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*January 18, 2004*

Honorable Mayor, Councilmembers and Citizens of Manhattan Beach  
Manhattan Beach City Hall  
Manhattan Beach, California 90266

The Comprehensive Annual Financial Report (CAFR) of the City of Manhattan Beach for the Fiscal Year Ended **June 30, 2004 (FY2004)** is hereby submitted. This report has been prepared in accordance with generally accepted accounting principles as set forth in the pronouncements of the Governmental Accounting Standards Board (GASB). This report is also in compliance with the relevant requirements of Governmental Accounting, Auditing and Financial Reporting published by the Government Finance Officers Association of the United States and Canada. Responsibility for the accuracy, completeness and fairness of the data presented, including all disclosures, rests with management. We believe the information presented is accurate in all material aspects, and that it is reported in a manner designed to fairly present the financial position and results of operations of the various funds, account groups, and component unit of the City of Manhattan Beach. All disclosures necessary to enable the reader to gain an understanding of the City's financial activities have been included.

***In terms of presentation and method, the 2004 report marks the second year of GASB statement 34 (GASB 34) implementation.*** Last year this report was completely reformatted to comply with the new reporting model developed by the GASB 34 and could not have been completed without City Council's full support in providing the resources and guidance needed to ensure financial reporting compliance. Transitioning to this new format involved several major steps including: completion of a citywide identification and assessment of Infrastructure valuations; completion of a utility cost allocation study; development of new accounting models to facilitate the new reporting; a shift in audit planning; redesign of the published CAFR; introduction of newly developed asset valuation and depreciation policies; and identification of new computerized fixed asset management tools. In FY 2004, these practices were continued in compiling this year-end report.

GASB statement 34 is intended to improve financial reporting by adding significant information not previously provided in local government financial statements. Some of the most significant changes in reporting as required by this new standard are as follows:

- A major addition is the inclusion of the government wide financial statements which were designed to show the reader the net assets and equity of the City as a whole and report on the total cost of providing city services. To do so this new accounting model introduces a Statement of Net Assets and a Statement of Activities which are newly presented in the forefront of the CAFR document.
- These particular statements are prepared using the accrual basis of accounting versus the modified accrual method applied in the traditional fund financial statements. In the past the full accrual method of accounting, which is typical of private sector reporting, was only utilized for the City's enterprise funds or business activity operations. This accrual basis of accounting recognized revenue as earned as opposed to actual receipt, and expenses are recorded when the transaction occurs rather than when payment is made. In so far as the accrual method is applied to the government wide statements only, a reconciliation between city wide and fund statements is provided as a key to understanding the differences in reporting methods and results.
- The new model includes an emphasis on the City's major funds as shown in the Government Fund Statements. These new statements along with the citywide statements are further analyzed in a new required narrative called the Management Discussion and Analysis (MDA). This MDA provides financial highlights and interprets the financial reports by analyzing changes with an emphasis on the change in net assets and results of operations. The MDA is also intended to disclose any significant economic or legislative events or decisions that affect the financial condition of the City.

In accordance with the above-mentioned guidelines, the accompanying report consists of three sections. The ***Introductory Section*** contains this transmittal letter, a list of the City's principal elected and appointed officials, and an organizational chart. The ***Financial Section*** consists of the Independent Auditors' Report, the Management Discussion and Analysis, the Government Wide Financial Statements, notes to the financial statements, and combining financial statements and schedules. The ***Statistical Section***, which is not audited, contains selected financial and demographic information, generally presented on a multi-year basis.

## **DESCRIPTION OF REPORTING ENTITY**

The City of Manhattan Beach was incorporated December 12, 1912, as a general law city in the State of California. The City operates under a Council-Manager form of government and provides the following services: police, fire, highway and streets, cultural and recreation, planning and zoning, utilities, and general administrative services.

The financial statements present the financial activity of the City of Manhattan Beach (the primary government) and its component unit. The component unit discussed below is included in the City's reporting entity because of the significance of its operational or financial relationships with the City, although it is a legally separate organization. However, the City of Manhattan Beach elected officials have continuing full or partial accountability for fiscal matters of this entity. The financial reporting entity consists of: (1) the City, (2) organizations for which the City is financially accountable, and (3) organizations for which the nature and significance of their relationship with the City are such that exclusion would cause the City's financial statements to be misleading or incomplete.

