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San Diego County Water Authority Financial Report

June 30, 1999
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Independent Auditor's Report

To the Board of Directors

San Diego County Water Authority

San Diego, California

We have audited the accompanying balance sheets of San Diego County Water Authority (the Authority) as of June 30, 1999 and 1998 and the related statements of revenues, expenses and changes in unreserved retained earnings, and cash flows for the years then ended. These financial statements are the responsibility of the Authority'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 and those standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures 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 San Diego County Water Authority as of June 30, 1999 and 1998, and the results of its operations and its cash flows for the years then ended in conformity with generally accepted accounting principles.

The Year 2000 supplementary information on page 23 is not a required part of the basic financial statements but is supplementary information required by the Government Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and do not express an opinion on it. In addition, we do not provide assurance that San Diego County Water Authority is or will become Year 2000 complaint, that the Authority's Year 2000 remediation efforts will be successful in whole or in part, or that parties with which the Authority does business are or will become Year 2000 compliant.

In accordance with Government Auditing Standards, we have also issued our report dated September 15, 1999, on our consideration of San Diego County Water Authority's internal control over financial reporting and our tests of compliance with certain provisions of laws, regulations, contracts and grants.

[Signed] *McGladrey & Pullen, LLP*

San Diego, California

September 15, 1999

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San Diego County Water Authority

Balance Sheets

June 30, 1999 and 1998

Assets		**1999**		1998
Current Assets				
Cash and cash equivalents (Note 3)	**$**	**40,664,000**	$	24,922,000
Accounts and taxes receivable		**48,761,000**		33,605,000
Inventories		**145,000**		6,891,000
Other current assets		**427,000**		400,000
Total current assets		**89,997,000**		65,818,000
Restricted and designated cash, cash equivalents and investments (Notes 3 and 4)				
Cash and cash equivalents		**182,460,000**		13,624,000
Investments		**113,579,000**		125,403,000
		296,039,000		139,027,000
Property, plant and equipment, net (Notes 2 and 7)		**803,100,000**		761,109,000
Other assets (Note 4)		**5,567,000**		5,118,000
	$	**1,194,703,000**	$	971,072,000

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See Notes to Financial Statements.

Liabilities and Equity	**1999**	1998
Current Liabilities		
Accounts payable and accrued liabilities	**$ 48,337,000**	$ 37,772,000
Current maturities of long-term debt (Note 4)	**17,117,000**	15,853,000
Total current liabilities	**65,454,000**	53,625,000
Long-term debt (Note 4)	**596,657,000**	434,935,000
Commitments and Contingencies (Notes 5 and 7)		
Equity		
Contributions in aid of construction	**19,884,000**	16,759,000
Retained earnings:		
Funds designated for rate stabilization	**41,075,000**	36,453,000
Undesignated	**471,633,000**	429,300,000
	512,708,000	465,753,000
Total equity	**532,592,000**	482,512,000
	$ 1,194,703,000	$ 971,072,000

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San Diego County Water Authority

Statements of Revenues, Expenses and Changes in Unreserved Retained Earnings

Years Ended June 30, 1999 and 1998

	1999	1998
Water sales	**$ 217,796,000**	$ 195,075,000
Operating expenses:		
Cost of sales	**179,332,000**	167,003,000
Depreciation and amortization	**12,786,000**	9,754,000

Operations and maintenance	**6,499,000**	6,306,000
Planning and reclamation	**2,267,000**	1,912,000
General and administrative	**8,359,000**	8,743,000
Total operating expenses	**209,243,000**	193,718,000
Operating income	**8,553,000**	1,357,000
Other revenues (expenses):		
Property taxes and in-lieu charges	**6,125,000**	5,773,000
Water availability and capacity charges	**31,783,000**	27,014,000
Interest expense	**(19,829,000)**	(12,262,000)
Investment income	**15,534,000**	11,302,000
Infrastructure access charges	**4,789,000**	
Other expenses (Note 2)		(2,480,000)
Total other revenues, net	**38,402,000**	29,347,000
Net income	**46,955,000**	30,704,000
Retained earnings at beginning of year	**465,753,000**	435,049,000
Retained earnings at end of year	**$ 512,708,000**	$ 465,753,000

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San Diego County Water Authority

Statements of Cash Flows

Years Ended June 30, 1999 and 1998

	1999	1998
Cash Flows from Operating Activities		
Operating income	**$ 8,553,000**	$ 1,357,000

Adjustments to reconcile operating income to net cash		
provided by operating activities:		
Depreciation and amortization	**12,786,000**	9,754,000
Water availability and capacity charges	**31,783,000**	27,014,000
Infrastracture access charges	**4,789,000**	
Amortization of loss on debt defeasded	**866,000**	
Loss (gain) on disposal of property and equipment	**360,000**	(4,000)
(Increase) decrease in:		
Accounts and taxes receivable	**(15,156,000)**	8,950,000
Inventories	**6,746,000**	3,605,000
Other current assets	**(27,000)**	(110,000)
Other assets	**(834,000)**	(1,176,000)
(Decrease) increase in accounts payable and		
accrued liabilities	**10,565,000**	(15,366,000)
Net cash provided by operating activities	**60,431,000**	34,024,000
Cash Flows from Investing Activities		
Investment income	**15,534,000**	11,302,000
Net proceeds from sales of investments	**11,824,000**	40,530,000
Net cash provided by investing activities	**27,358,000**	51,832,000
Cash Flows from Noncapital Financing Activities		
Property taxes and in-lieu charges	**6,125,000**	5,773,000
Net cash provided by noncapital		
financing activities	**6,125,000**	5,773,000
Cash Flows from Capital and Related Financing Activities		

