,521,573
Non-Major: State/Federal Grants Fund	-	233,457
Enterprise Funds		
Presidio of MPW Fund	-	585,765
Non-Major: Cemetery Fund	-	7,769
Internal Service Funds	-	110,055
	<u>\$ 2,458,619</u>	<u>\$ 2,458,619</u>

NOTE 3 – INTERFUND TRANSACTIONS (Continued)**C. Long-Term Interfund Advances**

At June 30, 2004 the funds below had made advances which were not expected to be repaid within the next year.

	<u>Advances From / To Other Funds</u>	
	<u>Receivable</u>	<u>Payable</u>
Governmental Funds		
General Fund	\$ 1,045,655	\$ -
Capital Projects Fund	-	415,000
Non-Major Funds		
Sewer/Storm Water System Improvement Fund	-	689,910
Low & Moderate Income Housing Fund	1,472,383	-
Debt Service Fund	-	1,472,383
Enterprise Funds		
Parking Fund	415,000	-
Non-Major Funds: Cemetery Fund	-	355,745
	<u>\$ 2,933,038</u>	<u>\$ 2,933,038</u>

The Sewer/Storm Water System Improvement fund received advances from the General Fund in Fiscal Year's 1999, 2000 and 2001 to be used for storm water projects. These advances are scheduled to be repaid in \$100,000 annual payments beginning in Fiscal Year 2004 and each subsequent year until the advance is paid in full.

The Debt Service fund advances from the Low & Moderate Income Housing fund are deferred set asides due to be repaid during the final three years of the City's Custom House Redevelopment Agency (estimated to be 2015 – 2018).

Cemetery fund received advances in Fiscal Year 2002 and 2003 from the General Fund to cover debt service payments related to the construction of columbarium niches. These advances will begin to be repaid to the General Fund after the debt service has been paid in 2012.

D. Repayment Agreement

In December 1993 the City Council and Redevelopment Agency (Agency) Board of Directors authorized repayment of certain costs incurred by the City on behalf of the Agency. The Repayment Agreement covers assets constructed by the City in the redevelopment areas, assets leased to the City from the Agency and projects paid for with debt financing.

The Repayment Agreement requires the Agency to make repayments annually out of available cash; repayments of \$3,748,827 were made in fiscal 2004. The entire amount due to the City is reported as a current liability of the Agency within these statements and in its own statements.

During the fiscal year, the City analyzed this repayment agreement and determined, based on a current tax increment cash flow analysis, that the Agency will be unable to liquidate a portion of the liability within its remaining life. Therefore, the City recorded an Allowance for Doubtful accounts in the amount of \$13,687,312. The City will periodically update the cash flow analysis and, if necessary, make an adjustment to the allowance for doubtful accounts.

NOTE 4 – LOANS AND MORTGAGES RECEIVABLE**A. *Downpayment Assistance Loans***

These are loans to qualified moderate income residents of the City or qualified moderate income individuals employed in the City for up to 15% of the purchase price of a residence in the City (to a maximum of \$45,000). Such loans bear simple interest at 5% per annum, with principal and interest deferred for the first five years. At the end of five years the City reviews the income status of the borrower. Based on such review, the balance of the loan is payable in monthly installments over a period of up to 15 years, or deferred for an additional period of five years with repayment upon sale or transfer of the residence. Due to the long-term nature of the interest receivable, interest on the loans is recorded only when it becomes available as net current assets.

B. *Rehabilitation Loans*

These are loans up to \$90,000 to qualifying low-income homeowners in the City. Such loans bear simple interest at 5% per annum, with principal and interest due upon the sale or transfer of the residence. Due to the long-term nature of the interest receivable, interest on the loans is recorded only when it becomes available as net current assets.

C. *Project Subsidy Loans*

In October 1997, the Agency entered into a Development Agreement and Ground Lease with a developer for the C-21 Redevelopment Mixed Use Project in the Custom House Redevelopment Project Area. Under the terms of the agreement, the developer constructed a theater/retail complex, which included affordable housing units. The developer agreed to provide on-site management of the housing units. The Agency agreed to provide a project subsidy loan to implement the project. No principal or interest repayment is required until 2018.

NOTE 5 – CAPITAL ASSETS

Capital assets, which include property, plant, equipment, and infrastructure assets (e.g., roads, bridges, sidewalks, and similar items), are reported in the applicable governmental or business-type activities columns in the government-wide financial statements. Capital assets are defined by the City as assets with an initial, individual cost of more than \$5,000 and an estimated useful life of 3 years or greater. For infrastructure to be capitalized, it must meet the elevated cost and useful life threshold of \$150,000 and 5 years or greater.

Per GASB Statement 34, which the City implemented in Fiscal Year 2003, the City has capitalized and reported major general infrastructure assets that were acquired (purchased, constructed, or donated), or that received major renovations, restorations, or improvements since Fiscal Year 2003.

In addition, this statement also requires that by the fiscal year ending June 30, 2007, it must retroactively record all its major infrastructure assets back to Fiscal Year 1981.

