

TRUCKEE MEADOWS WATER AUTHORITY  
COMPREHENSIVE ANNUAL FINANCIAL REPORT

JUNE 30, 2004 AND 2003

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**INTRODUCTORY SECTION**



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To the Board of Directors, Our Customers, and Bondholders:

We are pleased to submit the Comprehensive Annual Financial Report (CAFR) for the Truckee Meadows Water Authority (TMWA) for the Fiscal Year ended June 30, 2004. The purpose of the report is to provide the Board of Directors, our customers, and bondholders as well as other interested parties with reliable financial information about TMWA. TMWA's Finance Department has prepared the CAFR in accordance with accounting principles, generally accepted in the United States of America. We believe the report presented is accurate in all material respects, and the results of operations of TMWA and all necessary disclosures enable the reader to gain the maximum understanding of TMWA's financial activity.

The CAFR consists of four sections:

**Introductory Section-** This section comprises the letter of transmittal, which contains information relative to TMWA's background, a listing of TMWA's principal officers, organizational chart and other relevant information to assist the reader in understanding TMWA's operations, financial condition, and accomplishments. The Certificate of Achievement for Excellence in Financial Reporting for the fiscal year ended June 30, 2003 is also presented in the section.

**Financial Section-** This section consists of TMWA's basic financial statements, supplementary financial information and independent auditor's report on the basic financial statements, which also includes Management's Discussion and Analysis. The financial statements presented in this section were prepared in accordance with generally accepted accounting principles.

**Statistical Section-** This section comprises selected financial, operational and demographic information generally presented on an annual basis since the creation of TMWA on June 11, 2001.

**Compliance Section-** This section consists of information regarding TMWA's compliance with state statutes, in particular conformance with the Local Government Budget and Finance Act.

## **REPORTING ENTITY**

TMWA's financial activities are reported 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 activity. The activities of enterprise funds closely resemble those of an ongoing business in which the purpose is to preserve and add to financial resources and pay for operating expenses and certain capital expenses from operating revenues and capital contributions.

Enterprise funds account for operations that provide services on a continuous basis and are financed by revenues derived from user charges. Revenues are recognized when earned and expenses are recognized as incurred. TMWA has no component units associated with its financial reporting entity.

TMWA applies all applicable Governmental Accounting Standards Board (GASB) pronouncements in accounting and reporting for proprietary operations, as well as the following pronouncements issued on or before November 30, 1989 unless those pronouncements conflict with or contradict GASB pronouncements: Financial Accounting Standards Board (FASB) Statements and Interpretations, Accounting Principles Board (APB) Opinions, and Accounting Research Bulletins (ARB's) of the Committee on Accounting Procedure.

Nevada Revised Statutes requires that an independent certified public accounting firm selected by the Board of Directors audit TMWA's financial statements on an annual basis. The independent auditor's report for the fiscal years ended June 30, 2004 and 2003 are presented in the Financial Section of this report. TMWA complies with the Local Government Budget and Finance Act as embodied in Chapter 354 of the Nevada Revised Statutes.

## **FORMATION AND ORGANIZATION**

TMWA was formed as a Joint Powers Authority pursuant to chapter 277 of the Nevada Revised Statutes and is a political subdivision of the State of Nevada. TMWA is separate from its member agencies: City of Reno, City of Sparks and Washoe County. TMWA was formed in November 2000 for the purpose of acquiring the water division of Sierra Pacific Power Co. ("SPPCo"), a subsidiary of Sierra Pacific Resources ("SRP"), with the goal of retaining local control over the water resources of the area.

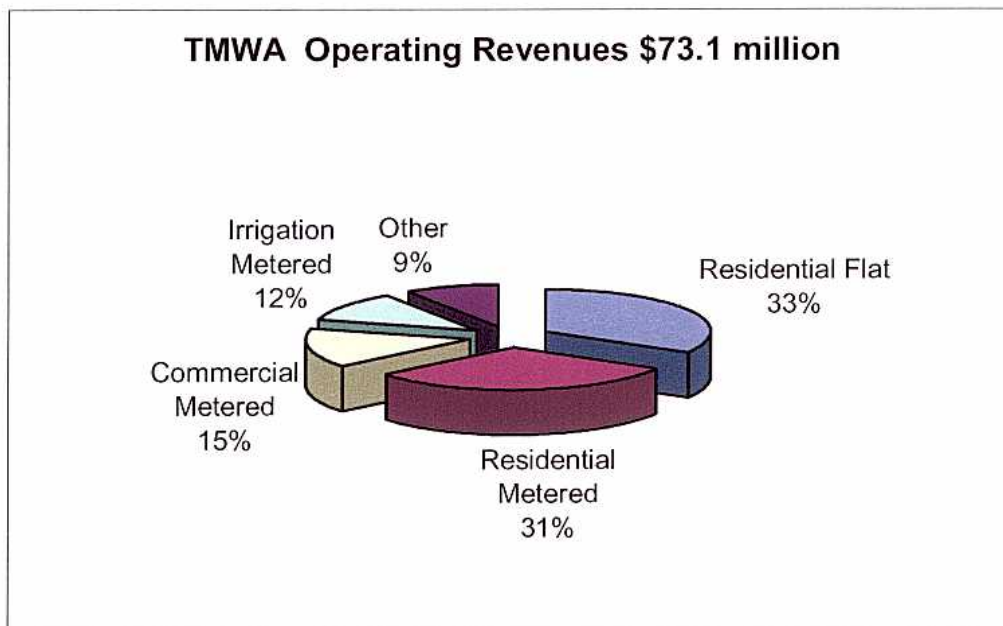
TMWA successfully participated in a blind competitive bid for the net assets of the SRP's water utility after the members submitted a joint "Proposal to Purchase the Water Utility Assets of Sierra Pacific Resources". These assets included four run of river hydroelectric plants along the Truckee River. These hydro facilities are essential for the operation of the water business and were part of the complete asset purchase. TMWA operates in a prescribed retail service area as described in the agreement between SPPCo and Washoe County dated June 25, 1996 as amended and the retail service territory can be modified from time to time pursuant to such agreement.