Purchase of property, plant and equipment	**(54,999,000)**	(82,314,000)
Proceeds from sale of property, plant and equipment	**289,000**	
Contributions in aid of construction	**3,125,000**	545,000
Proceeds from debt issue	**178,798,000**	195,273,000
Principal repayment of debt	**(16,720,000)**	(15,805,000)
Amount paid into escrow trust		(169,030,000)
Interest paid	**(19,829,000)**	(12,262,000)
Net cash provided by (used in) capital and		
related financing activities	**90,664,000**	(83,593,000)

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San Diego County Water Authority

Statements of Cash Flows (Continued)

Years Ended June 30, 1999 and 1998

		1999		1998
Increase in cash and cash equivalents		**184,578,000**		8,036,000
Cash and cash equivalents:				
Beginning		**38,546,000**		30,510,000
Ending	**$**	**223,124,000**	$	38,546,000
Supplemental Disclosures of Cash Flow Information:				
Cash paid during the year for interest	**$**	**28,733,000**	$	24,247,000
Interest capitalized during the year to construction				

in progress	**$**	**10,400,000**	$	12,700,000
Write-off of construction in progress	**$**		$	2,480,000

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Notes to financial statements

Note 1. Nature of business

The San Diego County Water Authority (the Authority) was organized on June 9, 1944 under the County Water Authority Act (the Act) for the primary purpose of providing a supplemental supply of imported water to its member agencies for domestic, municipal and agricultural uses. The Authority consists of 24 member agencies which are each represented by at least one person on the Authority's Board of Directors. The Authority is a member of The Metropolitan Water District of Southern California (MWD) and historically, the Authority has purchased from MWD all the water it requires to meet the demands of the member agencies. The Authority is currently in the process of seeking alternative assured sources of water in addition to the MWD. During 1999, the Authority executed the Imperial Irrigation District Water Transfer Agreement which will provide an alternative source of water.

The Metropolitan Water District Act provides a preferential right for the purchase of water by each of its constituent agencies. This preferential right is calculated using a formula, and based upon such formula, the Authority has a statutory preferential right to approximately 12% of MWD's total supply. The policy has never been applied to limit the Authority's purchases. In June 1995, MWD adopted an Integrated Resource Plan designed to meet 100% of its member agency water needs by a mix of imported water and development of additional local resources by its member agencies.

Basis of accounting

The Authority is accounted for as an enterprise fund (proprietary fund type). A fund is an accounting entity with a self-balancing set of accounts established to record the financial position and results of operations of a specific governmental activity. The activities of enterprise funds closely resemble those of ongoing businesses in which the purpose is to conserve and add to basic resources while meeting operating expenses from current revenues. Enterprise funds account for operations that provide services on a continuous basis and are substantially financed by revenues derived from user charges. As an enterprise fund, the Authority uses the accrual basis of accounting, revenues are recognized when earned and expenses are recognized as they are incurred. The Authority has elected not to apply Financial Accounting Standards Board Statements or Interpretations issued after November 30, 1989, as permitted by Governmental Accounting Standards.

Property taxes and in-lieu charges

The Authority is authorized under the Act to levy taxes on all taxable property within its boundaries for the purposes 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. A portion of the taxes are levied to meet the Authority's debt service requirements on its general obligation bonds.

Property taxes are levied annually by the Authority's 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 by December 10th and April 10th. The taxes levied are billed and collected by the County of San Diego and are remitted to the Authority throughout the year.

Member agencies of the Authority may elect to pay in-lieu charges instead of the tax levy. Included in the accompanying statements of revenues, expenses and changes in unreserved retained earnings for the years ended June 30, 1999 and 1998, are in-lieu charges of $793,000 and $692,000, respectively.

Inventories

Inventories consist primarily of water in storage and are stated at the lower of cost (first-in, first-out method) or market (market value - $180,000 and $10,178,000 at June 30, 1999 and 1998, respectively).

Property, plant and equipment

Depreciation is computed utilizing the straight-line method over the following estimated useful lives:

Water systems:	10 to 75 years
Buildings:	40 years
Other equipment:	5 to 15 years
Automobiles:	4 years

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Compensated absences

It is the Authority's policy to permit employees to accumulate earned but unused vacation benefits. Earned vacation pay to a maximum of 36 days (50 days for management) and 25% of accumulated sick leave may be paid upon termination of employment. Upon retirement the Authority pays 100% of sick leave up to 125 days and all earned vacation. Sick leave hours accrue at the rate of one day per month and employees may elect to receive cash for accumulated sick leave at the rate of two for one after accumulating 480 hours.

All accumulated vacation and vested sick leave pay is recorded as an expense and a liability at the time the benefit is earned.