NOTE 5 – CAPITAL ASSETS (Continued)**A. Value of Capital Assets**

All capital assets are valued at historical cost or estimated historical cost if actual historical cost is not available. The cost includes all ancillary charges necessary to place the asset in its intended location and condition for use. Contributed capital assets are valued at their estimated fair market value on the date contributed.

Major outlays for capital assets and improvements are capitalized as projects are constructed. For Proprietary funds, interest incurred during the construction phase is reflected in the capitalized value of the asset constructed, net of interest earned on the invested proceeds over the same period.

B. Depreciating Capital Assets

All capital assets with limited useful lives are depreciated over their estimated useful lives. The purpose of depreciation is to spread the cost of capital assets equitably among all users over the life of these assets. The amount charged to depreciation expense each year represents that year's pro-rata share of the cost of capital assets.

Depreciation is provided using mid-year convention (all assets receive exactly ½ year of depreciation in the acquisition and disposal year) along with the straight line method for the annual calculation. Thus, the cost of the asset is divided by its expected useful life in years and the result is charged to expense each year until the asset is fully depreciated. The City has assigned the useful lives listed below to capital assets:

Bridges, Roadways, Railroads, Bridges, Wharves	50 Years
Buildings	40 years
Building improvements	20 years
Improvements other than Buildings	30 years
Docks, Sea Walls, Bulkheads	30 Years
Vehicles	5-10 years
Machinery and Equipment	5-15 years

C. Capital Asset Contributions

Some capital assets may be acquired using federal and State grant funds, or they may be contributed by developers or other governments. These contributions are accounted for as revenues at the time the capital assets are contributed.

CITY OF MONTEREY

Notes to Basic Financial Statements

June 30, 2004

NOTE 5 – CAPITAL ASSETS (Continued)

D. Capital Asset Additions and Retirements

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

Primary Government	Balance June 30, 2003	Additions	Retirements	Transfers	Balance June 30, 2004
Governmental activities:					
Capital assets, not being depreciated:					
Land	\$ 26,786,171	\$ -	\$ (1)	\$ 919,881	\$ 27,706,051
Construction in progress	2,431,455	5,516,342	-	(1,673,064)	6,274,733
Total assets not being depreciated	<u>29,217,626</u>	<u>5,516,342</u>	<u>(1)</u>	<u>(753,183)</u>	<u>33,980,784</u>
Capital assets, being depreciated:					
Buildings and Improvements	50,281,979	-	-	(695,555)	49,586,424
Improvements other than buildings	16,495,525	93,373	-	52,885	16,641,783
Machinery and Equipment	12,681,425	683,801	(344,077)	-	13,021,149
Infrastructure	1,083,933	3,135,022	-	1,395,853	5,614,808
Total assets being depreciated	<u>80,542,862</u>	<u>3,912,196</u>	<u>(344,077)</u>	<u>753,183</u>	<u>84,864,164</u>
Less accumulated depreciation for:					
Buildings and Improvements	(17,363,539)	(983,117)	-	-	(18,346,656)
Improvements other than buildings	(8,053,152)	(535,007)	-	-	(8,588,159)
Machinery and Equipment	(8,062,247)	(1,157,550)	296,467	-	(8,923,330)
Infrastructure	(10,839)	(21,679)	-	-	(32,518)
Total accumulated depreciation	<u>(33,489,777)</u>	<u>(2,697,351)</u>	<u>296,467</u>	<u>-</u>	<u>(35,890,663)</u>
Total capital assets, being depreciated, net	<u>47,053,085</u>	<u>1,214,844</u>	<u>(47,610)</u>	<u>753,183</u>	<u>48,973,500</u>
Governmental activities capital assets, net	<u>\$ 76,270,711</u>	<u>\$ 6,731,186</u>	<u>\$ (47,611)</u>	<u>\$ -</u>	<u>\$ 82,954,284</u>
Business-type activities:					
Capital assets, not being depreciated:					
Land	\$ 9,205,157	\$ -	\$ -	\$ -	\$ 9,205,157
Construction in progress	-	-	-	-	-
Total assets not being depreciated	<u>9,205,157</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>9,205,157</u>
Capital assets, being depreciated:					
Buildings and Improvements	23,577,634	-	-	-	23,577,634
Improvements other than buildings	12,453,844	-	-	-	12,453,844
Machinery and Equipment	503,189	12,870	-	-	516,059
Infrastructure	-	-	-	-	-
Total assets being depreciated	<u>36,534,667</u>	<u>12,870</u>	<u>-</u>	<u>-</u>	<u>36,547,537</u>
Less accumulated depreciation for:					
Buildings and Improvements	(12,448,400)	(440,937)	-	-	(12,889,337)
Improvements other than buildings	(5,461,641)	(467,199)	-	-	(5,928,840)
Machinery and Equipment	(290,474)	(31,859)	-	-	(322,333)
Infrastructure	-	-	-	-	-
Total accumulated depreciation	<u>(18,200,515)</u>	<u>(939,995)</u>	<u>-</u>	<u>-</u>	<u>(19,140,510)</u>
Total capital assets, being depreciated, net	<u>18,334,152</u>	<u>(927,125)</u>	<u>-</u>	<u>-</u>	<u>17,407,027</u>
Business-type activities capital assets, net	<u>\$ 27,539,309</u>	<u>\$ (927,125)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 26,612,184</u>