An organization is fiscally dependent on the primary government if it is unable to adopt its own budget, levy taxes or set rates or charges, or issue bonded debt without approval by the primary government. In a blended presentation, a component unit's balances and transactions are reported in a manner similar to the balances and transactions of the City. Component units are presented on a blended basis when the component unit's governing body is substantially the same as the City's or the component unit provides services almost entirely to the City.

**Blended Component Units:** The financial statements of the City of Manhattan Beach include the financial activities of the Manhattan Beach Capital Improvements Corporation. The Capital Improvements Corporation was formed on August 6, 1996 and first used to issue debt to finance capital improvements to the City's water and wastewater systems. In FY2002 this corporation issued \$9,535,000 in debt to refinance existing ground lease commitments for the newly opened Marine Avenue Sports Fields resulting in long term savings of both interest and principal. In January 2003, this entity issued \$13.35 million in fixed rate Certificates of Participation for the construction of a new two level downtown subterranean parking structure and outdoor plaza. In the fiscal year subsequent to the term of this report, fixed rate Certificates of Participation, discussed further below, were issued to fully fund the construction of the City's new Police and Fire facility.

## **SERVICE EFFORTS AND MAJOR INITIATIVES**

### **Service Efforts**

In FY 2004, the City of Manhattan Beach maintained a high level of service to its residents and citizens. The City adhered once again to its financial policies and adopted financial plan as evidenced by the budget-to-actual reporting presented within this document. \$53.1 million was originally budgeted to support the City's many services and programs. \$21.2 million in capital projects was budgeted for the year. Budgetary limits were adhered to on a citywide basis with the General Fund reporting a healthy surplus once again. All funds performed as expected in line with the City's financial policy guidelines and planned reserves have been established.

Some of the key capital improvements completed and/or initiated in 2004 include the following:

- \$6.8 million for substantial completion a new two level subterranean public parking structure at Metlox.
- \$5.6 million of construction costs for the new police/fire facility beyond design and engineering cost incurred in FY 2003.
- \$1.6 million of citywide street improvements related continuing the street resurfacing program, aviation resurfacing, 13<sup>th</sup> Street extension, and completing Strand Walkway design.
- \$229 thousand for improvements to Polliwog Park. This expenditure marks the completion of the second phase of this exciting park improvement.
- \$1.4 million for a variety of Water, Sewer and Storm Water utility facility and line improvements.

## **Major Initiatives**

In FY 2004, the City of Manhattan Beach made significant progress on many of the key work plan items identified in the operating budget. A recap of these accomplishments follows:

***Public Safety Facility Project:*** In the current year the City outlined a specific financing plan for the future construction of a new public safety facility to replace existing Police and Fire buildings that are outdated and limited in space. In fact, the City issued \$12.9 million in fixed rate Certificates of Participation for this project. This financing action fully funds the construction of the City's new Police and Fire facility when combined with accumulated reserves dedicated over the past several years. Project design and valuation was completed and is estimated to cost \$41 million including costs incurred to date. In the November 2001 election, the City sought voter approval of a \$15 million General Obligation Bond to facilitate the financing of this facility. The required two-thirds approval was not attained and the City proceeded to develop an internal financing plan. Alternative financing options in procuring the remaining balance of required funds were presented to City Council in FY2002. The City designated specific reserves of \$25 million in the Capital Projects Fund for this improvement in line with projections and ultimately made a decision to limit debt issuance to \$12 million. The resulting debt service will be financed through dedicated revenues earmarked within the Capital Improvement Fund. From inception through June 30, 2004, \$8 million in costs have been incurred on this project which remains within budget and is targeted for completion December 2005.

***Metlox Improvements and Development:*** The City held a grand opening for the Metlox parking structure in January 2004. This structure holds 460 spaces which is a welcome addition to the City's downtown district. The public parking portion of the project was completed within budget and on schedule at a cost of \$14.6 million. Since the purchase of the Metlox site in 1997/1998 the City engaged a financial advisor, selected a development partner, completed conceptual design with community input, finalized an environmental impact report, and began construction in the current year. The private retail portion of this development will include a mix of hotel, retail, restaurant and office space elements, and the developer has entered into a long term ground lease with the City. This multi-million dollar project is projected to be a positive economic benefit adding to the City's ground lease, property, hotel, and retail tax revenue base. In concert with this private phase, the City will construct a 40,000 square foot town square along with the retail improvements. The City retains ownership of the underlying land, parking facilities and public open space. In May 2002 financing options were presented to City Council for the public parking and space component of this development. This resulted in a decision to debt finance \$11.6 million of the public project cost and increase dedicated parking meter revenues to assist funding the resulting future debt service. This plan was adopted and resulting certificates of participation were issued in January 2003. All debt financing, and capital transactions have been recorded in the parking enterprise fund and are backed by the strength of the City's overall credit. Construction on the private development began in the current year and the retail operations are schedule to open in the summer of 2005. City funded plaza improvements will be constructed contemporaneously.

