

MERCED IRRIGATION DISTRICT
AUDITED FINANCIAL STATEMENTS
December 31, 2008 and 2007

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Merced Irrigation District
Merced, California

We have audited the accompanying basic financial statements of the Merced Irrigation District (the District) as of December 31, 2008 and 2007 for the years then ended, as listed in the table of contents. These basic financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these basic financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the basic financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the basic financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall basic financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the financial position of the District as of December 31, 2008 and 2007 and the results of its operations and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis on pages 2 through 7 is not a required part of the basic financial statements but is supplementary information required by the Governmental 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 express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The Supplemental Information listed in the table of contents is presented for the purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Richardson & Company

April 30, 2009



MANAGEMENT'S DISCUSSION AND ANALYSIS

For the Year Ended December 31, 2008

Management's discussion and analysis of the Merced Irrigation District's (the District) financial performance provides an overview of the District's activities as well as its financial condition for the year ended December 31, 2008. The District's 2007 and 2006 financial results have been restated for purposes of providing comparative data. This discussion and analysis should be read in conjunction with the financial statements, including the notes to the financial statements, beginning on page 8.

The Balance Sheet presents assets and liabilities with the difference reported as net assets. Over time, increases and decreases in net assets may serve as a useful indicator of whether the financial position of the District is improving or deteriorating. The Balance Sheet provides the basis for evaluating the capital structure of the District and assessing its liquidity and financial flexibility.

The Statement of Revenue, Expenses, and Changes in Net Assets measures the success of the District's operations during the year and determines whether the District has recovered its costs through user fees and other charges, resulting in the changes in net assets.

The Statement of Cash Flows provides information about the District's cash receipts and cash payments resulting from operations, investing, and financing activities for the year.

Background

The District was established to provide irrigation water to farms in the central portion of the San Joaquin Valley located around the city of Merced. The District was organized under the California Water Code in 1919. Today, the District is comprised of 5 major operational enterprises: Water Operations, Parks and Recreation, Hydroelectric Project, Electric Services, and Storm Drainage.

The District provides irrigation water to approximately 90,000 acres within its 164,000 acre boundary. In addition, the District serves approximately 12,000 acres of agricultural lands outside its boundary, but within its 420,000 acre sphere of influence (SOI), which encompasses all lands within Merced Groundwater basin located in the eastern part of Merced County, in addition to lands adjacent to its boundary north of the Merced River. The District distributes water through 825 miles of earthen and concrete lined canals, and pipelines. The District also owns and operates more than 220 wells within its boundary for use in dry years. In 2008, the District delivered 210,919 acre feet of irrigation water to approximately 2,100 growers.

MERCED IRRIGATION DISTRICT

The District owns, operates and maintains five recreation areas adjacent to the lakes behind New Exchequer and McSwain Dams. The Lake McSwain Recreation Area is located adjacent to Lake McSwain. McClure Point, Barrett Cove, Horseshoe Bend and Bagby Recreation Areas are all located adjacent to Lake McClure. A total of six boat launch facilities are available in the Parks system. Over 600 campsites are available to the public on a year-round basis. Floating marinas are located on Lake McSwain and in two locations on Lake McClure for the boating public. Recreational activities enjoyed in the recreation areas include fishing, boating, swimming, camping, hiking and bicycling. In 2008, the various Parks locations had a combined 589,514 visitor days.

The District owns, operates and maintains the New Exchequer and McSwain dams, reservoirs, and hydroelectric facilities. These are the District's primary water storage facilities on the Merced River. They are located in the foothills on the western slope of the Sierra Nevada mountain range, approximately 23 miles northeast of Merced. The two dams and reservoirs are integral parts of the 1964 Merced River Development Project, and are licensed by the Federal Energy Regulatory Commission (FERC). New Exchequer Reservoir (Lake McClure) has a storage capacity of 1,024,600 acre feet, while McSwain Reservoir (Lake McSwain) has a storage capacity of 9,730 acre feet. The New Exchequer Dam Project was completed in 1967 as a multi-purpose facility providing facilities and water for all beneficial uses, including domestic and irrigation water, flood control, hydroelectric power generation, recreation, and the environment.

The District is authorized to act as an electric utility under the California Water Code. The District has owned and operated hydroelectric generating facilities on the Merced River since 1927. In 1995, the District exercised its authority to sell power to retail electric customers. The District offers its customers full requirements electric service including power supply and delivery to the customer. Since 1996, the District has connected over 7,700 customers to the District's electric system. The District's electric customers consumed 88 megawatts of peak electricity demand at the height of the 2008 summer season.

In addition to providing irrigation water, the District also uses portions of its existing irrigation distribution system for urban storm drainage by routing natural stream flows and runoff from urban developments away from populated areas. The District formed the Merced Irrigation District Drainage District #1 (MIDDID#1) in 1994. At the end of 2008, there were approximately 17,718 residential, commercial, industrial, and government parcels located primarily within the urban area of the District that received drainage service.

Required Financial Statements

This annual financial report consists of three parts: Management's Discussion and Analysis, the Basic Financial Statements, and Supplementary Information. The District's financial statements include the (1) Balance Sheet, (2) Statement of Revenues, Expenses, and Changes in Net Assets, and (3) Statement of Cash Flows. The financial statements are prepared using the accrual basis of accounting.

The Notes to the Financial Statements provide additional information that is essential to a full understanding of the financial data provided and are an integral part of the District's financial statements. The District provides a presentation of both the combined financial statements as well as supplemental combining financial statements which portray the individual major component funds.

The Financial Statements of the District report information about the District using accounting methods similar to those used by companies in the private sector. These statements offer short-term and long-term financial information about its activities. The *Balance Sheet* includes all of the District's assets and liabilities and provides information about the nature and amounts of investments in assets and obligations to District creditors as liabilities. It also provides the basis for computing rate of return, evaluating the capital structure of the District and assessing the liquidity and financial flexibility of the District.

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All of the current year's revenues and expenses are accounted for in the *Statement of Revenues, Expenses, and Changes in Net Assets*. These statements measure the District's operations over the past year and can be used to determine whether the District has successfully recovered all of its costs through its rates, fees, capacity and other charges. The District's profitability and credit worthiness can also be determined from these statements. They are prepared using the accrual basis of accounting by recognizing revenues in the period they are earned and expenses in the period they are incurred without regard to the period of cash receipt or payment.

The final required financial statement is the *Statement of Cash Flows*. The primary purpose of this statement is to provide information about the District's cash receipts and cash payments during the reporting period as well as net changes in cash resulting from operations, investing, and financing activities. The statement explains where cash came from and where cash was used and the change in the cash balance during the reporting period.

Financial Highlights

- The District's total assets increased by \$16.0 million in 2008, excluding derivative financial instruments which decreased by \$11.6 million. Total liabilities increased by \$16.0 million excluding the corresponding liability for unrealized losses on derivative instruments. The increase in assets and liabilities was primarily the result of the issuing of two new certificates of participations to refund two existing bonds and to generate additional funding for continued costs associated with the relicensing of the District's 1964 Merced River Hydroelectric Project.
- The District continued its efforts to obtain a new operating license for the hydroelectric project from the Federal Energy Regulatory Commission (FERC) by filing its Preliminary Application Document in November, 2008. The current license expires on February 28, 2014. The District fully expects to be granted a new license by the FERC.
- Operating revenue of \$71.5 million and operating expense of \$71.9 million resulted in a net loss from operations of \$0.4 million. Net non-operating expense of \$0.8 million is the result of total non-operating revenue of \$4.6 million offset by interest expense of \$5.4 million. The District also received capital contributions totaling \$1.3 million.
- The District's cash and cash equivalents increased by \$18.9 million in 2008. This was primarily due to additional bond funding for the continued costs of relicensing of the District's 1964 Merced River Hydroelectric Project including Exchequer and McSwain Dams.

MERCED IRRIGATION DISTRICT

Financial Analysis of the District

The District's Condensed Balance Sheets as of December 31 are as follows:

CONDENSED BALANCE SHEETS

	<u>2008</u>	<u>2007</u>	<u>2006</u>
ASSETS			
Capital assets, net	\$ 139,341,900	\$ 139,614,345	\$ 132,451,471
Other non-current assets	12,402,686	10,041,495	9,437,026
Current assets	60,717,410	58,394,422	55,189,709
Total assets	<u>\$ 212,461,996</u>	<u>\$ 208,050,262</u>	<u>\$ 197,078,206</u>
LIABILITIES			
Long-term liabilities	\$ 126,744,533	\$ 110,115,887	\$ 112,693,297
Other liabilities	5,308,307	4,649,887	4,923,528
Current liabilities	1,640,536	14,534,622	6,823,093
Total liabilities	<u>\$ 133,693,376</u>	<u>\$ 129,300,396</u>	<u>\$ 124,439,918</u>
NET ASSETS			
Invested in capital assets, net of related debt	\$ 37,589,323	\$ 37,895,293	\$ 36,688,013
Restricted	15,563,378	14,334,426	14,800,793
Unrestricted	25,615,919	26,520,147	21,149,482
Total net assets	<u>\$ 78,768,620</u>	<u>\$ 78,749,866</u>	<u>\$ 72,638,288</u>
Total liabilities and net assets	<u>\$ 212,461,996</u>	<u>\$ 208,050,262</u>	<u>\$ 197,078,206</u>

CONDENSED ASSETS DETAIL

	<u>2008</u>	<u>2007</u>	<u>2006</u>
Distribution system, net	\$ 76,164,340	\$ 75,283,982	\$ 69,992,658
Land and easements	13,144,380	13,144,380	13,138,738
Structures and improvements, net	28,790,979	29,559,510	29,240,415
Equipment, net	4,656,619	4,908,499	4,619,405
Intangible assets, net	1,928,488	2,055,044	2,181,074
Construction in progress	14,657,094	14,662,930	13,279,181
	<u>\$ 139,341,900</u>	<u>\$ 139,614,345</u>	<u>\$ 132,451,471</u>

MERCED IRRIGATION DISTRICT

Significant Capital Asset Activity – Overall, capital assets decreased by \$0.3 million in 2008 compared to \$7.2 million in 2007 due to significantly greater capital project spending in 2007 for both the electric system and the water distribution system. For 2007, the increase comprised of \$3.8 million in cash and non cash capital contributions and \$3.4 million in COP construction funding and cash reserves. The District continued to develop and improve its distribution system in 2008 in line with the slowing of area growth; the entire distribution system asset base including construction in progress increased by \$0.9 million in 2008 compared to \$6.7 million in 2007.

For additional information about the District’s capital assets, see Note C to the financial statements

Significant Long-term Debt Activity – Long-term debt increased by \$16.4 million in 2008 as a result of two 2008 refinancing bond issuances totaling \$29.1 million. This was offset by scheduled principal payments and refunds of \$12.9 million. At December 31, 2008 the District had long-term debt outstanding of \$123.6 million as compared to \$107.2 million in 2007 and \$110.2 million in 2006. The current amount is comprised of \$123.1 million of revenue bonds, certificates of participation and capital appreciation certificates of participation, and \$0.5 million of capital leases.

For additional information about the District’s long-term debt, see Note D of the financial statements.

Significant Net Asset Activity – The District’s net assets invested in capital assets decreased by \$0.3 million in 2008. This corresponds with the decrease in the District’s capital assets in 2008. The balance of net assets is comprised of \$15.6 million of restricted net assets which are subject to external restrictions on their use, and \$25.6 million of unrestricted net assets. The District’s assets exceeded liabilities by \$78.8 million. The District’s net assets invested in capital assets for 2007 increased by \$1.2 million over 2006 due to the District’s continuing expansion of its distribution system. Capital assets are not liquid nor are they available for future spending but have been acquired over time and through their utilization, provide the District with revenue.

The District’s Condensed Statements of Revenues, Expenses, and Changes in Net Assets for the years ended December 31 are as follows:

CONDENSED STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

	2008	2007	2006
Operating revenue	\$ 71,491,256	\$ 68,946,462	\$ 58,700,653
Operating expense	71,932,653	66,795,790	55,609,061
Net income from operations	(441,397)	2,150,672	3,091,592
Non-operating revenue (expense)	(794,137)	141,558	(132,305)
Net income before capital contributions	(1,235,534)	2,292,230	2,959,287
Capital contributions	1,254,288	3,819,348	5,373,889
Change in net assets	18,754	6,111,578	8,333,176
Net assets, beginning of year	78,749,866	72,638,288	64,305,112
Net assets, end of year	\$ 78,768,620	\$ 78,749,866	\$ 72,638,288

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Net loss from operations of \$0.4 million for 2008 decreased from \$2.1 million of income in 2007. The \$2.5 million decrease was due primarily to increased water distribution costs associated with increased groundwater pumping and decreased surface water sales as a result of dry year water conditions statewide. There was a decrease of \$.9 million in 2007 from 2006 due to an increase in power supply and water distribution costs. In 2008, net non-operating expense of \$0.8 million is the result of non-operating revenue of \$4.6 million offset by interest expense of \$5.4 million. Capital contribution revenue of \$1.3 million is comprised of non-cash developer contributions and third-party cash proceeds used for capital projects. The decrease in capital contribution revenue of \$2.6 million in 2008 is due to decreased developer-constructed electric infrastructure and the completion of state funded highway projects that resulted in irrigation infrastructure improvements compared to 2007.