NOTE 5 – CAPITAL ASSETS (Continued)***E. Depreciation Allocation***

Depreciation expense is charged to functions and programs based on their usage of the related assets. The amounts allocated to each function or program are as follows:

Governmental activities:	
General Government	\$ 162,824
Police	39,613
Fire	30,331
Public Works, including infrastructure assets	364,410
Community Development	18,112
Recreation and Community Service	720,919
Library	35,367
Public Facilities	265,047
Capital assets held by the City's internal service funds are charged to the various functions based on their usage	<u>1,060,728</u>
Total depreciation expense - governmental activities	<u><u>\$ 2,697,351</u></u>
Business-type activities:	
Marina	\$ 418,442
Cemetery	28,376
Parking	399,955
Materials Recovery Facility	<u>93,222</u>
Total depreciation expense - business-type activities	<u><u>\$ 939,995</u></u>

F. Assets not Capitalized

Art Collections, Library Reserve Collections, and Museum and Historical Collections, that are considered inexhaustible in that their value does not diminish over time, are not required to be capitalized if all of the following conditions are met:

- The collection is held for public exhibition, education, or research in furtherance of public service, rather than financial gain.
- The collection is protected, kept unencumbered, cared for, and preserved.
- The City maintains a policy that requires proceeds from sales to be used to acquire other items for collection

Living things will not be capitalized due to the high level of ongoing maintenance and/or training (animals) to extend its life and/or add usefulness. Some examples are; Trees, grass/sod, other vegetation, Police/fire dogs, horses or other animals.

Street related infrastructure items such as regular road maintenance with an expected life of less than 5 years (slurry seals) or traffic calming measures (street striping, speed bumps, medians, vegetation) are items that do not materially add to the value of the assets or extend its useful life.

CITY OF MONTEREY

Notes to Basic Financial Statements

June 30, 2004

NOTE 6 - LONG TERM DEBT

A. The City's Long-Term Debt

The City generally incurs long-term debt to finance projects or purchase assets that will have useful lives equal to or greater than the related debt.

B. Transactions and Balances

The following summarizes the City's long-term debt transactions and balances at June 30, 2004:

	Balance June 30, 2003	Retirements	Balance June 30, 2004	Due Within One Year
GOVERNMENTAL ACTIVITIES				
Lease Revenue Bonds Payable:				
1977 Custom House, 5.6%, due 4/1/04	\$ 445,000	\$ 445,000	\$ -	\$ -
1978 Conference Center, 5.93%, due 6/1/05	2,785,000	285,000	2,500,000	2,500,000
1999 Redevelopment Agency, 3.7-4.6% due 11/1/12	4,506,150	608,850	3,897,300	636,900
2002 Joint Powers Financing Authority, 4.0-5.0%, due 05/01/32	9,705,000	175,000	9,530,000	180,000
Loans Payable:				
Ashford Capital Corporation, 5.65%, due 9/13/05	19,421	6,122	13,299	6,467
CaLease Public Funding Corporation, 6.97%, due 8/15/04	19,613	12,850	6,763	6,763
County of Monterey 911 Dispatch Center various %, due 9/17	325,130	20,641	304,489	19,554
SunTrust Leasing Corporation, 4.24%, due 4/23/11	672,049	72,199	599,850	75,293
TOTAL GOVERNMENTAL ACTIVITIES	<u>\$18,477,363</u>	<u>\$ 1,625,662</u>	<u>\$16,851,701</u>	<u>\$ 3,424,977</u>
BUSINESS TYPE ACTIVITIES				
Lease Revenue Bonds Payable:				
1994 Materials Recovery Facility, 5.00-5.75%, due 3/1/18	\$ 3,510,000	\$ 110,000	3,400,000	\$ 125,000
1999 Redevelopment Agency, 3.7-4.6%, due 11/1/12	9,148,850	1,236,150	7,912,700	1,293,100
Loans Payable:				
State of California Small Craft Harbor Loans, (a), 4.50%, due 2024	5,551,582	236,383	5,315,199	247,020
TOTAL BUSINESS TYPE ACTIVITIES	<u>\$18,210,432</u>	<u>\$ 1,582,533</u>	<u>\$16,627,899</u>	<u>\$ 1,665,120</u>

The City had \$ 6,873,684 in restricted cash and investments at June 30, 2004 held by fiscal agents, which may only be disbursed for specified capital outlays or the for the payment of certain bonds. These funds have been invested only as permitted by either specific State statute or applicable City ordinance, resolution or bond indenture.

