



November 22, 1999

Honorable Mayor and City Council
Fred Meurer, City Manager
City of Monterey

I am pleased to present to you the 1998-99 Comprehensive Annual Financial Report (CAFR) for the City of Monterey. This "comprehensive" report is intended to present information that goes beyond the basic financial statements required by generally accepted accounting principles.

This report is presented in three sections: Introductory, Financial, and Statistical:

The Introductory Section includes this transmittal letter, a schedule of the City's principal officials, an organizational chart and reproductions of the awards received from the Government Finance Officers Association and the California Society of Municipal Finance Officers for last year's CAFR;

The Financial Section includes the unqualified opinion of our independent auditors, general purpose financial statements with accompanying notes, and supplemental statements;

The Statistical Section includes relevant financial and demographic information depicting the City's historical trends and other significant facts.

This report has been prepared by the Finance Department in accordance with generally accepted accounting principles (GAAP), as set forth in the pronouncements of the Governmental Accounting Standards Board (GASB) and the Financial Accounting Standards Board (FASB). Responsibility for the accuracy of the data including all disclosures rests with the City. We believe that the data as presented is accurate in all material respects, that it is presented in a manner designed to fairly set forth the financial position and results of operations of the City as measured by the financial activity of the various funds, and that all disclosures necessary to enable the reader to gain the full understanding of the City's financial affairs have been included.

This report includes all of the funds and account groups of the City of Monterey, the Redevelopment Agency of the City of Monterey and the Monterey Joint Powers Financing Authority.

City History and Overview

Las Bahia de los Pinos (Bay of Pines) was first discovered by Juan Rodriguez Cabrillo on November 17, 1542. This Spanish claim to California was reaffirmed in December, 1602, when Sebastian Viscaino officially named the port Monterey in honor of the Viceroy of New Spain who had ordered the expedition.

Founded on June 3, 1770 when Spanish soldiers claimed the land for King Charles III of Spain, the City was officially incorporated on May 30, 1850. Monterey served as the first capital of the State of California and the City's historic Colton Hall was the site of California's first constitutional convention where our state's constitution was signed in 1849.

The natural beauty, mild climate and unique attractions of Monterey draw an estimated 4 million visitors each year making our City one of the most popular destinations in the country. The Monterey Bay Aquarium, Old Fisherman's Wharf and Cannery Row are among the many interesting places to visit in Monterey.

Economic Conditions and Outlook

The City of Monterey's economic growth has continued on a positive trend in 1998-99, however, there has been a slowing of the growth seen in 1996-97 and 1997-98. Tourism continues to be the number one industry in Monterey. The tourism and hospitality industry accounts for approximately 60% of General Fund revenue. Transient occupancy tax represents the City's largest single revenue source, making up 29% of total General Fund revenues. In 1998-99, transient occupancy tax collections were up 2.4% to \$13 million. This follows increases of 9.3% and 7% achieved in 1996-97 and 1997-98, respectively. The growth rate has continued to slow following the opening of the "Outer Bay Exhibit" at the Monterey Bay Aquarium in early 1996 that fueled a "one-time" surge in tourism. Another expansion to the Monterey Bay Aquarium opened in the spring of 1999. However, this did not result in as significant an increase in tourism-related revenues.

The longer term outlook for Monterey continues to be fairly positive. Our forecast continues to be linked to a large degree that of the nearby Silicon Valley region and the State of California because these economies are continuing to grow. Monterey continues to have a strong though slowing, tourism industry.

Major Initiatives

Among the City's highest priorities is the "Window on the Bay" project. The goal is to purchase (on an opportunity-buying basis) land and buildings along the bayside of Del Monte Avenue, between Camino El Estero and the east City limit, for the improvement of Del Monte Avenue and the development of Monterey Bay Park. The first segment of the park was completed in December 1995 and includes beach volleyball courts, bikeways, walkways and open space. The City purchased a significant lot in the Phase A area of the "Window on the Bay" project in 1998-99 and, as of this writing, has closed escrow on yet another lot.

The execution of an agreement in 1997-98 between the City and the U.S. Army for the City to provide Public Works services at the Presidio of Monterey represents a unique partnership pertaining to the provision of municipal services on military installations. The City is providing street maintenance, sewer system maintenance, water system maintenance, storm drain maintenance and fence maintenance services, as well as other special project services. An additional agreement was executed for buildings and grounds maintenance during 1998-99. This is an important initiative for both the City and the U.S. Army. The goal of this program is for the Army to reduce its ongoing base operations costs and for the City to be fully reimbursed for the costs of providing these municipal services.