Contributions in aid of construction

Amounts received from member agencies and other entities for construction of service connections or other facilities are included in the accompanying balance sheets as contributions in aid of construction. Contributed service connections or other facilities are recorded as Authority assets and are depreciated in accordance with established policy for similar capital assets.

Capitalized interest

The Authority capitalizes interest on self-constructed assets during the period of construction. The amount of interest cost capitalized on qualifying assets acquired with proceeds of tax-exempt borrowings that are externally restricted to finance acquisition of specified assets is all interest cost of the borrowings less any interest earned on related interest-bearing investments acquired with such unexpended proceeds from the date of the borrowings until the assets are substantially complete and are ready for their intended use. Interest cost of tax-exempt borrowings is eligible for capitalization on other qualifying assets of the Authority when the specified qualifying assets are no longer eligible for interest capitalization. Interest cost capitalized during the years ended June 30, 1999 and 1998 was $10,400,000 and $12,700,000, respectively.

Revenue policies

The principal portion of the Authority's revenues is provided by sales of water. Water is delivered to member agencies on demand and revenue is recognized at the time of delivery. The Authority also has two other separate revenue sources as part of its Capital Finance Plan to fund the Capital Improvement Program. A water availability standby charge was put into effect in fiscal 1990 and generated revenue of $10,523,000 and

$10,660,000 for the years ended June 30, 1999 and 1998, respectively. In fiscal 1991, the Authority implemented a capacity charge on all new water meters purchased within the boundaries of the Authority, which generated revenue of $21,260,000 and $16,351,000 for the years ended June 30, 1999 and 1998, respectively.

Included in restricted cash, cash equivalents and investments at June 30, 1999 and 1998, is approximately $73,490,000 and $60,074,000, respectively, identified in the pay-as-you-go account. This account is used for future cash expenditures for capital improvement projects and consists of water availability standby and capacity charges.

On June 11, 1998, the Infrastructure Access Charge (IAC) was adopted by the Board of Directors as an additional source of fixed revenue to provide better coverage of the Authority's projected fixed expenditures. The IAC is levied on all retail water meters within the Authority's service area. Beginning on January 1, 1999, the IAC has been set at $1.00 per equivalent meter per month. The fixed charge is levied against each member agency for the purpose of maintaining a minimum ratio of projected fixed revenue to projected fixed expenditures of 25% in any future fiscal year. The IAC generated revenues of $4,789,000 for the year ended June 30, 1999. The IAC will be adjusted each year as part of the regular rate-setting process.

Cash and cash equivalents

Cash and cash equivalents consist of short-term highly liquid investments with maturities of 90 days or less at the date of purchase.

Investments

Investments with a maturity date of less than one year are stated at cost or amortized cost.

Investments with a maturity date greater than one year, including negotiable certificates of deposit, U.S. Government securities, Federal Agency securities and medium term notes are stated at fair value based on quoted market prices, where available. Investments in the State of California Local Agency Investment Fund (LAIF) are stated at fair value based on the fair value per share of the pool's underlying portfolio. The pool maintains investments with a par value equal to the fair value of the underlying portfolio. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments.

Budgets and budgetary accounting

Annual budgets adopted by the Board of Directors provide for operations, debt service and capital expenditures of the Authority. Budgetary controls are set by the Board of Directors. The Board of Directors adopts an operating budget at the beginning of the Authority's fiscal year. The legally adopted budget requires that expenditures not exceed appropriations in total for the Authority. The Board of Directors may make appropriation adjustments to the budget during the year as deemed necessary. The Authority adhered to the prescribed budget as discussed above for the years ended June 30, 1999 and 1998.

Note 2: Property, Plant and Equipment

Property, plant and equipment are recorded at cost and consist of the following:

			1999		1998
Water systems		**$**	**718,631,000**	$	517,009,000
Buildings			**30,968,000**		30,350,000
Automobiles and equipment			**13,951,000**		13,355,000
	Total cost of depreciable assets		**763,550,000**		560,714,000
	Less accumulated depreciation		**81,603,000**		70,924,000
	Net depreciable assets		**681,947,000**		489,790,000
Construction in progress			**121,153,000**		271,319,000
		$	**803,100,000**	$	761,109,000

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In June 1998 the Authority determined that certain construction projects were not viable and, consequently, related feasibility costs of $2,480,000 were expensed during the year ended June 30, 1998.

Note 3: Cash, Cash Equivalents and Investments

The California Government code requires California banks and savings and loan associations to secure public fund deposits by pledging government securities or mortgages as collateral. The market value of pledged securities or mortgages must equal at least 110% or 150%, respectively, of public fund deposits. The Authority currently requires government securities as collateral on all its investments with such institutions.

The Authority may waive collateral requirements for deposits which are fully insured up to $100,000 by the Federal Deposit Insurance Corporation (FDIC).

The surplus funds of the Authority may be invested in any of the following approved investments: treasury bills and/or notes; collateralized commercial bank certificates of deposit; collateralized savings and loan certificates of deposit; guaranteed investment contract deposits collateralized by direct U.S. Government obligations; State of California Local Agency Investment Fund (LAIF); domestic bankers acceptances; agency securities; commercial paper; repurchase agreements; reverse repurchase agreements, subject to certain limitations; medium term notes, and government money market funds. An advisory board has been established to monitor the LAIF's compliance with regulations and investment alternatives established by the State.