TMWA has no financial interdependence with its member agencies other than TMWA charges water customers Right of Way Toll (ROWT) Fees on billed water revenues in two jurisdictions, and remits these fees to the Cities of Reno and Sparks. Currently the City of Reno ROWT fee is 2%; the City of Sparks raised its ROWT fee to 5% in the fourth quarter of the fiscal year. TMWA also charges water customers a 1.5% fee for funding of the Regional Water Planning Commission (RWPC) activities. These fees are not considered TMWA revenues and TMWA only serves as a pass through entity for collecting and remitting these fees to the cities and RWPC.

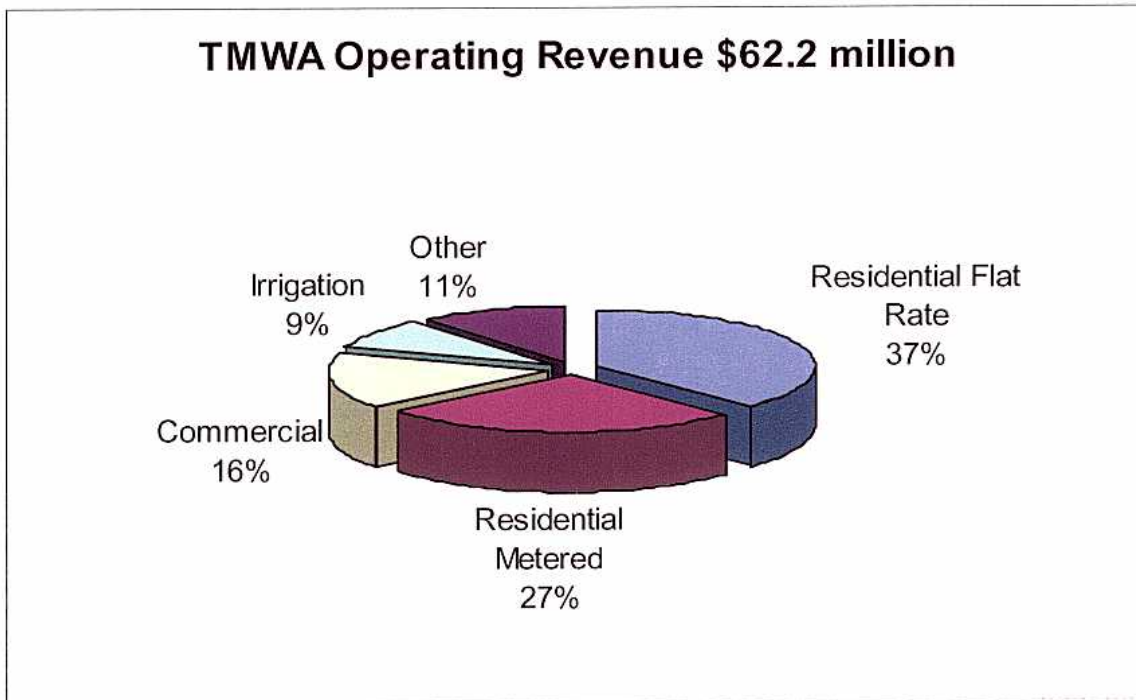
TMWA has broad powers to finance, construct and operate the water system, for the diversion, treatment, distribution, and retail sale of treated water to retail and wholesale customers. TMWA has full authority to set water rates for services subject to approval by the TMWA Board of Directors, without approval by any other entities. TMWA is a tax-exempt entity for purposes of federal taxes and State of Nevada property, sales and use taxes, as well as other state taxes. TMWA pays property taxes in Nevada and Sierra Counties, California for the privilege of storing water in private and federal reservoirs. TMWA has no taxing authority.

TMWA provides treated water under four wholesale contracts and over 84,000 residential, commercial and irrigation services in the Reno-Sparks metropolitan areas. The two wholesale customers are the Sun Valley General Improvement District (SVGID) and the Washoe County Department of Water Resources (WCDWR). SVGID, located north of Reno-Sparks, is served on a firm delivery basis and is wholly dependent upon TMWA water deliveries since this district has no source of water supply. The WCDWR purchases water from TMWA on a firm standby partial requirements basis since WCDWR can provide a significant portion of its own water demands with its groundwater resources.

The following graph depicts the proportion of billed revenues by customer class during fiscal year 2003-2004:



The following graph depicts the proportion of billed revenues by customer class during fiscal year 2002-2003:



The TMWA was created in November 2000 to accomplish the goal of purchasing the water assets of SPPCo. In the three years since TMWA began operations (June 11, 2001), the utility has successfully matured from a startup organization with certain customer care functions performed on a contractual basis by SPPCo. On August 4, 2002, TMWA took over all customer care responsibilities from SPPCo with the exception of some of the meter reading tasks.