Enterprise Fund bond discount and origination costs are amortized on a straight-line basis over the lives of the related debt issues. Governmental fund debt issuance costs are accounted for as expenditures when incurred.

CITY OF MONTEREY

Notes to Basic Financial Statements

June 30, 2004

NOTE 6 - LONG TERM DEBT (continued)

C. Repayment Requirements

At June 30, 2004 future annual principal and interest payment requirements for general long-term debt and enterprise fund long-term debt were as follows:

For the Year Ending June 30	Lease Revenue Bonds		Miscellaneous Loans		Totals
	Principal	Interest	Principal	Interest	
Governmental					
2005	\$ 3,316,900	\$ 748,120	\$ 108,077	\$ 34,938	\$ 4,208,035
2006	572,750	573,854	105,500	30,516	1,282,620
2007	595,950	551,071	102,644	26,153	1,275,818
2008	615,800	526,933	106,784	22,013	1,271,530
2009	617,550	502,056	111,093	17,704	1,248,403
2010-2014	2,828,350	2,115,038	310,393	33,785	5,287,566
2015-2019	1,460,000	1,690,173	79,910	5,009	3,235,092
2020-2024	1,845,000	1,303,915	-	-	3,148,915
2025-2029	2,360,000	794,500	-	-	3,154,500
2030-2033	1,715,000	174,250	-	-	1,889,250
TOTAL	\$ 15,927,300	\$ 8,979,910	\$ 924,401	\$ 170,118	\$26,001,729
Business Type					
2005	\$ 1,418,100	\$ 493,298	\$ 247,020	\$ 239,184	\$ 2,397,602
2006	922,250	447,324	258,134	228,068	1,855,776
2007	964,050	409,207	252,173	216,452	1,841,882
2008	1,019,200	368,235	263,521	205,104	1,856,060
2009	1,012,450	324,695	221,166	193,246	1,751,557
2010-2014	4,556,650	920,619	1,229,468	808,445	7,515,183
2015-2019	1,420,000	212,255	1,165,644	533,069	3,330,969
2020-2024	-	-	1,366,753	259,968	1,626,721
2025	-	-	311,320	14,009	325,329
TOTAL	\$ 11,312,700	\$ 3,175,633	\$ 5,315,199	\$ 2,697,547	\$22,501,079

The City's bond indentures contain significant limitations and restrictions regarding annual debt service requirements, maintenance of and flow of monies through various restricted accounts and minimum revenue bond coverages. City management believes the City is in compliance with all such indenture requirements.

D. Description of Major Debt Issues

Lease Revenue Bonds

On September 20, 1977, \$6,000,000 of Custom House Parking Facilities Lease Revenue Bonds, Series 1977, were issued to finance the construction of two parking structures. The bonds bear interest at 5.25% to 5.60% and mature April 1, 2004. Principal payments are due annually on April 1 and interest payments are due semi-annually on April 1 and October 1. The bonds are subject to early redemption at the discretion of the City upon payment of a redemption price equal to the outstanding principal and accrued interest, plus a premium of up to 2.5%. The bonds will be repaid from lease revenues from the City for the parking structures.

NOTE 6 - LONG TERM DEBT (continued)

On March 7, 1978, \$6,000,000 of Custom House Center Lease Revenue Bonds, Series 1978, were issued to refund the 1974 Custom House Center Lease Revenue Bonds, Series 1974. The bonds bear interest at 5.93% mature June 1, 2005. Principal payments are due annually on June 1 and interest payments are due semi-annually on June 1 and December 1. The bonds are subject to early redemption at the discretion of the City upon payment of a redemption price equal to the outstanding principal and accrued interest, plus a premium of up to 3%. The bonds will be repaid from lease revenues from the City for the Custom House Center.

On April 28, 1999, \$19,045,000 of Redevelopment Agency Lease Revenue Refunding Bonds, Series 1999, were issued to refund the Agency's 1992 and 1993 Lease Revenue Bonds and to prepay a lease entered into in 1998 by the City to construct the City's Columbarium. The bonds bear interest at 3.00% to 4.60% and are due November 1, 2012. Principal payments are due annually on November 1 and interest payments are due semi-annually on May 1 and November 1. Bonds maturing on or after November 1, 2004 are subject to early redemption at the discretion of the City upon payment of a redemption price equal to the outstanding principal and accrued interest, plus a premium of .25%. The bonds will be repaid from lease revenues from the City.

On February 15, 1994, \$4,045,000 of Lease Revenue Bonds, Series 1994, were issued to finance the construction of a Materials Recovery Facility. The bonds bear interest at 5.00% to 5.75% and are due March 1, 2018. Principal payments are due annually on March 1 and interest payments are due semi-annually on March 1 and September 1. The bonds are subject to early redemption at the discretion of the City upon payment of a redemption price equal to the outstanding principal and accrued interest, plus a premium of .25%. The bonds will be repaid from lease revenues received by the City for the materials recovery facility.

