NEW ISSUE – BOOK-ENTRY ONLY **INSURED RATINGS:** *Moody's: "Aaa"*
S&P's: "AAA"
(See "MISCELLANEOUS – Ratings" herein.)

In the opinion of Orrick, Herrington & Sutcliffe LLP, Bond Counsel, based upon an analysis of existing laws, regulations, rulings and court decisions, and assuming, among other matters, the accuracy of certain representations and compliance with certain covenants, interest on the Bonds is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986 and is exempt from State of California personal income taxes. In the further opinion of Bond Counsel, interest on the Bonds is not a specific preference item for purposes of the federal individual or corporate alternative minimum taxes, although Bond Counsel observes that such interest is included in adjusted current earnings when calculating federal corporate alternative minimum taxable income. Bond Counsel expresses no opinion regarding any other tax consequences related to the ownership or disposition of, or the accrual or receipt of interest on, the Bonds. See "TAX MATTERS" herein.

$889,062.35
ARENA UNION ELEMENTARY SCHOOL DISTRICT
(Mendocino County, California)
General Obligation Bonds, Election of 2003, Series 2005
(Bank Qualified)

Dated: Date of Delivery **Due:** August 1, as shown below

This cover page is not a summary of this issue; it is only a reference to the information contained in this Official Statement. Investors must read the entire Official Statement to obtain information essential to the making of an informed investment decision.

The Bonds are issued by the Arena Union Elementary School District (the "District") (i) to finance specific construction and modernization projects approved by the voters; and (ii) to pay costs of issuance of the Bonds. The Board of Supervisors of the County is empowered and is obligated to levy ad valorem taxes upon all property subject to taxation by the District, without limitation as to rate or amount (except as to certain personal property which is taxable at limited rates), for the payment of principal of and interest on the Bonds, all as more fully described herein. See "SECURITY AND SOURCE OF PAYMENT FOR THE BONDS."

The Bonds will be issued as capital appreciation Bonds (the "Bonds"). The Bonds will not bear current interest, but will increase in value by the accumulation of earned interest from their Denominational Amounts on the date of delivery to their respective Maturity Values. Interest on the Bonds will be compounded on each February 1 and August 1, commencing August 1, 2005. Payments of principal of and interest on the Bonds will be made by the Paying Agent, initially U.S. Bank National Association, to The Depository Trust Company, New York, New York ("DTC"), for subsequent disbursement to DTC Participants, who will remit such payments to the beneficial owners of the Bonds. See "THE BONDS – Payment of Principal and Interest."

The Bonds will be issued in book-entry form only, and will be initially issued and registered in the name of a nominee of DTC. Purchasers will not receive physical certificates representing their interests in the Bonds. See "THE BONDS – Form and Registration."

The scheduled payment of principal of and interest on the Bonds when due will be guaranteed under an insurance policy to be issued concurrently with the delivery of the Bonds by FINANCIAL SECURITY ASSURANCE INC. ("FSA"). See "BOND INSURANCE."

FSA®

The Bonds are not subject to redemption prior to their respective maturity dates. See "THE BONDS — Redemption."

MATURITY SCHEDULE

Maturity (August 1)	Denominational Amount	Yield to Maturity	Maturity Value	CUSIP[(1)] Number
2028	$86,342.40	5.000%	$320,000	04003PAV5
2030	63,838.50	5.080	265,000	04003PAW3
2031	62,595.50	5.120	275,000	04003PAX1
2032	62,373.20	5.140	290,000	04003PAY9
2033	60,966.00	5.160	300,000	04003PAZ6
2034	59,526.20	5.170	310,000	04003PBA0
2035	58,968.00	5.180	325,000	04003PBB8
2036	57,432.40	5.190	335,000	04003PBC6
2037	56,696.50	5.210	350,000	04003PBD4
2038	55,866.90	5.230	365,000	04003PBE2
2039	54,959.40	5.250	380,000	04003PBF9
2040	53,980.70	5.260	395,000	04003PBG7
2041	52,939.20	5.270	410,000	04003PBH5
2042	51,854.25	5.280	425,000	04003PBJ1
2043	50,723.20	5.290	440,000	04003PBK8

The Bonds will be offered when, as and if issued by the District and received by the Underwriter, subject to the approval of legality by Orrick, Herrington & Sutcliffe LLP, Bond Counsel. It is anticipated that the Bonds, in definitive form, will be available for delivery through the facilities of DTC on or about June 22, 2005.

AG EDWARDS℠

The date of this Official Statement is June 7, 2005.

This Official Statement does not constitute an offering of any security other than the original offering of the Bonds by the District. No dealer, broker, salesperson or other person has been authorized by the District to give any information or to make any representations other than as contained in this Official Statement, and if given or made, such other information or representation not so authorized should not be relied upon as having been given or authorized by the District.

The issuance and sale of the Bonds have not been registered under the Securities Act of 1933 in reliance upon an exemption under Section 3(a)2 thereof. This Official Statement does not constitute an offer to sell or a solicitation of an offer to buy in any state in which such offer or solicitation is not authorized or in which the person making such offer or solicitation is not qualified to do so, or to any person to whom it is unlawful to make such offer or solicitation.

The information set forth herein other than that furnished by the District, although obtained from sources which are believed to be reliable, is not guaranteed as to accuracy or completeness, and is not to be construed as a representation by the District. The information and expressions of opinion herein are subject to change without notice and neither delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the District since the date hereof. This Official Statement is submitted in connection with the sale of the Bonds referred to herein and may not be reproduced or used, in whole or in part, for any other purpose.

Other than with respect to information concerning Financial Security Assurance Inc. ("Financial Security") contained under the caption "Bond Insurance" and Appendix G specimen "Municipal Bond Insurance Policy" herein, none of the information in this Official Statement has been supplied or verified by Financial Security and Financial Security makes no representation or warranty, express or implied, as to (i) the accuracy or completeness of such information; (ii) the validity of the Bonds; or (iii) the tax exempt status of the interest on the Bonds.

IN CONNECTION WITH THIS OFFERING, THE UNDERWRITER MAY OVERALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICES OF THE BONDS AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME. THE UNDERWRITER MAY OFFER AND SELL THE BONDS TO CERTAIN SECURITIES DEALERS AND DEALER BANKS AND BANKS ACTING AS AGENT AT PRICES LOWER THAN THE PUBLIC OFFERING PRICES STATED ON THE COVER PAGE HEREOF AND SAID PUBLIC OFFERING PRICES MAY BE CHANGED FROM TIME TO TIME BY THE UNDERWRITER.

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$889,062.35
ARENA UNION ELEMENTARY SCHOOL DISTRICT
(Mendocino County, California)
General Obligation Bonds, Election of 2003, Series 2005
(Bank Qualified)

INTRODUCTION

This Official Statement, which includes the cover page and appendices hereto, is provided to furnish information in connection with the sale of the Arena Union Elementary School District General Obligation Bonds, Election of 2003, Series 2005 (the "Bonds").

This Official Statement speaks only as of its date, and the information contained herein is subject to change. Except as required by the Continuing Disclosure Certificate to be executed by the Arena Union Elementary School District (the "District"), the District has no obligation to update the information in this Official Statement. See "OTHER LEGAL MATTERS – Continuing Disclosure."

The purpose of this Official Statement is to supply information to prospective buyers of the Bonds. Quotations from and summaries and explanations of the Bonds, the resolution of the Board of Trustees of the District adopted on May 19, 2005, providing for the issuance of the Bonds, and the constitutional provisions, statutes and other documents described herein, do not purport to be complete, and reference is hereby made to said documents, constitutional provisions and statutes for the complete provisions thereof. Any statements in this Official Statement involving matters of opinion, whether or not expressly so stated, are intended as such and not as representations of fact. This Official Statement is not to be construed as a contract or agreement between the District and the purchasers or owners of any of the Bonds.

Copies of documents referred to herein and information concerning the Bonds are available from the District from the Superintendent, 45 Lake Street, Point Arena, CA 95468. The District may impose a charge for copying, handling and mailing such requested documents.

The District

The District, established in 1885, provides elementary educational services to residents of an area encompassing approximately 250 square miles located on the Mendocino County Coast and adjoining the Sonoma County line. The economy of the region consists primarily of wine and sparkling wine production, tourism and recreation, agriculture and food production, and retail and services. Recent decades have witnessed a fundamental shift to these economic activities from the area's traditional timber-related and commercial fishing industries.

The District currently operates one elementary school serving students in grades kindergarten through eight and one charter school serving students in grades kindergarten through twelve, serving approximately 316 students. As of July 1, 2004, the District employed approximately 36 employees including certificated (credentialed teaching) staff, classified (non-teaching) staff, and management personnel. The District has adopted a Fiscal Year 2004-05 general fund budget with total expenditures of approximately $5.1 million. Total assessed valuation of taxable property in the District in Fiscal Year 2004-05 is approximately $467 million.

The District is governed by an elected Board of Trustees consisting of seven members. The voting members are elected to overlapping four-year terms. The day-to-day operations are managed by a board-appointed Superintendent of Schools. Mark Iacuaniello has served as the Superintendent since 2001. Mr. Iacuaniello has served California schools as an educator for 18 years and a school administrator for 11 years.

For additional information about the District, see APPENDIX A: "INFORMATION RELATING TO THE DISTRICT'S OPERATIONS AND BUDGET."

THE BONDS

Authority for Issuance; Purpose

The Bonds are issued pursuant to the Constitution and laws of the State of California (the "State"), including the provisions of Chapter 3 of Part 1 of Division 2 of Title 5 of the Government Code of the State and other applicable provisions of law. The Bonds are authorized to be issued by a resolution adopted by the Board of Trustees of the District on May 19, 2005 (the "Resolution"). The Mendocino County Board of Supervisors has approved the sale and issuance of the Bonds by the District without further action by the County Board. The District received authorization at an election held on November 4, 2003, to issue bonds of the District in an aggregate principal amount not to exceed $3,700,000 to finance specific construction and modernization projects approved by the voters, summarized as follows: construction of a districtwide elementary school facility in Gualala and conversion of the existing Arena Elementary School into a middle school.

The measure required approval by at least 55% of the votes cast by eligible voters within the District, and received a vote of 74%. The Bonds are the second and final series of the authorized bonds to be issued.

Form and Registration

The Bonds will be issued in fully registered form only, without coupons, in denominations of $5,000 accreted value at maturity (the "maturity value") or any integral multiple thereof, except that the first numbered Bond may be issued in a denomination such that the maturity value of such Bond shall not be in an integral multiple of $5,000, and provided that no Bond shall have principal maturing on more than one principal maturity date. The Bonds will initially be registered in the name of Cede & Co., as nominee of The Depository Trust Company ("DTC"), New York, New York. DTC will act as security depository of the Bonds. Purchases of Bonds under the DTC book-entry system must be made by or through a DTC participant, and ownership interests in Bonds will be recorded as entries on the books of said participants. Except in the event that use of this book-entry system is discontinued for the Bonds, beneficial owners will not receive physical certificates representing their ownership interests. See APPENDIX F: "BOOK-ENTRY ONLY SYSTEM."

Payment of Principal and Interest

The Bonds will be dated as of the date of their delivery. The Bonds will not bear interest on a periodic basis; instead, each Bond will increase in value by the accumulation of earned interest from its initial principal (denominational) amount on the date of issuance (as stated on the cover hereof) to its Maturity Value on the date of maturity (as stated on the cover hereof). Interest commences to accrue on the date of delivery, and is compounded on each Interest Date, commencing August 1, 2005. The Maturity Value of the Bonds is payable in lawful money of the United States of America upon the surrender thereof at the principal corporate trust office of the Paying Agent at the maturity thereof.

The rate of interest at which a Bond's Maturity Value is discounted to its initial principal amount is known as the "Bond Yield," and is stated on the cover hereof. For any Bond, the value of principal plus accrued interest on any given Interest Date prior to maturity may be calculated by discounting the Maturity Value of the Bond from its maturity date to that Interest Date at a discount rate equal to the Bond Yield, assuming a year of 360 days comprising twelve 30-day months. The imputed value on any other date may be calculated on the basis of a straight-line interpolation between the values calculated for the Interest Dates immediately preceding and following the date in question.

The Underwriter has prepared the Tables of Accreted Values shown in Appendix H hereto, in order to provide the value per $5,000 of Maturity Value for each Bond on each Interest Date prior to maturity. See "TAX MATTERS" herein for Bond Counsel's discussion of the federal tax treatment of accrued interest on the Bonds.

Redemption

The Bonds *will not* be subject to optional or mandatory sinking fund redemption prior to their stated maturity dates.

Defeasance of Bonds

The District may pay and discharge any or all of the Bonds by depositing in trust with the Paying Agent or an escrow agent at or before maturity, money or non-callable direct obligations of the United States Treasury or other non-callable obligations the payment of the principal of and interest on which is guaranteed by a pledge of the full faith and credit of the United States of America, in an amount which will, together with the interest to accrue thereon and available moneys then on deposit in the Interest and Sinking Fund of the District, be fully sufficient to pay and discharge the indebtedness on such Bonds (including all principal, interest and redemption premiums) at or before their respective maturity dates, in the opinion of a Certified Public Accountant licensed to practice in the State.