Economic Factors and Rates

In 2008, The District experienced dramatic energy price increases and in response, implemented a rate surcharge effective September 1, 2008 which increased tariff rates by an average of 10.8%. The District was also able to buffer some of the energy price volatility through implementation of its risk management policies to stabilize electric prices over the longer term. These strategies were effective in addressing the energy price volatility. Even though the economic situation worsened in the region and state, the District continued to add electric load by 2.1% and increase revenues by 7.6% over 2007. For 2008, the District added approximately 146 new industrial, commercial, municipal, agricultural, and residential electric services.

In 2008, the District was impacted by a second consecutive critically dry year, resulting in increased costs to provide irrigation water and decreased overall water sales. The District is addressing these impacts through cost reduction measures, water conservation and efficiency improvement measures, and planned water rate increases. Certain parks and recreation fees were slightly increased to address increased operating costs and remain competitive with surrounding recreation areas. The Storm Drainage District added 233 parcels comprised of approximately 55 acres.

Request for Information

This financial report is designed to provide a general overview of the District's finances. Questions concerning the information provided in this report or requests for additional financial information should be addressed to Andre Urquidez, Chief Financial Officer, P.O. Box 2288, Merced, CA 95344-0288 or please call (209) 722-5761.

MERCED IRRIGATION DISTRICT

BALANCE SHEETS

December 31, 2008 and 2007

	<u>2008</u>	<u>2007</u>
ASSETS		
CAPITAL ASSETS, NET	\$ 139,341,900	\$ 139,614,345
OTHER NONCURRENT ASSETS		
Deferred relicense costs	6,800,666	5,156,638
Debt issuance costs	4,828,991	4,884,857
Regulatory costs for future recovery	<u>773,029</u>	
TOTAL OTHER NONCURRENT ASSETS	<u>12,402,686</u>	<u>10,041,495</u>
CURRENT ASSETS		
Cash and cash equivalents	24,617,901	21,991,821
Accounts receivable, net	5,957,295	7,495,497
Due from other governmental agencies	1,762,669	5,400,939
Accrued interest and taxes receivable	1,227,764	1,362,612
Inventory	4,615,283	4,323,258
Prepaid expenses and other current assets	943,698	878,387
Restricted cash and cash equivalents	34,317,529	18,066,936
Derivative financial instruments	<u>(12,724,729)</u>	<u>(1,125,028)</u>
TOTAL CURRENT ASSETS	<u>60,717,410</u>	<u>58,394,422</u>
TOTAL ASSETS	<u>\$ 212,461,996</u>	<u>\$ 208,050,262</u>

	<u>2008</u>	<u>2007</u>
LIABILITIES AND NET ASSETS		
LONG-TERM LIABILITIES		
Long-term debt	\$ 123,632,935	\$ 107,194,350
Accrued compensated absences	1,352,210	1,234,915
Accrued post-employment benefits	<u>1,759,388</u>	<u>1,686,622</u>
TOTAL LONG-TERM LIABILITIES	<u>126,744,533</u>	<u>110,115,887</u>
OTHER LIABILITIES		
Deferred public purpose program revenues	2,552,678	2,221,638
Deferred power cost reductions	1,100,000	1,500,000
Deposits	<u>1,655,629</u>	<u>928,249</u>
TOTAL OTHER LIABILITIES	<u>5,308,307</u>	<u>4,649,887</u>
CURRENT LIABILITIES		
Accounts payable	1,002,452	1,845,693
Accrued permission fees	899,812	834,290
Accrued power purchase expense	2,658,903	2,707,999
Other accrued expenses	535,252	779,447
Deferred revenue	4,254,237	4,788,022
Accrued interest payable	1,390,067	1,425,402
Deferred credit - unrealized loss on swap contracts	(12,724,729)	(1,125,028)
Current portion of long-term debt	<u>3,624,542</u>	<u>3,278,797</u>
TOTAL CURRENT LIABILITIES	<u>1,640,536</u>	<u>14,534,622</u>
TOTAL LIABILITIES	133,693,376	129,300,396
NET ASSETS		
Invested in capital assets, net of related debt	37,589,323	37,895,293
Restricted	15,563,378	14,334,426
Unrestricted	<u>25,615,919</u>	<u>26,520,147</u>
TOTAL NET ASSETS	<u>78,768,620</u>	<u>78,749,866</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 212,461,996</u>	<u>\$ 208,050,262</u>

The notes to the basic financial statements are an integral part of this statement.

MERCED IRRIGATION DISTRICT

STATEMENTS OF REVENUES, EXPENSES
AND CHANGES IN NET ASSETS

For the years ended December 31, 2008 and 2007

	<u>2008</u>	<u>2007</u>
OPERATING REVENUES		
Electric sales and services	\$ 50,215,471	\$ 46,034,044
Water sales and services	8,919,508	9,658,878
Hydroelectric sales and services	6,114,517	6,179,373
Water transfers	4,648,428	5,185,240
Recreation fees	1,564,837	1,821,687
Storm drainage fees	28,495	67,240
TOTAL OPERATING REVENUES	<u>71,491,256</u>	<u>68,946,462</u>
OPERATING EXPENSES		
Purchase of power	33,327,494	30,914,133
Water distribution	15,405,911	13,845,451
Electric transmission and distribution	13,907,862	13,287,593
Recreation	1,861,015	1,750,324
Storm drainage	54,207	57,705
Administrative and general	2,190,498	1,980,938
Depreciation and amortization	5,185,666	4,959,646
TOTAL OPERATING EXPENSES	<u>71,932,653</u>	<u>66,795,790</u>
NET (LOSS) INCOME FROM OPERATIONS	(441,397)	2,150,672
NON-OPERATING REVENUE (EXPENSES)		
Property taxes	2,565,214	2,524,649
Interest income	1,201,133	2,087,083
Other non-operating income	493,127	747,851
Gain on disposal of capital assets	373,361	111,695
Interest expense	(5,426,972)	(5,329,720)
TOTAL NON-OPERATING (EXPENSES) REVENUES	<u>(794,137)</u>	<u>141,558</u>
NET (LOSS) INCOME BEFORE CAPITAL CONTRIBUTIONS	(1,235,534)	2,292,230
CAPITAL CONTRIBUTIONS	1,254,288	3,819,348
TOTAL CAPITAL CONTRIBUTIONS	<u>1,254,288</u>	<u>3,819,348</u>
CHANGE IN NET ASSETS	18,754	6,111,578
Net assets at beginning of year	<u>78,749,866</u>	<u>72,638,288</u>
NET ASSETS AT END OF YEAR	<u>\$ 78,768,620</u>	<u>\$ 78,749,866</u>

The notes to the basic financial statements are an integral part of this statement.

MERCED IRRIGATION DISTRICT

STATEMENTS OF CASH FLOWS

For the years ended December 31, 2008 and 2007

	<u>2008</u>	<u>2007</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash receipts from customers	\$ 77,171,436	\$ 68,370,067
Cash paid to suppliers for goods and services	(57,036,583)	(51,181,623)
Cash paid to employees for services	<u>(11,383,184)</u>	<u>(10,690,224)</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES	8,751,669	6,498,220
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Property taxes received	2,556,310	2,567,187
Relicense costs incurred	(1,609,533)	(804,573)
Proceeds from issuance of debt	17,387,071	
Issuance costs paid	(155,426)	
Interest payments on long term debt	(30,533)	(200,004)
Other income/expenses	<u>493,127</u>	<u>749,996</u>
NET CASH PROVIDED BY NONCAPITAL FINANCING ACTIVITIES	18,641,016	2,312,606
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Acquisition and construction of capital assets	(4,284,882)	(10,301,154)
Proceeds from sale of equipment	409,538	138,836
Reimbursements received for capital assets	1,028,321	2,436,311
Principal payments on long-term debt	(2,523,708)	(2,704,103)
Proceeds from issuance of debt	683,143	
Issuance costs paid	(38,435)	
Interest payments on long-term debt	<u>(5,075,677)</u>	<u>(5,053,692)</u>
NET CASH USED BY CAPITAL AND RELATED FINANCING ACTIVITIES	(9,801,700)	(15,483,802)
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest received on investments	<u>1,285,688</u>	<u>2,133,877</u>
NET CASH PROVIDED BY INVESTING ACTIVITIES	<u>1,285,688</u>	<u>2,133,877</u>
INCREASE (DECREASE) IN CASH	18,876,673	(4,539,099)
Cash and cash equivalents at beginning of year	<u>40,058,757</u>	<u>44,597,856</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$ 58,935,430</u>	<u>\$ 40,058,757</u>
Cash and cash equivalents consist of the following:		
Unrestricted	\$ 24,617,901	\$ 21,991,821
Restricted	<u>34,317,529</u>	<u>18,066,936</u>
	<u>\$ 58,935,430</u>	<u>\$ 40,058,757</u>

(Continued)

MERCED IRRIGATION DISTRICT

STATEMENTS OF CASH FLOWS (Continued)

For the years ended December 31, 2008 and 2007

	2008	2007
RECONCILIATION OF NET INCOME FROM OPERATIONS TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Net income from operations	\$ (441,397)	\$ 2,150,672
Adjustments to reconcile net income from operations to net cash used for operating activities:		
Depreciation and amortization	5,185,666	4,959,647
Changes in operating assets and liabilities:		
Accounts receivable	1,597,399	(794,973)
Due from other governmental agencies	3,558,146	(4,367,440)
Inventory	(292,025)	(1,413,255)
Prepaid expenses and other current assets	(65,311)	263,328
Swap sale receivable		265,052
Accounts payable	(910,727)	543,052
Accrued permission fees	65,522	114,705
Accrued power purchase expense	(49,096)	477,471
Other accrued expenses	(211,204)	(157,450)
Deferred revenue	(533,785)	4,259,659
Deferred power cost reductions	(400,000)	(600,000)
Deposits	727,380	101,740
Deferred public purpose program revenues	331,040	224,619
Accrued postemployment benefits	72,766	349,744
Accrued compensated absences	117,295	121,649
	<u>\$ 8,751,669</u>	<u>\$ 6,498,220</u>
NONCASH INVESTING, CAPITAL AND FINANCING ACTIVITIES:		
Receipt of contributed electric system assets from developers	\$ 306,087	\$ 1,463,160
Change in derivative financial instruments	\$ (11,599,701)	\$ 1,868,125

The notes to the basic financial statements are an integral part of this statement.

MERCED IRRIGATION DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS

December 31, 2008 and 2007

NOTE A – REPORTING ENTITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The basic financial statements of the Merced Irrigation District (the District) have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to government units. The Governmental Accounting Standards Board (GASB) is the accepted standard setting body for establishing governmental accounting and financial reporting principles. As allowed by the GASB, the District has elected to apply to its proprietary activities Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee of Accounting Procedures issued after November 30, 1989 where not in conflict with GASB pronouncements. The more significant of the District's accounting policies are described below.

Reporting Entity: The District was organized in 1919 under the California Water Code to provide agricultural irrigation water to the farmers in the central portion of the San Joaquin Valley in and around eastern Merced County. The District owns and operates two dams and related reservoirs, hydroelectric generation facilities, recreation, and fish enhancement facilities in Merced and Mariposa Counties. The District also provides urban storm drainage and retail electric services in Merced County. The District is governed by a five member Board of Directors elected by the voters within the District for staggered, four year terms, every two years. As required by GAAP, the accompanying basic financial statements present the District and its component units. The component units discussed below are included in the District's reporting entity because of the significance of their operational and financial relationship with the District.

The District has created the Merced Irrigation District Public Facilities Financing Corporation (MIDPFFC) to provide assistance to the District in the issuance of debt and the Merced Irrigation District Drainage Improvement District #1 (MIDDID#1) to make annual assessments against properties that drain into a District facility for storm water drainage construction and maintenance expenses. Although legally separate from the District, the MIDPFFC and MIDDID#1 are reported as if they were part of the primary government because they share a common Board of Directors with the District and their sole purposes are to provide financing to the District under the debt issuance documents of the District and construction and maintenance of storm water drainage facilities, respectively. Debt issued by the MIDPFFC is reflected as debt of the District in these financial statements. The MIDPFFC issued debt for the construction of the administration building and the District leases the building from the MIDPFFC. This lease revenue is eliminated in these basic financial statements. The MIDPFFC and MIDDID#1 do not issue separate financial statements.

Participation in Joint Power Authorities: The San Joaquin River Group Authority (SJRG) was created in September, 1996 under a joint exercise of powers agreement between the District and the Modesto Irrigation District, Oakdale Irrigation District, South San Joaquin Irrigation District, Turlock Irrigation District, Friant Water Users Authority, and San Joaquin River Exchange Contractors Water Authority (the Parties) to represent the Parties as necessary in proceedings relating to the investigation, monitoring, planning, control, mitigation of water flow and non-flow issues, and to enhance the environmental conditions in the Delta which impact the parties. The SJRG is governed by a seven member commission made up of one member of the Governing Board of each Party. The agreement terminates in December, 2036, unless extended or terminated by the Parties. Upon termination of the Agreement, all of the SJRG assets will be returned to the respective Parties in the proportion to the contribution the Party made. Equipment, furniture or furnishings will be returned to the contributing Party. Any other property shall be converted to cash and distributed equally among the Parties.