***Strand Improvement Project:*** In FY 2004-2005 the City budget appropriated an additional \$2.5 million towards the \$4.5 million cost for this exciting and necessary project. This capital project will be cash funded in entirety. In the current year costs of approximately \$300,000 were incurred in furthering a City Council approved design for the entire length of the Strand. The project involves the replacement of the cement walkways, upgrades of all lighting and electrical elements, the renovation of strand drainage systems, the introduction of viewing alcoves, updates to trash receptacles, and replacement of exiting strand benches. This project, involved years of planning, community discussion and outreach and construction is scheduled to commence in FY 2005.

***Utility Under-grounding:*** In the current year the City successfully facilitated the creation of three beach front utility under-grounding utility districts valued at approximately \$5 million. Assessment District bonds were issued in August 2004 culminating several years of coordination by our City's Public Works department. Debt service for these bonds will be paid entirely through participating homeowner property tax assessments and the resulting bond proceeds reimbursed the City for all originating costs incurred in the project lifecycle. In the end result the assessment district voting process was received extremely well with approval percentages in the 70% range for all districts. All project dollars have been deposited with assigned trustee depositories and construction should begin in FY 2005.

***Financial Credit Rating:*** The City obtained a financial credit rating in anticipation of issuing bonds for the construction of public improvements at the Metlox site as well as a new Police/Fire facility. The results of the credit rating came in at that time at the highest possible rating, "AAA," from both S&P and Fitch. With this good news, the City proceeded with its plans to issue bonds for both facilities starting with Metlox Certificates of Participation which were sold in January 2003 at a size of \$13.3 million (including all issuance costs, reserve and capitalized interest requirements). The bond issuance for Police/Fire, took place in November 2004 at a value of \$12.9 million. The City realized a healthy General Fund surplus in 2003, over \$4 million, and used these resources to increase cash funding in deriving the final debt sizing. The City's credit rating was updated with this latest bond issuance and again received a rating of "AAA" from S&P and Fitch. Furthermore, we are very pleased that a similar rating was received from Moody's as part of this bond sale.

***Ongoing Water/Wastewater System Upgrade:*** In September 1996, the City issued \$4,615,000 in Certificates of Participation through the Manhattan Beach Capital Improvements Corporation to finance the upgrade of the City's water and wastewater systems. Through this aggressive five-year capital project, important Water and Sewer infrastructure improvements have been made throughout the City. Net revenues of the Water and Wastewater Funds secure the 30-year issue. As of June 30, 2004 all construction fund balances for Water and Wastewater have been expended. The related remaining debt service is recorded in each respective enterprise fund for a total outstanding principal amount of \$4,105,000.

## FINANCIAL CONTROLS AND PROCEDURES

**Financial Policies:** Throughout the years, the City of Manhattan Beach has followed a fiscally conservative philosophy of building and maintaining healthy financial reserves. This practice has allowed the City to continue providing quality services to its residents in a time when many local agencies were being forced to cut back due to fiscal constraints. In 1997-1998, the City Council approved the City's first set of financial policies, designed to promote sound financial management and ensure that the City's fiscal integrity remains intact as staff and Councilmembers change. This Comprehensive Annual Financial Report reflects the implementation of these financial guidelines and presents all fund reserves and designations in an effort to define fund balance commitments and obligations as of the financial report date.

**Internal Control Structure:** Management of the City is responsible for establishing and maintaining fiscal internal controls designed to safeguard the assets of the government from loss, theft or misuse, and to ensure that accounting data is accurately compiled to allow for the preparation of financial statements in conformity with generally accepted accounting principles. The internal control structure is designed to provide reasonable, but not absolute assurance that these objectives are met. The concept of reasonable assurance recognizes that: (1) the cost of controls should not exceed the benefits likely to be derived; and (2) the valuation of costs and benefits require estimates and judgments by management.