If at any time the District shall pay or cause to be paid or there shall otherwise be paid to the Owners of any or all outstanding Bonds all of the principal, interest and premium, if any, represented by such Bonds when due, or as described above, or as otherwise provided by law, then such Owners shall cease to be entitled to the obligation of the County to levy and collect taxes to pay the Bonds and such obligation and all agreements and covenants of the District and of the County to such Owners under the Resolution shall thereupon be satisfied and discharged and shall terminate, except only that the District shall remain liable for payment of all principal, interest and premium, if any, represented by the Bonds, but only out of moneys on deposit in the Interest and Sinking Fund or otherwise held in trust for such payment, provided, that the unclaimed moneys provisions described below shall apply in all events.

Unclaimed Moneys

Any money held in any fund created pursuant to this Resolution, or by the Paying Agent in trust, for the payment of the principal of, redemption premium, if any, or interest on the Bonds and remaining unclaimed for two years after the principal of all of the Bonds has become due and payable (whether by maturity or upon prior redemption) shall be transferred to the Interest and Sinking Fund of the District for payment of any outstanding bonds of the District payable from said fund; or, if no such bonds of the District are at such time outstanding, said moneys shall be transferred to the general fund of the District as provided and permitted by law.

Application and Investment of Bond Proceeds

The proceeds from the sale of the Bonds will be deposited in the County treasury to the credit of the Building Fund of the District. Any premium or accrued interest received will be deposited in the Interest and Sinking Fund of the District in the County treasury. Earnings on the investment of moneys in either fund will be retained in that fund and used only for the purposes to which that fund may lawfully be applied. Moneys in the Building Fund may only be applied for the purposes for which the Bonds were approved. Moneys in the Interest and Sinking Fund may only be applied to make payments of interest, principal, and premium, if any, on bonds of the District.

All funds held by the County Treasurer under the Resolution shall be invested at the County Treasurer's discretion pursuant to law and the investment policy of the County, unless otherwise directed in writing by the District to be invested in the Local Agency Investment Fund in the Treasury of the State of California. See APPENDIX E: "MENDOCINO COUNTY INVESTMENT POLICIES AND PRACTICES; DESCRIPTION OF INVESTMENT POOL."

Estimated Sources and Uses of Funds

The proceeds of the Bonds are expected to be applied as follows:

Arena Union Elementary School District
General Obligation Bonds, Election of 2003, Series 2005
Estimated Sources and Uses of Funds

Sources of Funds	
Initial Principal Amount of Bonds	$889,062.35
Original Issue Premium	160,783.75
Total Sources	$1,049,846.10
Uses of Funds	
Deposit to Building Fund	$889,062.35
Deposit to Interest and Sinking Fund	8,203.75
Costs of Issuance[1]	152,580.00
Total Uses	$1,049,846.10

[1] Includes financial advisor fees, bond counsel fees, disclosure counsel fees, underwriter's discount, municipal bond insurance premium, rating agency fees, printing fees and other miscellaneous expenses.

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Annual Debt Service

Upon issuance of the Bonds, scheduled debt service (without regard to optional redemption) will be as follows:

Arena Union Elementary School District
General Obligation Bonds
Debt Service—Bond Year Basis
Series 2004 Bonds

Year Ending August 1	Outstanding Series 2004 Bonds Debt Service	2005 Bonds Principal	2005 Bonds Interest Paid at Maturity	Total Debt Service	Total All Debt Service
2005	$67,220.00	--	--	--	$67,220.00
2006	139,440.00	--	--	--	139,440.00
2007	144,340.00	--	--	--	144,340.00
2008	149,100.00	--	--	--	149,100.00
2009	158,680.00	--	--	--	158,680.00
2010	162,905.00	--	--	--	162,905.00
2011	171,915.00	--	--	--	171,915.00
2012	175,515.00	--	--	--	175,515.00
2013	183,827.50	--	--	--	183,827.50
2014	191,696.26	--	--	--	191,696.26
2015	199,096.26	--	--	--	199,096.26
2016	206,002.50	--	--	--	206,002.50
2017	217,390.00	--	--	--	217,390.00
2018	223,015.00	--	--	--	223,015.00
2019	233,065.00	--	--	--	233,065.00
2020	242,315.00	--	--	--	242,315.00
2021	254,615.00	--	--	--	254,615.00
2022	265,815.00	--	--	--	265,815.00
2023	272,175.00	--	--	--	272,175.00
2024	287,815.00	--	--	--	287,815.00
2025	297,090.00	--	--	--	297,090.00
2026	310,390.00	--	--	--	310,390.00
2027	321,875.00	--	--	--	321,875.00
2028	17,085.00	86,342.40	233,657.60	320,000.00	337,085.00
2029	349,237.50	--	--	--	349,237.50
2030		63,838.50	201,161.50	265,000.00	265,000.00
2031		62,595.50	212,404.50	275,000.00	275,000.00
2032		62,373.20	227,626.80	290,000.00	290,000.00
2033		60,966.00	239,034.00	300,000.00	300,000.00
2034		59,526.20	250,473.80	310,000.00	310,000.00
2035		58,968.00	266,032.00	325,000.00	325,000.00
2036		57,432.40	277,567.60	335,000.00	335,000.00
2037		56,696.50	293,303.50	350,000.00	350,000.00
2038		55,866.90	309,133.10	365,000.00	365,000.00
2039		54,959.40	325,040.60	380,000.00	380,000.00
2040		53,980.70	341,019.30	395,000.00	395,000.00
2041		52,939.20	357,060.80	410,000.00	410,000.00
2042		51,854.25	373,145.75	425,000.00	425,000.00
2043		50,723.20	389,276.80	440,000.00	440,000.00
Total	$5,241,620.02	$889,062.35	$4,295,937.65	$5,185,000.00	$10,426,620.02

SECURITY AND SOURCE OF PAYMENT FOR THE BONDS

General

In order to provide sufficient funds for repayment of principal and interest when due on the Bonds, the Board of Supervisors of the County is empowered and is obligated to levy *ad valorem* taxes upon all property subject to taxation by the District, without limitation as to rate or amount (except as to certain personal property which is taxable at limited rates). Such taxes are in addition to other taxes levied upon property within the District. When collected, the tax revenues will be deposited by the County in the District's Interest and Sinking Fund, which is required to be maintained by the County and to be used solely for the payment of bonds of the District.

The scheduled payment of principal of (or, in the case of Bonds, the accreted value) and interest on the Bonds when due will be guaranteed under an insurance policy to be issued concurrently with the delivery of the Bonds by FINANCIAL SECURITY ASSURANCE INC. ("FSA"). See "BOND INSURANCE."

Assessed Valuation of Property Within the District

All property (real, personal and intangible) is taxable unless an exemption is granted by the California Constitution or United States law. For assessment and tax collection purposes, property is classified either as "secured" or "unsecured," and is listed accordingly on separate parts of the assessment roll. The "secured roll" is that part of the assessment roll containing State-assessed property and other property (real or personal) for which there is a lien on real property sufficient, in the opinion of the County Assessor, to secure payment of the taxes. All other property is "unsecured", and is assessed on the "unsecured roll". Shown in the following table is the assessed valuation of property in the District in the last several years.

Arena Union Elementary School District
Summary of Taxable Assessed Valuation

Fiscal Year	Local Secured	Utility	Unsecured	Total
1999-00	$335,538,484	$178,800	$10,181,577	$345,898,861
2000-01	353,208,871	178,800	10,127,248	363,514,919
2001-02	374,880,253	178,800	9,337,375	384,396,428
2002-03	398,199,516	178,800	9,109,514	407,487,830
2003-04	429,143,648	268,200	9,253,201	438,665,049
2004-05	456,980,023	268,200	9,876,940	467,125,163

Source: California Municipal Statistics, Inc.

The District may issue bonds in an amount up to 1.25% of the assessed valuation of taxable property within its boundaries. The District's gross bonding capacity is estimated at $5,839,065 million, and the District's net bonding capacity is $3,029,065 (before taking into account the issuance of the Bonds). In accordance with the law which permitted the Bonds to be approved by a 55% popular vote, bonds approved by the District's voters at the November 4, 2003 election may not be issued unless the District projects that repayment of all outstanding bonds approved at the election will require a tax rate no greater than $30.00 per $100,000 of assessed value. Based on the assessed value of taxable property in the District at the time of issuance of the Bonds, the District projects that the maximum tax rate required to repay the Bonds will be $30.00 per $100,000 of assessed value.

Taxation of State-Assessed Utility Property. A portion of property tax revenue of the District is derived from utility property subject to assessment by the State Board of Equalization ("SBE"). State-assessed property, or "unitary property," is property of a utility system with components located in many taxing jurisdictions assessed collectively as part of a "going concern" rather than as individual parcels of real or personal property. Unitary and certain other state-assessed property is allocated to the counties by the SBE, taxed at special county-wide rates, and the tax revenues distributed to taxing jurisdictions (including the District) according to statutory formulae generally based on the distribution of taxes in the prior year.

Ongoing changes in the structure of California electric utility industry and in the way in which components of the industry are owned and regulated, including the sale of electric generation assets to largely unregulated, nonutility companies, may affect how utility assets are assessed in the future, and which local agencies are to receive the property taxes. The District is unable to predict the impact of these changes on its utility property tax revenues, or whether future legislation or litigation may affect ownership of utility assets or the State's methods of assessing utility property and allocating tax revenues to local taxing agencies, including the District.

Assessed Valuation by Land Use. The following table gives a distribution of taxable property located in the District by principal purpose for which the land is used, and the assessed valuation and number of parcels for each use.

Arena Union Elementary School District
2004-05 Taxable Assessed Valuation and Parcels by Land Use

	2004-05 Assessed Valuation [1]	% of Total	No. of Parcels	% of Total
Non-Residential:				
Recreational/Cabins	$ 89,826,207	19.66%	585	16.09%
Commercial	46,742,992	10.23	139	3.82
Rural/Forest & Timber	41,804,979	9.15	836	22.99
Vacant Commercial	5,086,915	1.11	55	1.51
Industrial	1,422,483	0.31	13	0.36
Government/Social/Institutional	830,430	0.18	10	0.28
Vacant Industrial	82,321	0.02	4	0.11
Subtotal Non-Residential	$185,796,327	40.66%	1,642	45.16%
Residential:				
Single Family Residence	$214,579,807	46.96%	1,072	29.48%
Vacant Residential	42,114,962	9.22	769	21.15
Mobile Home	10,365,011	2.27	132	3.63
2+ Residential Units/Apartments	4,123,916	0.90	21	0.58
Subtotal Residential	$271,183,696	59.34%	1,994	54.84%
Total	$456,980,023	100.00%	3,636	100.00%

Source: California Municipal Statistics, Inc.
[1] Local Secured Assessed Valuation; excluding tax-exempt property.

Largest Taxpayers in District. The twenty taxpayers in the District with the greatest combined assessed valuation of taxable property on the 2004-05 tax roll, and the assessed valuations thereof, are shown in the following table.

Arena Union School District
Largest 2004-05 Local Secured Taxpayers

	Property Owner	Primary Land Use	2004-05 Assessed Valuation	% of Total[1]
1.	Coastal Bridges LLC	Forest & Timber	$4,500,184	0.98%
2.	James R. and Kazuko A. Popplewell	Commercial	3,650,209	0.80
3.	The Bower LP	Shopping Center	3,586,100	0.78
4.	Gualala Redwoods Inc.	Forest & Timber	3,485,045	0.76
5.	Karen J. and William G. Hay, Jr.	Rural	3,466,626	0.76
6.	Mendocino Redwood Company LLC	Forest & Timber	2,983,284	0.65
7.	David A. Duffield	Recreational	2,055,362	0.45
8.	Robert N. and Marcia R. Valentine	Recreational	2,020,572	0.44
9.	Gualala Cypress Village Inc.	Commercial	1,968,802	0.43
10.	John and Victoria Tanti	Commercial	1,889,520	0.41
11.	Raymond E. and Sydney DeFay Feeney	Residential	1,839,014	0.40
12.	George E. and Kathleen H. Myers	Residential	1,731,739	0.38
13.	Coast Construction Company	Vacant Commercial	1,580,295	0.35
14.	Lena M. Price	Commercial	1,474,997	0.32
15.	Gregory A. Jirak	Commercial	1,438,453	0.31
16.	Robert W. and Roberta J. Sundstrom	Commercial	1,402,780	0.31
17.	Pioneer Resources LLC	Forest & Timber	1,323,368	0.29
18.	SantaRosa Campway Inc.	Commercial	1,246,848	0.27
19.	Dale S. Miller	Commercial	1,246,069	0.27
20.	Anthony H. Gaussoin	Residential	1,237,004	0.27
	TOTAL		$44,126,271	9.66%

Source: California Municipal Statistics, Inc.
[1] 2004-05 Local Secured Assessed Valuation: $456,980,023

Tax Rates, Levies, Collections and Delinquencies

The annual property tax rate is limited to 1% of the full cash value, plus the amount necessary to pay all obligations legally payable from *ad valorem* taxes in the current year. The rate of tax necessary to pay fixed debt service on the Bonds in a given year depends on the assessed value of taxable property in that year. Economic and other factors beyond the District's control, such as a general market decline in land values, reclassification of property to a class exempt from taxation, whether by ownership or use (such as exemptions for property owned by State and local agencies and property used for qualified educational, hospital, charitable or religious purposes), or the complete or partial destruction of taxable property caused by natural or manmade disaster, such as earthquake, flood, fire, toxic dumping, etc., could cause a reduction in the assessed value of taxable property within the District and necessitate a corresponding increase in the annual tax rate to be levied to pay the principal of and interest on the Bonds.