The Walnut Energy Center Authority (WECA) was created in December, 2003 under a joint exercise of powers agreement between the District and the Turlock Irrigation District (TID) (the Parties) for the purpose of providing an entity that can assist in providing financings through the sale and issuance of bonds for projects which are authorized in the Joint Powers Act. WECA is administered by a Commission which is comprised of members of the Board of Directors of TID, sitting ex officio, together with one member of the Board of Directors of the District. The agreement terminates in December, 2033, unless extended or terminated by the Parties. Upon termination of the agreement all of the WECA assets shall be distributed to TID.

MERCED IRRIGATION DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2008 and 2007

NOTE A – REPORTING ENTITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Basis of Presentation: The District's resources are allocated to and accounted for in these basic financial statements as an enterprise fund type of the proprietary fund group. The enterprise fund is used to account for operations that are financed and operated in a manner similar to a private business enterprise, where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges, or where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other policies. Net assets represent the amount available for future operations.

Basis of Accounting: The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. The enterprise fund type is accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operation of the District are included on the balance sheet. Net assets are segregated into amounts invested in capital assets, net of related debt, amounts restricted and amounts unrestricted. Enterprise fund type operating statements present increases (i.e., revenues) and decreases (i.e., expenses) in total net assets.

The District uses the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. Grant revenue is recognized when program expenditures are incurred in accordance with program guidelines. When funds are received in advance of program expenditures, they are recorded as deferred revenues until earned. Earned but unbilled electric and water services are accrued as revenue. Electrical infrastructures that are constructed by private developers are contributed to the District, which then become the responsibility of the District to maintain. These infrastructures are recorded as capital contributions when they pass inspection by the District and the estimated costs are capitalized and included as a part of the electric transmission and distribution system.

Operating revenues and expenses consist of those revenues and expenses that result from the ongoing principal operations of the District. Operating revenues consist primarily of charges for services. Non-operating revenues and expenses consist of those revenues and expenses that are related to financing and investing types of activities and result from nonexchange transactions or ancillary activities.

The District is in possession of both restricted and unrestricted cash. Restricted cash is held in reserve and is spent exclusively for the intended purpose. In the event that the designated restricted cash is insufficient to complete the intended purpose, unrestricted cash is utilized.

Use of Estimates: The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Reclassifications: Certain reclassifications have been made to 2007 balances to agree to the 2008 presentation. These reclassifications had no effect on previously reported change in net assets.

Regulatory Deferrals: The Board has the authority to establish the level of rates charged for all District services. As a regulated entity, the District's financial statements are prepared in accordance with Statement of Financial Accounting Standards (SFAS) No. 71 "Accounting for the Effects of Certain Types of Regulation", which requires that the effects of the rate-making process be recorded in the financial statements. Accordingly, certain expenses and credits, normally reflected in the Change in Net Assets as incurred, are recognized when included in rates and recovered from, or refunded to, customers.

MERCED IRRIGATION DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2008 and 2007

NOTE A – REPORTING ENTITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

A portion of the District’s annual power supply requirement is purchased from the Western Area Power Administration (WAPA). In 2006, due to increased hydroelectric production by WAPA, the District’s allotment was significantly higher than anticipated. The comparatively low cost of this power offset higher priced power, causing a reduction of the District’s expected overall power supply cost in 2006. This reduction in cost resulted in excess net income that is available to offset the projected power supply cost increase in future years. The power supply cost reduction was deferred in accordance with SFAS 71 for the benefit of future customer rate stabilization and is recorded as deferred power cost reductions on the Balance Sheet. At December 31, 2008 and 2007, the deferred power cost reductions were \$1,100,000 and \$1,500,000, respectively.

A portion of the District water sales revenue is derived from water transfers to state and/or federal agencies for environmental purposes based upon the District’s ability to make such water resources available to meet flow objectives in the Merced River, San Joaquin River or the Delta. In 2007, the District was able to negotiate several transfer agreements which resulted in excess net income available to offset the projected low water sales and increasing costs in future years. A portion of the excess revenue, \$4,600,000, was deferred in accordance with SFAS 71 for the benefit of future customer rate stabilization and is recorded as deferred water revenue on the Balance Sheet. At December 31, 2008 and 2007, the deferred water revenues were \$3,200,000 and \$4,600,000, respectively.

The amount reported as regulatory costs for future recovery represents the accretion of interest on capital appreciation certificates of participation until such time as these costs will be covered by hydroelectric sales in the future.

Capital Assets: Capital assets are recorded at historical cost. Contributed assets are valued at estimated fair value on the date received. Depreciation is calculated using the straight-line method over the following estimated useful lives:

Description	Estimated Life
Landscaping	10 - 40 years
Building and structures	10 - 100 years
Transmission and distribution systems	15 - 50 years
Machinery	30 - 35 years
Vehicles	3 - 10 years
Equipment	3 - 40 years
Intangible assets	10 - 50 years

Maintenance and repairs are charged to operations when incurred. It is the District’s policy to capitalize all capital assets with a cost of more than \$5,000. Costs of assets sold or retired, and the related amounts of accumulated depreciation, are eliminated from the accounts in the year of sale or retirement and the resulting gain or loss is included in the operating statement.

Deferred Relicense Costs: The District is deferring the costs of studies, legal counsel and various consultants associated with relicensing the 1964 Merced River Development Project with the Federal Energy Regulatory Commission until the license is renewed. The project is expected to be relicensed in 2014, at which time these costs will be amortized to expense over the new license period.

Bond Discounts, Premiums, Deferred Amount on Refunding and Issuance Costs: Bond discounts, premiums, as well as issuance costs, are deferred and amortized over the life of the bonds. Bonds payable are reported net of the applicable bond discounts and premiums. Issuance costs are reported as noncurrent assets. For current refundings and advance refundings resulting in the defeasance of debt, the difference between the reacquisition price and the net carrying amount of the old debt is deferred and amortized as a component of interest expense over the remaining life of the old debt or the life of the new debt, whichever is shorter.

MERCED IRRIGATION DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2008 and 2007

NOTE A – REPORTING ENTITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Accounts Receivable: Accounts receivable arise from billings to customers for water and electricity usage and include an estimate for unbilled revenues earned from the dates the customers were last billed to the end of the year. An estimate of the uncollectible amount is \$38,000 at December 31, 2008 and \$540,620 at December 31, 2007.

Due from Other Governmental Agencies: Due from other agencies represents reimbursements due from other agencies for services performed and for water and electricity delivered.

Inventory: Inventory is stated at average cost. Inventory consists of parts and supplies.

Derivative Financial Instruments: The District uses swap agreements to hedge the impact of market volatility of electricity and natural gas commodity prices for purchases of electricity for the District's retail load. The District records these derivative financial instruments at fair value on its balance sheet. Fair value is estimated by comparing contract prices to forward market prices quoted by third party market participants. While the District enters into swap agreements for hedging purposes, it currently does not formally declare the contracts as hedging activities at the time of executing the trade. The Board defers recognition of the unrealized gains or losses from such instruments for rate-making purposes; the balance is reflected as deferred credit-unrealized (loss) gain on swap agreements on the balance sheet and is charged or credited into electricity supply costs as the related asset or liability is utilized.

Compensated Absences: The District's policy allows employees to accumulate earned but unused vacation, which will be paid to employees upon separation from service to the District, subject to a vesting policy. All or a portion of unused sick leave is paid out upon retirement. The District accrues the liability for vacation and sick leave when the employee earns the right to the benefit.

Deferred Public Purpose Revenues: The District is required by the Public Utilities Code to establish a usage-based charge on its electricity sales of 2.85%, which is collected as part of the electric billings. These revenues are to be used for energy efficiency and conservation programs, renewable energy resources, research and development and to provide assistance to low-income customers. These revenues are deferred until qualifying expenses are incurred.

Purchased Power Expenses: The District's electricity needs are provided through electricity purchase agreements. Expenses from such agreements, along with associated interconnection costs, are recorded as the cost of electricity in the period the electricity is received. The net cash payments or receipts incurred under the swap agreements are reported as a component of cost of electricity supply in the statement of revenues, expenses and changes in net assets in the period in which the underlying electricity supply delivery occurs.

Property Taxes: The District receives property taxes from Merced County. Property taxes receivable are recorded in the fiscal year for which the tax is levied based on the assessed value as of September 1 of the preceding fiscal year. They become a lien on the first day of the year they are levied. Secured property tax is levied on September 1 and due in two installments, on November 1 and March 1. They become delinquent on December 10 and April 10, respectively. Unsecured property taxes are due on July 1, and become delinquent on August 31. The District elected to receive the property taxes from the County under the Teeter Bill Program. Under this Program, the District receives 100% of the levied property taxes in periodic payments, with the County assuming responsibility for delinquencies.

Cash and Cash Equivalents: The District considers all highly liquid debt instruments purchased with an initial maturity of three months or less to be cash equivalents, including restricted assets, along with all pooled deposits and investments in the Local Agency Investment Fund, which are available upon demand.

MERCED IRRIGATION DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2008 and 2007

NOTE B – CASH AND INVESTMENTS

Cash and investments as of December 31, are classified in the accompanying financial statements as follows:

	<u>2008</u>	<u>2007</u>
Cash and cash equivalents	\$ 24,617,901	\$ 21,991,821
Restricted cash and cash equivalents	<u>34,317,529</u>	<u>18,066,936</u>
Total cash and investments	<u>\$ 58,935,430</u>	<u>\$ 40,058,757</u>

Cash and investments as of December 31, consisted of the following:

Cash on hand	\$ 3,120	\$ 3,120
Deposits with financial institutions	<u>17,350,531</u>	<u>15,109,377</u>
Total cash and deposits	17,353,651	15,112,497
Money market mutual funds	31,396,025	13,983,172
Counterparty pooled deposit	1,750,000	
Guaranteed investment contract		2,855,164
Investments in LAIF	<u>8,435,754</u>	<u>8,107,924</u>
Total investments	<u>41,581,779</u>	<u>24,946,260</u>
Total cash and investments	<u>\$ 58,935,430</u>	<u>\$ 40,058,757</u>

Investment policy: California statutes authorize districts to invest idle or surplus funds in a variety of credit instruments as provided for in the California Government Code, Section 53600, Chapter 4 - Financial Affairs. The table below identifies the investment types that are authorized for the District by the California Government Code (or the District's investment policy, where more restrictive) that address interest rate risk, credit risk, and concentration of credit risk. This table does not address investments of debt proceeds held by bond trustee that are governed by the provisions of debt agreements of the District, rather than the general provisions of the California Government Code or the District's investment policy. During the year ended December 31, 2008, the District's permissible investments included the following instruments:

MERCED IRRIGATION DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2008 and 2007

NOTE B – CASH AND INVESTMENTS (Continued)

Authorized Investment Type	Maximum Maturity	Maximum % of Portfolio	Maximum Investment in One Issuer
Local Agency Bonds	5 years	None	None
U.S. Treasury Obligations	5 years	None	None
U.S. Agencies Securities	5 years	None	None
California Local Agency Debt	5 years	None	None
Banker's Acceptances	180 days	40%	30%
Commercial Paper	180 days	15%	10%
Negotiable Certificates and Time Deposits	5 years	30%	None
Repurchase Agreements	1 year	None	None
Medium Term Notes	5 years	30%	None
Mutual Funds	N/A	20%	10%
Money Market Mutual Funds	N/A	20%	10%
Mortgage Pass-Through Securities	5 years	20%	None
County Pooled Investment Funds	N/A	None	None
Local Agency Investment Funds (LAIF)	N/A	None	None
JPA Pools (Other investment pools)	N/A	None	None

*Excluding amounts held by bond trustees that are not subject to California Government Code restrictions.

As of December 31, 2008, the District invested \$23,139,475 in a single money market fund, representing 56% of the District's investment balances. The District complied with all other provisions of California Government Code (or the District's investment policy, where more restrictive) pertaining to the types of investments held, institutions in which deposits were made and security requirements. The District will continue to monitor compliance with applicable statutes pertaining to public deposits and investments.

Investments Authorized by Debt Agreements: Investment of debt proceeds held by bond trustee are governed by provisions of the debt agreements, rather than the general provisions of the California Government Code or the District's investment policy. The table below identifies certain provisions of these debt agreements that address interest risk, credit risk and concentration risk.

Authorized Investment Type	Maximum Maturity	Maximum % of Portfolio	Maximum Investment in One Issuer
Local Agency Bonds	5 years	None	None
U.S. Treasury Obligations	5 years	None	None
U.S. Agencies Securities	5 years	None	None
California Local Agency Debt	5 years	None	None
Banker's Acceptances	1 year	None	None
Commercial Paper	None	None	None
Negotiable Certificates and Time Deposits	None	None	None
Repurchase Agreements	30 days	None	None
Investment Agreements	None	None	None
Money Market Mutual Funds	N/A	None	None
Mortgage Pass-Through Securities	5 years	20%	None
Local Agency Investment Funds (LAIF)	N/A	None	None

MERCED IRRIGATION DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2008 and 2007

NOTE B – CASH AND INVESTMENTS (Continued)

Interest rate risk: Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. One of the ways the District manages its exposure to interest rate risk is by purchasing a combination of shorter term and longer term investments and by timing cash flows from maturities so that a portion of the portfolio is maturing or coming close to maturity evenly over time as necessary to provide the cash flow and liquidity needed for operations.