TMWA's financial position has remained stable over the last three years of operation. Liquidity levels remain relatively constant year over year with sufficient cash resources to finance operating expenses and near term capital spending requirements. In June 2003, TMWA's Board of Directors adopted facility charges, to collect from new developments to pay for the construction of new storage, supply, and treatment facilities. In September 2003, TMWA's Board of Directors adopted revised customer rate schedules designed to increase water sales revenues annually by \$10 to \$11 million, with the rate increase effective October 1, 2003. TMWA operating revenues increased \$9.5 million in fiscal year 2003-2004 as a result of this rate increase. The remainder of the revenue increase was due to higher deliveries of water to new and existing customers.

These board actions were taken in response to results of a five-year financial forecast, which indicated the need for adopting these new fees and customer rates. The goal of TMWA, as adopted by the Board, is to maintain a coverage ratio of 1.5x, sufficient to meet minimum debt service coverage requirements and fund a majority of rehabilitative capital projects on a pay-as-you-go basis. These measures were deemed necessary to maintain system infrastructure in a prudent manner and insure that TMWA's bondholders are adequately protected. There are no other restrictions, commitments, or other limitations that would restrict the unrestricted cash assets for use in meeting TMWA's obligations.

TMWA is governed by a seven-member board comprised of three Directors appointed by the City of Reno, two Directors appointed by the City of Sparks, one Director appointed by Washoe County, and one-at-large Director who shall be an elected official from the governing body of a Member, nominated by the appointed Directors and approved by the governing body of each of the Members. A Director who is not an elected official and the at-large Director shall be appointed for a term of two years. No Director who is an elected official may serve beyond his or her term of office. A Director may not receive compensation from TMWA for services as a Director but can be reimbursed for reasonable expenses in conducting TMWA business. No payments have been made to any Director.

The General Manager of TMWA is the chief administrative officer who is appointed and serves at will and at the pleasure of the TMWA Board. The General Manager is responsible to the Board for the proper and efficient administration of TMWA with the power to plan, organize, and direct all TMWA activities, appoint and remove employees, authorize expenses within the approved budget and enter into contracts as authorized by the Board. Three managing directors and five managers are responsible for implementing and coordinating departmental activities. All operational, customer services, new businesses, financial and administrative functions of TMWA are highly integrated.

The Water Operations and Maintenance function is headed by the Director of Water Operations and supported by four managers. These managers direct water treatment and distribution activities, hydroelectric and system maintenance activities, water quality and special project activities, system planning, engineering and construction responsibilities.

The Customer Relations function is headed by the Director of Customer Relations who oversees the bundled customer services provided by outside contractors, new service processes, inspection services, community relations, water conservation activities and other community efforts.

The Water Planning and Resource function is under the supervisory responsibility of the Director of Water Resources who oversees the development of surface and groundwater resources, and administers the purchase and sale of land and water rights. This department also oversees GIS and Information Technology activities.

The Finance and Administration function, headed by the Manager of Finance and Administrative Services is responsible for centralized services and support to operating functions. Accounting, human resources and purchasing activities are provided under contract by the City of Reno but these responsibilities are under the direct supervision of this area, which is responsible for the financial reporting, budgeting, and strategic financial planning of TMWA.

## **ECONOMIC OUTLOOK AND WATER RESOURCES**

TMWA operates in a service territory that has exhibited steady customer/premise growth. The Reno-Sparks Metropolitan area is a very desirable location due to its favorable climate, numerous outdoor recreational activities, and minimal taxes, in addition to gaming opportunities. The Reno-Sparks metropolitan area is also centrally located in the Pacific region affording efficient distribution of goods throughout this region of the United States. Nevada's favorable

business tax environment provides opportunities for certain industries to locate in Northern Nevada. Presently, the Reno-Sparks metropolitan and adjacent areas are experiencing steady residential growth coupled with growth in medium sized manufacturing and distribution businesses.

To meet the demands of regional growth, TMWA prepared a very detailed Water Resource Plan for the years 2005-2025 that was adopted by the Board in March 2003. This extensive plan addresses current water resources, future water resources, and water rights availability as well as defined drought standards. The focal point of the Water Resource Plan is the population and water demand forecasts for the TMWA service territory. These forecasts rely upon the results of TMWA's Population and Employment Econometric Model for Washoe County. This time series model simultaneously forecasts population and employment in Washoe County using historical employment and population data from 1969 to 2000.

For the year 2000 the total population of Washoe County was determined to be approximately 339,000 citizens of whom 251,000, or 74%, reside in TMWA's retail service territory. By the year 2025 TMWA predicts Washoe County to have approximately 488,000 citizens of which 360,000, or again 74%, reside in TMWA's retail service territory. Based upon these population forecasts, water demands are expected to be 110,000 acre-feet in the year 2025, a 34% increase over the 87,000-acre feet of water produced in the year 2003. This increase in water demand assumes the full metering of the TMWA water system by the year 2010. Actual completion of metering the entire water system is expected in the next two to three years

TMWA's current water resources consist of 138,000 acre-feet of decreed, storage, and irrigation rights sufficient to generate water supplies for customer demands. TMWA does not have to rely upon its privately owned stored water (POSW) held in upstream reservoirs or all its groundwater resources for demands in average or above average precipitation years since these rights are held in reserve for drought years. TMWA relies primarily on the Truckee River and will resort only to POSW and additional ground water in years with less than average precipitation.