As required by State Law, the District utilizes the services of the County for the assessment and collection of taxes for District purposes. District taxes are collected at the same time and on the same tax rolls as are County, city and other special district taxes.

Taxes are levied for each fiscal year on taxable real and personal property assessed as of the preceding January 1. Assessments may be adjusted during the course of the year when property changes ownership or new construction is completed. Assessments may also be appealed by taxpayers. When necessitated by changes in assessed value in the course of a year, a supplemental assessment is prepared, and taxes are pro-rated for the portion of the tax year remaining after the change.

Property taxes on the secured roll are due in two equal installments, on November 1 and February 1 of each fiscal year, and become delinquent on December 10 and April 10, respectively. A penalty of 10% attaches immediately to all delinquent payments. If the taxes have not been paid by June 30, the tax is deemed to be in default. Secured roll property may thereafter be redeemed by payment of a penalty of 1.5% per month to the time of redemption, plus costs and a redemption fee. If the taxes are unpaid for a period of five years or more, the tax-defaulted property is subject to sale at a public auction by the County Treasurer.

Property taxes on the unsecured roll are due as of the lien date of January 1 and become delinquent if unpaid on August 31. A 10% penalty attaches to delinquent taxes on property on the unsecured roll, and an additional penalty of 1.5% per month begins to accrue on November 1. To collect unpaid taxes, the County Treasurer may obtain a judgment lien upon and cause the sale of all property owned by the taxpayer in the County, and may seize and sell personal property, improvements and possessory interests of the taxpayer. The County Treasurer may also bring a civil suit against the taxpayer for payment.

The following table shows real property tax collections and delinquencies in the District for the last several years.

Arena Union Elementary School District
Secured Tax Charges and Delinquencies

	Secured Tax Charge [(1)]	Amount Del. June 30	% Del. June 30
1998-99	$3,226,790.03	$88,587.51	2.75%
1999-00	3,307,275.20	83,848.67	2.54
2000-01	3,481,239.80	99,998.74	2.87
2001-02	3,690,556.72	98,548.69	2.67
2002-03	3,922,431.16	58,169.52	1.48
2003-04	4,244,013.94	91,188.97	2.15

Source: California Municipal Statistics, Inc.
(1) One-percent General Fund levy by the County within the School District.

The following table shows *ad valorem* property tax rates for the last several years in a typical Tax Rate Area of the District (TRA 52-002). TRA 52-002 comprises approximately 49.56% of the total assessed value of taxable property in the District:

Arena Union Elementary School District
Summary of *Ad Valorem* Tax Rates
Typical Total Tax Rate (TRA 52-002)

	2000-01	2001-02	2002-03	2003-04	2004-05
General	1.000	1.000	1.000	1.000	1.000
Sonoma County Joint Community College	-	-	.025	.025	.025
Point Arena High School District	.024	.024	.020	.020	.019
Arena Union School District	-	-	-	-	.030
Total	1.024	1.024	1.045	1.045	1.074

Source: California Municipal Statistics, Inc.

Teeter Plan. The County has adopted the Alternative Method of Distribution of Tax Levies and Collections and of Tax Sale Proceeds (the "Teeter Plan"), as provided for in Section 4701 and following of the California Revenue and Taxation Code. Under the Teeter Plan, each participating local agency levying property taxes in the County, including school districts, receives the full amount of uncollected taxes credited to its fund (including delinquent taxes, if any), in the same manner as if the full amount due from taxpayers had been collected. In return, the County receives and retains delinquent payments, penalties and interest as collected, that would have been due the local agency. The County applies the Teeter Plan to taxes levied for repayment of school district bonds.

The Teeter Plan is to remain in effect unless the County Board of Supervisors orders its discontinuance or unless, prior to the commencement of any fiscal year of the County (which commences on July 1), the Board of Supervisors receives a petition for its discontinuance from two-thirds of the participating revenue districts in the County. The Board of Supervisors may also, after holding a public hearing on the matter, discontinue the Teeter Plan with respect to any tax levying agency or assessment levying agency in the County if the rate of secured tax delinquency in that agency in any year exceeds three percent of the total of all taxes and assessments levied on the secured roll in that agency.

Direct and Overlapping Debt. The following table was prepared by California Municipal Statistics Inc., and is included for general information purposes only. The District has not reviewed this table for completeness or accuracy and makes no representations in connection therewith. The first column in the table names each public agency which has outstanding debt as of March 1, 2005, and whose territory overlaps the District in whole or in part. Column 2 shows the percentage of each overlapping agency's assessed value located within the boundaries of the District. This percentage, multiplied by the total outstanding debt of each overlapping agency (which is not shown in the table) produces the amount shown in column 3, which is the apportionment of each overlapping agency's outstanding debt to taxable property in the District.

The table generally includes long-term obligations sold in the public credit markets by the public agencies listed. Such long-term obligations generally are not payable from revenues of the District (except as indicated) nor are they necessarily obligations secured by land within the District. In many cases, long-term obligations issued by a public agency are payable only from the general fund or other revenues of such public agency.

Arena Union Elementary School District
Direct and Overlapping Bonded Debt

2004-05 Assessed Valuation: $467,125,163

DIRECT AND OVERLAPPING TAX AND ASSESSMENT DEBT:	% Applicable	Debt 3/1/05	
Sonoma County Joint Community College District	0.998%	$ 443,012	
Point Arena Joint Union High School District	35.344	1,456,173	
Arena Union School District	100.000	2,810,000	(1)
Mendocino County Anchor Bay Assessment District	100.000	185,000	
TOTAL DIRECT AND OVERLAPPING TAX AND ASSESSMENT DEBT		$4,894,185	
OVERLAPPING GENERAL FUND OBLIGATION DEBT:			
Mendocino County Certificates of Participation	7.063%	$2,094,180	
Mendocino County Pension Obligations	7.063	7,058,056	
Sonoma County Joint Community College District General Fund Obligations	0.998	27,146	
TOTAL OVERLAPPING GENERAL FUND OBLIGATION DEBT		$9,179,382	
COMBINED TOTAL DEBT		$14,073,567	(2)

(1) Excludes the Bonds to be sold.
(2) Excludes tax and revenue anticipation notes, enterprise revenue, mortgage revenue and tax allocation bonds and non-bonded capital lease obligations.

Ratios to 2004-05 Assessed Valuation:
Direct Debt ($2,810,000) 0.60%
Total Direct and Overlapping Tax and Assessment Debt 1.05%
Combined Total Debt 3.01%

STATE SCHOOL BUILDING AID REPAYABLE AS OF 6/30/04: $0

Source: California Municipal Statistics, Inc.

The information in the following section is provided by Financial Security Assurance Inc. ("FSA") for use in securities disclosure documents. The District makes no representation regarding the accuracy or completeness thereof, or of any information in the documents incorporated by reference in the following section.

BOND INSURANCE

Bond Insurance Policy

Concurrently with the issuance of the Bonds, Financial Security Assurance Inc. ("Financial Security") will issue its Municipal Bond Insurance Policy for the Bonds (the "Policy"). The Policy guarantees the scheduled payment of the accreted value of the Bonds when due as set forth in the form of the Policy included as an exhibit to this Official Statement.

The Policy is not covered by any insurance security or guaranty fund established under New York, California, Connecticut or Florida insurance law.

Financial Security Assurance Inc.

Financial Security is a New York domiciled financial guaranty insurance company and a wholly owned subsidiary of Financial Security Assurance Holdings Ltd. ("Holdings"). Holdings is an indirect subsidiary of Dexia, S.A., a publicly held Belgian corporation, and of Dexia Credit Local, a direct wholly-owned subsidiary of Dexia, S.A. Dexia, S.A., through its bank subsidiaries, is primarily engaged in the business of public finance, banking and asset management in France, Belgium and other European countries. No shareholder of Holdings or Financial Security is liable for the obligations of Financial Security.

At March 31, 2005, Financial Security's total policyholders' surplus and contingency reserves were approximately $2,321,918,000 and its total unearned premium reserve was approximately $1,672,672,000 in accordance with statutory accounting principles. At March 31, 2005, Financial Security's total shareholder's equity was approximately $2,726,667,000 and its total net unearned premium reserve was approximately $1,356,678,000 in accordance with generally accepted accounting principles.

The financial statements included as exhibits to the annual and quarterly reports filed by Holdings with the Securities and Exchange Commission are hereby incorporated herein by reference. Also incorporated herein by reference are any such financial statements so filed from the date of this Official Statement until the termination of the offering of the Bonds. Copies of materials incorporated by reference will be provided upon request to Financial Security Assurance Inc.: 350 Park Avenue, New York, New York 10022, Attention: Communications Department (telephone (212) 826-0100).

The Policy does not protect investors against changes in market value of the Bonds, which market value may be impaired as a result of changes in prevailing interest rates, changes in applicable ratings or other causes. Financial Security makes no representation regarding the Bonds or the advisability of investing in the Bonds. Financial Security makes no representation regarding the Official Statement, nor has it participated in the preparation thereof, except that Financial Security has provided to the Issuer the information presented under this caption for inclusion in the Official Statement.

TAX MATTERS

In the opinion of Orrick, Herrington & Sutcliffe LLP ("Bond Counsel"), based upon an analysis of existing laws, regulations, rulings, and court decisions, and assuming, among other matters, the accuracy of certain representations and compliance with certain covenants, interest on the Bonds is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986 (the "Code") and is exempt from State of California personal income taxes. Bond Counsel is of the further opinion that interest on the Bonds is not a specific preference item for purposes of the federal individual or corporate alternative minimum taxes, although Bond Counsel observes that such interest is included in adjusted current earnings when calculating corporate alternative minimum taxable income. A complete copy of the proposed form of opinion of Bond Counsel is contained in Appendix C hereto.

To the extent the issue price of any maturity of the Bonds is less than the amount to be paid at maturity of such Bonds (excluding amounts stated to be interest and payable at least annually over the term of such Bonds), the difference constitutes "original issue discount," the accrual of which, to the extent properly allocable to each beneficial owner thereof, is treated as interest on the Bonds which is excluded from gross income for federal income tax purposes and State of California personal income taxes. For this purpose, the issue price of a particular maturity of the Bonds is the first price at which a substantial amount of such maturity of the Bonds is sold to the public (excluding bond houses, brokers, or similar persons or organizations acting in the capacity of underwriters, placement agents or wholesalers). The original issue discount with respect to any maturity of the Bonds accrues daily over the term to maturity of such Bonds on the basis of a constant interest rate compounded semiannually (with straight-line interpolations between compounding dates). The accruing original issue discount is added to the adjusted basis of such Bonds to determine taxable gain or loss upon disposition (including sale, redemption, or payment on maturity) of such Bonds. Beneficial owners of the Bonds should consult their own tax advisors with respect to the tax consequences of ownership of Bonds with original issue discount, including the treatment of beneficial owners who do not purchase such Bonds in the original offering to the public at the first price at which a substantial amount of such Bonds is sold to the public.

Bonds purchased, whether at original issuance or otherwise, for an amount higher than their principal amount payable at maturity (or, in some cases, at their earlier call date) ("Premium Bonds") will be treated as having amortizable bond premium. No deduction is allowable for the amortizable bond premium in the case of bonds, like the Premium Bonds, the interest on which is excluded from gross income for federal income tax purposes. However, the amount of tax-exempt interest received, and a beneficial owner's basis in a Premium Bond, will be reduced by the amount of amortizable bond premium properly allocable to such beneficial owner. Beneficial owners of Premium Bonds should consult their own tax advisors with respect to the proper treatment of amortizable bond premium in their particular circumstances.

The Code imposes various restrictions, conditions and requirements relating to the exclusion from gross income for federal income tax purposes of interest on obligations such as the Bonds. The District has made certain representations and covenanted to comply with certain restrictions, conditions and requirements designed to ensure that interest on the Bonds will not be included in federal gross income. Inaccuracy of these representations or failure to comply with these covenants may result in interest on the Bonds being included in gross income for federal income tax purposes, possibly from the date of original issuance of the Bonds. The opinion of Bond Counsel assumes the accuracy of these representations and compliance with these covenants. Bond Counsel has not undertaken to determine (or to inform any person) whether any actions taken (or not taken), or events occurring (or not occurring), or any other matters coming to Bond Counsel's attention after the date of issuance of the Bonds may adversely affect the value of, or the tax status of interest on, the Bonds.