Information about the sensitivity of the fair values of the District’s investments (including investments held by bond trustee) to market interest rate fluctuations is provided by the following table that shows the distribution of the District’s investments by maturity:

	<u>Remaining Maturity (in Months)</u>	
	<u>Total</u>	<u>12 Months or less</u>
Local Agency Investment Funds	\$ 7,264,251	\$ 7,264,251
Held by bond trustee:		
Money Market Mutual Funds	31,396,025	31,396,025
Local Agency Investment Funds	1,171,503	1,171,503
Held by counterparty		
Pooled cash	<u>1,750,000</u>	<u>1,750,000</u>
	<u>\$ 41,581,779</u>	<u>\$ 41,581,779</u>

Credit Risk: Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. Presented below is the minimum rating required by (where applicable) the California Government Code, the District’s investment policy, or debt agreements, and the actual rating as of year end for each investment type.

	<u>Minimum Legal Rating</u>	<u>Total</u>	
		<u>AAA/Aaa</u>	<u>Unrated</u>
Local Agency Investment Funds	Unrated	\$ 7,264,251	\$ 7,264,251
Held by bond trustee:			
Money Market Mutual Funds	AAA/Aaa	31,396,025	\$ 31,396,025
Local Agency Investment Funds	Unrated	1,171,503	1,171,503
Held by counterparty:			
Pooled cash	Unrated	<u>1,750,000</u>	<u>1,750,000</u>
		<u>\$ 41,581,779</u>	<u>\$ 31,396,025</u>
			<u>\$ 10,185,754</u>

Concentration of Credit Risk: The investment policy of the District limits the amount that can be invested in any one issuer to the lesser of the amount stipulated by the California Government Code or 50% of total investments, with the exception of U.S. Treasury obligations, U.S. Agency Securities and LAIF. As of December 31, 2008, the District had no individual investment that exceeded 5% of its total investments.

MERCED IRRIGATION DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2008 and 2007

NOTE B – CASH AND INVESTMENTS (Continued)

Custodial credit risk: Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty (e.g., broker-dealer) to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The California Government Code and the District's investment policy do not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits, other than the following provision for deposits: The California Government Code requires that a financial institution secure deposits made by state or local governmental units by pledging securities in an undivided collateral pool held by a depository regulated under state law (unless so waived by the governmental unit). The market value of the pledged securities in the collateral pool must equal at least 110% of the total amount deposited by the public agencies. California law also allows financial institutions to secure public agency deposits by pledging first trust deed mortgage notes having a value of 150% of the secured public deposits.

At December 31, 2008, the carrying amount of the District's deposits was \$17,350,531 and the balance in financial institutions was \$18,375,935. Of the balance in financial institutions, \$573,165 was covered by federal depository insurance and \$17,802,770 was collateralized as required by State law (Government Code Section 53630), by the pledging financial institution with assets held in a common pool for the District and other governmental agencies, but not in the name of the District.

Investment in LAIF: LAIF is stated at fair value. The LAIF is a special fund of the California State Treasury through which local governments may pool investments. The total fair value amount invested by all public agencies in LAIF is \$63,610,592,461 managed by the State Treasurer. Of that amount, 12.93% is invested in structured notes and asset-backed securities. The Local Investment Advisory Board (Board) has oversight responsibility for LAIF. The Board consists of five members as designated by State Statute. The fair value of the District's investment in this pool is reported in the accompanying financial statements at amounts based upon the District's pro-rata share of the fair value provided by LAIF for the entire LAIF portfolio (in relation to the amortized cost of that portfolio). The balance available for withdrawal is based on the accounting records maintained by LAIF, which are recorded on an amortized cost basis.

MERCED IRRIGATION DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2008 and 2007

NOTE C – CAPITAL ASSETS

Capital asset activity for the years ended December 31, 2008 and 2007 are as follows:

	Balance January 1, 2008	Additions	Disposals	Transfers and Adjustments	Balance December 31, 2008
Capital assets, not being depreciated:					
Land	\$ 13,144,380				\$ 13,144,380
Construction in progress	14,662,930	\$ 3,943,293		\$ (3,949,129)	14,657,094
Total capital assets, not being depreciated	<u>27,807,310</u>	<u>3,943,293</u>		<u>(3,949,129)</u>	<u>27,801,474</u>
Capital assets, being depreciated:					
Landscaping	6,446,704		\$ (854)		6,445,850
Buildings and structures	50,317,317	54,990	(542,456)	316,077	50,145,928
Water distribution system	15,453,812		(21,205)	719,829	16,152,436
Electric transmission and distribution system	76,781,497	6,669	(84,734)	2,839,123	79,542,555
Machinery and equipment	9,411,592	19,874	(218,161)	74,100	9,287,405
Vehicles	7,851,472	481,659	(255,390)		8,077,741
Intangible plant	8,432,444	84,484			8,516,928
Total capital assets being depreciated	<u>174,694,838</u>	<u>647,676</u>	<u>(1,122,800)</u>	<u>3,949,129</u>	<u>178,168,843</u>
Less accumulated depreciation for:					
Landscaping	(4,551,445)	(255,996)	854		(4,806,587)
Buildings and structures	(22,653,066)	(872,630)	531,483		(22,994,213)
Water distribution system	(4,317,330)	(403,850)			(4,721,180)
Electric transmission and distribution system	(12,633,997)	(2,249,236)	73,763		(14,809,470)
Machinery and equipment	(6,632,016)	(210,907)	213,271		(6,629,652)
Vehicles	(5,722,549)	(602,379)	246,052		(6,078,876)
Intangible plant	(6,377,400)	(232,243)	21,204		(6,588,439)
Total accumulated depreciation	<u>(62,887,803)</u>	<u>(4,827,241)</u>	<u>1,086,627</u>		<u>(66,628,417)</u>
Total capital assets being depreciated, net	<u>111,807,035</u>	<u>(4,179,565)</u>	<u>(36,173)</u>	<u>3,949,129</u>	<u>111,540,426</u>
CAPITAL ASSETS, NET	<u>\$ 139,614,345</u>	<u>\$ (236,272)</u>	<u>\$ (36,173)</u>	<u>\$ -</u>	<u>\$ 139,341,900</u>

MERCED IRRIGATION DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2008 and 2007

NOTE C – CAPITAL ASSETS (Continued)

	Balance January 1, 2007	Additions	Disposals	Transfers and Adjustments	Balance December 31, 2007
Capital assets, not being depreciated:					
Land	\$ 13,138,738			\$ 5,642	\$ 13,144,380
Construction in progress	13,279,181	\$ 10,045,256		(8,661,507)	14,662,930
Total capital assets, not being depreciated	<u>26,417,919</u>	<u>10,045,256</u>		<u>(8,655,865)</u>	<u>27,807,310</u>
Capital assets, being depreciated:					
Landscaping	5,671,728			774,976	6,446,704
Buildings and structures	49,671,126	23,531		622,660	50,317,317
Water distribution system	13,884,724	642,463		926,625	15,453,812
Electric transmission and distribution system	70,537,061			6,244,436	76,781,497
Machinery and equipment	9,338,901	46,465		26,226	9,411,592
Vehicles	6,976,850	979,095	\$ (104,473)		7,851,472
Intangible plant	8,343,998	27,504		60,942	8,432,444
Total capital assets being depreciated	<u>164,424,388</u>	<u>1,719,058</u>	<u>(104,473)</u>	<u>8,655,865</u>	<u>174,694,838</u>
Less accumulated depreciation for:					
Landscaping	(4,313,506)	(237,939)			(4,551,445)
Buildings and structures	(21,788,933)	(864,133)			(22,653,066)
Water distribution system	(3,921,774)	(395,556)			(4,317,330)
Electric transmission and distribution system	(10,507,353)	(2,126,644)			(12,633,997)
Machinery and equipment	(6,418,415)	(213,601)			(6,632,016)
Vehicles	(5,277,931)	(521,951)	77,333		(5,722,549)
Intangible plant	(6,162,924)	(214,476)			(6,377,400)
Total accumulated depreciation	<u>(58,390,836)</u>	<u>(4,574,300)</u>	<u>77,333</u>		<u>(62,887,803)</u>
Total capital assets being depreciated, net	<u>106,033,552</u>	<u>(2,855,242)</u>	<u>(27,140)</u>	<u>\$ 8,655,865</u>	<u>111,807,035</u>
CAPITAL ASSETS, NET	<u>\$ 132,451,471</u>	<u>\$ 7,190,014</u>	<u>\$ (27,140)</u>	<u>\$ -</u>	<u>\$ 139,614,345</u>

MERCED IRRIGATION DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2008 and 2007

NOTE D – LONG-TERM LIABILITIES

Long-term liabilities include long-term debt, capital leases and accrued compensated absences. The activity of the District's long-term liabilities during the years ended December 31, 2008 and 2007 are as follows:

	Balance January 1, 2008	Additions	Repayments	Balance December 31, 2008	Due Within One Year
Long-term debt:					
Merced River					
Development Bonds	\$ 9,535,000		\$ (1,270,000)	\$ 8,265,000	\$ 1,315,000
1998 Note payable	329,806		(329,806)		
2001 Certificates of Participation	5,505,000		(5,505,000)		
2003 Revenue Certificates of Participation	14,120,000		(220,000)	13,900,000	230,000
2005 Electric System Refunding Revenue Bonds	63,050,000		(300,000)	62,750,000	1,115,000
2005 Revenue Certificates of Participation	15,000,000		(260,000)	14,740,000	275,000
2005 Warrants	5,000,000		(5,000,000)		
2008 Water and Hydro Refunding Revenue Certificates of Participations		\$ 6,335,000		6,335,000	575,000
2008 Water and Hydro Capital Appreciation Revenue Certificates of Participations		22,718,863		22,718,863	
	<u>112,539,806</u>	<u>29,053,863</u>	<u>(12,884,806)</u>	<u>128,708,863</u>	<u>3,510,000</u>
Capital leases	<u>673,825</u>		<u>(130,746)</u>	<u>543,079</u>	<u>114,542</u>
Total	113,213,631		<u><u>\$ (13,015,552)</u></u>	129,251,942	<u><u>\$ 3,624,542</u></u>
Add:					
Deferred amount on refunding	(4,202,906)			(4,126,029)	
Bond discounts	(354,333)			(316,956)	
Bond premiums	1,816,755			1,675,491	
Accretion of capital appreciation certificates				773,029	
Less: Current portion of Long-term debt	<u>(3,278,797)</u>			<u>(3,624,542)</u>	
Total long-term debt	<u><u>\$ 107,194,350</u></u>			<u><u>\$ 123,632,935</u></u>	
Accrued compensated absences	<u><u>\$ 1,234,915</u></u>	<u><u>\$ 117,295</u></u>		<u><u>\$ 1,352,210</u></u>	

MERCED IRRIGATION DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2008 and 2007

NOTE D – LONG-TERM LIABILITIES (Continued)

	Balance January 1, 2007	Additions	Repayments	Balance December 31, 2007	Due Within One Year
Long-term debt:					
Merced River					
Development Bonds	\$ 10,755,000		\$ (1,220,000)	\$ 9,535,000	\$ 1,270,000
1998 Note payable	349,167		(19,361)	329,806	329,806
2001 Certificates of Participation	6,265,000		(760,000)	5,505,000	790,000
2003 Revenue Certificates of Participation	14,330,000		(210,000)	14,120,000	220,000
2003 Taxable Electric System Revenue Warrants					
2005 Electric System Refunding Revenue Bonds	63,050,000			63,050,000	300,000
2005 Revenue Certificates of Participation	15,000,000			15,000,000	260,000
2005 Warrants	5,000,000			5,000,000	
Pioneer Substation Note Payable	334,909		(334,909)		
	<u>115,084,076</u>		<u>(2,544,270)</u>	<u>112,539,806</u>	<u>3,169,806</u>
Capital leases	833,658		(159,833)	673,825	108,991
	<u>115,917,734</u>		<u>\$ (2,704,103)</u>	<u>113,213,631</u>	<u>\$ 3,278,797</u>
Add:					
Deferred amount on refunding	(4,559,330)			(4,202,906)	
Bond discounts	(380,748)			(354,333)	
Bond premiums	1,962,145			1,816,755	
Less: Current portion of Long-term debt	<u>(2,696,648)</u>			<u>(3,278,797)</u>	
Total long-term debt	<u>\$ 110,243,153</u>			<u>\$ 107,194,350</u>	

Accrued compensated

Long-Term Debt: Long-term debt consists of the following at December 31, 2008:

Merced River Development Bonds: On July 1, 1964, the District issued the Merced River Development Revenue Bonds in the amount of \$36,000,000. Serial and term bonds in the amount of \$9,660,000 and \$26,340,000, respectively, were issued with various call features. Proceeds from these bonds were used to construct the New Exchequer Dam and McSwain Dam, expand the hydroelectric plant, increase irrigation water supply and increase flood control storage. The bonds are to be retired from the proceeds of the power contract with the Pacific Gas and Electric Company dated June 25, 1964 for the sale of power. The interest rate is 3.75%. Semi-annual principal and interest payments ranging from \$402,406 to \$808,188 are due on January 1 and July 1 through July 1, 2014.

MERCED IRRIGATION DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2008 and 2007

NOTE D – LONG-TERM LIABILITIES (Continued)

1998 Note Payable: On April 13, 1998, the District purchased 610 acres of land in Mariposa County to provide road access and additional park development in exchange for cash of \$154,750 and an installment note of \$464,250. The note is secured by the land. The interest rate on the note is 8%. Principal and interest payments of \$11,681 are due quarterly through April 2008. A final principal payment of \$319,535 was paid on April 13, 2008.