TMWA's future water resources will be the product of a number of efforts, which include expanded drought storage, acquisition of additional rights from agricultural users and/or the acquisition of additional storage in upstream reservoirs. TMWA is a very active supporter and participant in the Truckee River Operating Agreement (TROA) process. TROA is intended to provide TMWA customers with certainty regarding the operation of the system and additional drought supplies for existing as well as new customers. TMWA will continue toward TROA implementation because of the numerous benefits it provides through expanded drought storage, water quality benefits, expanded recreation, protection of endangered species, interstate allocation of Tahoe and Truckee rights, and litigation resolution.

The availability of water rights is integral to securing additional supplies of water for municipal and industrial use. Reviews of available Truckee River water rights show sufficient water rights exist to meet future water service commitments through the water-planning horizon, 2005-2025. However, acquiring and transferring these water rights, which can be fractionated, and require resolution of title issues, will require investments of time and money before they can be transferred for TMWA use.

TMWA continues to work closely with the cities of Reno, Sparks, and with Washoe County and the Pyramid Lake Paiute Tribe to explore opportunities that satisfy TMWA operating requirements, while enhancing Truckee River water flows in the Lower Truckee River, and improve Lower Truckee River water quality. Since the number of Truckee Meadows water rights is limited, close coordination of the various water interests must occur to avoid undue stress to the water rights market.

## **TMWA MILESTONES**

In May 2003, TMWA refined a five-year financial plan after the annual budget cycle. The planning horizon was very important because TMWA will begin paying the principal component of its acquisition debt on July 1, 2005. The first principal payment will be \$6.5 million in addition to current annual interest payments of \$23.6 million. Funding of this payment must begin in July 2004 with monthly deposits to the bond trustee at \$543,000 per month.

Based upon financial projections, TMWA determined that revenues in fiscal year 2005-2006 would be insufficient to cover projected operating expenses of \$35.6 million, annual debt service payments averaging \$30.1 million, and fund rehabilitative capital reinvestments in the water system approximating \$15.0 million per year. The total revenue deficiency was projected to be about \$20.0 million.

Based upon financial projections, TMWA management proposed, and the TWMA Board adopted in June of 2003 new facility charges to finance new capital projects for growth driven water system capacity. The new rates became fully effective December 31, 2003.

Concurrent with the adoption of developer facility charges, discussions began on a cost of service study to revise customer rates. TMWA kept the commitment to customers that water rates would not be adjusted for two years after the startup of business on June 11, 2001. The water rates inherited from SPPCo were based on investor owned utility methodologies and did not completely reflect the cost of service. The cost allocation method chosen by TMWA was the commodity-demand approach, one of the more common cost allocation methodologies.

The reason for selecting this method of cost allocation was to design rates that would preserve water resources consistent with other TMWA water conservation programs, control peak demands on water system infrastructure, and utilize existing plant capacities as efficiently as possible. The overall average rate increase over the three years beginning in fiscal year 2003-2004 was calculated at 39%. In September 2003, the TMWA Board adopted a three-year rate implementation plan and approved phase one of a proposed three-year rate increase.

The TMWA Board agreed in August 2003 that a minimum debt coverage ratio of a 1.5x will meet annual debt service requirements and will fund the majority of rehabilitative capital projects on a pay-as-you-go basis. TMWA's commitment to system rehabilitation was outlined in the Engineers Report prepared by CH2M Hill, an engineering consulting firm, as part of TMWA's acquisition process. This report was an essential part of the 2001 Series A and B Bond Offering Memorandum.

This report recommended expanded water system rehabilitation efforts in the form of increased water main replacements, increased polybutylene and galvanized service replacements, storage improvements, upstream dam and spillway improvements, armoring of the Highland Canal that feeds raw water into the Chalk Bluff Water Treatment Plant, with increased emphasis on rebuilding pump stations and other pressure enhancements. The Engineers Report emphasized the need to increase water main replacements from the original rate of two miles per year to eight miles per year. All these initiatives have been formally incorporated into TMWA's Capital Improvement Plans.

Beginning in fiscal year 2004-2005, TMWA will initiate a ten-year planning horizon for funding of future capital improvement programs. To begin this process, the 20-year Facility Plan will be revised and TMWA operations and finance personnel will conduct a detailed analysis of areas for system improvements. Also, updated costs will be presented. This effort is expected to be completed by the end of calendar year 2004 and will provide expectations on the future level of developer facility charges and customer rate increases.

## **WATER QUALITY**

TMWA's highest priority is the protection of public health through modern water treatment techniques and water quality monitoring efforts. TMWA's primary source of water is the Truckee River, which sources at Lake Tahoe and other tributaries to the Truckee River, travels into Nevada through the Reno-Sparks Metropolitan area with the terminus of the river at Pyramid Lake, approximately a 120-mile distance. The river's water quality is excellent but additional steps are taken to purify the water to meet safe drinking water standards that were set forth by the United States Department of Environmental Protection in the early 90's. To meet new water quality regulations TMWA's predecessor built the 69 million gallons per day (MGD) Chalk Bluff treatment plant and modernized the existing 25 MGD Glendale treatment plant in the 1994-1996 timeframe. The Chalk Bluff treatment facility has been expanded to 84 MGD in the past year.