**Budgetary Controls and Changes:** The City of Manhattan Beach maintains budget controls. The objective of these controls is to ensure compliance with legal provisions embodied in the annual appropriated budget approved by the City Council. Budget control is primarily maintained at the fund level in the governmental fund types. The City maintains a centralized purchasing function as one method of accomplishing budgetary controls. All purchase orders are reviewed by Purchasing and Finance management to assure adequate budget funding before binding commitments are finalized. Additionally, all machinery and equipment purchases are processed through centralized warehouse receiving to further strengthen internal controls. The City's financial software includes a full encumbrance purchasing accounting system with real time approval and budget checking capabilities. Full encumbrance accounting allows for the speedy identification of fund obligations at the time of requisition, providing tremendous budgetary control. The Comprehensive Annual Financial Report isolates all encumbrance obligations existing at June 30, 2003, related to governmental funds, and presents them as fund balance reserves on the respective balance sheets.

**Cash Management:** It is the City's policy to invest all temporarily idle short-term funds and longer-term reserves in a manner that will maximize return without sacrificing security and jeopardizing liquidity requirements. Idle funds are invested in accordance with the Government Code and a formal investment policy approved by the City Council. The policy, which is reviewed and updated annually, allows investments in a variety of specific instruments such as Certificates of Deposit, Bankers Acceptances, U.S. Government and Agency securities, Repurchase Agreements, Commercial Paper, and the State's Local Agency Investment Fund.

***Risk Management.*** The City is a member of the Independent Cities Risk Management Authority (ICRMA), a joint powers authority consisting of twenty-eight medium-sized California municipalities, for the purpose of pooling the City of Manhattan Beach's risk for general liability losses with those of other member cities. The City's self-insured retention is \$500,000 per occurrence for Liability and \$750,000 for Worker's Compensation. Under the ICRMA, insurance coverage in excess of the self-insured amount is provided up to a limit of \$50,000,000. Premiums for excess insurance coverage are set annually based upon actual claims experience as well as other factors.

## **EXECUTIVE FINANCIAL OVERVIEW**

This top level overview is presented as a supplement to the more detailed and comprehensive analysis presented in the following Management Discussion and Analysis (MDA). As such it serves to highlight key financial performance indicators for our major funds. We encourage all readers to review the MDA for a further analysis of the City's financial condition.

### **General Fund**

The General fund is the primary operating fund of the City of Manhattan Beach and it suffices to say that the 2003 year reflects very good financial results. In fact, this fund outpaced expectations coming in with an operating surplus of \$3.6 million. We attribute this performance to our continued adherence to prudent financial planning and policy setting, conservative budgeting, and faithful monitoring and stewardship by all city staff. At the end of the current fiscal year the total General Fund balance reached \$20.6 million after \$975,000 of transfers out to the Capital Improvement Fund. Under the GASB 34 model this fund reports an unreserved fund balance of \$20.24 million before policy and City Council designations. With financial policy, liability and uncertainty reserve limits considered, this fund reports an unreserved and undesignated fund balance of \$7.6 million which remains available for use at City Council's discretion at year end. As indicated above a portion of these funds were utilized to reduce the bond sizing for our new Police and Fire facility.

During the current fiscal year, General Fund revenues exceeded expenses by approximately \$3.6 million. After transfer activity, the fund balance increased by \$2.7 million. The transfer activity included:

- \$975,000 into the Capital Improvement Fund to further build reserves for the construction of the Strand Walkway and public safety facility.
- \$75,000 from County parking lot operations per contract.

The City's Policy Reserves and designations discussed above and presented in the General Fund at year end include the following:

- \$6.9 million in an ongoing operational financial policy reserve designed to cover 20% of budgetary funding requirements.
- \$2 million in economic uncertainty reserves to protect against sudden changes in the economic or legislative climate.
- \$2 million in pension stabilization reserves which was established in the current year given the known high dollar increases in employee retirement costs on the near horizon.
- \$1.6 million in reserves to cover vested employee leave benefits.

Although the rate growth has slowed from early 2000 levels, the City's General Fund revenue base continues to do well. This can be noted by the following trends:

<b>Revenue</b>	<b>2003 Actual</b>	<b>2004 Actual</b>	<b>Variance</b>
Property Tax	10.0 M	11.1 M	1.1 M
Sales Tax	7.2 M	7.3 M	.1 M
Hotel Tax	1.7 M	1.9 M	.2 M
Business License Tax	2.0 M	2.1 M	.1 M
License and Permits	1.5 M	1.6 M	.1 M
Fines	1.9 M	2.2 M	.3 M
Interest and Rent	3.1 M	2.3 M	(.8 M)
Vehicle In-Lieu	2.3 M	1.9 M	(.4 M)
Services	5.6 M	5.9 M	.3 M

On an overall basis, General Fund revenues increased by a respectable margin, 3%, and came in at 107% of our annual budget estimates with property tax being the clear front runner. Sales tax remained relatively flat while Hotel Tax showed a good gain in contrast to the past two years. Charges for services were bolstered by the completion of a new utility cost allocation study in FY 2003 and maintained prior year levels. On the other side of the equation, interest income has fallen heavily as predicted given the large use of cash reserves in a falling interest rate environment. Additionally, vehicle registration fee collections are down reflecting the State's two year deferral of such revenue. These results are quite reassuring considering the challenges that faced us at the State level this past year.