Certain requirements and procedures contained or referred to in the Resolution, the Tax Certificate of the District dated the date of issuance of the Bonds, and other relevant documents may be changed and certain actions (including, without limitation, defeasance of the Bonds) may be taken or omitted under the circumstances and subject to the terms and conditions set forth in such documents. Bond Counsel expresses no opinion as to any Bond or the interest thereon if any such change occurs or action is taken or omitted upon the advice or approval of bond counsel other than Orrick, Herrington & Sutcliffe LLP.

Although Bond Counsel is of the opinion that interest on the Bonds is excluded from gross income for federal income tax purposes and is exempt from State of California personal income taxes, the ownership or disposition of, or the accrual or receipt of interest on, the Bonds may otherwise affect a Beneficial owner's federal, state or local tax liability. The nature and extent of these other tax consequences depends upon the particular tax status of the Beneficial owner or the Beneficial owner's other items of income or deduction. Bond Counsel expresses no opinion regarding any such other tax consequences.

Future legislation, if enacted into law, or clarification of the Code may cause interest on the Bonds to be subject, directly or indirectly, to federal income taxation, or otherwise prevent Beneficial owners from realizing the full current benefit of the tax status of such interest. The introduction or enactment of any such future legislation or clarification of the Code may also affect the market price for, or marketability of, the Bonds. Prospective purchasers of the Bonds should consult their own tax advisers regarding any pending or proposed federal tax legislation, as to which Bond Counsel expresses no opinion.

The opinion of Bond Counsel is based on current legal authority, covers certain matters not directly addressed by such authorities, and represents Bond Counsel's judgment as to the proper treatment of the Bonds for federal income tax purposes. It is not binding on the Internal Revenue Service or the courts. Furthermore, Bond Counsel cannot give and has not given any opinion or assurance about the future activities of the District, or about the effect of future changes in the Code, the applicable regulations, the interpretation thereof or the enforcement thereof by the IRS. The District has covenanted, however, to comply with the requirements of the Code.

Bond Counsel's engagement with respect to the Bonds ends with the issuance of the Bonds, and, unless separately engaged, Bond Counsel is not obligated to defend the District or the Beneficial owners regarding the tax-exempt status of the Bonds in the event of an audit examination by the IRS. Under current procedures, parties other than the District and its appointed counsel, including the beneficial owners, would have little, if any, right to participate in the audit examination process. Moreover, because achieving judicial review in connection with an audit examination of tax-exempt bonds is difficult, obtaining an independent review of IRS positions with which the District legitimately disagrees may not be practicable. Any action of the IRS, including but not limited to selection of the Bonds for audit, or the course or result of such audit, or an audit of bonds presenting similar tax issues, may affect the market price for, or the marketability of, the Bonds, and may cause the District or the beneficial owners to incur significant expense.

OTHER LEGAL MATTERS

Legal Opinion

The validity of the Bonds and certain other legal matters are subject to the approving opinion of Orrick, Herrington & Sutcliffe LLP, San Francisco, California, Bond Counsel. A complete copy of the proposed form of Bond Counsel opinion is contained in Appendix C hereto. Bond Counsel undertakes no responsibility for the accuracy, completeness or fairness of this Official Statement.

Bank Qualified

The District has designated the Bonds as "qualified tax-exempt obligations" within the meaning of Section 265(b)(3)(B) of the Internal Revenue Code of 1986, as amended. Pursuant to that section, a qualifying financial institution will be allowed a deduction from its own federal corporate income tax for the portion of interest expense the financial institution is able to allocate to designated "bank-qualified" investments.

Legality for Investment in California

Under provisions of the California Financial Code, the Bonds are legal investments for commercial banks in California to the extent that the Bonds, in the informed opinion of the bank, are prudent for the investment of funds of depositors, and, under provisions of the Government Code of the State, are eligible securities for the deposit of public moneys in the State.

No Litigation

No litigation is pending or threatened concerning the validity of the Bonds, or the District's ability to receive *ad valorem* taxes and to collect other revenues, or contesting the District's ability to issue and retire the Bonds. The District is not aware of any litigation pending or threatened questioning the political existence of the District or contesting the title to their offices of District or County officials who will sign the Bonds and other certifications relating to the Bonds, or the powers of those offices. A certificate (or certificates) to that effect will be furnished to purchasers at the time of the original delivery of the Bonds.

The District is routinely subject to lawsuits and claims. In the opinion of the District, the aggregate amount of the uninsured liabilities of the District under these lawsuits and claims will not materially affect the financial position or operations of the District.

Continuing Disclosure

The District has covenanted for the benefit of the holders and beneficial owners of the Bonds to provide certain financial information and operating data relating to the District (the "Annual Report") by not later than nine months following the end of the District's fiscal year (currently ending June 30), commencing with the report for the 2004-05 Fiscal Year (which is due no later than April 1, 2006), and to provide notices of the occurrence of certain enumerated events, if material. The Annual Report will be provided to any person upon written request. The notices of material events will be filed by the District with each Nationally Recognized Municipal Securities Information Repository or with the Municipal Securities Rulemaking Board, and with the State information repository, if any. The specific nature of the information to be contained in the Annual Report or the notices of material events is summarized in APPENDIX D: "FORM OF CONTINUING DISCLOSURE CERTIFICATE." These covenants have been made in order to assist the Underwriter in complying with Securities and Exchange Commission Rule 15c2-12(b)(5). The District has never failed to comply in all material respects with any previous undertakings with regard to said Rule to provide annual reports or notices of material events.

MISCELLANEOUS

Ratings

The Bonds have received the rating of "Aaa" by Moody's Investors Service ("Moody's") and "AAA" by Standard & Poor's Rating Services ("Standard & Poor's"), based upon the issuance by Financial Security Assurance Inc. of a municipal bond insurance policy with respect to the Bonds at the time of delivery of the Bonds. Each rating agency generally bases its ratings on its own investigations, studies and assumptions. The District has provided certain additional information and materials to each rating agency (some of which does not appear in this Official Statement). The ratings reflect only the views of the respective rating agency, and any explanation of the significance of any rating may be obtained only from Moody's at 99 Church Street, New York, NY 10007, (212) 553-0882, and from Standard & Poor's at 55 Water Street, New York, NY 10041, (212) 208-1022. There is no assurance that any rating will continue for any given period of time or that it will not be revised downward or withdrawn entirely by the rating agency, if, in the judgment of the rating agency, circumstances so warrant. Any such downward revision or withdrawal of a rating may have an adverse effect on the market price of the Bonds. The District undertakes no responsibility to oppose any such downward revision, suspension or withdrawal.

Professionals Involved in the Offering

Orrick, Herrington & Sutcliffe LLP is acting as Bond Counsel and as Disclosure Counsel with respect to the Bonds, and will receive compensation from the District contingent upon the sale and delivery of the Bonds. California Financial Services is acting as financial advisor to the District with respect to the Bonds, and will receive compensation from the District contingent upon the sale and delivery of the Bonds.

Underwriting

The Bonds are being purchased by A. G. Edwards & Sons, Inc. (the "Underwriter") pursuant to a bond purchase contract by and among the District, the County and the Underwriter, dated June 7, 2005, at a price of $897,266.10 (calculated as the principal amount of the Bonds of $889,062.35, plus original issue premium of $160,783.75, less costs of issuance of the Bonds of $101,100.00, less underwriting compensation of $10,000.00, less bond insurance premium of $41,480.00). Pursuant to the purchase contract, the obligation of the Underwriter to purchase the Bonds is subject to certain terms and conditions to be satisfied by the District and the County.

The Underwriter has certified the re-offering prices or yields set forth on the inside cover hereof. The Underwriter may offer and sell the Bonds to certain dealers and others at prices lower than the offering prices stated on the cover page. The offering prices may be changed from time to time by the Underwriter.

The District has duly authorized the delivery of this Official Statement.

ARENA UNION ELEMENTARY SCHOOL DISTRICT

By: /s/ Mark Iacuaniello

Superintendent

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APPENDIX A

INFORMATION RELATING TO THE DISTRICT'S OPERATIONS AND BUDGET

The information in this appendix concerning the operations of the District, the District's finances, and State funding of education, is provided as supplementary information only, and it should not be inferred from the inclusion of this information in this Official Statement that the principal of or interest on the Bonds is payable from the general fund of the District or from State revenues. The Bonds are payable from the proceeds of an ad valorem *tax approved by the voters of the District pursuant to all applicable laws and Constitutional requirements, and required to be levied by the County on property within the District in an amount sufficient for the timely payment of principal and interest on the Bonds. See "SECURITY AND SOURCE OF PAYMENT FOR THE BONDS."*

FINANCIAL AND DEMOGRAPHIC INFORMATION

General

The District, established in 1885, provides elementary educational services to residents of an area encompassing approximately 250 square miles located on the Mendocino County Coast and adjoining the Sonoma County line. The economy of the region consists primarily of wine and sparkling wine production, tourism and recreation, agriculture and food production, and retail and services. Recent decades have witnessed a fundamental shift to these economic activities from the area's traditional timber-related and commercial fishing industries.

The District currently operates one elementary school serving students in grades kindergarten through eight and one charter school serving students in grades kindergarten through twelve, serving approximately 316 students. As of July 1, 2004, the District employed approximately 36 employees including certificated (credentialed teaching) staff, classified (non-teaching) staff, and management personnel. The District has adopted a Fiscal Year 2004-05 general fund budget with total expenditures of approximately $5.1 million. Total assessed valuation of taxable property in the District in Fiscal Year 2004-05 is approximately $467 million.

Arena Union Elementary School District
Total K-8 Enrollment

Fiscal Year	Arena Enrollment	Charter Enrollment	Total Enrollment
2000-01	287	73	360
2001-02	271	70	341
2002-03	242	88	330
2003-04	230	86	316
2004-05 budgeted	222	94	316

The District is governed by an elected Board of Trustees consisting of 7 members. The voting members are elected to 4-year terms. The day-to-day operations are managed by a board-appointed Superintendent of Schools. Mark Iacuaniello has served as the Superintendent since 2001. Mr. Iacuaniello has served California schools as an educator for 18 years and a school administrator for 11 years.

Consolidation with the High School District

Under the Education Code, when two school districts share a common board of trustees, upon adoption of certain consents and taking certain board actions, two such districts may be deemed one district for all purposes including, but not limited to budget and personnel matters, with two specific exceptions (the districts continue to be treated separately for (i) state apportionments and allowances, and allocation of property tax revenues, and (ii) holding title to property and indebtedness). The District shares a common board with the Point Arena Union High

School District. In order to gain various operational efficiencies and reduce expenditures, pursuant to Education Code Section 35110 and following, the District consolidated its operations with the Point Arena Union High School District on July 1, 2004.

State Funding of Education; State Budget Process

General. As is true for all school districts in California, District operating income consists primarily of two components: a State portion funded from the State's general fund and a locally generated portion derived from the District's share of the 1% local *ad valorem* property tax authorized by the State Constitution. School districts may be eligible for other special categorical funding, including for State and federal programs. The District receives approximately 14% of its revenues from State funds, budgeted at $386,460 in Fiscal Year 2004-05. As a result, decreases in State revenues, or in State legislative appropriations made to fund education, may significantly affect District operations.

According to the State Constitution, the Governor is required to propose a budget to the California Legislature no later than January 10 of each year, and a final budget must be adopted by a two-thirds vote of each house of the Legislature no later than June 15, although this deadline is routinely breached. The budget becomes law upon the signature of the Governor, who may veto specific items of expenditure. On May 29, 2002, the State Court of Appeal held in *White v. Davis* (also referred to as *Jarvis v. Connell*) that the State Controller cannot disburse State funds after the beginning of the fiscal year until the adoption of the budget bill or an emergency appropriation, unless the expenditure is (i) authorized by a continuing appropriation found in statute, or (ii) mandated by the Constitution (such as appropriations for salaries of elected state officers), or (iii) mandated by federal law (such as payments to State workers at no more than minimum wage). The court specifically held that the State Constitution does not mandate or otherwise provide for appropriations for school districts without an adopted budget. Nevertheless, the Controller believes that statutory implementation of the constitutional school funding formula provides for a continuing appropriation of State funding for schools, and has indicated that payment of such amounts would continue during a budget impasse. Special and categorical funds would not be appropriated until a budget or emergency appropriation is adopted. The Controller has posted guidance as to what can and cannot be paid during a budget impasse at its website: **www.sco.ca.gov**. Should the Legislature fail to pass the budget or emergency appropriation before the start of any fiscal year, the District might experience delays in receiving certain expected revenues. The District is authorized to borrow temporary funds to cover its annual cash flow deficits, and as a result of the *White* decision, the District might find it necessary to increase the size or frequency of its cash flow borrowings, or to borrow earlier in the fiscal year. The District does not expect the *White* decision to have any long-term effect on its operating budgets.