On May 23, 2002, \$9,860,000 of Lease Revenue Bonds, Series 2002 were issued to provide funds for the expansion of the Monterey Sports Center and the purchase of the Catellus East parcel. The bonds bear interest at 4.0% to 5.0% and are due May 1, 2032. Principal payments are due annually on May 1 and interest payments are due semi-annually on May 1 and November 1. The bonds are subject to early redemption at the discretion of the City upon payment of a redemption price equal to the outstanding principal and accrued interest, plus a premium that varies based on the redemption period of 0.00% to 2.00%.

Loans Payable

On various dates from 1975 to 1997, the State of California made loans to the City to finance various marina construction and improvement projects. These Small Craft Harbor loans bear interest at 4.50% to 4.70% and mature 28 to 30 years from the award date. Principal and interest payments are due annually on August 1. The loans will be repaid from fees and rentals charged by the City for marina facilities.

On August 15, 1996, an agreement was entered into by the City and CaLease Public Funding Corporation with a principal amount of \$84,739 to finance the City Hall lighting upgrade. Semiannual payments of \$6,999 began on February 15, 1997 and will conclude on August 15, 2004. The agreement has an interest rate of 6.97%.

On July 10, 2001, the City signed a Building Construction and Funding Agreement dated July 1, 2001, with the County of Monterey for a principal amount of \$343,547. This represents the City's

NOTE 6 - LONG TERM DEBT (continued)

share of the cost to construct and fund a consolidated dispatch center for 9-1-1 emergency communications. Payments of principal and interest are due annually on September 30. Annual interest is determined by applying the average quarterly rate of interest earned by the Monterey County Treasurer's pooled investment fund. The final payment is due on September 30, 2016. Payments will be made from the City's General Fund.

On September 13, 2001 the City entered into a lease agreement with Ashford Capital Corporation for the purchase of three copiers for the Monterey Public Library. The principal amount of the agreement is \$32,433. Payments of principal and interest, at the rate of 5.65%, are due annually on September 13. The final payment is due on November 19, 2005. Payments will be made from the Library Trust Fund.

On October 23, 2001, an agreement was entered into with SunTrust Leasing Corporation to purchase two fire engines and one fire rescue vehicle. The agreement calls for an interest rate of 4.24% with principal and interest payments of \$49,968 made each year on April 23 and October 23. The final payment is due on April 23, 2011.

Special Assessment Debt Without Governmental Commitment

Special assessment districts exist in various parts of the City to provide improvements to properties located in those districts. Properties are assessed for the cost of improvements; these assessments are payable over the term of the debt issued to finance the improvements and must be sufficient to repay this debt. The City has no direct or contingent liability or moral obligation for repayment of these bonds, which are not included in the general debt of the City. The outstanding balance of these issues at June 30, 2004 was \$90,000.

NOTE 7 - SEGMENT INFORMATION FOR ENTERPRISE FUNDS

The City maintains enterprise funds that account for the operations of the marina, cemetery, parking operations, recycling facility, Presidio public works contract, Navy Services and telecommunication network. These funds are intended to be self-supporting, primarily through user fees charged for services rendered.

Of these funds, the City's non-major enterprise funds include the following 4 segments; The Cemetery, Materials Recovery Facility, Navy Services and Institutional Network funds.

The Cemetery Fund accounts for all cemetery related revenues and expenditures. The Materials Recovery Facility Fund was established in fiscal year 1994-95, and accounts for the revenues and leases payments for this facility. The Navy Services Fund was established to account for costs and revenues pertaining to the Navy services contract. The Institutional Network Fund was established to account for costs and revenues pertaining to the agreement contracted with AT&T, in operating a communication network for educational institutions, City buildings and agencies, and other entities.

CITY OF MONTEREY

Notes to Basic Financial Statements

June 30, 2004

NOTE 7 – SEGMENT INFORMATION FOR ENTERPRISE FUNDS (continued)

Fiscal 2004 segment information is as follows:

Condensed Statement of Net Assets

	<u>Cemetery</u>	<u>Materials Recovery</u>	<u>Navy Services</u>	<u>Institutional Network</u>
Assets:				
Current assets	\$ 10,523	\$ 303,192	\$ 174,026	\$ 404,215
Restricted assets	100,040	436,584	-	-
Capital assets	907,986	2,750,056	-	-
Other assets	10,676	51,782	-	-
Total assets	<u>1,029,225</u>	<u>3,541,614</u>	<u>174,026</u>	<u>404,215</u>
Liabilities:				
Current liabilities	137,948	194,567	2,724	1,210
Noncurrent liabilities	849,745	3,275,000	-	-
Total liabilities	<u>987,693</u>	<u>3,469,567</u>	<u>2,724</u>	<u>1,210</u>
Net assets:				
Invested in capital assets, net of related debt	317,486	(649,944)	-	-
Restricted for debt service	100,040	436,584	-	-
Unrestricted	(375,994)	285,407	171,302	403,005
Total net assets	<u>\$ 41,532</u>	<u>\$ 72,047</u>	<u>\$ 171,302</u>	<u>\$ 403,005</u>