FINANCIAL INFORMATION

Accounting System and Budgetary Control

The City's accounting records for general government operations are maintained on a modified accrual basis, with the revenues being recorded when measurable and available. Expenditures are recorded when the services or goods are received and the liabilities incurred. Accounting records for the City's proprietary activities are maintained on the accrual basis, with revenues recorded when earned and expenses when incurred.

In maintaining the City's accounting system, consideration is given to the adequacy of internal controls. Internal controls are designed to provide reasonable assurance regarding the safeguarding of assets against loss from unauthorized use or disposition, and to ensure the reliability of financial records for preparing financial statements and maintaining accountability for assets. The concept of reasonable assurance recognizes that the cost of control should not exceed the benefits likely to be derived. The evaluation of costs and benefits requires continuing estimates and judgments by City management. We believe that the City's system of internal accounting controls continues to adequately safeguard assets and provide reasonable assurance that financial transactions are properly recorded.

Formal budgetary integration is employed as a management control device. Commitments for materials and services, such as purchase orders and contracts, are recorded as encumbrances in order to reserve that portion of the applicable appropriation. Encumbrance accounting is employed as an extension of formal budgetary integration in the General, Special Revenue, and Capital Projects funds. Encumbrances at year-end lapse then are added to the following year's budgeted appropriations. Encumbrances are reported at year-end as reservations of fund balances.

General Governmental Revenues

Revenue (GAAP basis) for the General Fund, the Special Revenues Funds, Capital Projects Fund and the Debt Service Fund totaled \$48,099,206 in fiscal year 1998-99. The amounts of revenues from various sources, their percentage to total revenues for these funds, and increase or decrease from the prior year are as follows:

<u>Revenue Source</u>	<u>1998-99</u>	<u>Percent of Total</u>	<u>1997-98</u>	<u>Increase (Decrease)</u>	<u>Percent of Increase (Decrease)</u>
Taxes	\$29,350,879	61%	\$28,676,226	\$674,653	2%
Intergovernmental	3,758,169	8%	2,386,235	1,371,934	57%
Investment Income	2,066,792	5%	2,267,104	(200,312)	(9%)
Rental Income	1,966,288	4%	1,990,422	(24,134)	(1%)
Licenses & Permits	2,707,024	6%	2,520,945	186,079	7%
Charges for Services	7,154,410	15%	6,667,208	487,202	7%
Other	<u>758,741</u>	1%	<u>675,866</u>	<u>82,875</u>	12%
Total Revenue	<u>\$47,762,303</u>	100%	<u>\$45,184,006</u>	<u>\$2,578,297</u>	6%

The increase in tax revenues is due primarily to increases in transient occupancy tax (\$310,000), and property tax (\$190,000). Revenues from charges for services have increased as a result of fees from the Monterey Sports Center, Conference Center, sewer and storm water fees. The significant increase in intergovernmental revenues is due to new or increased grant revenues such as the Surface Transportation Program (\$665,000) and Federal Highway Administration grants (\$358,000).

General Government Expenditures

Expenditures (GAAP basis) for the General Fund, the Special Revenues Funds, Capital Projects Fund and the Debt Service Fund amounted to \$50,016,899 in fiscal year 1998-99. Expenditures by function, their percentage to total expenditures for these funds, and change from the prior year are as follows:

<u>Expenditure Function</u>	<u>1998-99</u>	<u>Percent of Total</u>	<u>1997-98</u>	<u>Increase (Decrease)</u>	<u>Percent of Increase (Decrease)</u>
General Government	\$3,973,910	8%	\$3,617,949	\$355,961	10%
Public Safety	12,404,860	25%	11,962,411	442,449	4%
Public Works	9,238,000	18%	8,865,270	372,730	4%
Community Development	2,344,327	5%	2,343,108	1,219	.05%
Culture and Recreation	6,036,249	12%	5,791,288	244,961	4%
Public Facilities	3,373,947	7%	3,109,863	264,084	8%
Capital Outlay	10,122,544	20%	6,255,229	3,895,829	62%
Debt Service	<u>2,523,062</u>	5%	<u>2,276,496</u>	<u>218,052</u>	10%
Total Expenditures	<u>\$50,016,899</u>	100%	<u>\$44,221,614</u>	<u>\$5,795,285</u>	13%

The overall increase in City expenditures is due to increased costs for personnel, supplies, services, and particularly for Capital Improvement Projects.

The increase in General Government expenditures is largely due to a significant increase in litigation and court costs incurred by the City Attorney's Office (\$100,000) and an increase in recruitment related expenditures incurred by the Personnel Office (\$50,000).

The increase in Public Facilities expenditures is due to the Conference Center Sales and Marketing program (\$140,000) and to the Museum operations (\$137,000) for costs associated with the development of the Presidio Museum and other special event expenses such as the Sesquicentennial celebration, the First Night celebration and the Whalefest.