TMWA spends nearly \$0.9 million per year on monitoring water quality by analyzing nearly 10,000 samples per year at 150 locations throughout the TMWA water system. TMWA lab specialists perform water quality tests for nearly 100 different chemical, physical, and biological attributes. Test results are published each year in the Annual Water Quality Report, which is mailed to every TMWA customer. TMWA adheres strictly to every standard set by the United States Environmental Protection Agency. These standards are administered and enforced by Nevada State Division of Health.

TMWA is also subject to the new arsenic regulation, as promulgated by the United States Environmental Protection Agency. The Nevada State Division of Health enforces these federal rules. Under present standards, TMWA will be required to be in compliance with the new arsenic standards by January 1, 2006. The drinking water standard for arsenic compliance has been reduced from 50 parts per billion, (ppb) to 10 ppb, making ten of TMWA's wells subject to the new regulations. The arsenic levels in these wells range from 11ppb to 25 ppb. TMWA will submit our prepared compliance plan to the Nevada Department of Health as soon as they formally adopt regulations, which are expected in late 2004. The expected cost of compliance is

estimated to be between \$12.0 million and \$22.0 million. Refer to Note 8 in the accompanying TMWA financial statements for more information.

## **WATER CONSERVATION**

Water conservation is a high priority at TMWA. Prudent use of the area's water resources extends this vital resource to periods of dry weather patterns and reduces or defers further investments in new plant and system capacities. The purpose of water conservation at TMWA is to promote wise use of water through a number of initiatives. TMWA's current conservation programs are designed to achieve 10% annual water savings as part of the conservation goal agreed to in the 1996 Water Conservation Agreement between the Regional Water Planning Commission, TMWA's predecessor SPPCo, the Pyramid Lake Paiute Tribe, and the United States. The backbone of water conservation in the Truckee Meadows is the Water Meter Retrofit Program.

### **The Water Meter Retrofit Program**

In 1995, the conversion of TMWA's 44,651 flat rate services to metered services began. As of June 30, 2004, TMWA estimates that only 11,000 residential metering facilities remain to be installed. The estimated cost to complete this endeavor is estimated to be about \$12.0 million.

The complete metering of the TMWA water system is expected to achieve at least a 10% reduction in water demands annually. Developers, through a charge of \$1,830 for every acre-foot of new water demand, provide funding of this endeavor. These funds are considered restricted cash assets as represented on TMWA's balance sheet.

Complete metering of TMWA's system will also allow for determination of system losses and focus financial resources to areas of the service territory that requires system rehabilitation.

### **Twice a Week Watering**

TMWA's predecessor, SPPCo, initiated this voluntary program in the late 1980's in an effort to avoid investment in new facilities brought on by growing demands. During the 1987 to 1994 period, twice a week watering became mandatory and has remained in place since. This program was continued even though more productive weather patterns relieved the drought pattern. The main purpose of this program is to more evenly distribute the peak demands for water during a summer week, which translates to less peaking demand on system capacities. Consequently more efficient use of plant capacities can be realized, minimizing further investment in plant.

### **Landscape Efficiency Program**

This program promotes the use of attractive drought tolerant plants for the high desert climate experienced in Western Nevada. The program is augmented by certain irrigation customers, such as common area turf, road median landscapes, as well as certain commercial customers participating in an irrigation program based on data supplied by evaporation-transpiration sensing equipment. This equipment controls the amount of irrigation based upon moisture levels

in turf areas. Also during periods of wet weather patterns, irrigation is deferred until such time as turf moisture levels indicate irrigation must be applied. Results on a limited group of participants indicate irrigation reduction of at least 10%, resulting in lower water bills and again less demand on plant facilities.

### **Water Audit Program**

This program assists residential customers in the evaluation of both indoor and outdoor water use. TMWA water conservation consultants visit residents and businesses to measure the amount of water applied to lawns and landscape. After evaluation of information, recommendations are made to the customer on how to adjust consumption without damaging landscape.

TMWA responds to high bill complaints to assist customers with identifying the source of potential water leaks. Water leaks are often found to exist in the service line from the meter to the house, which is the responsibility of the homeowner. Sometimes homeowners are unaware of the amount of water loss that can occur from a leaking plumbing fixture inside the home. TMWA also furnishes water saving fixtures to interested homeowners.

### **Classroom Education**

TMWA participates in a number of community events that promote conservation and responsible water use education. TMWA works with various schools by presenting information about the area's water resources, how these resources are used, and the benefits of water conservation.

## **WATER RESOURCE AND PLANNING**

TMWA's water planning department undertakes a number of water resource planning activities. In addition to this water planning activity, TMWA also maintains water rights for present service needs, issues will-serve commitment letters to developers, requires and accepts permanent dedication of water rights from developers to obtain water service, and manages the Water Meter Retrofit Fund. This department also is an active purchaser of water rights on the open market from which will-serve commitment letters are sold to new applicants for service.

TMWA's water planning activities are driven by Article 5 of the Joint Power's Authority which required that within the first two years of TMWA's existence a Water Resource Plan and be formulated. The primary purpose of water resource planning for the Truckee Meadows is to determine how to supply the water needs of current and future customers with current and future water resources during drought and non-drought years. Water resource planning is a dynamic process utilizing the most recent water usage, snow pack, river flow, and population data available.