Deposits

At June 30, 1999, the carrying amount of the Authority's deposits was $1,763,000 and the bank balance was $1,356,000. Of the bank balance, $106,000 was covered by federal depository insurance. The remaining balance was collateralized by the general investment portfolio pledged by the financial institution as security for total public fund deposits.

Investments

The Authority's investments are categorized to give an indication of the level of custodial credit risk assumed by the Authority at year-end. Category 1 includes investments that are insured, collateralized or registered or for which the securities are held by the Authority or its agent in the Authority's name. Category 2 includes uninsured and unregistered investments for which the securities are held by the broker's or dealer's trust department or agent in the Authority's name. Category 3 includes uninsured and unregistered investments for which the securities are held by the broker or dealer, or by its trust department or agent but not in the Authority's name, and uncollateralized investments and cash deposits.

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	Category			Total	Fair
	1	2	3	Cost	Value
U.S. Treasury securities	$ 61,700,000	$	$	$ 61,700,000	$ 61,563,000
Agency securities	26,206,000			26,206,000	26,099,000
Prime commercial paper	19,010,000			19,010,000	19,010,000
Corporate notes	10,048,000			10,048,000	9,915,000
Negotiable certificates of deposit	16,002,000			16,002,000	16,002,000
	$ 132,966,000	$	$	$ 132,966,000	$ 132,589,000
Investments in State Treasurer's investment pool				163,627,000	163,627,000

Private Export Funding Corporation deposits	931,000	931,000
Money market funds	38,499,000	38,499,000
Total cash equivalents and investments	$ 336,023,000	$ 335,646,000
Cash		1,057,000
Total cash, cash equivalents and investments		336,703,000
Less:		
Cash, cash equivalents and investments restricted for bond service requirements		41,075,000
Other restricted and designated cash, cash equivalents and investments		254,964,000
		296,039,000
Current unrestricted cash and cash equivalents		$ 40,664,000

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Note 4: Long-Term Debt

Long-term debt consists of the following:

	1999	1998
1998A Water Revenue Certificates of Participation, net of unamortized discount of $1,161,000	**$ 178,839,000**	$
1997A Water Revenue Certificates of Participation, net of unamortized premium of $2,695,000 (1998: $2,875,000) and unamortized loss from refunding of $15,654,000		

(1998: $16,701,000)		**149,211,000**	148,489,000
1993 Water Revenue Refunding Certificates of Participation		**106,090,000**	111,570,000
1991 Water Revenue Certificates of Participation		**101,895,000**	111,670,000
1966 Waterworks General Obligation Bonds		**7,545,000**	8,865,000
Commercial Paper		**70,000,000**	70,000,000
Other		**194,000**	194,000
		613,774,000	450,788,000
Less amounts due within one year		**17,117,000**	15,853,000
	$	**596,657,000**	$ 434,935,000

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1998A Water Revenue Certificates of Participation

To provide funds for the design and construction of the Authority's Emergency Storage Project and other water system improvements in furtherance of the Authority's Capital Improvement Program, the Authority issued 1998A Water Revenue Certificates of Participation on October 15, 1998, in the aggregate principal amount of $180,000,000.

The Series 1998A Serial Certificates with an aggregate principal amount of $100,000,000 have stated interest rates ranging from 4.75% to 5.25% payable semi-annually on May 1 and November 1. These certificates mature serially through May 1, 2018, subject to optional prepayments beginning 2008.

The Term Certificates with an aggregate principal amount of $80,000,000 have stated interest rates ranging from 4.75% to 5.00% payable semi-annually on May 1 and November 1. An amount of $17,310,000 of these Term Certificates are due May 1, 2002 at a price of 99.750%, $19,035,000 are due May 1, 2024 at a price of 93.114% and $43,655,000 are due May 1, 2028.

The 1998A Water Revenue Certificates were issued at a discount of $1,202,000 and issuance costs were $965,000. The Authority issued the 1998A Certificates at a true interest cost of 4.95%. The net interest cost to the Authority on the 1998A Certificates for the year ended June 30, 1999 was approximately 4.57%.

The certificates require that a reserve be maintained in an amount equal to the lesser of $15,391,555 or maximum annual debt service on the 1998A Certificates. Included in restricted cash, cash equivalents and investments is $141,423,000 at June 30, 1999 which represents unexpended Water Revenue Certificates of Participation proceeds.

1997A Water Revenue Refunding Certificates of Participation

On December 1, 1997, the Authority issued Water Revenue Refunding Certificates of Participation in the amount of $162,315,000 with stated interest rates between 4.00% and 5.75% to refund, in advance, $74,035,000 of the 1991A Certificates with stated interest rates between 6.25% and 6.40% and $80,000,000 of the 1991B Certificates with interest payable at rates determined by auction every fifth week, not to exceed a blended rate of 6.3%.