2001 Certificates of Participation (Water Utility Facilities Improvements): On December 1, 2001, the District issued 2001 Certificates of Participation in the amount of \$9,780,000. Proceeds from these Certificates were used to advance refund the District's 1993 Certificates of Participation that were used to finance certain water system improvements and the remaining balance was used to finance the construction of the new administration building. Interest rates ranged from 3.60% to 4.75%. Principal payments ranging from \$120,000 to \$845,000 were due annually on November 1 through November 1, 2027. Interest payments ranging from \$6,056 to \$117,590 were due semi-annually on May 1 and November 1, through November 1, 2027. The District was required to maintain a ratio of water system net revenues to debt service of at least 120%. These bonds were advance refunded by the 2008 Refunding Revenue Certificates of Participation as of June 24, 2008.

2003 Revenue Certificates of Participation (Electric System Project): On March 1, 2003, the District issued 2003 Revenue Certificates of Participation in the amount of \$15,000,000. The proceeds were used to finance the cost of certain improvements to the electric system. The Certificates are secured by a lien on the District's electric system net revenues. Interest rates range from 4.5% to 5.7%. Principal payments ranging from \$230,000 to \$945,000 are due annually on September 1 through September 1, 2036. Interest payments ranging from \$26,933 to \$385,653 are due semi-annually on March 1 and September 1 through September 1, 2036. The District is required to maintain a ratio of electric system net revenues to debt service of at least 125%.

2005 Electric System Refunding Revenue Bonds: On November 10, 2005, the District issued 2005 Electric System Refunding Revenue Bonds in the amount of \$63,050,000. Proceeds from these bonds were used to advance refund the District's 2001 Electric System Refunding Revenue Bonds and the 2002 Revenue Certificate of Participation. The Bonds are secured by a lien on the District's electric system net revenues. Interest rates range from 3.3% to 5.75%. Principal payments ranging from \$1,115,000 to \$4,045,000 are due annually on September 1, through September 1, 2036. Interest payments ranging from \$106,181 to \$1,571,831, are due semi-annually on March 1, and September 1, through September 1, 2036. The District is required to maintain a ratio of electric system net revenues to debt service of at least 125%.

2005 Revenue Certificates of Participation (2005 Electric System Project): On November 10, 2005, the District issued 2005 Revenue Certificates of Participation in the amount of \$15,000,000. The proceeds are to be used to finance the cost of certain improvements to the electric system of the District. The Bonds are secured by a lien on the District's electric system net revenues. Interest rates range from 3.30% to 5.25%. Principal payments ranging from \$275,000 to \$950,000 are due annually on September 1 through September 1, 2036. Interest payments ranging from \$24,938 to \$361,251 are due semi-annually on March 1, and September 1, through September 1, 2036. The District is required to maintain a ratio of electric system net revenues to debt service of at least 125%.

2005 Warrants: On September 22, 2005, the District issued 2005 Warrants in the amount of \$5,000,000. Proceeds from the warrants are to be used to finance the costs of relicensing the District's 1964 Merced River Development Project. The interest rate is 4.00%. A single principal payment of \$5,000,000 was due July 1, 2009. Interest payments of \$100,000 were due semi-annually on January 1, and July 1, through July 1, 2009. These warrants were advance refunded by the 2008 Capital Appreciation Revenue Certificates of Participation issued on June 24, 2008.

Pioneer Substation Note Payable: On May 21, 2003, the District purchased the Pioneer Substation from Foster Farms for \$2,009,433. The terms of the sale agreement required the District to pay \$334,909 at the close of escrow and execute an installment note of \$1,674,544. This note is non-interest bearing. Payments of \$334,909 are due annually on December 31 through December 31, 2007. This note was paid off as of December 31, 2007.

MERCED IRRIGATION DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2008 and 2007

NOTE D – LONG-TERM LIABILITIES (Continued)

2008 A Refunding Revenue Certificates of Participation (Water and Hydroelectric System Projects): On June 24, 2008, the District issued 2008 Refunding Revenue Certificates of Participation in the amount of \$6,335,000. Proceeds were used to advance refund the District’s 2001 Certificates of Participation (Water Utility Facilities Improvements). The certificates are secured by a lien on the District’s Water Operations and Hydroelectric net revenues. Interest rates range from 3% to 4.625%. Principal payments ranging from \$435,000 to \$600,000 are due annually, starting on September 1, 2009 through September 1, 2020. Interest payments ranging from \$13,875 to \$146,067 are due semi-annually on March 1, and September 1 through September 1, 2020. The District is required to maintain a ratio of water operation net revenues to debt service of 120% until 2014 and a ratio of water operations and hydroelectric net revenue to debt service of 125% thereafter.

2008 B Capital Appreciation Revenue Certificates of Participation: On June 24, 2008, the District issued 2008 Capital Appreciation Revenue Certificates of Participation in the amount of \$22,718,863. Proceeds were used to advance refund the 2005 Warrants and to continue to finance the costs of relicensing the District’s 1964 Merced River Development Project. The certificates are secured by a lien on the District’s Water Operations and Hydroelectric net revenues. Interest rates range from 6.35% to 6.75%. Interest on these certificates is compounded semi-annually at March 1 and September 1 commencing September 1, 2008. The interest cost is accreted from date of issuance to maturity. The certificates mature on September 1, 2023, 2033 and 2038; however, mandatory prepayments on these certificates begin on September 1, 2015, September 1, 2024 and September 1, 2034 for each certificate maturity date, respectively. Principal payments ranging from \$1,832,445 to \$387,550 are due annually starting September 1, 2015 through September 1, 2038. Interest payments ranging from \$1,039,143 to \$2,487,450 are due annually starting September 1, 2015 through September 1, 2038. The District is required to maintain a ratio of water operations and hydroelectric net revenue to debt service of 125%.

The following is a schedule of long-term debt, excluding capital leases:

Year Ended December 31,	Principal	Interest	Total
2009	\$ 3,510,000	\$ 5,227,352	\$ 8,737,352
2010	3,620,000	5,058,263	8,678,263
2011	3,730,000	4,928,876	8,658,876
2012	3,705,000	4,791,674	8,496,674
2013	3,880,000	4,625,405	8,505,405
2014-2018	21,371,230	25,738,713	47,109,943
2019-2023	21,400,515	25,515,116	46,915,631
2024-2028	22,196,090	23,459,370	45,655,460
2029-2033	26,140,198	19,515,545	45,655,743
2034-2038	19,155,830	13,976,277	33,132,107
Total	<u>\$ 128,708,863</u>	<u>\$ 132,836,591</u>	<u>\$ 261,545,454</u>

MERCED IRRIGATION DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2008 and 2007

NOTE D – LONG-TERM LIABILITIES (Continued)

Pledged Revenues: The District has pledged future electric customer revenues, net of specified operating expenses, to repay \$15,000,000 of Revenue Certificates of Participation issued in March 2003, \$63,050,000 of Electric System Refunding Revenue Bonds issued in November 2005, and \$15,000,000 of Revenue Certificates of Participation issued in November 2005. Proceeds from the bonds provided financing for improvements to the electric system. The bonds are payable solely from electric customer net revenues and are payable through September 2036. Annual principal and interest payments on the bonds are expected to require approximately 80% of net revenues. The total principal and interest remaining to be paid on the bonds is \$175,208,432. Principal and interest paid for the current year and total electric customer net revenues were \$5,445,569 and \$6,882,922, respectively.

The District has pledged future water operations and hydroelectric system revenues, net of specified operating expenses, to repay \$6,335,000 of Revenue Refunding Certificates of Participation issued in June 2008, and \$22,718,863 of Capital Appreciation Revenue Certificates of Participation issued in June 2008. Proceeds from the certificates provided financing for improvements to the water system and relicensing of the hydroelectric facility. The certificates are payable solely from water operations and hydroelectric net revenues and are payable through September 2038. Annual principal and interest payments on the certificates are expected to require approximately 80% of net revenues. The total principal and interest remaining to be paid on the certificates is \$77,070,771. Principal and interest paid for the current year and total electric customer net revenues were \$117,590 and \$2,496,553, respectively.

Capital Leases: The District’s capital lease represents the present value of the sublease payments related to the electric distribution system and related facilities at the former Castle Air Force Base. The interest rate used to calculate the present value of the future minimum sublease payments is 4%. Payments on this sublease represent 7.5% of gross revenues received by the District from the sale of electric services to customers of the District in the Castle area and are due through 2013, at which time ownership of the electric distribution system will be transferred to the District.

The following is a schedule of the future minimum lease payments required under capital leases and the present value of the net minimum lease payments at December 31, 2008:

2009	\$ 134,181
2010	134,181
2011	134,181
2012	134,181
2013	<u>56,604</u>
Total minimum lease payments	593,328
Less: Amount representing interest	<u>(50,249)</u>
Present value of minimum lease payments	<u><u>\$ 543,079</u></u>

Arbitrage: The Tax Reform Act of 1986 instituted certain arbitrage restrictions with respect to the issuance of tax exempt bonds after August 31, 1986. Arbitrage regulations deal with investments of all tax-exempt bond proceeds at an interest yield greater than the interest paid to the bondholders. Generally, all interest paid to bond holders can be retroactive if applicable rebates are not reported and paid to the Internal Revenue Service at least every five years. The District performed calculations of excess investments earnings on various bonds and financings and at December 31, 2007, the District was in a positive arbitrage position in the amount of \$30,906 relating to the 2005 warrants. At December 31, 2008, the District had no arbitrage liability.

Refundings: In June 2008, the District issued the 2008 A Refunding Revenue Certificates of Participation in the amount of \$6,335,000 with an average interest rate of 4.47%, to refund \$5,552,732 of the 2001 Certificates of Participation with an average interest rate of 4.65%. The net proceeds from this issuance were deposited into an irrevocable trust to provide for all future debt service payments for the 2001 Certificates of Participation. As

MERCED IRRIGATION DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2008 and 2007

NOTE D – LONG-TERM LIABILITIES (Continued)

a result, the 2001 Certificates of Participation are considered defeased and the liability for these certificates has been removed from the District's financial statements.

The District completed the advance refunding to reduce its total debt service payments through 2011. The net economic loss (difference between the present value of the old and new debt service payments) of the 2008 A Refunding Revenue Certificates of Participation is \$23,926. The advance refunding resulted in differences between the reacquisition price and the net carrying amount of the outstanding debt of \$271,108 at December 31, 2008, net of accumulated amortization. This deferred amount on refunding, reported in the accompanying financial statements as a reduction in long-term debt, is being charged to operations over 13 years using the bonds-outstanding method.

In June 2008, the District issued the 2008 B Capital Appreciation Revenue Certificates of Participation in the amount of \$22,718,863 with an average interest of 6.64%, to refund \$5,106,792 of the 2005 Warrants with an interest rate of 4%. The net proceeds from this issuance were deposited into an irrevocable trust to provide for all future debt service payments for the 2005 Warrants. As a result, the 2005 Warrants are considered defeased and the liability for this bond has been removed from the District's financial statements.

The 2008 Capital Appreciation Revenue Certificates of Participation were issued to refinance the 2005 Warrants which mature in 2009 and to acquire additional funds to continue financing the costs associated with the relicensing of the District's 1964 Merced River Development Project. The advance refunding resulted in differences between the reacquisition price and the net carrying amount of the outstanding debt of \$22,890 at December 31, 2008, net of accumulated amortization. This deferred amount on refunding, reported in the accompanying financial statements as a reduction in long-term debt, is being charged to operations over 31 years using the bonds-outstanding method.

NOTE E – ENERGY SUPPLY PURCHASES AND COMMITMENTS

The District relies on various power supply agreements to serve its customers' electricity requirements. The District has power supply agreements with the Turlock Irrigation District (TID), Western Area Power Administration (Western), and Iberdrola Renewables, Inc. (Iberdrola), formerly PPM Energy, Inc. (PPM). Furthermore, TID provides wheeling, interconnection and ancillary services to the District under an interconnection agreement. The District has engaged The Energy Authority (TEA), to assist with coordination of these agreements according to the District's resource management plan. The major agreements are described as follows:

Turlock Irrigation District: In 2007, the District amended and extended its current power supply agreement with TID from the period of January 1, 2006 through April 2008, out through April 30, 2009, while maintaining the transaction charge reduction of \$.25 per megawatt-hour for the period January 1, 2007 through the end of the agreement. This partial requirements power supply agreement provides power for all of the District's power requirements with the exception of the power supplied by WAPA. The price of this power supply is tied to the Daily Dow Jones North Path 15 index times 106% plus \$4.75 per megawatt-hour.

The contract amendment also implemented several changes to other original contract terms. The amendment allows the energy price to be adjusted by any congestion charges and losses between the Delivery Point and the NP 15 location. It reduces the transmission loss percentage applied to the power purchased from TID from 3% to 2% for the period May 1, 2008 through April 30, 2009. Also, beginning December 31, 2007, the District is required to supply sufficient generating reserves to meet the Resource Adequacy Policy established by the Turlock Board of Directors for TID. The District's purchases in 2008 and 2007 totaled \$33,735,882 and \$27,440,820, respectively.

Western Area Power Administration: Western markets power from the Central Valley Project (CVP) and Washoe Project. The District began operating under the base resource contract on January 1, 2005. This contract provides for the District to receive .33201% of WAPA's base resource, which is power available for marketing after project

MERCED IRRIGATION DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2008 and 2007

NOTE E – ENERGY SUPPLY PURCHASES AND COMMITMENTS (Continued)

power requirements. The current contract is scheduled to expire December 31, 2024. The District’s composite price for power was approximately \$36.18 and \$25.01 per megawatt hour in 2008 and 2007, respectively. The District’s purchases in 2008 and 2007 totaled \$360,636 and \$302,302, respectively.