State income tax and other receipts can fluctuate significantly from year to year, depending on economic conditions in the State and the nation. Because funding for education is closely related to overall State income, as described in this section, funding levels can also vary significantly from year to year, even in the absence of significant education policy changes. A brief description of the adopted State budget for 2004-05 is included below; however, the District cannot predict how State income or State education funding will vary over the entire term to maturity of the Bonds, and the District takes no responsibility for informing owners of the Bonds as to any such annual fluctuations. Information about the State budget and State spending for education is regularly available at various State-maintained websites. Text of proposed and adopted budgets may be found at the website of the Department of Finance, **www.dof.ca.gov**, under the heading "California Budget." An impartial analysis of the budget is posted by the Office of the Legislative Analyst at **www.lao.ca.gov**. In addition, various State of California official statements, many of which contain a summary of the current and past State budgets and the impact of those budgets on school districts in the State, may be found at the website of the State Treasurer, **www.treasurer.ca.gov**. The information referred to is prepared by the respective State agency maintaining each website and not by the District, and the District can take no responsibility for the continued accuracy of these internet addresses or for the accuracy, completeness or timeliness of information posted there, and such information is not incorporated herein by these references.

Aggregate State Education Funding. Under Proposition 98, a constitutional and statutory amendment adopted by the State's voters in 1988 and amended by Proposition 111 in 1990 (now found at Article XVI, Sections 8 and 8.5 of the Constitution), a minimum level of funding is guaranteed to school districts, community college districts, and other State agencies that provide direct elementary and secondary instructional programs for kindergarten through grade 14 (K-14).

The guaranteed funding amount for K-14 education is based on prior-year funding, as adjusted through various formulas and tests that take into account State proceeds of taxes, local property tax proceeds, school enrollment, per-capita personal income, and other factors. The State's share of the guaranteed amount is based on State general fund tax proceeds and is not based on the general fund in total or on the State budget. The local share of the guaranteed amount is funded from local property taxes. The total guaranteed amount varies from year to year and throughout the stages of any given fiscal year's budget, from the Governor's initial budget proposal to actual expenditures, as the various factors change. Over the long run, the guaranteed amount will increase as enrollment and per capita personal income grow. On average, about 40 percent of State general fund tax proceeds are spent on the State's share of Proposition 98 funding.

The Proposition 98 funding guarantee may be suspended for one year at a time by enactment of an urgency statute. In subsequent years in which State general fund revenues are growing faster than personal income (or sooner, as the Legislature may determine), the funding level must be restored to the guaranteed amount. However, the amount of underfunding during suspension of Proposition 98 will result in permanent savings to the State.

In the past, when State general fund revenues have failed to reach budgeted levels, the State has implemented a number of retroactive funding adjustments and deferrals, distorting funding over many years, making cross-year comparisons difficult, and making short- and long-term budgeting difficult for school and college districts. In several years in the early 1990s, as the State's economy was sliding into a recession, the State's budgeted allocations for school and college districts proved to be more than Proposition 98 would have required. The excess amounts were later treated by the State as advances to K-14 education against subsequent years' Proposition 98 minimum funding levels, resulting in aggregate funding reductions of over $1 billion in those years. In 2002-03 and 2003-04, the worsening State financial position again resulted in retroactive adjustments as well as current-year cuts. The Legislative Analyst reports that legislative actions in mid-Fiscal Year 2002-03 eliminated $2.5 billion from budgeted Proposition 98 funding through a combination of deferral of expenditures to Fiscal Year 2003-04, use of one-time funds, captured program savings, and other cuts. In general, deferral of education expenditures and reductions in the components of Proposition 98 funding have the effect of reducing the base from which future Proposition 98 minimum funding levels are calculated. Legislation enacted in March 2003 permanently defers the apportionment of Proposition 98 funds, scheduled each year for June, to each July 2, and thus from one fiscal year to the next. These and other techniques will significantly reduce the minimum guarantee requirement for Fiscal Years 2003-04 and beyond.

Recent Developments Regarding State Finances. Since early 2001 the State has faced significant financial challenges, with an economic recession in 2001 and a sluggish recovery in 2002 and 2003 (with greatest impacts in the high technology, internet, and telecommunications sectors, especially in Northern California); weakened exports; and most particularly, large stock market declines between 2000 and 2002, with attendant declines in stock option values and capital gains realizations. These adverse fiscal and economic factors have resulted in an erosion of State general fund tax revenues. The three largest State general fund tax sources are personal income, sales and use, and corporate taxes. The bulk of the revenue declines were from personal income taxes, principally from reduced capital gains realizations and stock option income.

This revenue drop resulted in a shortfall between State revenues and anticipated spending demands during the past three fiscal years resulting in a total accumulated deficit of approximately $22 billion. Two measures intended to address the existing cumulative budget deficit and to implement structural reform were approved at the March 2, 2004 statewide primary election. The California Economic Recovery Bond Act (Proposition 57) authorized the issuance of up to $15 billion of bonds to finance the State negative general fund reserve balance as of June 30, 2004 and other general fund obligations undertaken prior to June 30, 2004. The Balanced Budget Amendment (Proposition 58) requires the State to adopt and maintain a balanced budget and establish a reserve, and restricts future long-term deficit-related borrowing. The State has issued $11.3 billion of the authorized bonds.

2004-05 Governor's Budget. The Governor signed the State 2004-05 Fiscal Year budget on July 31, 2004, although additional pending legislation is expected to affect final budget totals. The following information is adapted from the Legislative Analyst's budget analyses: The budget relies heavily on new debt and does not address identified structural imbalances between revenues and spending. The budget addresses the current revenue shortfall through program savings, borrowing, local government contributions, and funding shifts, including: (i) suspending Proposition 98 and reducing spending in higher education, corrections, state operations, and social services programs; (ii) borrowing $11.3 billion through the issuance of Economic Recovery Bonds; (iii) diverting $1.3 billion from local governments to augment revenues in 2004-05 and 2005-06; and (iv) using $1.2 billion in bond proceeds related to newly approved tribal gaming compacts to repay in 2004-05 transportation loans otherwise due in 2005-06.

With respect to the funding of K-12 education, the budget proposes Proposition 98 funding for grades K through 12 of $42.1 billion, or $2.3 billion less than the Proposition 98 guaranteed amount. The budget provides $560 million in one-time funds to meet prior years' Proposition 98 obligations, but defers another $1 billion of such obligations through the 2014-15 budget year. The budget provides both statutory and discretionary growth and cost-of-living adjustments to revenue limits ($1.154 billion) and most categorical programs ($335 million), and provides $120 million for increased unemployment insurance costs. The budget provides $270 million in additional revenue limit funding to partially restore the $350 million general purpose reduction school districts experienced in 2003-04, and provides additional funding for revenue limit equalization across districts ($110 million). The budget augments instructional materials by $188 million and deferred maintenance by $173 million. In addition, in connection with the settlement of a class action lawsuit, *Williams v. State of California*, brought against the State on behalf of students in the most poorly funded schools, the 2004-05 budget provides $138 million in one-time funds for instructional materials for the lowest performing schools, and sets aside $50 million for implementation of the settlement in 2004-05, primarily for facility improvements to the neediest schools. Future years' budgets will have to address further settlement terms calling for over $800 million in facilities improvements and additional programmatic support.

Proposition 1A. Beginning in 1992-93, the State has satisfied a portion of its Proposition 98 obligations by shifting part of the 1% local *ad valorem* property tax revenues otherwise belonging to cities, counties, special districts, and redevelopment agencies, to school and college districts through a local Educational Revenue Augmentation Fund (ERAF) in each county. In response to a statewide ballot initiative sponsored by affected local agencies, the Legislature proposed an amendment to the State Constitution, which the State's voters approved as "Proposition 1A" at the November 2004 election.

Proposition 1A is intended to, among other things, stabilize local government revenue sources by restricting the State's control over local property taxes. Beginning in Fiscal Year 2008-09, the State will be able to divert up to eight percent of local property tax revenues for State purposes (including, but not limited to, funding K-12 education) only if: (i) the Governor declares such action to be necessary due to a State fiscal emergency; (ii) two-thirds of both houses of the Legislature approve the action; (iii) the amount diverted is required by statute to be repaid within three years; (iv) the State does not owe any repayment for past property tax or Vehicle License Fee diversions to local agencies; and (v) such property tax diversions do not occur in more than two of any ten consecutive fiscal years. Because ERAF shifts will be capped and limited in frequency, school and college districts that receive Proposition 98 funding from the State will be more directly dependent upon the State's general fund.

Allocation of State Funding to Districts. Under Education Code Section 42238 and following, each school district is determined to have a target funding level: a "base revenue limit" per student multiplied by the district's student enrollment measured in units of average daily attendance ("A.D.A.").

The base revenue limit is calculated from the district's prior-year funding level, as adjusted for a number of factors, such as inflation, special or increased instructional needs and costs, employee retirement costs, especially low enrollment, increased pupil transportation costs, etc. Generally, the amount of State funding allocated to each school district is the amount needed to reach that district's base revenue limit after taking into account certain other revenues, in particular, locally generated property taxes. This is referred to as State "equalization aid" or colloquially as "backfill." To the extent local tax revenues increase due to growth in local property assessed valuation, the additional revenue is offset by a decline in the State's contribution.

Enrollment can fluctuate due to factors such as population growth, competition from private, parochial, and public charter schools, inter-district transfers in or out, and other causes. Losses in enrollment will cause a school district to lose operating revenues, without necessarily permitting the district to make adjustments in fixed operating costs.

The District's revenue limit income per A.D.A. is budgeted to be $5,686 for 2004-05, compared to approximately $5,222 for 2003-04. The District's recent A.D.A. history for grade K through grade 8 (K-8) is set forth in the table below:

Arena Union Elementary School District
Total K-8 (P-2)
Average Daily Attendance

Fiscal Year	Average Daily Attendance
1997-98	330
1998-99[(1)]	299
1999-00	254
2000-01	254
2001-02	248
2002-03	222
2003-04	209
2004-05[(2)]	209

(1) Commencing in Fiscal Year 1998-99, State law requires average daily attendance to be computed without including excused absences.
(2) Fiscal Year 2004-05 Budget, adopted July 1, 2004.

In its most recent adopted budget, the District estimates that it will receive $1.6 million in aggregate revenue limit income in 2004-05, or approximately 57% of its total general fund revenues. This amount represents an increase of approximately 3% from the $1.5 million that the District received in 2003-04. State funds for special (categorical) programs are budgeted at $363,014, including the State lottery fund portion. Lottery funds may not be used for non-instructional purposes, such as the acquisition of real property, the construction of facilities, or the financing of research. School districts receive lottery funds proportional to their total A.D.A. The District's State lottery revenue is budgeted at approximately $217 per A.D.A.

The District adopted its own 2004-05 budget prior to the adoption of the State budget. Certain adjustments may have to be made throughout the year based on actual State funding and actual attendance. The District cannot make any predictions regarding the disposition of additional pending budget legislation or its effect on school finance, or whether the State will make additional cuts or enhancements to education funding during Fiscal Year 2004-05. In addition, the District's budgeted A.D.A. is an estimate used for planning purposes only, and does not represent a prediction as to the actual attendance or the District's actual funding level for 2004-05.

Local Sources of Education Funding

The principal component of local revenues is a school district's property tax revenues, i.e., each district's share of the local 1% property tax, received pursuant to Sections 75 and following and Sections 95 and following of the California Revenue and Taxation Code. Education Code Section 42238(h) itemizes the local revenues that are counted towards the base revenue limit before calculating how much the State must provide in equalization aid. The more local property taxes a district receives, the less State equalization aid it is entitled to; ultimately, a school district whose local property tax revenues exceed its base revenue limit is entitled to receive no State equalization aid, and receives only its special categorical aid, which is deemed to include the "basic aid" of $120 per student per year guaranteed by Article IX, Section 6 of the Constitution. Such districts are known colloquially as "basic aid districts." Districts that receive some equalization aid are commonly referred to as "revenue limit districts."

The District is currently a "basic aid" district. Local property tax revenues account for approximately 99% of the District's aggregate revenue limit income, and are budgeted at $1.5 million, or 57% of total general fund revenue in 2004-05. The County is a "Teeter Plan" county, which means that the District is made whole for any delinquencies in payment of property taxes by local property owners. Property tax levy and collection procedures (including the Teeter Plan) are discussed under "SECURITY AND SOURCE OF PAYMENT FOR THE BONDS - Tax Rates, Levies, Collection and Delinquencies" in the front portion of this Official Statement. For a discussion of legal limitations on the ability of the District to raise revenues through local property taxes, see "CONSTITUTIONAL AND STATUTORY PROVISIONS AFFECTING DISTRICT REVENUES AND APPROPRIATIONS" below.

Under California law, a city or county can create a redevelopment agency in territory within one or more school districts. Upon formation of a "project area" of a redevelopment agency, all property tax revenues attributable to the growth in assessed value of taxable property within the project area (known as "tax increment") belong to the redevelopment agency, causing a loss of tax revenues to other local taxing agencies, including school districts, from that time forward. For revenue limit districts, any loss of local property taxes is made up by an increase in State equalization aid, until the base revenue limit is reached. For basic aid districts, the loss of tax revenues is not reimbursed by the State. In neither case are taxes collected for payment of debt service on school bonds affected or diverted. Certain school districts may enter into "pass-through agreements" with their local redevelopment agencies in order to receive a portion of the tax increment revenue that would otherwise belong to the redevelopment agency (provided such revenue is not pledged and needed to pay debt service on redevelopment agency tax-increment bonds), and in some cases the pass-through is mandated by statute (in which case it cannot be pledged to pay redevelopment agency bonds).