The Authority issued the 1997A Certificates at a true interest cost of 4.92%. The Serial Certificates with an aggregate principal amount of $144,285,000, have stated interest rates ranging from 4.00% to 5.75% payable semi-annually on May 1 and November 1. These certificates mature serially through May 1, 2018, subject to optional prepayments beginning in 2008. The Series 1997A Term Certificates, with an aggregate principal amount of $18,030,000, have an interest rate of 4.75%, are due May 1, 2020, and are subject to optional prepayments beginning in 2008. The net interest cost to the Authority on the 1997A certificates for the years ended June 30, 1999 and 1998 was approximately 4.91% and 4.57%, respectively.

The Certificates require that a reserve be maintained in an amount equal to the lesser of 10% of the principal amount, 100% of the maximum annual debt service, or 125% of the average annual debt service. A surety bond in the amount of $15,196,610 has been obtained by the Authority and issued in satisfaction of the requirement.

The 1997A Water Revenue Refunding Certificates were issued at a premium of $2,958,000 with issuance costs of $1,342,000. The advance refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of $17,183,000. This difference, reported in the accompanying financial statements as a decrease in bonds payable, is being charged to operations through the year 2020 using the effective interest method. Included in interest expense for the years ended June 30, 1999 and 1998 is amortization of approximately $1,047,000 and $400,000, respectively, of net deferred amounts. The Authority completed the advance refunding to reduce its total debt service payments over the next twenty-two years by $20,896,000 and to obtain an economic gain (difference between the present values of the old and new debt service payments) of $5,530,000.

1993 Water Revenue Refunding Certificates of Participation

To provide funds for the refunding of the 1989A Water Revenue Certificates of Participation, the Authority issued the 1993A Certificates in February 1993 in the aggregate principal amount of $135,650,000. The Series 1993A Current Interest Certificates, with an aggregate principal amount of $85,050,000, have stated interest rates ranging from 3.50% to 5.50% payable semi-annually on May 1 and November 1. These certificates mature serially through May 1, 2005 and are not subject to prepayment. The Series 1993A Floating Auction Tax Exempts (the FLOATS), with an aggregate principal amount of $25,300,000, carry an interest rate determined by auction every 28 days. The FLOATS are due April 22, 2009, subject to mandatory prepayments beginning in 2006. The Series 1993A Residual Interest Tax Exempt Securities (the RITES) with an aggregate principal amount of $25,300,000 carry interest rates determined by a fixed component and an auction rate component payable every 28 days, not to exceed 5.75% in aggregate. The RITES mature serially between April 26, 2006 and April 22, 2009 and are not subject to mandatory prepayment. Interest rates are subject to minimum and maximum limits and may be fixed by the holder. The net interest cost to the Authority on the 1993A certificates for the years ended June 30, 1999 and 1998 was approximately 5.75% and 5.64%, respectively.

The Certificates require that a reserve be maintained in an amount equal to the lesser of $13,565,000, 100% of the maximum annual installment payments, or 125% of average annual installment payments. A surety bond has been obtained by the Authority and issued in satisfaction of this requirement.

The 1993 Certificates were issued to defease the 1989A Certificates which were called and retired on May 1, 1997.

1991 Water Revenue Certificates of Participation

To provide funds for the acquisition and construction of water system improvements, the Authority issued Series 1991A and 1991B Water Revenue Certificates of Participation in November 1991 in the aggregate principal amount of $300,000,000. The Series 1991A Certificates, with an aggregate principal amount of $89,265,000 carry stated interest rates ranging from 5.20% to 6.125% payable semi-annually on May 1 and November 1. These Certificates mature serially through May 1, 2003 and may be redeemed, at the option of the Authority, at premiums decreasing from 2% in 2001 to 1% in 2003. Included in Certificates of Participation at June 30, 1999 and 1998 is $45,195,000 and $54,970,000, respectively.

The Series 1991B Certificates consist of Short-Term Auction Rate and Complementary Auction Rate Certificates in the aggregate principal amount of $56,700,000 with interest payable at rates determined by auction every fifth week, not to exceed an aggregate net cost to the Authority of 6.3%. These Certificates mature April 21, 2011. Included in Certificates of Participation at June 30, 1999 and 1998 is $56,700,000.

The net interest cost to the Authority on the Series 1991A and 1991B Water Revenue Certificates of Participation for the years ended June 30, 1999 and 1998 was approximately 6.19% and 6.17%, respectively.

The Certificates require that a reserve be maintained in an amount of $21,446,000, representing the lesser of 100% of the maximum annual payments, or 125% of the average annual payments.

1966 Waterworks General Obligation Bonds

During 1968, the Authority issued General Obligation Bonds in the aggregate principal amount of $30,000,000 with stated interest rates ranging from 4.50% to 5.50% payable semi-annually on April 1, and October 1, for the construction of a second pipeline to the second aqueduct. The bonds mature serially through October 1, 2003 and may be redeemed on or after October 1, 1980 at premiums decreasing from 3.50% in 1980 to .50% in 2002.