The large increase in the Capital Projects expenditures is due in part to several large projects including \$2,000,000 of Wharf II Improvements, \$900,000 of Sewer Line Camera Work, \$550,000 of Del Monte Avenue Improvements and \$1,000,000 of Street Resurfacing.

Enterprise Operations

The Marina Fund operating revenues increased by 6% to \$1.6 million in 1998-99 and operating expenses increased by 57% due to the increased depreciation costs of the recent Marina improvements. However, the Marina improvements have resulted in lower repair costs and lower utility costs.

The Cemetery Fund experienced a 7% increase in operating revenue due in part to the opening of the new 1,000 niche columbarium in 1998. Operating expenses increased by 27% due to the increased depreciation costs for the new columbarium, and non-operating expenses increased as a result of debt service for payments for the columbarium debt.

Parking Fund revenues decreased more than 1% to \$4.7 million in 1998-99. Operating expenses increased 13% resulting in net operating income of nearly \$685,000. After factoring in debt service and transfers, the Parking Fund ended the year with a loss of \$52,000. Parking fees were increased in the Fall of 1999 to help reverse this trend.

Risk Management

The City is self-insured for its general liability and workers' compensation liability for up to \$500,000 and \$300,000 per occurrence, respectively. Excess coverage for general liabilities is provided by Insurance Company of the State of Pennsylvania in a joint purchase through the Authority for California Cities Excess Liability (ACCEL), a joint powers authority of which the City is a member. The City has purchased insurance with a commercial carrier for workers' compensations claims above \$300,000. Property damage risks are covered on an occurrence basis up to \$25,000,000, with a \$100,000 deductible, by commercial insurance purchased from independent third parties.

Cash Management

The City maintains a cash and investment pool that is available for the use of all funds. Cash temporarily idle during the year was invested in U.S. Government Securities, corporate notes and the California Local Agency Investment Fund (LAIF). At June 30, 1999, 11% of the \$44,347,236 pool was invested in LAIF, 65% in U.S. Government Securities, and 21% in corporate notes. A small amount (3%) representing trust assets is invested in a variety of preferred and common stock. At June 30, 1999, investments in the City Treasury include instruments with a variety of interest rate terms. Approximately 89% of such instruments bear interest at fixed rates. The remaining 11%

bears interest at floating rates which vary directly with changes in market interest rates, based on various indices.

Debt Administration

At June 30, 1999, the City had \$36,567,544 in long-term debt (not including compensated absences). This includes \$28,830,000 in lease revenue bonds issued by the Redevelopment Agency and the Joint Powers Financing Authority, \$6,402,665 in loans from the State of California (largely for the Marina) and a \$913,050 loan for the new cemetery columbarium.

On May 1, 1999, the Redevelopment Agency issued lease revenue refunding bonds of \$19,045,000 to refund the 1992 and the 1993 Lease Revenue Bonds. In addition, a portion of the 1999 Bond proceeds was used to repay the loan for the new cemetery columbarium on July 30, 1999. As a result of the refunding, the total debt service requirement was reduced by \$1,425,025, which resulted in an economic gain (the difference between the present value of the debt service payments on the old and the new debt) of \$983,000.

OTHER INFORMATION

Independent Audit

Article 6 of the City Charter requires an annual audit of the City's financial records by independent certified public accountants. The accounting firm of Deloitte & Touche LLP was selected by the City Council to perform the audit. In addition to meeting the requirements of the City Charter, the audit was also designed to meet the requirements of the Federal Single Audit Act of 1984, Single Audit Act Amendments of 1996 and related OMB Circular A-133, "Audits of States, Local Governments and Non-profit Organizations." The auditor's report on the general-purpose financial statements and combining and individual fund statements and schedules is included in the financial section of the report. The auditor's reports related specifically to the single audit are included in the Single Audit report, which is a separate document.

Award

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the City of Monterey for its Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 1998. The City has also been awarded the Certificate of Achievement Award for Financial Reporting by the California Society of Municipal Finance Officers (CSMFO).

In order to be awarded a Certificate of Achievement, a government must publish an easily readable and efficiently organized CAFR whose contents conform to rigorous program standards. Such reports must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe our current report continues to conform to the Certificate of Achievement Program requirements and we are submitting it to the GFOA and CSMFO to determine its eligibility for another certificate.

Acknowledgments

The preparation of the Comprehensive Annual Financial Report on a timely basis was made possible by the dedicated service of the entire staff of the finance department. Each member of the department has my sincere appreciation for the contributions made in the preparation of this report.

In closing, without the leadership and support of the Council and City Manager, preparation of this report would not have been possible.

Sincerely,

Don Rhoads
Finance Director