Iberdrola Renewables Inc.: The District entered into a 25 year power supply agreement with Iberdrola in 2003 for energy generated by a wind energy project. This is a non-firm power supply contract to purchase 5 megawatts of installed capacity, which is expected to generate 16,000 megawatt-hours of energy annually for the District at a fixed price of \$54.95 per megawatt-hour. The District entered into a subsequent agreement to sell this wind energy back to Iberdrola from January 1, 2006, through January 1, 2008. In 2007, this agreement was extended through January 1, 2009, and in 2008 it was further extended through March 31, 2009. The price per megawatt-hour is 90% of the Powerdex hourly index at North Path 15 minus \$1.00. The District’s purchases in 2008 and 2007 totaled \$720,395 and \$744,408, respectively. The District’s sales back to Iberdrola in 2008 and 2007 totaled \$820,039 and \$618,034, respectively.

The District purchases swap agreements to manage market price risk under its current and previous agreements. All ongoing electricity swap agreements settle against the North Path 15 daily price index. This index was selected to link the swap agreements to the cost of electricity under the TID agreement. The District’s objective in executing swap agreements is to fix its costs for power supply and hedge market price exposure. The net amount of electricity swap settlements paid in 2008 and 2007 were \$(236,813) and \$3,771,110, respectively. The District has provided assurance deposits to one of the counterparties as collateral for swap agreements in the amount of \$1,750,000 at December 31, 2008.

The fair values of the electricity price swap agreements are based on forward prices from established indices for the applicable region and discounted using the District’s estimated cost of funds of 5.5% at December 31, 2008 and 2007. The estimated fair values of the District’s swap agreements as of December 31, are as follows:

	2008			2007		
	Fixed Payment Obligation	Fair Value	Net Loss	Fixed Payment Obligation	Fair Value	Net Loss
Electricity Swaps	\$ 45,991,490	\$ 33,266,761	\$(12,724,729)	\$ 35,459,615	\$ 34,334,587	\$ (1,125,028)

The District is exposed to credit risk related to non-performance by its wholesale counterparties under the terms of these swap agreements. The District evaluates the creditworthiness of its counterparties at the time of inception of the International Swap Dealers Association, Inc. (ISDA) agreement and at the time each swap transaction is executed, but the District does not currently have a formal evaluation policy. The District does contract with several counterparties to mitigate the risk of non-performance by any one counterparty.

NOTE F – NET ASSETS

Restrictions: The restricted portion of net assets is the result of external constraints placed on net asset use by creditors (such as through debt covenants), grants, contributors, or laws or regulations of other governments or constraints imposed by law through statutory provisions or legislation. Restricted net assets include the following at December 31:

MERCED IRRIGATION DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2008 and 2007

NOTE F – NET ASSETS (Continued)

	<u>2008</u>	<u>2007</u>
Debt service payments	\$ 11,733,444	\$ 9,328,275
Power swap pledged collateral	1,750,000	
Recreation plan operations and maintenance	1,136,345	1,120,912
Mariposa County water rights settlement	937,086	1,023,662
Recreation plan future stage construction	6,503	6,413
Federal Energy Regulatory Commission (FERC) Relicensing Costs		2,855,164
	<u>\$ 15,563,378</u>	<u>\$ 14,334,426</u>

The restrictions are for the following:

Restricted for debt service payments represents debt service reserves required by the related debt covenants.

Restricted for power swap pledged collateral represents cash on deposit with Constellation Power Source for collateralization of power swaps.

Restricted for recreation plan operations and maintenance represents unspent State of California grant proceeds restricted for the District's recreation plan operations and maintenance.

Restricted for Mariposa County water rights settlement represents unspent State of California grant proceeds restricted for the remaining unpaid Mariposa County water rights commitment.

Restricted for recreation plan future stage construction represents unspent State of California grant proceeds restricted for the third stage of onshore recreation facilities improvements, including fishing access sites, at Lake McClure and Lake McSwain in accordance with the District's recreation plan.

Restricted for FERC Relicensing costs represents proceeds from warrants issued to fund costs to be incurred for relicensing the District's hydroelectric facility with FERC.

Designations: Designations of unrestricted net assets are imposed by the Board of Directors to reflect future spending plans of current resources. Designations may be modified, amended or removed by Board action. At December 31, designations included:

	<u>2008</u>	<u>2007</u>
Rate stabilization	\$ 5,400,000	\$ 7,000,000
Electric Services working capital reserve	5,500,000	5,000,000
Parks capital project reserve	160,000	160,000
Total	<u>\$ 11,060,000</u>	<u>\$ 12,160,000</u>

The designations are for the following:

Designated for rate stabilization represents the amount set aside for the funding of future unplanned water pumping costs.

Designated for Electric Services working capital reserve represents the amount set aside for future Electric Services working capital requirements.

Designated for future capital projects within the parks.

MERCED IRRIGATION DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2008 and 2007

NOTE G – EMPLOYEES’ RETIREMENT PLAN

Plan Description: The District contributes to the California Public Employees Retirement System (CalPERS), an agent multiple-employer public employee defined benefit pension plan. CalPERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and their beneficiaries. CalPERS acts as a common investment and administrative agent for participating public employers within the State of California. All permanent full and part-time District employees working at least 1,000 hours per year are eligible to participate in CalPERS. Under CalPERS, benefits vest after five years of service. Upon retirement, participants are entitled to an annual retirement benefit, payable for life, in an amount equal to a benefit factor, based on years of service, multiplied by their highest average monthly salary over thirty-six consecutive months of employment. Copies of the CalPERS annual financial report may be obtained from their Executive Office, 400 P Street, Sacramento, CA 95814.

Funding Policy: Active plan members are required to contribute 7% of their annual covered salary, of which the District contributes 6% of annual covered salaries on behalf of District employees and for their account at December 31, 2008. Contributions made by the District on behalf of the employees were \$620,281 and \$497,160 for the years ended December 31, 2008 and 2007, respectively. The District is required to contribute at an actuarially determined rate; the rate for January 1 to June 30, 2008 was 11.67% and for July 1 to December 31, 2008 was 11.47%. The contribution requirements of plan members and the District are established and may be amended by CalPERS.

Annual Pension Cost: For the years ending December 31, 2008 and 2007, the District incurred an annual pension cost of \$1,196,992 and \$1,194,927, respectively. The required contribution was determined as part of the June 30, 2005 and 2006 actuarial valuations using entry age actuarial cost method. The actuarial assumptions included (a) 7.75% investment rate of return (net of administrative expenses); (b) projected salary increases that vary in duration of service ranging from 3.25% to 14.45% for miscellaneous members and (c) 3.25% payroll growth adjustment. Both (a) and (b) include an inflation component of 3%. The actuarial value of the plan’s assets was determined using techniques that smooth the effects of short-term volatility in the market value of investments over a 15 year period (smoothed market value). The plan’s excess assets are being amortized as a level percentage of projected payroll on a closed basis. The average remaining amortization period at June 30, 2006 was 25 years.

Three-Year Trend Information for the District

<u>Fiscal Year Ending</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage Of APC Contributed</u>
December 31, 2006	\$ 1,248,543	100%
December 31, 2007	1,194,927	100%
December 31, 2008	1,196,992	100%

Required Supplementary Information - Funded Status of Plan

<u>Actuarial Valuation Date</u>	<u>Entry Age Actuarial Accrued Liability</u>	<u>Actuarial Assets Value</u>	<u>(Excess Assets) Unfunded Liability</u>	<u>Funded Ratio</u>	<u>Covered Payroll</u>	<u>Unfunded Liability as a % of Covered Payroll</u>
6/30/2005	\$ 36,272,673	\$ 28,701,283	\$ 7,571,390	79.10%	\$ 8,854,119	85.50%
6/30/2006	39,366,263	31,839,500	7,526,763	80.88%	9,413,485	80.00%
6/30/2007	42,986,190	35,170,081	7,816,109	81.80%	10,284,234	76.00%

MERCED IRRIGATION DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2008 and 2007

NOTE H – POSTEMPLOYMENT HEALTH CARE BENEFITS

Plan Description: The District administers a single employer defined benefit other postemployment healthcare (OPEB) plan providing health plan coverage to eligible retired employees and their eligible dependents. The District maintains the same medical plans for its retirees as for its active employees. Benefits are paid until the retiree, spouse or surviving spouse, becomes eligible for Medicare. Employees become eligible to retire and receive healthcare benefits upon reaching the age of 60 with 5 years of service to the District. The OPEB Plan does not issue a publicly available financial report.

Funding Policy: The contribution requirements of plan members and the District are established and may be amended by the Board of Directors. The required contribution is based on projected pay-as-you-go financing requirements. For 2008, the District contributed \$142,460 to the plan, which represents 94% of the cost of current year premiums for eligible retired plan members and their spouses. Plan members receiving benefits contributed \$9,270, or approximately 6% of the total premiums, through their required contribution of \$90 for spouse coverage.

Annual OPEB Cost and Net OPEB Obligation: The District’s annual OPEB cost (expense) is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years. The following table shows the components of the District’s annual OPEB cost for the year, the amount actually contributed to the plan, and changes in the District’s net OPEB obligation to the OPEB plan:

Annual required contribution	\$ 215,226
Contributions made (premium payments made)	<u>(142,460)</u>
Increase in net OPEB obligation	72,766
Net OPEB obligation, beginning of year	<u>1,686,622</u>
Net OPEB obligation, end of year	<u>\$ 1,759,388</u>

The District had an OPEB obligation of \$1,686,622 as of the implementation of GASB Statement No. 45, which was less than the actuarial accrued liability of \$1,873,768. However, the OPEB obligation will be increased prospectively to the actuarial accrued liability amount. The District’s annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for 2008 were as follows:

<u>Year Ended</u>	<u>Annual OPEB Cost</u>	<u>Percentage of Annual OPEB Cost Contributed</u>	<u>Net OPEB Obligation</u>
December 31, 2008	\$ 215,226	33.18%	\$ 1,759,388

Funded Status and Funding Progress: As of January 1, 2008, the most recent actuarial valuation date, the actuarial accrued liability for benefits was \$1,873,768, all of which was unfunded. The covered payroll (annual payroll of active employees covered by the plan) was \$11,162,000, and the ratio of the UAAL to the covered payroll was 16.79%.

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information below, presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

MERCED IRRIGATION DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2008 and 2007

NOTE H – POSTEMPLOYMENT HEALTH CARE BENEFITS (Continued)

Actuarial Methods and Assumptions: Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets consistent with the long-term perspective of the calculations.

In the January 1, 2008 actuarial valuation, the projected unit credit actuarial method was used. The actuarial assumptions included a 5% investment rate of return (net of administrative expenses), which is based on the employer’s own investments. The annual healthcare-cost trend rates are as follows: for medical premiums, 10% initially, reduced by 1% decrements to an ultimate rate of 5% after six years; for dental premiums, 7% every other year, with the first assumed July 1, 2010; for vision insurance premiums, 5% every third year, with the next increase in January, 2009. Life insurance premiums are not assumed to change from current levels. The assumptions also includes a 3.25% annual increase in covered payroll and a 3% inflationary factor. The UAAL is being amortized as a level percentage of projected payroll on an open basis. The remaining amortization period at January 1, 2008, was 30 years.

Required Supplementary Information
Schedule of Funding Progress for the Retiree Health Plan

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL)– Simplified Entry Age (b)	Unfunded AAL (UAAL) (b - a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
January 1, 2008	\$ -	\$ 1,873,768	\$ 1,873,768	\$ -	\$ 11,162,000	16.79%

NOTE I – INSURANCE

The District participates in the Association of California Water Agencies Joint Powers Insurance Authority (ACWA/JPIA) a public entity risk pool of California water agencies, for general and auto liability, public officials liability, property damage, fidelity, dam failure and workers’ compensation insurance. ACWA/JPIA provides insurance through the pool up to a certain level, beyond which group-purchased commercial excess insurance is obtained.

The District pays an annual premium to ACWA/JPIA that includes its pro-rata share of excess insurance premiums, charges for the pooled risk, claims adjusting and legal costs, and administrative and other costs to operate the ACWA/JPIA. The District’s deductibles and maximum coverages are as follows:

Coverage	ACWA/JPIA	Insurance	Commercial Deductible
General and Auto Liability (Includes public officials liability)	\$ 1,000,000	\$ 59,000,000	None
Property Damage	50,000	100,000,000	\$5,000 to 25,000
Fidelity	100,000		1,000
Workers' Compensation liability	2,000,000	Statutory	None
Dam failure liability		5,000,000	50,000

MERCED IRRIGATION DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2008 and 2007

NOTE I – INSURANCE

The District continues to carry commercial insurance for all other risks of loss to which the District is exposed. Settled claims have not exceeded commercial insurance coverage in any of the past three fiscal years. Effective January 1, 1996, the District changed to ACWA/JPIA for workers' compensation liability coverage. Prior to January 1, 1996, the District was self-insured for workers' compensation. The District has recorded an accrual of \$25,327 and \$27,042 at December 31, 2008 and 2007, respectively, related to claims that were incurred during the self-insured period.