District Budget Process and County Review

State law requires school districts to maintain a balanced budget in each fiscal year. The State Department of Education imposes a uniform budgeting and accounting format for school districts.

Under current law, a school district governing board must adopt and file with the county superintendent of schools a tentative budget by July 1 in each fiscal year. The District is under the jurisdiction of the Mendocino County Superintendent of Schools.

The county superintendent must review and approve or disapprove the budget no later than August 15. The county superintendent is required to examine the adopted budget for compliance with the standards and criteria adopted by the State Board of Education and identify technical corrections necessary to bring the budget into compliance with the established standards. If the budget is disapproved, it is returned to the District with recommendations for revision. The District is then required to revise the budget, hold a public hearing thereon, adopt the revised budget and file it with the county superintendent no later than September 8. Pursuant to State law, the county superintendent has available various remedies by which to impose and enforce a budget that complies with State criteria, depending on the circumstances, if a budget is disapproved. After approval of an adopted budget, the school district's administration may submit budget revisions for governing board approval.

Subsequent to approval, the county superintendent will monitor each district under its jurisdiction throughout the fiscal year pursuant to its adopted budget to determine on an ongoing basis if the district can meet its current or subsequent year financial obligations. If the county superintendent determines that a district cannot meet its current or subsequent year obligations, the county superintendent will notify the district's governing board of the determination and may then do either or both of the following: (a) assign a fiscal advisor to enable the district to meet those obligations or (b) if a study and recommendations are made and a district fails to take appropriate action to meet its financial obligations, the county superintendent will so notify the State Superintendent of Public Instruction, and then may do any or all of the following for the remainder of the fiscal year: (i) request additional information regarding the district's budget and operations; (ii) develop and impose, after also consulting with the district's board, revisions to the budget that will enable the district to meet its financial obligations; and (iii) stay or rescind any action inconsistent with such revisions. However, the county superintendent may not abrogate any provision of a collective bargaining agreement that was entered into prior to the date upon which the county superintendent assumed authority.

A State law adopted in 1991 (known as "A.B. 1200") imposed additional financial reporting requirements on school districts, and established guidelines for emergency State aid apportionments. Under the provisions of A.B. 1200, each school district is required to file interim certifications with the county superintendent (on December 15, for the period ended October 31, and by mid-March for the period ended January 31) as to its ability to meet its financial obligations for the remainder of the then-current fiscal year and, based on current forecasts, for the subsequent fiscal year. The county superintendent reviews the certification and issues either a positive, negative or qualified certification. A positive certification is assigned to any school district that will meet its financial obligations for the current fiscal year and subsequent two fiscal years. A negative certification is assigned to any school district that will be unable to meet its financial obligations for the remainder of the fiscal year or subsequent fiscal year. A qualified certification is assigned to any school district that may not meet its financial obligations for the current fiscal year or two subsequent fiscal years. A school district that receives a qualified or negative certification may not issue tax and revenue anticipation notes or certificates of participation without approval by the county superintendent. The District has never received a qualified or negative certification.

Accounting Practices

The accounting policies of the District conform to generally accepted accounting principles in accordance with the definitions, instructions and procedures of the California School Accounting Manual, as required by the State Education Code. Revenues are recognized in the period in which they become both measurable and available to finance expenditures of the current fiscal period. Expenditures are recognized in the period in which the liability is incurred.

Robertson, Cahill & Associates, CPAs, Ukiah, California, serves as independent auditor to the District and excerpts of its report for Fiscal Year Ended June 30, 2004, are attached hereto as APPENDIX B. The District considers its audited financial statements to be public information, and accordingly no consent has been sought or obtained from the auditor in connection with the inclusion of such statements in this Official Statement. The auditor has made no representation in connection with inclusion of the audit excerpts herein that there has been no material change in the financial condition of the District since the audit was concluded. The District is required by law to adopt its audited financial statements following a public meeting to be conducted no later than January 31 following the close of each fiscal year.

District Expenditures

The largest part of each school district's general fund budget is used to pay salaries and benefits of certificated (credentialed teaching) and classified (non-instructional) employees. Changes in salary and benefit expenditures from year to year are generally based on changes in staffing levels, negotiated salary increases, and the overall cost of employee benefits.

In its 2004-05 budget, the District projects that it will expend approximately $2 million in salaries and benefits, or approximately 70% of its general fund expenditures. This amount represents an increase of approximately 5% from the $1.9 million the District expended in 2003-04. For the fiscal year 2002-03, the District and Point Arena Joint Union High School District shared equally the costs of a common administration. However, beginning in fiscal year 2003-04, the District paid only 40% of such costs while the Point Arena Joint Union High School District paid 60%.

The District is required by State law and regulation to maintain various reserves. The District is required to maintain a reserve for economic uncertainties in the amount of 5% of its total (adjusted) general fund expenditures, based on its total student attendance. Legislation enacted in connection with the 2003-04 State budget negotiations has granted school districts greater flexibility in the funding and use of these and certain other reserved funds. In 2003-04 and 2004-05, the District is only required to maintain a reserve for economic uncertainties in the amount of

1.5% of its total expenditures. The District has budgeted an unrestricted general fund reserve of $341,346 which represents 5% of total expenditures.

Labor Relations. As of July 1, 2004, 37 employees were represented by labor organizations, as shown in the table below. The remainder are not represented by any formal bargaining unit.

Arena Union Elementary School District
Labor Organizations

Labor Organization	Represented Employees	Contract Expiration
Arena Union Teachers Organization	19	July 1, 2003[1]
California School Employees Association South Coast Chapter #343	18	July 1, 2005

(1) Currently under negotiation for a contract expiring in 2006. Negotiations expect to be settled by June 30, 2005.

Retirement Programs. The District participates in the State Teachers' Retirement System ("STRS") for all full-time and some part-time certificated employees. Each school district is required by statute to contribute 8.25% of eligible employees' salaries to STRS on a monthly basis. Employees are required to contribute 8% of eligible salary. The State is required to contribute as well. The District's employer contribution to STRS was approximately $82,844 for Fiscal Year 2003-04 and is budgeted at $84,454 in Fiscal Year 2004-05.

The District also participates in the California Public Employees' Retirement System ("CalPERS") for all full-time and some part-time classified employees. For many years, school districts were not required to contribute to CalPERS due to favorable investment of CalPERS funds, but beginning in 2002-03, the District was required to contribute toward CalPERS, at a State-determined percentage of CalPERS-eligible salaries. In the current budget year, the total contribution is budgeted at $41,038, compared to a Fiscal Year 2003-04 expense of $36,757.

The District is unable to predict what the amount of State pension liabilities will be in the future, or the amount of the contributions which the District may be required to make. STRS and CalPERS liabilities are more fully described in **APPENDIX B: "EXCERPTS FROM FINANCIAL STATEMENTS OF THE DISTRICT FOR THE FISCAL YEAR ENDED JUNE 30, 2004,"** Note 15.

Accrued Vacation and other Obligations: The long-term portion of accumulated and unpaid employee vacation for the District as of June 30, 2004, was $8,578. See **APPENDIX B: "EXCERPTS FROM FINANCIAL STATEMENTS OF THE DISTRICT FOR THE FISCAL YEAR ENDED JUNE 30, 2004,"** Note 6.

Summary of District Revenues and Expenditures

The following table summarizes the District's actual or budgeted general fund revenue, expenditures and fund balances for Fiscal Years 2000-01 through 2004-05. Excerpts of the District's audited financial statements for the year ending June 30, 2004, are reproduced in Appendix B. The final (unaudited) statement of receipts and expenditures for each fiscal year ending June 30 is required by State law to be approved by the District's Board of Trustees by September 15, and the audit report must be filed with the Mendocino County Superintendent of Schools and State officials by December 15 of each year.

General Fund
Revenues, Expenditures and Fund Balances
2000-01 through 2004-05

	2000-01 Actual(1)	2001-02 Actual(1)	2002-03 Actual(1)	2003-04 Actual(1)	2004-05 Budget(2)
REVENUE/RECEIPTS					
Revenue Limit Sources:					
State Apportionments	$ 135,088	$ 134,635	$ 86,212	$ 14,205	$ 23,446
Local Sources	1,266,933	1,365,462	1,479,195	1,547,536	1,580,579
Federal Revenue	309,965	504,416	524,748	329,471	450,208
Other State Revenue	481,677	444,171	387,879	355,441	363,014
Other Local Revenue	346,686	336,428	310,225	341,885	376,051
TOTAL	$2,540,349	$2,785,112	$2,788,259	$2,588,538	$2,793,298
EXPENDITURES/DISBURSEMENTS					
Certificated Salaries	841,133	959,421	1,062,218	1,015,603	1,083,479
Classified Salaries	333,745	383,855	428,068	382,330	436,892
Employee Benefits	339,577	381,423	487,449	514,572	502,870
Books and Supplies	139,332	175,535	150,407	114,122	111,130
Services/ Other Operating Expenditures	400,469	401,863	422,229	383,071	352,053
Capital Outlay		79,344	21,796	--	--
Other Outgo				370,952	396,919
Direct Support Indirect Costs				(2,064)	(3,330)
TOTAL	$2,054,256	$2,381,441	$2,572,167	$2,778,586	$2,880,013
Excess of Revenues Over (Under) Expenditures	486,093	403,671	216,092	(190,048)	(86,715)
Contributions					
Operating transfers in	12,000	10,860			
Operating transfers out	(12,937)	(10,000)			
Other uses and transfers in					
Other uses and transfers out	(274,901)	(285,809)	(334,584)	(8,470)	(1,938)
TOTAL	($275,838)	($284,949)	($334,584)	($8,470)	($1,938)
EXCESS OF REVENUE, OTHER SOURCES OVER/(UNDER) EXPENDITURES, OTHER USES	210,255	118,722	(118,492)	(198,518)	(88,653)
Fund Balance, Beginning of Year	418,031	628,286	747,008	628,516	429,998
Fund Balance, End of Year	$628,286	$747,008	$628,516	$429,998	$341,346

(1) Excerpted from the District's audited Financial Statements.
(2) Second Interim Report as of April 21, 2005.

District Debt Structure

Tax and Revenue Anticipation Notes. The District has issued Tax and Revenue Anticipation Notes ("TRANs") through the California School Cash Reserve Program Authority for the past three years, as shown in the table below. The District's TRANs are a general obligation of the District, payable from the District's general fund and any other lawfully available moneys. Additionally, the District has approved 2005-2006 tax and revenue anticipation notes to be issued in the principal amount of $700,000.

Issuance Date	Principal Amount	Interest Rate	Yield	Due Date
July 3, 2001	$700,000	4.00%	2.65%	July 3, 2002
July 3, 2002	325,000	3.00	1.67	July 2, 2003
July 3, 2003	75,000	2.00	0.90	July 6, 2004
July 6, 2004	305,000	1.60	2.47	July 5, 2005

General Obligation Bonds. In 2003 the voters of the District approved a bond proposition authorizing the issuance of $3,700,000 to finance specific construction and modernization projects approved by the voters. The District issued its first series of bonds under this measure on July 8, 2004 in the amount of $2,810,000. As of July 1, 2004, the entire principal amount currently remains outstanding.

Capital Financing Plan

The District has developed a capital financing plan that includes facilities improvement needs of approximately $4.2 million. The District anticipates that the $3 million of authorized general obligation bonds, plus State grants and developer fees that the District has received or expects to receive, will be sufficient to complete all such improvements.

Insurance, Risk Pooling and Joint Powers Arrangements

The District participates in the Northern California Schools Insurance Group (NCSIG), a joint venture under a Joint Powers Agreement among 135 local school districts in Northern California. The District purchases comprehensive general liability and property damage from NCSIG. For property damage, the District has a deductible of $1,000 per occurrence; NCSIG covers damage up to $100,000 via a self-insured retention, purchases excess coverage through Northern California Regional Excess Insurance Fund (NorCal Relief) for coverage of the next $150,000 per occurrence, and purchases excess property insurance in the commercial market to a policy limit of $99,750,000 per occurrence through NorCal ReLiEF. For liability insurance, the District has a deductible of $1,000 per occurrence; NCSIG covers liability up to $150,000 via a self-insured retention, purchases excess general liability coverage through NorCal ReLiEF to a policy limit of $850,000 per occurrence, and purchases additional excess liability coverage to $14,000,000 per occurrence through Schools Excess Liability Fund (SELF). The District purchases workers' compensation coverage at levels required by statute in the commercial market through SIGNAL, another joint powers authority of which the District is a member.