TMWA's published water plan was developed with the purpose of establishing a water budget and resource plan for the Authority, reflect water supplies available to TMWA, the peaking capacity required for delivery of water supplies, and the means by which such requirements will be met. TMWA also prepares, updates, and oversees the implementation of a water conservation

plan for the use of municipal, industrial, and domestic water supplies within the retail service area of TMWA.

A critical subject in the greater Truckee Meadows is the establishment of a drought-planning standard for the region. This topic, of much debate, was discussed with TMWA's Member Agencies and many interested parties over the course of several months. The outcome of these discussions was presented to the TMWA Board. The TMWA Board passed a resolution to adopt a nine-year drought standard for future water planning and budgeting purposes. This standard is one year greater than the longest drought experienced in the last century. A nine-year drought could be expected to occur once in 375 years.

## **FINANCIAL INFORMATION**

### **Internal controls**

TMWA employs various internal controls for the safeguarding of assets against losses from unauthorized use or disposition. TMWA's management is responsible for establishing and maintaining a system of internal controls designed to meet these objectives. Another purpose of internal controls is to ensure that accounting data are compiled to allow for the preparation of financial statements in accordance with generally accepted accounting principles. The internal control structure is designed to provide reasonable assurance that these objectives are met. When establishing or reviewing internal controls, management weighs the cost to implement such controls over the benefits derived from implementing such controls. TMWA management is constantly looking for opportunities to improve or redesign internal controls. A key component of TMWA's internal controls is its budgetary controls.

### **Budgetary Controls**

TMWA is legally required to prepare, present to the TMWA Board and adopt an annual budget in conformance with Chapter 354 of the Nevada Revised Statutes. These statutes comprise the Administration of Local Government Budget and Finance Act, which stipulates that the Board be presented with a tentative budget by April 15 of each year, with formal adoption of the budget after a public hearing on the third Thursday of May of each year. The adopted budget is then filed with the Nevada Department of Taxation.

TMWA is also required to prepare a Capital Improvement Plan for review and formal acceptance by the TMWA Board. This plan is a comprehensive compilation of all capital projects and capital outlays expected during the ensuing fiscal year. TMWA's Board is kept informed of TMWA's financial performance throughout the fiscal year at scheduled Board meetings. The General Manager, as the chief administrative officer, is authorized to approve all expenses that are within the budget. This authority is conferred upon the General Manager by virtue of the cooperative agreement between the City of Reno, City of Sparks, and the County of Washoe. This arrangement allows for the efficient operation of TMWA.

In fiscal year 2004, TMWA approved a ten year Capital Improvement Plan with a ten year spending level of \$357.9 million. Much of this spending will be directed towards increasing system capacity funded with developer facility charges and major system rehabilitation programs funded through customer water rates. TMWA has provided for mitigation of arsenic in this Capital Improvement Plan. It is difficult to quantify the exact cost of arsenic mitigation until such time the State of Nevada Environmental Protection Agency adopts rules to implement the new standard.

### **BUDGET ANALYSIS AND VARIANCES**

Actual operating revenues were \$5.1 million over budget for fiscal year ended June 30, 2004. Total budgeted operating revenues were \$68.0 million as compared to \$73.1 million in actual revenue. Charges for water sales were \$4.1 million over budget and hydroelectric and other operating sales were \$1.0 million over budget.

Total operating expenses of \$44.7 million were nearly exactly on budget of \$44.9 million. Greater than anticipated spending on service and supplies of \$0.5 million was offset by lower actual spending on operating salaries and wages of \$0.5 million, lower employee benefit spending of \$0.4 million. Depreciation expense was \$0.2 million greater than budget because of greater than expected developer infrastructure contributions. Lower operating wages and salaries were due to field personnel being assigned to capital projects during the winter season and holding vacant positions open as long as possible. Employee benefit spending was less than budgeted because of less spending on health care expenses. Services and supplies spending was slightly higher than budget, but was not due to greater spending on any one particular expense.

Non-operating revenues, essentially investment income, were \$0.1 million less than budgeted. Greater than budgeted capitalized interest income was the reason for the variance. Interest expense was \$0.4 million less than budgeted. Variations in capitalizing interest expense to construction projects will create minor variances between budgeted and actual interest expense.

Capital contribution revenues \$13.8 million greater than budget. Contributions to the meter retrofit program were \$3.2 million greater than budget because these contributions are directly related to water right/will-serve sales. Consequently, contributions for water right/will serve sales were greater by \$4.5 million.

Developer infrastructure contributions were \$1.9 million greater than budget because of numerous completions of the dedication process for subdivision water mains, water services, and one pump station. Other capital contributions, such as feeder main and other infrastructure oversizing, were \$2.4 million greater than budget, indicative of a healthy construction environment.

Total Capital Improvement Plan expenditures were originally budgeted for \$44.7 million in fiscal year 2003-2004. Actual spending was approximately \$37.0 million. Delays in construction of three storage tanks were the primary reason for the reduction in capital spending.

As reflected in the Statement of Cash Flows, TMWA financed the operating budget, and revised capital improvement plans from operating cash flow, developer cash contributions, and investment income. As of June 30, 2004, TMWA has approximately \$42.7 million of financial resources to fund future capital projects.