NOTE J – COMMITMENTS AND CONTINGENCIES

Mariposa County Water Rights Settlement: On March 1, 1960, the District entered into an agreement with Mariposa County for a fifty year right to stream flow from the Merced River. In exchange for this right, the District agreed to pay \$5,000,000 in annual installments of not less than \$100,000, which are due annually on March 1. The agreement is secured by a lien on interest earned on certain accounts held in trust.

Litigation: The District is party to various claims, legal actions and complaints that arise in the normal operation of business. Management and the District's legal counsel believe that there are no material loss contingencies that would have a material adverse impact on the financial position of the District.

Federal and State Regulatory Issues: The District has a conditional license with the Federal Energy Regulatory Commission to operate its 1964 Merced River Development Project through February 2014. The District is working to renew this license.

NOTE K – LINE OF CREDIT

The District had a \$7,000,000 line of credit that expired on June 15, 2008. The interest rate on this line of credit was the Wall Street Journal prime rate plus 1% adjustable monthly. At December 31, 2007, no amount was outstanding on this line of credit. The District did not have a line of credit at December 31, 2008.

NOTE L – DISCLOSURE OF SEGMENT INFORMATION

The District has issued separate revenue bonds to finance its electric and water operations. These operations are accounted for within the District, but investors in those bonds rely solely on the revenue generated by the individual activities for repayment. Summary financial information for each segment is presented below. Electric Services operates the retail electric system. The Water Operations operates the District's irrigation water supply system and consists of the Water Utility, San Joaquin River Agreement, Water Transfers, MID Public Facilities Financing Corporation, and the Water Utility Facility Improvement Funds.

MERCED IRRIGATION DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2008 and 2007

NOTE L – DISCLOSURE OF SEGMENT INFORMATION

	2008		2007	
	Electric Services	Water Operations	Electric Services	Water Operations
CONDENSED BALANCE SHEET				
Assets:				
Capital assets	\$ 72,643,088	\$ 34,014,696	\$ 73,090,880	\$ 33,740,282
Other assets	4,370,636	92,128	4,682,824	155,156
Interfund receivables		182,010		
Current assets	14,552,996	19,290,652	26,233,246	37,878,180
Total assets	<u>91,566,720</u>	<u>53,579,486</u>	<u>104,006,950</u>	<u>71,773,618</u>
Liabilities:				
Long-term and other liabilities	93,083,889	7,797,638	93,441,221	7,752,266
Interfund payables		(11,145,382)		5,320,812
Other current liabilities	(5,868,333)	4,899,961	5,208,444	7,238,835
Total liabilities	<u>87,215,556</u>	<u>1,552,217</u>	<u>98,649,665</u>	<u>20,311,913</u>
Net assets:				
Invested in capital assets, net of related debt	(14,826,349)	27,996,556	(13,398,226)	28,045,334
Restricted	9,143,131	1,583,885	7,472,831	1,154,174
Unrestricted	10,034,382	22,446,828	11,282,680	22,262,197
Total net assets	<u>\$ 4,351,164</u>	<u>\$ 52,027,269</u>	<u>\$ 5,357,285</u>	<u>\$ 51,461,705</u>
CONDENSED STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS				
Operating revenues (pledged against bonds)	\$ 50,215,471	\$ 13,567,936	\$ 46,144,731	\$ 14,844,118
Depreciation and amortization expense	(2,688,737)	(1,349,029)	(2,613,081)	(1,230,153)
Other operating expenses	(43,552,979)	(17,724,616)	(40,545,794)	(15,990,574)
Operating income	<u>3,973,755</u>	<u>(5,505,709)</u>	<u>2,985,856</u>	<u>(2,376,609)</u>
Non-operating revenues (expenses):				
Property taxes		2,328,056		2,306,705
Other non-operating revenues	266,140	1,577,198	771,055	1,869,466
Interest expense	(4,786,687)	(247,783)	(4,572,191)	(343,367)
Capital contributions	578,848	675,307	1,485,339	2,334,009
Transfers in	532,041	3,173,866	421,882	2,390,197
Transfers out	(1,570,218)	(1,435,371)	(984,051)	(1,269,177)
Change in net assets	<u>(1,006,121)</u>	<u>565,564</u>	<u>107,890</u>	<u>4,911,224</u>
Beginning net assets	<u>5,357,285</u>	<u>51,461,705</u>	<u>5,249,395</u>	<u>46,550,481</u>
Ending net assets	<u>\$ 4,351,164</u>	<u>\$ 52,027,269</u>	<u>\$ 5,357,285</u>	<u>\$ 51,461,705</u>

MERCED IRRIGATION DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2008 and 2007

NOTE L – DISCLOSURE OF SEGMENT INFORMATION (Continued)

	<u>2008</u>		<u>2007</u>	
	<u>Electric Services</u>	<u>Water Operations</u>	<u>Electric Services</u>	<u>Water Operations</u>
CONDENSED STATEMENT OF CASH FLOWS				
Net cash provided (used) by:				
Operating activities	\$ 11,962,463	\$ (9,415,705)	\$ 744,846	\$ 2,748,322
Noncapital financing activities	56,750	2,396,664	107,641	3,271,722
Capital and related financing activities	(6,854,925)	(304,583)	(9,575,456)	(3,210,083)
Investing activities	<u>240,337</u>	<u>865,750</u>	<u>705,961</u>	<u>1,208,289</u>
Net increase (decrease)	5,404,625	(6,457,874)	(8,017,008)	4,018,250
Beginning cash and cash equivalents	<u>11,596,093</u>	<u>22,089,062</u>	<u>19,613,101</u>	<u>18,070,812</u>
Ending cash and cash equivalents	<u><u>\$ 17,000,718</u></u>	<u><u>\$ 15,631,188</u></u>	<u><u>\$ 11,596,093</u></u>	<u><u>\$ 22,089,062</u></u>

MERCED IRRIGATION DISTRICT

BALANCE SHEETS BY FUND

December 31, 2008

	Electric Services	Water Utility	Hydroelectric	Parks	Drainage Improvement District #1
ASSETS					
CAPITAL ASSETS, NET	\$ 72,643,088	\$ 33,992,539	\$ 28,246,712	\$ 3,451,433	\$ 854,881
OTHER NONCURRENT ASSETS					
Deferred relicense costs					
Debt issuance costs	4,370,636	92,128			
Regulatory costs for future recovery					
TOTAL OTHER NONCURRENT ASSETS	4,370,636	92,128			
CURRENT ASSETS					
Cash and cash equivalents	5,821,689	13,509,525	975	1,480	696,455
Accounts receivable, net	5,485,521	440,123	3,001	26,786	1,028
Due from other governmental agencies	222,227	603,239			
Accrued interest and taxes receivable	8,071	1,110,756	99	93	107,197
Inventory	4,417,687	197,596			
Prepaid expenses and other current assets	143,501	198,736	115,875	41,452	9,649
Due from other funds					259,370
Restricted cash and cash equivalents	11,179,029	1,583,885	1,354,737	1,142,848	
Derivative financial instruments	(12,724,729)				
TOTAL CURRENT ASSETS	14,552,996	17,643,860	1,474,687	1,212,659	1,073,699
TOTAL ASSETS	\$ 91,566,720	\$ 51,728,527	\$ 29,721,399	\$ 4,664,092	\$ 1,928,580

San Joaquin River Agreement Fund	Merced Irrigation District Public Facilities Financing Corporation	Water Transfers	Water Utility Facility Improvement Fund	Federal Energy Regulatory Commission Fund	General Operations	Eliminating Entries	Totals
			\$ 22,157		\$ 131,090		\$ 139,341,900
				\$ 6,800,666			6,800,666
				366,227			4,828,991
				773,029			773,029
				7,939,922			12,402,686
\$ 537,778					4,049,999		24,617,901
937,203					11,771	\$ (10,935)	5,957,295
				1,548			1,762,669
					262,674		1,227,764
171,811							4,615,283
20,161,171	\$ 5,660,812					(26,081,353)	943,698
				19,057,030			34,317,529
<u>21,807,963</u>	<u>-</u>	<u>5,660,812</u>	<u>-</u>	<u>19,058,578</u>	<u>4,324,444</u>	<u>(26,092,288)</u>	<u>(12,724,729)</u>
<u>\$ 21,807,963</u>	<u>\$ -</u>	<u>\$ 5,660,812</u>	<u>\$ 22,157</u>	<u>\$ 26,998,500</u>	<u>\$ 4,455,534</u>	<u>\$ (26,092,288)</u>	<u>\$ 212,461,996</u>

MERCED IRRIGATION DISTRICT

BALANCE SHEETS BY FUND (Continued)

December 31, 2008

	Electric Services	Water Utility	Hydroelectric	Parks	Drainage Improvement District #1
LIABILITIES AND NET ASSETS					
LONG-TERM LIABILITIES					
Long-term debt	\$ 87,770,793	\$ 5,443,140	\$ 6,950,000		
Accrued compensated absences	190,687	802,735	103,000	\$ 132,421	\$ 3,024
Accrued post-employment benefits	229,845	1,035,649	137,930	179,939	3,352
TOTAL LONG-TERM LIABILITIES	88,191,325	7,281,524	7,190,930	312,360	6,376
OTHER LIABILITIES					
Deferred public purpose program revenues	2,552,678				
Deferred power cost reductions	1,100,000				
Deposits	1,239,886	408,402		1,221	
TOTAL OTHER LIABILITIES	4,892,564	408,402		1,221	
CURRENT LIABILITIES					
Accounts payable	223,398	349,628	272,682	25,393	160
Accrued permission fees	899,812				
Accrued power purchase expense	2,658,903				
Other accrued expenses	180,373	145,575	88,128	24,520	(304)
Deferred revenue		512,179	542,058		
Accrued interest payable	1,159,368	75,730	154,969		
Due to other funds		14,425,898	1,795,013	4,316,527	
Deferred credit - unrealized (loss) gain on swap contracts	(12,724,729)				
Current portion of long-term debt	1,734,542	575,000	1,315,000		
TOTAL CURRENT LIABILITIES	(5,868,333)	16,084,010	4,167,850	4,366,440	(144)
TOTAL LIABILITIES	87,215,556	23,773,936	11,358,780	4,680,021	6,232
NET ASSETS					
Invested in capital assets, net of related debt	(14,826,349)	27,974,399	19,981,712	3,451,433	854,881
Restricted	9,143,131	1,583,885	1,354,737	1,142,848	
Unrestricted	10,034,382	(1,603,693)	(2,973,830)	(4,610,210)	1,067,467
TOTAL NET ASSETS	4,351,164	27,954,591	18,362,619	(15,929)	1,922,348
TOTAL LIABILITIES AND NET ASSETS	\$ 91,566,720	\$ 51,728,527	\$ 29,721,399	\$ 4,664,092	\$ 1,928,580

San Joaquin River Agreement Fund	Merced Irrigation District Public Facilities Financing Corporation	Water Transfers	Water Utility Facility Improvement Fund	Federal Energy Regulatory Commission Fund	General Operations	Eliminating Entries	Totals
				\$ 23,469,002			\$ 123,632,935
\$ 35,260					\$ 85,083		1,352,210
72,452					100,221		1,759,388
<u>107,712</u>				<u>23,469,002</u>	<u>185,304</u>		<u>126,744,533</u>
							2,552,678
							1,100,000
					6,120		1,655,629
					<u>6,120</u>		<u>5,308,307</u>
27,808				96,049	18,269	\$ (10,935)	1,002,452
							899,812
14,041				17,045	65,874		2,658,903
	\$ 3,200,000						535,252
							4,254,237
			\$ 68,693	1,252,927	4,222,295	(26,081,353)	1,390,067
							(12,724,729)
<u>41,849</u>		<u>3,200,000</u>	<u>68,693</u>	<u>1,366,021</u>	<u>4,306,438</u>	<u>(26,092,288)</u>	<u>3,624,542</u>
149,561		3,200,000	68,693	24,835,023	4,497,862	(26,092,288)	133,693,376
			22,157		131,090		37,589,323
				2,338,777			15,563,378
<u>21,658,402</u>		<u>2,460,812</u>	<u>(68,693)</u>	<u>(175,300)</u>	<u>(173,418)</u>		<u>25,615,919</u>
<u>21,658,402</u>		<u>2,460,812</u>	<u>(46,536)</u>	<u>2,163,477</u>	<u>(42,328)</u>		<u>78,768,620</u>
<u>\$ 21,807,963</u>	<u>\$ -</u>	<u>\$ 5,660,812</u>	<u>\$ 22,157</u>	<u>\$ 26,998,500</u>	<u>\$ 4,455,534</u>	<u>\$(26,092,288)</u>	<u>\$ 212,461,996</u>