In addition to the above, the District participates in 4 joint powers arrangements with: (1) Northern California Schools Insurance Group for the property and liability insurance for its member school districts; (2) Schools Insurance Group Northern Alliance for the self-insurance plan and system for workers' compensation claims against member public educational agencies; (3) Schools Excess Liability Fund (SELF) for the self-funding and risk management for excess liability for California public educational agencies; and (4) Mendocino County Youth Project for the variety of services to children, youth, and their families throughout the County. The District is not a member of any other joint powers agencies or authorities. The District shares surpluses and deficits of each JPA in proportion to its participation in each. The District's potential liabilities under its arrangement with these JPAs are described in APPENDIX B: "EXCERPTS FROM FINANCIAL STATEMENTS OF THE DISTRICT FOR THE FISCAL YEAR ENDED JUNE 30, 2004", Note 13. The District does not directly bear liability for the losses of other members of NCSIG; however in the event of numerous large local losses, NCSIG's self-insured retention fund could be exhausted, and member districts such as the District could be required to make further contributions to cover member claims.

Charter Schools

There is currently 1 charter school operating in the District. Charter schools receive revenues from the State and from each district in which they operate for each student enrolled in the charter school, and thus effectively reduce revenues available for students enrolled in regular district-operated schools. In addition, each school district is required to accommodate charter school students originating in the district in facilities comparable to those provided to regular district students, for each charter school with enrollment of at least 80 in-district students. The District cannot predict whether or not in the future any charter schools will be formed or commence operation in the District.

CONSTITUTIONAL AND STATUTORY PROVISIONS AFFECTING DISTRICT REVENUES AND APPROPRIATIONS

Limitations on Revenues

Article XIIIA of the California Constitution. Article XIIIA of the State Constitution, adopted and known as Proposition 13, was approved by the voters in June 1978. Section 1(a) of Article XIIIA limits the maximum *ad valorem* tax on real property to 1% of "full cash value," and provides that such tax shall be collected by the counties and apportioned according to State law. Section 1(b) of Article XIIIA provides that the 1% limitation does not apply to *ad valorem* taxes levied to pay interest and redemption charges on (i) indebtedness approved by the voters prior to July 1, 1978, or (ii) bonded indebtedness for the acquisition or improvement of real property approved on or after July 1, 1978, by two-thirds of the votes cast on the proposition, or (iii) bonded indebtedness incurred by a school district or community college district for the construction, reconstruction, rehabilitation or replacement of school facilities or the acquisition or lease of real property for school facilities, approved by 55% of the voters of the district, but only if certain accountability measures are included in the bond proposition. The tax for payment of the District's general obligation bonds falls within the exception for bonds approved by a 55% vote.

Section 2 of Article XIIIA defines "full cash value" to mean the county assessor's valuation of real property as shown on the Fiscal Year 1975-76 tax bill, or, thereafter, the appraised value of real property when purchased, newly constructed, or a change in ownership has occurred. The full cash value may be adjusted annually to reflect inflation at a rate not to exceed 2% per year, or to reflect a reduction in the consumer price index or comparable data for the area under taxing jurisdiction, or may be reduced in the event of declining property value caused by substantial damage, destruction or other factors. Legislation enacted by the State Legislature to implement Article XIIIA provides that, notwithstanding any other law, local agencies may not levy any *ad valorem* property tax except the 1% base tax levied by each County and taxes to pay debt service on indebtedness approved by the voters as described above.

Since its adoption, Article XIIIA has been amended a number of times. These amendments have created a number of exceptions to the requirement that property be reassessed when purchased, newly constructed or a change in ownership has occurred. These exceptions include certain transfers of real property between family members, certain purchases of replacement dwellings for persons over age 55 and by property owners whose original property has been destroyed in a declared disaster, and certain improvements to accommodate disabled persons and for seismic upgrades to property. These amendments have resulted in marginal reductions in the property tax revenues of the District.

Both the California State Supreme Court and the United States Supreme Court have upheld the validity of Article XIIIA.

Section 51 of the Revenue and Taxation Code permits county assessors who have reduced the assessed valuation of a property as a result of natural disasters, economic downturns or other factors, to subsequently "recapture" such value (up to the pre-decline value of the property) at an annual rate higher than 2%, depending on the assessor's measure of the restoration of value of the damaged property. The constitutionality of this procedure was challenged in a lawsuit brought in 2001 in the Orange County Superior Court and in similar lawsuits brought in other counties, on the basis that the decrease in assessed value creates a new “base year value” for purposes of Proposition 13 and that subsequent increases in the assessed value of a property by more than 2% in a single year violate Article XIII A. On appeal, the California Court of Appeal upheld the recapture practice in 2004, and the State Supreme Court declined to review the ruling, leaving the recapture law in place. A drop in assessed valuation would not result in any long-term loss of taxes levied to pay the District’s bonds, but would instead cause the County to raise the rate of *ad valorem* taxes to generate revenues sufficient for the payment of principal of and interest on such bonds.

Article XIIIC and Article XIIID of the California Constitution. On November 5, 1996, the voters of the State approved Proposition 218, the so-called “Right to Vote on Taxes Act”. Proposition 218 added Articles XIIIC and XIIID to the State Constitution, which contain a number of provisions affecting the ability of local agencies, including school districts, to levy and collect both existing and future taxes, assessments, fees and charges. Among other things, Article XIIIC establishes that every tax is either a “general tax” (imposed for general governmental purposes) or a “special tax” (imposed for specific purposes); prohibits special purpose government agencies such as school districts from levying general taxes; and prohibits any local agency from imposing, extending or increasing any special tax beyond its maximum authorized rate without a two-thirds vote. Article XIIIC also provides that no tax may be assessed on property other than *ad valorem* property taxes imposed in accordance with Articles XIII and XIIIA of the California Constitution and special taxes approved by a two-thirds vote under Article XIIIA, Section 4.

Article XIIIC also provides that the initiative power shall not be limited in matters of reducing or repealing local taxes, assessments, fees and charges. The State Constitution and the laws of the State impose a duty on the county treasurer-tax collector to levy a property tax sufficient to pay debt service on school bonds coming due in each year. The initiative power cannot be used to reduce or repeal the authority and obligation to levy such taxes which are pledged as security for payment of the Bonds or to otherwise interfere with performance of the duty of the District and the County with respect to such taxes. Legislation adopted in 1997 provides that Article XIIIC shall not be construed to mean that any owner or beneficial owner of a municipal security assumes the risk of or consents to any initiative measure which would constitute an impairment of contractual rights under the contracts clause of the U.S. Constitution.

Article XIIID deals with assessments and property-related fees and charges. Article XIIID explicitly provides that nothing in Article XIIIC or XIIID shall be construed to affect existing laws relating to the imposition of fees or charges as a condition of property development; however it is not clear whether the initiative power is therefore unavailable to repeal or reduce developer and mitigation fees imposed by the District. Developer fees are neither pledged nor available to pay the Bonds.

The interpretation and application of Proposition 218 will ultimately be determined by the courts with respect to a number of the matters discussed above, and it is not possible at this time to predict with certainty the outcome of such determination.

Expenditures and Appropriations

Article XIIIB of the California Constitution. In addition to the limits Article XIIIA imposes on property taxes that may be collected by local governments, certain other revenues of the State and local governments are subject to an annual “appropriations limit” or “Gann Limit” imposed by Article XIIIB of the State Constitution, which effectively limits the amount of such revenues that government entities are permitted to spend. Article XIIIB, approved by the voters in June 1979, was modified substantially by Proposition 111 in 1990. The appropriations limit of each government entity applies to “proceeds of taxes,” which consist of tax revenues, state subventions and certain other funds, including proceeds from regulatory licenses, user charges or other fees to the extent that such proceeds exceed “the cost reasonably borne by such entity in providing the regulation, product or service.” “Proceeds of taxes” excludes tax refunds and some benefit payments such as unemployment insurance. No limit is imposed on the appropriation of funds which are not “proceeds of taxes,” such as reasonable user charges or fees, and certain other non-tax funds.

Article XIIIB also does not limit appropriation of local revenues to pay debt service on bonds existing or authorized by January 1, 1979, or subsequently authorized by the voters, appropriations required to comply with mandates of courts or the federal government, appropriations for qualified capital outlay projects, and appropriation by the State of revenues derived from any increase in gasoline taxes and motor vehicle weight fees above January 1, 1990, levels. The appropriations limit may also be exceeded in cases of emergency; however, the appropriations limit for the three years following such emergency appropriation must be reduced to the extent by which it was exceeded, unless the emergency arises from civil disturbance or natural disaster declared by the Governor, and the expenditure is approved by two-thirds of the legislative body of the local government.

The State and each local government entity has its own appropriations limit. Each year, the limit is adjusted to allow for changes, if any, in the cost of living, the population of the jurisdiction, and any transfer to or from another government entity of financial responsibility for providing services. Each school district is required to establish an appropriations limit each year. In the event that a school district's revenues exceed its spending limit, the district may increase its appropriations limit to equal its spending by taking appropriations limit from the State.

Proposition 111 requires that each agency's actual appropriations be tested against its limit every two years. If the aggregate "proceeds of taxes" for the preceding two-year period exceeds the aggregate limit, the excess must be returned to the agency's taxpayers through tax rate or fee reductions over the following two years. If the State's aggregate "proceeds of taxes" for the preceding two-year period exceeds the aggregate limit, 50% of the excess is transferred to fund the State's contribution to school and college districts.

In Fiscal Year 2003-04, the District had an appropriations limit of $1,823,663 and estimates an appropriations limit in 2004-05 of $1,823,663.

Future Initiatives. Article XIIIA, Article XIIIB, Article XIIIC, Article XIIID, as well as Propositions 98 and 111, were each adopted as measures that qualified for the ballot pursuant to the State's initiative process. From time to time other initiative measures could be adopted, further affecting District revenues or the District's ability to expend revenues.

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APPENDIX B

EXCERPTS FROM FINANCIAL STATEMENTS OF THE DISTRICT
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

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ARENA UNION ELEMENTARY SCHOOL DISTRICT

ANNUAL FINANCIAL REPORT

JUNE 30, 2004

ROBERTSON, CAHILL & ASSOCIATES, CPAs
A Professional Corporation

ARENA UNION ELEMENTARY SCHOOL DISTRICT
ORGANIZATION
JUNE 30, 2004

The Arena Union Elementary School District (District) was established on July 13, 1885, and is comprised of an area of approximately 250 square miles located on the Mendocino Coast and adjoins the Sonoma County line. There were no changes in the boundaries of the District during the current year. The District currently operates one elementary school. The District also maintains an independent study program. There is a charter school within the District.

GOVERNING BOARD

Name	Office	Term Expires
Mr. William Meyers	President	2007
Ms. Linda Zeni-Andersen	Member	2005
Ms. Alice Combs	Member	2005
Mr. Michael Combs	Member	2005
Mr. Bill Lawson	Member	2007
Ms. Leslie Olson	Member	2007

ADMINISTRATION

Mr. Mark Iacuaniello, Superintendent
Ms. Judy Murray, Business Manager

ADDRESS OF DISTRICT OFFICE

P.O. Box 87
Point Arena, California 95468

ARENA UNION ELEMENTARY SCHOOL DISTRICT
JUNE 30, 2004

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ARENA UNION ELEMENTARY SCHOOL DISTRICT
JUNE 30, 2004

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INDEPENDENT AUDITOR'S REPORT

Board of Education
Arena Union Elementary School District
Point Arena, California

We have audited the accompanying financial statements of the governmental activities each major fund, and the aggregate remaining fund information of the Arena Union Elementary School District (District), as of and for the year ended June 30, 2004, which collectively comprise the District's basic financial statements, as listed in the table of contents. These financial statements are the responsibility of the District's management. Our responsibility is to express an opinion 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; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the State Controller's *Standards and Procedures for Audits of California K-12 Local Educational Agencies*. 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 our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Arena Union Elementary School District as of June 30, 2004, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As described in Note 1, the District has implemented a new financial reporting model, as required by the provisions of GASB Statement No. 34, Basic Financial Statements – and *Management's Discussion and Analysis – for State and Local Governments*, as well as Statement No. 37 "*Basic Financial Statements and Management's Discussion and Analysis – for State and Local Governments Omnibus,*" Statement No. 38 "*Certain Financial Statement Note Disclosures,*" and Statement No. 39 "*Determining Whether Certain Organizations are Component Units* – an amendment of GASB Statement No. 14," as of June 30, 2004.

The Management's Discussion and Analysis on pages 3 through 10 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, consisting 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.

In accordance with *Government Auditing Standards*, we have also issued our report dated February 19, 2005, on our consideration of the District's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Arena Union Elementary School District's basic financial statements. The accompanying financial and statistical information listed in the table of contents, including the Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis and is not a required part of the financial statements of the Arena Union Elementary School District. The other supplementary information listed in the table of contents is not required part of the basic financial statements and is presented for purposes of additional analysis as required by the State Controller's *Standards and Procedures for the Audits of California K-12 Local Educational Agencies*. 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.

Robertson, Cahill & Associates, CPAs

Lakeport, California
February 19, 2005

ARENA UNION ELEMENTARY SCHOOL DISTRICT
Management's Discussion and Analysis
June 30, 2004

INTRODUCTION

Our discussion and analysis of Arena Union Elementary School District (District) financial performance provides an overview of the District's financial activities for the fiscal year ended June 30, 2004. It should be read in conjunction with the District's financial statements, which follow this section.