TMWA continued funding of required cash reserves as prescribed by TMWA's bond covenants. TMWA funded the operations and maintenance reserve with an additional \$0.2 million. TMWA is required to contribute to this reserve fund and maintain a reserve balance equal to one-sixth of TMWA's revised final operating budget. TMWA also contributed \$2.0 million to the renewal and replacement reserve account to bring the balance in this account to \$5.5 million. TMWA is required to fund this account at the rate of \$2.0 million annually until such time the balance in this reserve account reaches \$10.0 million. The TMWA Board of Directors adopted a resolution to increase the water rate stabilization account to \$1.8 million from \$0.5 million. This increase was funded from investment proceeds that were in excess of budget.

### **Cash Management**

Presently, TMWA has approximately \$112.8 million in unrestricted and restricted cash (refer to Note 4 to the financial statements). Forty one percent (41%) of the total cash is invested in various investment contracts with major banks. The weighted average return on investments for the fiscal year 2003-2004 was 4.1%, generating nearly \$4.4 million in investment income before capitalization of investment income pursuant to FASB 62. One investment contract with a balance of \$51.7 million expired on June 1, 2004. TMWA has placed \$63.0 million in a new investment portfolio with the goal of meeting liquidity needs for the upcoming fiscal year. The return on these investments is approximately 2.0% because of the short term duration of the portfolio.

### **Risk Management**

To protect against risk of loss, TMWA has purchased various insurance policies. These policies include Property, General Liability, Auto Liability, Public Officials Liability, Employment Practices Liability and Commercial Pollution Legal Liability coverage. Unfortunately, since September 11, 2001 the insurance industry has changed considerably with insurance premiums for all lines of insurance coverage increasing substantially over the last three years. Although the property insurance premiums have begun to stabilize, premiums on the other lines of insurance have increased. TMWA has continued to insure with only "A" rated carriers.

TMWA's major treatment plants, two reservoirs, and operations center are all covered under a policy underwritten by Affiliated FM Insurance Company. This policy provides for a blanket limit of \$185,000,000 of all risk insurance coverage, subject to standard exclusions. Coverage also provided for are \$50.0 million for Earthquake with the exclusion of assets in California; \$25.0 million in Flood with the Glendale Treatment Plant specifically excluded; and \$9.0 million for Loss of Earnings. The loss of earnings coverage allows TMWA to avoid the use of the bond reserves established pursuant to bond covenants as provided for in the 2001 Series A and Series B bond issues in the event an insured loss occurs. The deductible for Earthquake and Flood coverage is \$100,000 per location. The deductible for all other covered perils is \$25,000.

Granite States Insurance Company (an AIG Company) provides General Liability and Automobile Liability coverage for the first \$1,000,000 in limits. The General Liability policy is subject to a \$25,000 per occurrence Self Insured Retention. The Auto Liability coverage is subject to a \$10,000 deductible per accident. TMWA has purchased another \$10.0 million liability policy in excess of the primary \$1,000,000 in coverage. The excess Umbrella Liability Policy is written with the New Hampshire Insurance Company (an AIG Company).

The Employer's Insurance Company of Nevada (EICON) provides worker's compensation insurance for TMWA employees. This is a fully insured program with no deductible and coverage has been issued for statutory limits as required by the State of Nevada. The policy also provides \$1,000,000 in limits for Employers Liability coverage. TMWA participates in the health insurance programs of the City of Reno.

The Gulf Insurance Group provides Crime coverage for \$250,000, subject to a \$10,000 deductible. The policy includes coverage for Employee Dishonesty, Forgery or Alteration, and various theft conditions.

The American International Specialty Lines Insurance Company provides Commercial Pollution Liability coverage. This policy was placed when TMWA purchased the water assets from SPPCo. The policy was written for \$50,000,000 in limits and is subject to a \$100,000 deductible for each incident. The Products Pollution coverage is limited to \$35,000,000. The policy extended from June 11, 2001 to June 11, 2011.

## **PENSION AND DEFERRED COMPENSATION PLANS**

TMWA participates in the Nevada Public Employees Retirement System (PERS), a multiple-employer-defined-benefit pension plan. PERS provides retirement and disability benefits, annual cost of living adjustments, and death benefits to plan members and beneficiaries. PERS is the common investment and administrative agent for participating public entities within the State of Nevada. Benefits levels and all administrative requirements are established by statute. TMWA has elected to make contributions on behalf of its employees, but all employees are allowed to choose between two funding options.

Under the first option, TMWA funds all contributions to PERS, the second option is a 50/50 option whereby the employee funds one-half of the contributions and TMWA funds the other one-half of the contributions. Under the first option the employees are not entitled to reimbursement of their contributions if they leave the employ of TMWA prior to vesting. An employee vests with PERS after five years of cumulative employment with the PERS system. Under option two the employee can be reimbursed for the employee's contributions only, but have no rights to any investment earnings. Contribution requirements are established by state statute.

In addition, TMWA provides deferred compensation plans in accordance with Sections 401(a) and 457 of the Internal Revenue Code. TMWA's eligible employees can elect to defer a portion of their salary until future years. The employees are not liable for income taxes on amounts deferred until funds are withdrawn. All plan assets are held for the exclusive benefit of the plan

participants and their beneficiaries. Because plan assets are for the benefit of TMWA employees and beneficiaries, the plan assets and corresponding liability to pay participants are not recognized in the accompanying financial statements.