Prior Year Defeasance of Debt

In the prior year, the Authority defeased $74,035,000 of the 1991A Certificates and $80,000,000 of the 1991B Certificates, by placing the net proceeds of $163,931,000 from the 1997A Water Revenue Refunding Certificates of Participation plus an additional amount of $5,099,000 of the 1991A and 1991B Certificates reserve funds and other monies, in an irrevocable trust to provide for all future debt service payments on the $74,035,000 1991A Certificates of Participation and the $80,000,000 1991B Certificates of Participation. Accordingly, the trust account assets and the liabilities for the defeased bonds are not included in the Authority's financial statements. At June 30, 1999, $154,035,000 of Certificates outstanding are considered defeased.

Commercial Paper

The Authority has a commercial paper program through which it can borrow up to $250,000,000 for periods of up to 270 days. Currently, the amount that can be borrowed is limited to $110,000,000, the amount of the revolving credit and term loan agreement that supports a portion of the program. The revolving credit and term loan agreement, unless otherwise extended, will terminate on November 7, 2000. During the term of the agreement, the Authority is obligated to pay a usage fee of .10% on the utilized commitment and .06% on the unutilized commitment. Currently, no advances have been made under the revolving credit and term loan agreement. The Authority maintains remarketing arrangements with two dealers at a total cost of .05% on the outstanding commercial paper. The commercial paper notes are secured and payable solely from net water revenues and are subordinate to the water revenue certificates of participation. At June 30, 1999 and 1998, $70,000,000 of commercial paper is outstanding at a weighted average interest rate of 2.90% and 3.56%, respectively. The commercial paper outstanding at June 30, 1999 and 1998 is classified as long-term since the Authority intends to maintain the program for the foreseeable future. Included in restricted cash, cash equivalents and investments for the year ended June 30, 1998 was $16,116,000, which represented unexpended commercial paper proceeds. At June 30, 1999 all commercial paper proceeds were expended.

Certain outstanding debt agreements require the Authority to maintain a minimum level of operational earnings. Exclusive of the tax revenue and debt servicing costs associated with voter-approved general obligation bonds and other voter-approved debt, net water revenues, as defined by the agreements, must equal or exceed 120% of all other debt servicing costs (principal and interest). The Authority was in compliance with all of its covenants, including meeting its debt service ratio requirement.

In fiscal 1990, the Authority established a water rate stabilization fund for the purpose of identifying amounts available to mitigate future water rate increases. The Authority will transfer portions of its net water revenues (as defined) which exceed its debt service ratio requirement, into the rate stabilization fund and from time to time transfer amounts from its rate stabilization fund into net water revenues to meet its debt service ratio requirements. There were no transfers during the year ended June 30, 1999. As of June 30, 1999 and 1998, the balance in this fund, which is included in restricted cash, cash equivalents and investments, totaled $41,075,000 and $36,453,000, respectively, and is also reflected as designated retained earnings in the accompanying balance sheets.

Included in other assets are deferred financing costs of $5,520,000 and $4,981,000, net of accumulated amortization of $2,635,000 and $2,210,000, at June 30, 1999 and 1998, respectively. The deferred financing costs are being amortized over the life of the related obligations.

The aggregate principal and interest payments on long-term debt at June 30, 1999 are due as follows:

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		Principal Payment		Interest Payment		Total Debt Service
2000	$	17,117,000	$	30,774,000	$	47,891,000
2001		20,509,000		29,286,000		49,795,000
2002		22,127,000		28,487,000		50,614,000
2003		22,861,000		26,915,000		49,776,000
2004		24,081,000		25,475,000		49,556,000
Thereafter		507,079,000		231,535,000		738,614,000
	$	613,774,000	$	372,472,000	$	986,246,000

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Note 5: Plan description

The Authority's defined benefit pension plan, Miscellaneous Plan of the San Diego County Water Authority (Authority's Plan), provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. The Authority's Plan is part of the Public Agency portion of the California Public Employees Retirement System (CalPERS), an agent multiple-employer plan administered by CalPERS, which acts as a common investment and administrative agent for participating public employers within the State of California. A menu of benefit provisions as well as other requirements are established by State statutes within the Public Employees' Retirement Law. The Authority's Plan selects optional benefit provisions from the benefit menu by contract with CalPERS and adopts those benefits through local ordinance. CalPERS issues a separate comprehensive annual financial report. Copies of the CalPERS annual financial report may be obtained from the CalPERS Executive Office - 400 P Street - Sacramento, CA 95814.

Funding policy

The Authority has elected to make contributions on behalf of its employees at the required amount of 7% of their annual covered salary. The Authority is required to contribute the actuarially determined remaining amounts necessary to fund the benefits for its members. The actuarial methods and assumptions used are those adopted by the CalPERS Board of Administration. The required employer contribution rate for the year ended June 30, 1999 was 8.003%. The contribution requirements of the plan members are established by State statute and the employer contribution rate is established and may be amended by CalPERS.

Annual pension cost

For fiscal year ended June 30, 1999, the Authority's annual pension cost was $1,620,000 and the Authority actually contributed $1,620,000. The required contribution was determined as part of the June 30, 1997 actuarial valuation using the entry age normal actuarial cost method with the contributions determined as a percent of pay. The actuarial assumptions included (a) 8.25% investment rate of return (net of administrative expenses); (b) projected salary increases that vary by duration of service ranging from 3.75% to 14.20% for miscellaneous members; and (c) 3.75% cost-of-living adjustment. Both (a) and (b) include an inflation component of 3.50% The actuarial value of the Authority Plan's assets was determined using a technique that smoothes the effect of short-term volatility in the market value of investments over a two to five year period depending on the size of investment gains and/or losses. All assets in excess of these entry age normal accrued liability, as of June 30, 1997, are now amortized over time, thus reducing the employee contribution rate.