Condensed Statement of Revenues, Expenses and Changes in Net Assets

	<u>Cemetery</u>	<u>Materials Recovery</u>	<u>Navy Services</u>	<u>Institutional Network</u>
Charges for services	\$ 196,234	\$ -	\$ 229,402	\$ 110,954
Miscellaneous Revenue	-	307,532	-	30,901
Depreciation expense	(29,563)	(99,117)	-	-
Other operating expenses	(257,800)	(10,353)	(200,273)	(116,710)
Operating income	<u>(91,129)</u>	<u>198,062</u>	<u>29,129</u>	<u>25,145</u>
Nonoperating revenues (expenses):				
Investment earnings	5,545	28,877	2,609	9,153
Interest and fiscal charges	(32,614)	(198,415)	(1,491)	(13,892)
Transfers in	50,897	9,500	-	-
Transfers out	(3,884)	-	-	-
Change in net assets	(71,185)	38,024	30,247	20,406
Beginning net assets	112,717	34,023	141,055	382,599
Ending net assets	<u>\$ 41,532</u>	<u>\$ 72,047</u>	<u>\$ 171,302</u>	<u>\$ 403,005</u>

Condensed Statement of Cash Flows

	<u>Cemetery</u>	<u>Materials Recovery</u>	<u>Navy Services</u>	<u>Institutional Network</u>
Net cash provided (used) by:				
Operating activities	\$ (57,624)	\$ 297,179	\$ 5,734	\$ (13,408)
Noncapital financing activities	173,291	9,500	-	-
Capital and related financing activities	(125,433)	(310,665)	(1,491)	(13,892)
Investing activities	9,371	5,411	1,947	6,789
Net increase (decrease)	<u>(395)</u>	<u>1,425</u>	<u>6,190</u>	<u>(20,511)</u>
Beginning cash and cash equivalents	395	299,826	95,245	382,599
Ending cash and cash equivalents	<u>\$ -</u>	<u>\$ 301,251</u>	<u>\$ 101,435</u>	<u>\$ 362,088</u>

NOTE 8 – NET ASSETS**A. Net Assets**

GASB Statement 34 adds the concept of Net Assets, which is measured on the full accrual basis, to the concept of Fund Balance, which is measured on the modified accrual basis. Net Assets is the excess of all the City's assets over all its liabilities, regardless of fund. Net Assets are divided into three captions under GASB Statement 34. These captions apply only to Net Assets, which is determined only at the Government-wide level, and are described as follows:

Invested in Capital Assets, net of related debt describes the portion of Net Assets which is represented by the current net book value of the City's capital assets, less the outstanding balance of any debt issued to finance these assets.

Restricted describes the portion of Net Assets which is restricted as to use by the terms and conditions of agreements with outside parties, governmental regulations, laws, or other restrictions which the City cannot unilaterally alter. These principally debt service requirements and redevelopment funds restricted to low and moderate income purposes.

Unrestricted describes the portion of Net Assets which is not restricted to use.

NOTE 9- PENSION PLANS**A. CALPERS Safety and Miscellaneous Employees Plans**

Substantially all City employees are eligible to participate in pension plans offered by California Public Employees Retirement System (CALPERS), an agent multiple employer defined benefit pension plan which acts as a common investment and administrative agent for its participating member employers.

CALPERS provides retirement and disability benefits, annual cost of living adjustments and death benefits to plan members, who must be public employees and beneficiaries. The City's employees participate in the separate Safety (police and fire) and Miscellaneous (all other) Employee Plans. Benefit provisions under both Plans are established by State statute and City resolution. Benefits are based on years of credited service, equal to one year of full time employment. Funding contributions for both Plans are determined annually on an actuarial basis as of June 30 by CALPERS; the City must contribute these amounts. The Plans' provisions and benefits in effect at June 30, 2004, are summarized as follows:

	<u>Safety</u>	<u>Miscellaneous</u>
Benefit vesting schedule	5 years service	5 years service
Benefit payments	monthly for life	monthly for life
Retirement age	50	55
Benefits per year of service, as a percent of salary	3.00%	1.426%-2.418%
Required employee contribution rates	9%	7%
Required employer contribution rates (FY 2004)	17.77%	2.98%

CALPERS' audited annual financial statements are available at P.O. Box 942709, Sacramento, CA 94229-2709.

CITY OF MONTEREY

Notes to Basic Financial Statements

June 30, 2004

NOTE 9- PENSION PLANS (Continued)

CALPERS determines contribution requirements using a modification of the Entry Age Normal Method. Under this method, the City's total normal benefit cost for each employee from date of hire to date of retirement is expressed as a level percentage of the related total payroll cost. Normal benefit cost under this method is the level amount the City must pay annually to fund an employee's projected retirement benefit. This level percentage of payroll method is used to amortize any unfunded actuarial liabilities. The actuarial assumptions used to compute contribution requirements are also used to compute the actuarial accrued liability. The City does not have a net pension obligation since it pays these actuarially required contributions monthly.