General Fund expenditures came in 3% below budget resulting in the surplus noted above. On the other hand, compared to last year, expenses have risen by 7%, or \$2.2 million mostly driven by salary, pension, and insurance costs. Clearly, rising costs are a significant challenge that reinforces the need to maintain prudent, proactive and conservative planning while maintaining tight budgetary controls. Maintaining such controls is critical to assure healthy surplus margins in future years. Although the current year performance is strong, the rate of expense increase outweighs the rate of revenue growth which is a trend worthy of our attention.



## **Other Funds**

### **Capital Improvement Funds**

This year saw the introduction of two new funds to this category. In FY 2004 the Police and Fire Construction Fund (PFC) was added as well as the Utility Under-Grounding Fund (UAD). These funds were added to manage the construction of the two related major capital projects. The previously established Capital Improvement Fund (CIP) was originally created to drive capital planning for general government operations and continues in this same capacity.

In FY 2004, the CIP Fund performed as expected and is well positioned to fund our most important capital infrastructure projects. Dedicated revenues in this fund amounted to \$1.2 million and capital expenditures equaled \$779,000. This fund transferred \$17.5 million to the newly create PFC Fund to seed the construction of this new safety facility.

At June 30, 2004 the total balance in the CIP Fund was \$9.2 million. Of this balance, \$8.2 million has been specifically earmarked for planned infrastructure projects leaving an unreserved and undesignated balance of \$22,154. Key designations at year end include:

- \$5.5 million for the construction of a new Police/ Fire facility
- \$2.6 million for improvements to the Strand walkway
- \$100 thousand for improvements to Artesia Boulevard

At the end of the current fiscal year the total fund balance in the PFC Fund was \$12 million which is completely dedicated for the construction of the new facility. This balance reflects the transfer in of \$17.5 million from the CIP fund reduced by \$5.7 million in current year construction costs. \$8 million has been expended on this project from inception through June 30, 2004.

At the end of the current fiscal year the total fund balance in the UAD Fund was \$1.5 million reflecting home owner assessment pre-payments held in trust for the future construction of these facilities. Bonds were issued in the subsequent period making up the balance of the \$5.1 million project cost. The total amount of cash holdings in this fund is restricted from use.

### **Special Revenue and Enterprise Funds**

All other Governmental and Business Type funds performed within budget and have met financial projections and expectations. The City continues to see significant cost increases in insurance claims although we were pleased that a transfer into that Fund from the General fund was not necessary as had been the case in past years. Our city, along with the State, has identified rising insurance costs as one of the financial challenges to be reckoned with in future years. Ultimately the solution to this issue can only come through legislative change at both the State and/or Federal level.

## **Trust and Agency Funds**

In several cases, the City acts as a custodian of funds held for the benefit of others which mostly relates to the administration of employee pension and 401(a) compensation plan. It is significant to note that this financial report does not include the value of trust holdings in the employees' 457 deferred compensation plan valued at \$11,342,229 at June 30, 2004. This recognizes enacted legislation establishing the City as a plan trustee and protecting these employee-owned assets from external creditors.

***Deferred Compensation Plan for Full-Time Employees:*** Management employees receive a City-paid contribution ranging from 2.5% to 4.5% of their salary into a 401(a) plan. The liability balances for these deferred compensation plans are recorded in the Special Deposits Fund along with restricted deposits held for safety operations and our Employee Section 125 Flexible Spending Plan.

***City Pension Plans:*** This fund is used to account for the supplemental retirement and single highest year programs, dormant plans which were previously offered by the City. The Pension Trust Fund is used to account for the distribution of these plans for former employees still receiving benefits.

## **THIRD PARTY ADMINISTERED PENSION PLANS**

***Defined Benefit Pension Plan:*** The City contracts with the California Public Employees Retirement System (CalPERS) for certain retirement, disability, death and survivor benefits for full-time employees. The annual actuarial valuation by CalPERS changes from year to year, and the City's contribution rates are modified accordingly.