## ACKNOWLEDGEMENTS

The timely preparation of this report could not be done without the assistance of TMWA finance personnel, finance consultants, and the management and employees of TMWA. We would like to thank the Board of Directors, TMWA customers, and the development community, for their commitment to the long-term financial stewardship of TMWA.

Respectfully submitted,



Lori Williams  
General Manager



Jeffrey P. Tissier, CPA  
Manager of Financial and Administrative Services

**TRUCKEE MEADOWS WATER AUTHORITY  
LIST OF PRINCIPAL OFFICIALS**

**TMWA Board of Directors**

Tony Armstrong, Mayor, City of Sparks, Chair of the Board

Mike Carrigan, Councilperson, City of Sparks, Vice Chair of the Board

Bob Cashell, Mayor, City of Reno, Board Member

David Aiazzi, Councilperson, City of Reno, Board Member

Carlo Panicari, Retired Businessperson, Board Member

Peter Sferrazza, Washoe County Commissioner, Board Member

**Management**

Lori Williams, General Manager

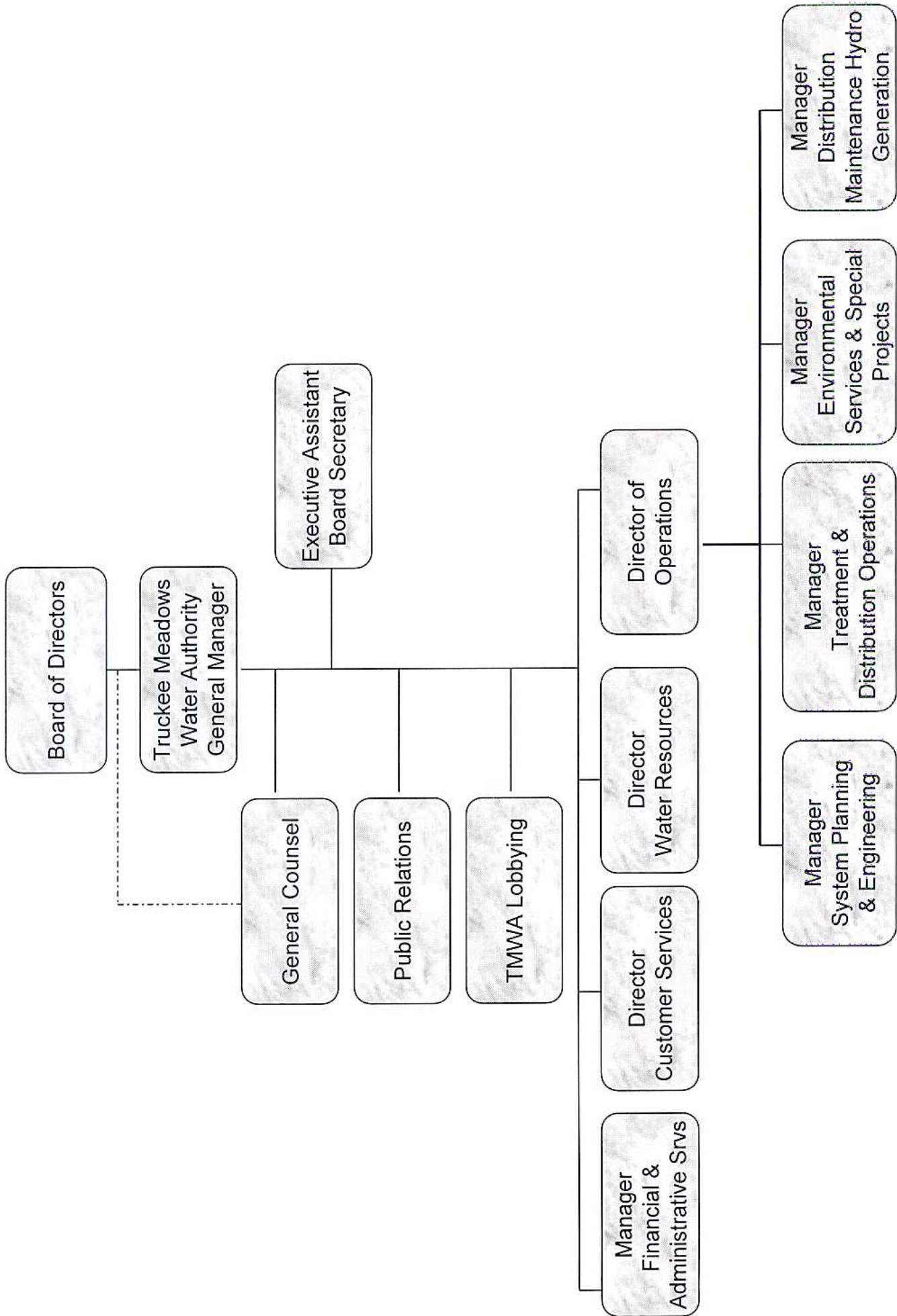
Sylvia Harrison, General Counsel

Mark Foree, PE, Director of Operations

Kim Mazeris, Director of Customer Relations

John Erwin, Director of Resource Planning & Development

Jeffrey Tissier, CPA, Manager of Financial & Administrative Services



# Certificate of Achievement for Excellence in Financial Reporting

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For its Comprehensive Annual  
Financial Report  
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*Nancy L. Zjelde*

President

*Jeffrey R. Enos*

Executive Director