CALPERS uses the market related value method of valuing the Plan's assets. An investment rate of return of 8.25% is assumed, including inflation at 3.5%. Annual salary increases are assumed to vary by duration of service. Changes in liability due to plan amendments, changes in actuarial assumptions, or changes in actuarial methods are amortized as a level percentage of payroll on a closed basis over twenty years. Investment gains and losses are accumulated as they are realized and ten percent of the net balance is amortized annually.

The Plans' actuarial values (which differ from market value) and funding progress over the most recently available three years are set forth below at their actuarial valuation date of June 30, 2003:

Safety Plan Actuarial

Valuation Date	Entry Age Accrued Liability	Value of Assets	Unfunded (Overfunded) Liability	Funded Ratio	Annual Covered Payroll	Unfunded (Overfunded) Liability as % of Payroll
2001	64,777,460	65,481,114	(703,654)	101.1%	7,065,851	(10.0%)
2002	69,840,105	61,926,007	7,914,098	88.7%	7,430,338	106.5%
2003	75,062,291	63,396,858	11,665,433	84.5%	7,592,083	153.7%

Miscellaneous Plan Actuarial

Valuation Date	Entry Age Accrued Liability	Value of Assets	Unfunded (Overfunded) Liability	Funded Ratio	Annual Covered Payroll	Unfunded (Overfunded) Liability as % of Payroll
2001	65,469,932	79,161,057	(13,691,125)	120.9%	18,119,830	(75.6%)
2002	71,673,472	74,500,048	(2,826,576)	103.9%	19,389,559	(14.6%)
2003	81,732,075	75,409,550	6,322,525	92.3%	20,079,812	31.5%

PERS has reported that the value of the net assets in the Plans held for Pension Benefits changed as follows during the year ended June 30, 2003, the most recently available:

	Safety	Miscellaneous
Beginning Balance at June 30th	\$ 61,926,007	\$ 74,500,048
Contributions received	1,878,691	1,488,523
Benefits and Refunds Paid	(2,635,238)	(3,068,118)
Expected Investment Earnings Credited	5,078,306	6,082,387
Expected Actuarial Value of Assets at June 30th	<u>\$ 66,247,766</u>	<u>\$ 79,002,840</u>
Market Value of Assets at June 30th	\$ 57,633,507	\$ 68,551,136
Actuarial Value of Assets at June 30th	\$ 63,396,858	\$ 75,409,550

NOTE 9- PENSION PLANS (Continued)**B. *Deferred Compensation Plan***

City employees may defer a portion of their compensation under a City sponsored Deferred Compensation Plan created in accordance with Internal Revenue Code Section 457. Under this plan, participants are not taxed on the deferred portion of their compensation until distributed to them; distributions may be made only at termination, retirement, death or in an emergency as defined by the Plan.

The laws governing deferred compensation plan assets require plan assets to be held by a trust for the exclusive benefit of plan participants and their beneficiaries. Since the assets held under these plans are not the City's property and are not subject to City control, they have been excluded from these financial statements.

C. *Post Employment Benefits Other Than Pensions*

The City provides limited health care benefits through PERS to eligible retired employees. Benefits provided require sharing of cost by retirees. During the year ended June 30, 2004 the City paid \$11,315 for its share of benefits on behalf of 97 participants.

NOTE 10 - RISK MANAGEMENT**A. *Coverage***

The City is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees, health benefits for employees and natural disasters. The City retains the risk for its general liability, auto physical damage and worker's compensation liability. All risk management activities are accounted for in internal service funds.

A summary of the City's per-occurrence limits follows:

	<u>General liability</u>	<u>Workers' compensation</u>
Retained risk	Up to \$1,000,000	Up to \$400,000
Coverage through:		
pooled insurance	\$1,000,000 to \$2,000,000	\$400,000 to \$5,000,000
excess insurance	\$2,000,000 to \$20,000,000	\$5,000,000 to \$100,000,000

Coverage above the retained risk amount for workers' compensation is provided through insurance purchased by the City. Coverage above the retained risk amount for general liability is provided through a joint purchase of coverage from insurance carriers by the Authority for California Cities Excess Liability (ACCEL), a joint powers authority whose purpose is to develop and fund programs of excess insurance for its members. The Board of Directors of ACCEL consists of representatives of its member cities.

The City's deposits with ACCEL are in accordance with formulas established by ACCEL. Actual surpluses or losses are shared according to a formula developed from overall loss costs and spread to member entities on a percentage basis after a retrospective rating. The City sent deposits to ACCEL for the year ended June 30, 2004 in the amount of \$184,305.

NOTE 10 - RISK MANAGEMENT (Continued)

Financial statements may be obtained from ACCEL, 500 Washington Street, Suite 300, San Francisco, CA 94111.