Three year trend information for Miscellaneous Plan of the San Diego County Water Authority

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Fiscal Year Ended June 30	Annual Pension Cost (APC)	Percentage of APC Contribution	Net Pension Obligation
1997	1,541,000	100%	
1998	1,492,000	100%	
1999	1,620,000	100%	

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Required supplementary information

Funded status of plan

Valuation Date June 30	Entry Age Normal Accrued Liability	Actuarial Value of Assets	Unfunded/ (Overfunded) Liability UAAL*	Funded Ratio	Annual Covered Payroll	UAAL* as a % of Payroll
1995	$ 17,325,910	$ 16,757,966	$ 567,944	96.7%	$ 9,400,709	6.042%
1996	19,880,679	19,986,401	(105,722)	100.5%	8,942,657	(1.182%)
1997	20,675,551	24,027,237	(3,351,686)	116.2%	8,969,774	(37.366%)

* Unfunded Actuarial Accrued Liability

Note 6: Deferred Compensation Plan

The Authority has adopted a deferred compensation plan in accordance with Section 457 of the Internal Revenue Code. Generally, all eligible employees may defer receipt of a portion of their salary until future years. The employees are not liable for income taxes on amounts deferred until the funds are withdrawn. At June 30, 1999 and 1998, assets of the Plan totaled $10,412,000 and $8,359,000, respectively.

In prior years, all of the Plan assets, until paid or made available to the employees or their beneficiaries, were the sole property of the Authority, subject to the claims of the Authority's general creditors. The Plan was amended during the year ended June 30, 1998, in accordance with recent changes in the Internal Revenue Code, so that all assets are now held for the exclusive benefit of the participants and their beneficiaries. Therefore, the plan assets and corresponding liability to the participants are no longer recognized in the accompanying financial statements.

Note 7. Commitments and Contingencies

Insurance

The Authority is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Authority is a participant in the Association of California Water Agencies Joint Powers Insurance Authority (JPIA) for the purpose of providing general liability insurance for the member agencies. The Authority had a self-insured retention level of $50,000 per claim for auto and general liability for the years ended June 30, 1999 and 1998. The total coverage limit is $50,000,000 at June 30, 1999. The program provides for up to $100,000,000 in coverage for property damage with a $25,000 deductible.

The Authority is also a participant in the JPIA for the purpose of providing insurance coverage for workers compensation. Liabilities under this program are accrued and charged to expense when the claims are reasonably determinable and when the existence of the Authority's liability is probable. There is no self-insurance retention required for the years ended June 30, 1999 and 1998. The total coverage under this policy is $5,500,000.

The amount of settlements did not exceed insurance coverage for the past three years for either JPIA coverages.

Construction projects

The Authority is committed to a long-range effort to increase the present aqueduct capacity, obtain additional water from a variety of sources, including water marketing, provide additional storage within the county and maximize the use of existing storage reservoirs. The Authority's current Capital Improvement Program (the Program) is budgeted at approximately $1.0 billion, to be expended over the next ten years.

The Authority has outstanding signed construction contract commitments in excess of $25,000,000 as of June 30, 1999.

Litigation

The Authority is subject to lawsuits and claims which arise out of the normal course of business. In the opinion of management, based upon the opinion of legal counsel, the disposition of such actions of which it is aware will not have a material effect on the financial position, results of operations or liquidity of the Authority.

Emergency Storage Project

On June 4, 1998, the Board of Directors approved the Emergency Storage Project (ESP) which will develop approximately 90,100 acre-feet of resources storage and supporting distribution facilities to supplement emergency water supplies available to the region in case of prolonged interruption of the imported water supply. The project is estimated to cost $736 million on an inflated basis. A combination of debt and funding from operations will be used to finance these requirements. The ratio of debt to cash used will be that which provides the smoothest water rate increase pattern over the planning horizon.

The design and construction phase of the ESP is scheduled to take place in phases between 1999 and 2011 in order to minimize water rate increases, comply with air quality protection conditions of the permit and preserve the flexibility in sizing of critical project components. The project includes the following major components:

- Design and construction of a reservoir and related infrastructure within the Olivenhain Water District. The project includes pipelines and pump stations to connect the reservoir to the Second Aqueduct and Lake Hodges. The Olivenhain and Lake Hodges facilities are scheduled for completion in 2008.
- Modifications to the existing San Vicente Dam, which would raise the dam by 54 feet, and construction of a related pipeline and pump stations which will connect the reservoir to the Second Aqueduct. The completion of the expansion of the San Vicente facilities is scheduled for 2010.