MERCED IRRIGATION DISTRICT

SCHEDULE OF REVENUES, EXPENSES
AND CHANGES IN FUND NET ASSETS BY FUND

For the year ended December 31, 2008

	Electric Services	Water Utility	Hydroelectric	Parks	Drainage Improvement District #1
OPERATING REVENUES					
Electric sales and services	\$ 50,215,471				
Water sales and services		\$ 8,919,508			
Hydroelectric sales and services			\$ 6,114,517		
Water transfers					
Recreation fees				\$ 1,564,837	
Rental income					
Administrative services					
Storm drainage fees					\$ 28,495
TOTAL OPERATING REVENUES	50,215,471	8,919,508	6,114,517	1,564,837	28,495
OPERATING EXPENSES					
Purchase of power	33,327,494				
Water distribution		14,722,100			
Electric transmission and distribution	10,223,800		3,680,418		
Recreation				1,861,015	
Storm drainage					54,207
Administrative and general	1,685	2,318,705	135,785		25,685
Depreciation and amortization	2,688,737	1,341,641	715,724	335,542	24,288
TOTAL OPERATING EXPENSES	46,241,716	18,382,446	4,531,927	2,196,557	104,180
NET INCOME (LOSS) FROM OPERATIONS	3,973,755	(9,462,938)	1,582,590	(631,720)	(75,685)
NON-OPERATING REVENUE (EXPENSES)					
Property taxes		2,328,056			237,158
Interest income	204,413	804,246	6,843	16,060	20,874
Other non-operating income	56,750	372,728	45,532	5,924	34
Gain on disposal of capital assets	4,977	375,952	(27,253)	18,692	
Interest expense	(4,786,687)	(108,131)	(351,734)		
Transfers in	532,041	2,385,158			11,941
Transfers out	(1,570,218)	(1,330,573)	(150,407)	(194,147)	(55,524)
TOTAL NON-OPERATING REVENUE (EXPENSES)	(5,558,724)	4,827,436	(477,019)	(153,471)	214,483
NET INCOME (LOSS) BEFORE CAPITAL CONTRIBUTIONS	(1,584,969)	(4,635,502)	1,105,571	(785,191)	138,798
CAPITAL CONTRIBUTIONS	578,848	675,307		133	
CHANGE IN NET ASSETS	(1,006,121)	(3,960,195)	1,105,571	(785,058)	138,798
Net assets at beginning of year	5,357,285	36,460,414	17,257,048	769,129	1,783,550
Fund Balance Transfer		(4,545,628)			
Net assets at end of year	\$ 4,351,164	\$ 27,954,591	\$ 18,362,619	\$ (15,929)	\$ 1,922,348

San Joaquin River Agreement Fund	Merced Irrigation District Public Facilities Financing Corporation	Water Transfers	Water Utility Facility Improvement Fund	Federal Energy Regulatory Commission Fund	General Operations	Eliminating Entries	Totals
							\$ 50,215,471
							8,919,508
							6,114,517
\$ 4,648,428							4,648,428
	\$ 146,779					\$ (146,779)	1,564,837
					\$ 2,481,860	(2,481,860)	
							28,495
<u>4,648,428</u>	<u>146,779</u>				<u>2,481,860</u>	<u>(2,628,639)</u>	<u>71,491,256</u>
							33,327,494
830,515	75					(146,779)	15,405,911
				\$ 26,644		(23,000)	13,907,862
							1,861,015
							54,207
					2,190,498	(2,481,860)	2,190,498
	7,388			29,825	42,521		5,185,666
<u>830,515</u>	<u>7,463</u>			<u>56,469</u>	<u>2,233,019</u>	<u>(2,651,639)</u>	<u>71,932,653</u>
3,817,913	139,316			(56,469)	248,841	23,000	(441,397)
							2,565,214
17,733	336			129,863	765		1,201,133
6,203					28,956	(23,000)	493,127
					993		373,361
	(139,652)			(40,768)			(5,426,972)
557,110	27,956	\$ 203,642			44,742	(3,762,590)	
(94,603)			\$ (10,195)	(32,626)	(324,297)	3,762,590	
<u>486,443</u>	<u>(111,360)</u>	<u>203,642</u>	<u>(10,195)</u>	<u>56,469</u>	<u>(248,841)</u>	<u>(23,000)</u>	<u>(794,137)</u>
4,304,356	27,956	203,642	(10,195)				(1,235,534)
							1,254,288
4,304,356	27,956	203,642	(10,195)				18,754
17,354,046	(4,573,584)	2,257,170	(36,341)	2,163,477	(42,328)		78,749,866
	4,545,628						
<u>\$ 21,658,402</u>	<u>\$ -</u>	<u>\$ 2,460,812</u>	<u>\$ (46,536)</u>	<u>\$ 2,163,477</u>	<u>\$ (42,328)</u>	<u>\$ -</u>	<u>\$ 78,768,620</u>

MERCED IRRIGATION DISTRICT

SCHEDULE OF CASH FLOWS BY FUND

December 31, 2008

	Electric Services	Water Utility	Hydroelectric	Parks	Drainage Improvement District #1
CASH FLOWS FROM OPERATING ACTIVITIES					
Cash receipts from customers	\$ 52,399,510	\$ 9,018,024	\$ 7,084,142	\$ 1,555,352	\$ 27,479
Cash paid to suppliers for goods and services	(42,211,157)	(13,959,404)	(3,025,136)	(877,248)	(79,489)
Cash paid to employees for services	(2,137,683)	(6,378,817)	(881,708)	(753,627)	(22,736)
Cash receipts/payments to other funds	3,911,793	1,028,245	(1,109,533)	231,810	(741)
NET CASH PROVIDED (USED) FOR OPERATING ACTIVITIES	11,962,463	(10,291,952)	2,067,765	156,287	(75,487)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES					
Non-operating interfund transfers		291,631			
Property taxes received		2,426,349			129,961
Relicense costs incurred					
Proceeds from issuance of debt					
Issuance costs paid					
Interest payments on long-term debt					
Other income/expenses	56,750	372,728	45,532	5,924	34
NET CASH PROVIDED (USED) BY NONCAPITAL FINANCING ACTIVITIES	56,750	3,090,708	45,532	5,924	129,995
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES					
Acquisition and construction of capital assets	(1,626,249)	(1,427,353)	(810,863)	(196,400)	
Proceeds from the sale of equipment	8,560	378,579		20,899	
Reimbursements received for capital assets	272,757	755,431		133	
Principal payments on long-term debt	(910,746)	(329,806)	(1,270,000)		
Proceeds from issuance of debt		683,143			
Issuance costs paid		(38,435)			
Interest payments on long-term debt	(4,599,247)	(13,091)	(345,749)		
NET CASH USED BY CAPITAL AND RELATED FINANCING ACTIVITIES	(6,854,925)	8,468	(2,426,612)	(175,368)	
CASH FLOWS FROM INVESTING ACTIVITIES					
Interest received on investments	240,337	847,681	10,304	19,343	20,874
NET CASH PROVIDED BY INVESTING	240,337	847,681	10,304	19,343	20,874
INCREASE (DECREASE) IN CASH	5,404,625	(6,345,095)	(303,011)	6,186	75,382
Cash and cash equivalents at beginning of year	11,596,093	21,438,505	1,658,723	1,138,142	621,073
CASH AND CASH EQUIVALENTS AT END OF YEAR	\$ 17,000,718	\$ 15,093,410	\$ 1,355,712	\$ 1,144,328	\$ 696,455

San Joaquin River Agreement Fund	Merced Irrigation District Public Facilities Financing Corporation	Water Transfers	Water Utility Facility Improvement Fund	Federal Energy Regulatory Commission Fund	General Operations	Eliminating Entries	Totals
\$ 4,736,350	\$ 146,779	\$ 3,750,000			\$ 2,481,959	\$ (4,028,159)	\$ 77,171,436
(513,705)	(76)		\$ (185,893)	\$ (26,644)	(1,290,850)	5,133,019	(57,036,583)
(265,001)					(943,612)		(11,383,184)
<u>(3,963,847)</u>	<u>553,442</u>	<u>(3,750,000)</u>	<u>368,198</u>		<u>3,812,493</u>	<u>(1,081,860)</u>	
(6,203)	700,145		182,305	(26,644)	4,059,990	23,000	8,751,669
	(700,247)			408,616			2,556,310
				(1,609,533)			(1,609,533)
				17,387,071			17,387,071
				(155,426)			(155,426)
				(30,533)			(30,533)
<u>6,203</u>					<u>28,956</u>	<u>(23,000)</u>	<u>493,127</u>
6,203	(700,247)			16,000,195	28,956	(23,000)	18,641,016
			(182,305)		(41,712)		(4,284,882)
					1,500		409,538
							1,028,321
	(13,156)						(2,523,708)
							683,143
							(38,435)
	<u>(117,590)</u>						<u>(5,075,677)</u>
	(130,746)		(182,305)		(40,212)		(9,801,700)
<u>17,733</u>	<u>336</u>			<u>128,315</u>	<u>765</u>		<u>1,285,688</u>
<u>17,733</u>	<u>336</u>			<u>128,315</u>	<u>765</u>		<u>1,285,688</u>
17,733	(130,512)			16,101,866	4,049,499		18,876,673
<u>520,045</u>	<u>130,512</u>			<u>2,955,164</u>	<u>500</u>		<u>40,058,757</u>
<u>\$ 537,778</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 19,057,030</u>	<u>\$ 4,049,999</u>	<u>\$ -</u>	<u>\$ 58,935,430</u>

MERCED IRRIGATION DISTRICT

SCHEDULE OF CASH FLOWS BY FUND (Continued)

December 31, 2008

	Electric Services	Water Utility	Hydroelectric	Parks	Drainage Improvement District #1
RECONCILIATION OF NET INCOME (LOSS) FROM OPERATIONS TO NET CASH PROVIDED (USED) FOR OPERATING ACTIVITIES:					
Net income (loss) from operations	\$ 3,973,755	\$ (9,462,938)	\$ 1,582,590	\$ (631,720)	\$ (75,685)
Adjustments to reconcile net income (loss) from operations to net cash provided (used) for operating activities:					
Depreciation and amortization	2,688,737	1,341,641	715,724	335,542	24,288
Transfers to/from other funds	(1,038,177)	1,147,957	(150,407)	(194,147)	(43,583)
Changes in operating assets and liabilities:					
Accounts receivable	1,039,835	144,840	427,567	(8,286)	(1,016)
Due from other governmental agencies	(222,227)	(57,549)			
Inventory	(326,404)	34,379			
Prepaid expenses and other current assets	9,761	185,772	(5,169)	(4,402)	1,726
Accounts payable	(347,421)	(278,692)	(132,023)	14,779	
Accrued permission fees	65,522				
Accrued power purchase expense	(49,096)				
Other accrued expenses	15,392	(332,270)	22,016	25,403	(706)
Deferred revenue		324,157	542,058		
Deferred power cost reduction	(400,000)				
Due to/from other funds	4,948,285	(2,438,417)	(1,094,911)	425,957	17,157
Deposits	1,035,391	(312,932)		(1,199)	
Deferred public purpose program revenues	331,040				
Accrued postemployment benefits	229,845	(650,973)	137,930	179,939	3,352
Accrued compensated absences	8,225	63,073	22,390	14,421	(1,020)
	<u>\$ 11,962,463</u>	<u>\$ (10,291,952)</u>	<u>\$ 2,067,765</u>	<u>\$ 156,287</u>	<u>\$ (75,487)</u>
NONCASH INVESTING, CAPITAL AND FINANCING ACTIVITIES:					
Receipt of contributed electric system assets from developers	\$ 306,087				
Change in derivative financial instruments	\$ (11,599,701)				

San Joaquin River Agreement Fund	Merced Irrigation District Public Facilities Financing Corporation	Water Transfers	Water Utility Facility Improvement Fund	Federal Energy Regulatory Commission Fund	General Operations	Eliminating Entries	Totals
\$ 3,817,913	\$ 139,316			\$ (56,469)	\$ 248,841	\$ 23,000	\$ (441,397)
462,507	7,388 27,956	\$ 203,642	\$ 305,049	29,825	42,521 (279,555)		5,185,666 441,242
87,922		3,750,000			(6,021)	480	1,597,399 3,558,146 (292,025)
(55,988) 20,250			(185,893)		(197,011) (1,247)	(480)	(65,311) (910,727) 65,522 (49,096)
9,344	(1)	(1,400,000)			49,618		(211,204) (533,785) (400,000)
(4,426,354)	525,486	(2,553,642)	63,149		4,092,048 6,120		(441,242) 727,380 331,040
72,452 5,751					100,221 4,455		72,766 117,295
<u>\$ (6,203)</u>	<u>\$ 700,145</u>	<u>\$ -</u>	<u>\$ 182,305</u>	<u>\$ (26,644)</u>	<u>\$ 4,059,990</u>	<u>\$ 23,000</u>	<u>\$ 8,751,669</u>
							\$ 306,087 \$(11,599,701)

MERCED IRRIGATION DISTRICT

2008 DEBT SERVICE COVERAGE RELATED TO OUTSTANDING COP'S AND BONDS

ELECTRIC SERVICES

Net Income	\$ (1,006,121)
Add Back:	
Depreciation and amortization expense	2,688,737
Bond interest expense	4,760,008
Operating transfer out	1,119,000
Less:	
Capital contribution revenue	(578,848)
Inter-fund interest expense	<u>(99,841)</u>
Reconciled net revenue	<u>\$ 6,882,935</u>
2008 COP debt service related to outstanding COP's and Bonds	\$ 5,445,569
Debt service coverage	126%

MERCED IRRIGATION DISTRICT

2008 DEBT SERVICE COVERAGE RELATED TO OUTSTANDING COP'S AND BONDS

WATER OPERATIONS

Net Income	\$ 565,564
Add Back:	
Depreciation and amortization expense	1,349,029
Bond interest expense	239,090
Less:	
Capital contribution revenue	(675,307)
Interfund interest expense	(190,068)
Operating transfer in	<u>(1,119,000)</u>
Reconciled net revenue	<u>\$ 169,308</u>
2008 COP debt service related to outstanding COP's	\$ 117,590
Debt service coverage	144%