Property risks are covered on an occurrence basis up to \$500,000,000 with a \$50,000 deductible, by commercial insurance purchased from independent third parties. No settlement amounts have exceeded commercial or ACCEL insurance coverage for each of the past three years.

B. Liability for Uninsured Claims

The liability for the uninsured portion of claims and judgments included in the internal service fund is based on the results of a bi-annual actuarial study obtained by the City. The liability includes amounts for claims incurred but not reported (IBNR). The total liability is calculated by considering the effects of inflation, recent claim settlement trends, including frequency and amount of payouts and other economic social factors and is based on a 90% probability level (IBNR is based on the expected level). Claims and judgments, including a provision for claims incurred but not reported are recorded when a loss is deemed probable of assertion and the amount of the loss is reasonably determinable. Internal annual premiums are charged to the City's funds by the internal service funds using various allocation methods that include actual costs and trends in claims experience.

Claims activities for the years ended June 30, 2004 and 2003 are presented as follows:

	Workers' Compensation	General Liability	Total	
			2004	2003
Beginning balance	\$ 5,437,000	\$ 1,431,400	\$ 6,868,400	\$ 6,868,400
Liability for current fiscal year claims	1,791,000	560,000	2,351,000	1,851,000
Change in liability for prior fiscal year claims and claims incurred but not reported (IBNR)	(3,040,639)	(553,096)	(3,593,735)	(496,640)
Claims paid	1,504,639	23,696	1,528,335	(1,354,360)
Ending balance	<u>\$ 5,692,000</u>	<u>\$ 1,462,000</u>	<u>\$ 7,154,000</u>	<u>\$ 6,868,400</u>

NOTE 11 – EMPLOYMENT BENEFIT – INSURANCE COVERAGE

The City contracts with CalPERS to provide a Cafeteria type health insurance plan for its employees. The City pays the first \$32.20 of the monthly premium per employee. In addition, as a part of the Cafeteria plan, per approved Memorandum of Understanding (MOU) with its bargaining groups, the City also provides between \$ 347.31 and \$ 791.00 per month per employee which can be used towards insurance premiums or other employment benefits. Dental and vision insurance is provided at no cost to its employees (dependent dental insurance premiums are paid by the employee). The City also provides long-term disability for certain employees and life insurance to all but its part-time, seasonal employees.

CITY OF MONTEREY

NOTE 12 – PRESIDIO MUNICIPAL SERVICES AGENCY

At the request of the U.S. Army in 1997 the City and the City of Seaside formed the Presidio Municipal Services Agency (the “Presidio Agency”) under the Joint Exercise of Powers Act of the State of California. The sole function of the Presidio Agency is to coordinate the provision of services by each member City in the operation and maintenance of the U.S. Army’s Presidio facilities in Monterey. The Presidio Agency has no employees; the City of Monterey provides approximately 80% of the services required along with all the Presidio Agency’s administrative and financing requirements; the City of Seaside provides the remainder. The City’s share of these services is reported in the Presidio of Monterey Public Works Enterprise Fund.

The governing body of the Presidio Agency consists of two members, one appointed by each member city. As a separate legal entity, the Presidio Authority exercises full powers and authorities within the Joint Powers Agreement. Obligations of the Presidio Authority are not those of the member cities. Financial statements of the Presidio Agency may be obtained from the City of Monterey, Monterey, California, 93940.

NOTE 13 - COMMITMENTS AND CONTINGENCIES

The City participates in several federal and state grant programs. These programs have been audited by the City’s independent accountants in accordance with the provisions of the federal Single Audit Act of 1984 as amended in 1996 and applicable State requirements. No cost disallowances were proposed as a result of these audits; however, these programs are still subject to further examination by the grantors and the amount, if any, of expenditures which may be disallowed by the granting agencies cannot be determined at this time. The City expects such amounts, if any, to be immaterial.

The City is subject to litigation arising in the normal course of business. In the opinion of the City Attorney there is no pending litigation which is likely to have a material adverse effect on the financial position of the City.

NOTE 14 – STEWARDSHIP AND COMPLIANCE

At June 30, 2004, several non-major funds had an excess of expenditures over budget as follows:

Gas tax	\$ 20,236	Sports center	\$ 4,734
Parking adjustments	\$ 5,042	Tidelands	\$ 37,131
Low and moderate income housing	\$ 57,091	Library	\$ 7,273
Park dedication	\$ 535	Museum	\$ 840
Public safety training and services	\$ 60,825	Special deposits	\$ 230,884
Public education & government access	\$ 9,482	Debt service	\$ 674,519
Senior center programs	\$ 8,153	Scholtz park	\$ 1,199

Also at June 30, 2004, the State/Federal Grants fund had a deficit fund balance of \$52,193 and the Debt Service Fund had a deficit fund balance of \$56,061,267. The former is due to advances due to the general fund in which the corresponding grants have not been completed. The later deficit is due to the repayment agreement between the City and the Agency (see note 3D), in which the Agency makes payments as cash (from property tax increment) is received and available.