Imperial Irrigation District Water Transfer Agreement

On April 29, 1998, the Board of Directors approved the "Agreement for the Transfer of Conserved Water by and between the Imperial Irrigation District (IID) and San Diego County Water Authority" (the agreement). The terms of the agreement provide for the transfer of conserved agricultural water, as defined by the agreement, from the IID to the Authority, subject to certain terms and conditions. The duration of the agreement is for forty-five years with renewal provisions for an additional thirty years. The quantity of conserved water to be transferred during year 1 of the agreement will be 20,000 acre feet per year (AFY) beginning in 2002. This amount will increase by 20,000 AFY until a stabilized quantity of between 130,000 AFY and 200,000 AFY is reached. The determination of the quantity to be transferred within this range is solely at the discretion of the IID. The agreement provides for the transfer of up to 100,000 AFY of additional quantities of conserved water after year 10 of the agreement, subject to availability. The proposed agreement is conditioned upon, among other things, the availability of a minimum of 130,000 AFY.

The agreement includes a formula to determine the water's price that includes a discount from the price of

MWD water (starting at 25% in the first year of the agreement and declining over the next seventeen years to 5%) after an adjustment for the Authority's cost to convey the water to MWD's Colorado River Aqueduct. Under the current MWD pricing structure and Authority conveyance cost estimates, the price of the transferred water would normally be less to the Authority than the cost of MWD supplied water and would compare favorably to other sources of supply.

On July 22, 1998, the Authority and IID filed a joint petition with the State Water Resources Control Board's (SWRCB) Division of Water Rights for approval of a Long-Term Conserved Water Transfer Agreement and Change in Point of Diversion and Place of Use. The water transfer is subject to SWRCB review and approval pursuant to the continuing retained jurisdiction of the SWRCB over IID's conversation activities under both SWRCB Decision 1600, SWRCB Water Rights Order 88-20, Article X, Section 2 of the California Constitution and certain provisions of the Water Code.

On November 10, 1998, the Authority and MWD agreed to an exchange contract which will facilitate the IID transfer. Under the terms of the contract, the Authority will deliver water it acquires from IID to MWD, in exchange for the same amount of MWD water. The agreement would terminate thirty years after the start of deliveries from IID to the Authority. Based on the exchange price structure established by the contract, the total cost of the transferred water to the Authority during the initial 10 years of deliveries would be less than MWD supplied water.

The Authority is currently discussing with IID conforming certain terms of the agreement with the exchange contract. These discussions could lead to minor modifications in the agreement.

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Note 8: Pronouncement Issued But Not Yet Adopted

In June 1999, the Governmental Accounting Standards Board issued Statement of Governmental Accounting Standards No. 34, "Basic Financial Statements - and Management's Discussions and Analysis - for State and Local Governments". This Statement establishes new financial reporting requirements for state and local governments throughout the United States. Statement No. 34 is effective in three phases based on a government's total annual revenues. It will be effective for the Authority for the year ending June 30, 2002. The Authority has not completed its assessment of the effect that the adoption of Statement No. 34 will have on its financial statements.

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Supplementary Information

Year 2000 Issue

The Year 2000 issue is the result of shortcomings in many electronic data processing systems and other electronic equipment that may adversely affect a government's future operations. Because many software programs eliminate the first two digits from a year reference in most applications, the data processing system may not be able to distinguish between the year 2000 and the year 1900 which may cause the programs to process data incorrectly or stop processing data altogether. There are other possible complications as well.

The following stages have been identified as necessary to implement a Year 2000 compliant system:

Awareness Stage - Encompasses establishing a budget and project plan for dealing with the Year 2000 issue.

Assessment Stage - When the government actually begins the process of identifying all of the mission critical systems and individual components of those systems.

Remediation Stage - When the government actually makes changes to systems and equipment.

Validation/Testing Stage - When the government validates and tests the changes made during the conversation/remediation process.

In November 1998 the Authority began the process to identify and convert its mission critical computer systems to be Year 2000 compliant including non traditional imbedded microprocessor systems. The Authority's plan includes a risk assessment process which requires identification and conversion of those systems determined to be crucial for the uninterrupted provision of services to the residents of the County. The Authority plans to have all mission critical system conversions completed through the validation/testing stage by September 1999. The following summarizes the stages of work in process or completed as of June 30, 1999 to make computer systems and other microprocessor based equipment critical to conducting operations prepared for Year 2000 operations:

Mission critical systems completed through the remediation and validation/testing stages include:

- Peoplesoft Financials, Payroll and Human Resources
- Maximo PSDI
- SCADA Software and Equipment
- Microsoft Office Suite
- Servers, Network Components and Networked PC Workstations

The validation/testing stages of the above were completed subsequent to June 30, 1999.

The Authority has not been tracking the amounts of funds expended towards the Year 2000 issue. The Year 2000 costs are included within the Informational Systems budget.

The Authority has full emergency plans in place per the State of California standards. The emergency plans contain temporary operating procedures that the Authority intends to use for continuing operations should systems fail due to unpredicted Year 2000 problems.

Because of the unprecedented nature of the Year 2000 issue, its effect and the success of related remediation efforts will not be fully known until the year 2000 and thereafter. Management cannot assure that the Authority is or will be successful in whole or in part, or that parties with whom the Authority does business will be Year 2000 compliant.

END OF FINANCIAL STATEMENTS