***Retirement Plan for Part-Time Employees:*** From 1990 to 1997, the City of Manhattan Beach provided its own retirement plan for Part-time, Seasonal and Temporary employees not eligible for participation in the California Public Employees Retirement System. This plan was eliminated in June 1997, as the City opted to provide the Public Agency Retirement System (PARS) program instead.

## **Significance of GASB 34 on Capital Asset Presentation**

Although many impacts of GASB 34 on these financial statements were discussed above, one would be remiss not to point out the tremendous reporting impact that this pronouncement has on the City's valuation and treatment of Capital Assets. In this regard we encourage the reader to review the notes and the Management Discussion and Analysis for this important information.

GASB 34 now requires that local governments quantitatively value and capitalize all owned asset including capital infrastructure. This infrastructure includes such highly visible and material items as streets, walkways, lights, signs, buildings, etc. Consequently this pronouncement requires that these assets be depreciated in full compliance with accrual accounting methodology. This presentation of capital assets was always required of our enterprise funds in the past and now it is required when reporting the government wide financial statements for all such funds.

In the end result a valuation of all City Infrastructure was completed and these results have been included in the financial statements. At the end of the day government wide capital assets have been valued on a gross basis at \$150 million and \$110 million on a net basis after depreciation. These values are presented at original estimated cost and, as such, their replacement cost would be considerably higher. Increases over last year exceeded \$16 million before depreciation most of which results from the \$5.6 million capitalization of Police and Fire facility improvements and \$6.8 million in capitalized costs to complete the newly opened downtown underground parking structure. The remaining asset increase result improvements to city roadways, parks and utilities.

## **OTHER INFORMATION**

***Independent Audit:*** The accounting firm of Vavrinek, Trine, Day and Co., LLP, was selected by the City to perform the annual audit. The auditors' report on the general purpose financial statements and combining and individual fund statements and schedules is included in the financial section of the City's Comprehensive Annual Financial Report. The City was not required to conduct a single-audit, an audit of Federal Grant Funding, and, as such, no separate single audit opinion and report is included.

***Acknowledgments:*** Preparation of this report could not have been accomplished without the efficient and dedicated services of the Finance Department staff. We would like to express our appreciation to all members of the department, particularly Russell Morreale, Henry Mitzner, Sherry Morelan, Steve Charelian, Luisa Camba, Sande Johnson and Eugene Wee who assisted and contributed to its preparation. A special thanks is extended to Lance, Soll & Lunghard, LLP our new independent auditors, for their professionalism and diligence in preparing this year end financial report and again to Russell Morreale & Henry Mitzner for coordinating this audit transition in this second year of GASB 34 implementation. We would also like to thank the Mayor, members of the City Council, and the City Treasurer for their leadership and support, without which the preparation of this report would not have been possible.

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Geoff Dolan, City Manager

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Bruce Moe, Finance Director



Brandon W. Burrows  
Donald L. Parker  
Michael K. Chu  
David E. Hale  
*A Professional Corporation*  
Donald G. Slater  
Richard K. Kikuchi

*Certified Public Accountants*

*Retired*  
Robert C. Lance  
1914-1994  
Richard C. Soll  
Fred J. Lunghard, Jr.  
1928-1999

## INDEPENDENT AUDITORS' REPORT

To the Honorable Mayor and Members of the City Council  
Manhattan Beach, City Hall  
City of Manhattan Beach, California

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the City of Manhattan Beach, California, as of and for the year ended June 30, 2004, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City of Manhattan Beach's management. Our responsibility is to express opinions on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the City of Manhattan Beach as of June 30, 2004, and the respective changes in financial position and cash flows, where applicable, and the respective budgetary comparison for the General Fund, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 12, 2004 on our consideration of the City of Manhattan Beach's internal control over financial reporting and our tests of its compliance with certain laws, regulations, contracts and grants.

The management's discussion and analysis on pages 3 through 18 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 required supplementary information. However, we did not audit the information and express no opinion on it.





To the Honorable Mayor and Members of the City Council  
Manhattan Beach, City Hall  
City of Manhattan Beach, California

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplemental schedules listed in the accompanying table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements of the City of Manhattan Beach. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly presented in all material respects in relation to the basic financial statements taken as a whole. The scope of our audit did not include the supplemental statistical schedules listed in the table of contents, and we do not express an opinion on them.

*Lance, Soll & Lunghard, LLP*

November 12, 2004