The Management's Discussion and Analysis (MD&A) is an element of the new reporting model adopted by the Governmental Accounting Standards Board (GASB) in their Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments,* issued June 1999; and GASB Statement No. 37, *Basic Financial Statement – and Management Discussion and Analysis – for State and Local Governments: Omnibus,* an amendment to GASB Statement No. 21 and No. 34, issued in June 2001.

FINANCIAL HIGHLIGHTS

- Total net assets were $2,581,346 at June 30, 2004. This was an increase of $677,706 (36%) over the prior year.
- Overall revenues were $3,712,200, which exceeded expenses of $3,034,494 an increase of $677,706.

OVERVIEW OF FINANCIAL STATEMENTS

This annual report consists of three parts – management's discussion and analysis (this section), the basic financial statements, and required supplementary information. The three sections together provide a comprehensive overview of the District. The basic financial statements are comprised of two kinds of statements that present financial information from different perspectives:

- **Government-wide financial statements**, which comprise the first two statements, provide both short-term and long-term information about the entity's overall financial position.
- **Fund financial statements** focus on reporting the individual parts of the District operations in more detail. The fund financial statements comprise the remaining statements.
    - **Governmental funds** statements tell how general government services were financed in the short term as well as what remains for future spending.
    - **Proprietary fund** statements provide both short and long-term information about the District's internal service (vision insurance) fund.
    - **Fiduciary fund** statements provide both short and long-term information about the Staywell Foundation employee health private purpose expendable trust fund.

The financial statements also include notes that explain some of the information in the statements and provide more detailed data. The basic financial statements are followed by a section of required and other supplementary information that further explain and support the financial statements.

Government-Wide Statements

The government-wide statements report information about the District as a whole using accounting methods similar to those used by private-sector companies. The Statement of Net Assets includes all of the government's assets and liabilities. All of the current year's revenues and expenses are accounted for in the Statement of Activities regardless of when cash is received or paid.

The two government-wide statements report the District's net assets and how they have changed. Net Assets - the difference between the assets and liabilities - is one way to measure the District's financial health or position.

- Over time, increases or decreases in the District's net assets are an indicator of whether its financial health is improving or deteriorating, respectively.
- To assess the overall health of the District, one needs to consider additional non-financial factors such as changes in enrollment, changes in the property tax base, changes in program funding by the Federal and State governments, and condition of facilities.

The government-wide financial statements of the District include government activities. All of the District's basic services are included here, such as regular education, food service, maintenance and general administration. Revenue limit funding and federal and state grants finance most of these activities.

Fund Financial Statements

The fund financial statements provide more detailed information about the District's individual funds- not the District as a whole. Funds are accounting devices that the District uses to keep track of specific sources of funding and spending for particular programs. Some funds are required to be established by State law and by bond covenants. The Board of Trustees establishes other funds to control and manage money for particular purposes or to show that the District is meeting legal responsibilities for using certain revenues. At this time the District maintains three types of funds as described below:

- <u>Governmental funds</u> – Most of the District's basic services are included in governmental funds, which generally focus on (1) how cash and other financial assets that can readily be converted to cash flow in and out and (2) the balances left at year-end that are available for spending. Consequently, the governmental funds statements provide a detailed short-term view that helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the District's programs. Because this information does not encompass the additional long-term focus of the government-wide statements, we provide additional information following the governmental funds statements that explains the relationship (or differences) between them.
- <u>Proprietary fund</u> – The District maintains an internal service fund to account for self-insurance for employee dental and vision insurance. Since the sole purpose of these funds is to service the governmental funds, the net assets are included in the government-wide financial statements. The net change is also reported in the government-wide financial statements; however revenues and expenses are eliminated to prevent duplication.
- <u>Fiduciary fund</u> – The District maintains one private purpose expendable trust fund to account for the Staywell Employee Health Benefit side fund. The fund maintains restricted net assets for vested employee benefits and potentially vested employee benefits.

FINANCIAL ANALYSIS OF THE ENTITY AS A WHOLE

Net Assets

The District's combined net assets were $2,581,346 at June 30, 2004. See Table 1.

Table 1: Net Assets

	Governmental Activities		Percent
	2004	2003	Change
ASSETS			
Cash	$ 1,247,106	(1)	(1)
Other Current Assets	292,492	(1)	(1)
Capital Assets, Net of Accumulated Depreciation	1,238,461	(1)	(1)
TOTAL ASSETS	$ 2,778,059	(1)	(1)
LIABILITIES			
Current Liabilities	$ 188,135	(1)	(1)
Long-Term Liabilities	8,578	(1)	(1)
TOTAL LIABILITIES	$ 196,713	(1)	(1)
NET ASSETS			
Invested in Capital Assets, Net of Related Debt	$ 1,238,461	(1)	(1)
Restricted	856,883	(1)	(1)
Unrestricted	486,002	(1)	(1)
TOTAL NET ASSETS	$ 2,581,346	(1)	(1)

(1) The District did not restate its 2003 financial statements in this first year of implementation of GASB 34. Comparative information will be provided in future years.

Changes in Net Assets

The District's total revenues were $3,712,200. The District received State facility funding comprising 23% of all revenues. The majority of the remaining revenues comes from local property taxes (54%) with State revenue limit sources comprising only .5%; Federal and State grants accounted for 27% and local sources comprised the remaining 18.5%

The total cost of all programs and services was $3,034,494. The District's expenses are predominately related to educating and caring for students (68%). Administrative activities accounted for just 8% of total costs. Plant services, which represents the facilities maintenance and operations costs represents 9% of all costs. Ancillary services, which includes the Student Body, community services, enterprise services and transfers between agencies accounted for 15% of all expenses.

Table 2: Changes in Net Assets

	Governmental Activities		Percent
	2004	2003	Change
REVENUES			
Program Revenues:			
Charges for Services	$ 73,160	(1)	(1)
Operating Grants and Contributions	880,216	(1)	(1)
Capital Grants and Contributions	851,589	(1)	(1)
General Revenues:			
Property Taxes	1,541,326	(1)	(1)
Unrestricted Federal and State Aid	226,646	(1)	(1)
Other Local	139,263	(1)	(1)
TOTAL REVENUES	3,712,200	(1)	(1)
EXPENSES			
Instruction	1,450,340	(1)	(1)
Instruction-Related Services	263,964	(1)	(1)
Pupil Services	355,898	(1)	(1)
General Administration	237,777	(1)	(1)
Plant Services	272,493	(1)	(1)
Ancillary Services	29,085	(1)	(1)
Community Services	52,839	(1)	(1)
Enterprise Services	1,146	(1)	(1)
Transfers Between Agencies	370,952	(1)	(1)
TOTAL EXPENSES	3,034,494	(1)	(1)
NET INCREASE (DECREASE) IN NET ASSETS	$ 677,706	(1)	(1)

(1) The District did not restate its 2003 financial statements in this first year of implementation of GASB 34. Comparative information will be provided in future years.

Governmental Activities

The net cost of all governmental activities this year was $1,229,529.

Table 3 presents the cost of each of the District's functions as well as each function's net cost (total cost less fees generated by the activities and intergovernmental aid). The net cost reflects what was funded by charges for services, operating grants and capital grants and contributions.

Table 3: Net Cost of Governmental Activities

	Total Cost of Services		Net Cost of Services	
	2004	2003	2004	2003
EXPENSES				
Instruction	$ 1,450,340	(1)	$ 93,307	(1)
Instruction-Related Services	263,964	(1)	198,595	(1)
Pupil Services	355,898	(1)	95,079	(1)
General Administration	237,777	(1)	206,418	(1)
Plant Services	272,493	(1)	258,782	(1)
Ancillary Services	29,085	(1)	6,381	(1)
Community Services	52,839	(1)	-	(1)
Enterprise Services	1,146	(1)	15	(1)
Transfers Between Agencies	370,952	(1)	370,952	(1)
TOTAL EXPENSES	$ 3,034,494	(1)	$ 1,229,529	(1)

(1) The District did not restate its 2003 financial statements in this first year of implementation of GASB 34. Comparative information will be provided in future years.

FINANCIAL ANALYSIS OF THE DISTRICT'S FUNDS

The financial performance of the District as a whole is reflected in its governmental funds as well. As the District completed the year, its governmental funds reported a combined fund balance of $1,318,235, a decrease of $97,020, over last year's ending fund balance of $1,415,255. Capital funds increased $134,405 as construction activities carried over into the summer of 2004. Non-capital funds decreased $231,425. This decrease was due to deferred maintenance activities utilizing accumulated resources, the increase in benefit costs and an increase in salary costs due to the negotiated raises. A table showing the District's individual funds and their fund balances at June 30, 2004 in comparison to June 30, 2003 is shown on the following page.

Table 4: Fund Balance Comparison

	Governmental Activities 2004	Governmental Activities 2003	Percent Change
FUNDS			
Governmental:			
General	$ 429,998	$ 628,516	-31.6%
Child Development	75	75	0.0%
Cafeteria Special Revenue	3,138	4,307	-27.1%
Deferred Maintenance	48,580	94,367	-48.5%
Foundation Special Revenue	24,624	9,234	166.7%
Student Body	17,327	18,668	-7.2%
Capital Facilities	162,476	94,114	72.6%
County School Facilities	632,017	565,974	11.7%
Total Governmental	1,318,235	1,415,255	-6.9%
Proprietary:			
Internal Service:			
Vision	33,228	30,288	9.7%
Total Proprietary	33,228	30,288	9.7%
Fiduciary:			
Trust:			
Staywell Foundation	32,540	28,934	12.5%
Total Fiduciary	32,540	28,934	12.5%
TOTAL FUNDS	$ 1,384,003	$ 1,474,477	-6.1%

General Fund Budgetary Highlights

Over the course of the year, the District revises its annual budget to reflect unexpected changes in revenues and expenditures. A schedule of the District's original and final budget amounts compared with actual revenues and expenses is provided in the required supplementary section of the audited financial report.

DIFFERENCES BETWEEN ORIGINAL AND FINAL BUDGET AND ACTUAL AMOUNTS

Education Code Section 1622(a) requires LEA's to adopt their budget for the following school year no later than June 30th of each year, which is prior to adoption of the State Budget. The District's original budget, adopted June, 2003, was based on known and unknown factors, and was adopted as a preliminary planning document. The District follows the budget reporting cycles defined by Education Code and revises their operating budget to reflect changes in revenues and expenses throughout the school year. The differences between the original budget amounts and the actual amounts reflect the many changes that occur during the school year as a result of changing revenues and program needs. The District's General Fund final actual expenditures increased 9% over the adopted budget of $2,546,740.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

At June 30, 2004, the District had invested $1,238,461 net of accumulated depreciation in capital assets, including land, construction in progress and buildings and improvements. See Table 4. More detailed information about the District's capital assets is presented in the notes to the financial statements.

The District completed a state funded modernization project that renovated the multi purpose room, the office, hallways, rooms 6, 7, 8, 11 and 12 and upgraded fire alarms and ADA accessibility through out the campus. The multi purpose room and walkways were re-roofed and a new toilet room was added. Some new paving and fencing were also part of the completed projects.

Table 5: Capital Assets

	Governmental Activities		Percent
	2004	2003	Change
CAPITAL ASSETS			
Land	$ 50,000	$ 50,000	0.0%
Construction in Progress	962,205	176,660	444.7%
Buildings and Improvements	595,409	595,409	0.0%
Accumulated Depreciation	(369,153)	(357,245)	3.3%
NET CAPITAL ASSETS	$ 1,238,461	$ 464,824	166.4%

Although the District did not restate its 2003 financial statements in this first year of implementation of GASB 34, it was necessary to restate capital assets in the preparation of the government-wide statements. The only change on the 2003/2004 year was the accumulation of depreciation expense.

Long-Term Debt

At year-end, the District had $8,578 in long-term debt. This amount represents the District's compensated absences payable.

Table 6: Long-Term Debt

	Governmental Activities		Percent
	2004	2003	Change
LONG-TERM DEBT			
Compensated Absences	$ 8,578	$ 6,727	27.5%
TOTAL LONG-TERM DEBT	$ 8,578	$ 6,727	27.5%

Although the District did not restate its 2003 financial statements in this first year of implementation of GASB 34, the District had previously maintained a schedule of long-term debt which was used in the preparation of the government-wide statements.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

At the time these financial statements were prepared and audited, the District was aware of several circumstances that could affect its future financial health:

- The District is a Basic Aid district, and is therefore not immediately impacted by declines in enrollment, however enrollment figures impact many areas of a District's finances, and is therefore closely monitored. The District's enrollment appears to have stabilized after the establishment of the Charter School.
- The uncertainty of federal and state funding can have a profound impact on the financial health of the District, however no major changes are anticipated in restricted funding streams for the 2004/2005 year.
- The MCOE SELPA and the member LEA must currently meet Maintenance of Effort (MOE) requirements for Special Education Funding. While at this point the district is not having a problem with MOE the SELPA as a whole could fail the MOE in future fiscal years which would mean the loss of federal special education funding for all member districts.
- The continuing increases in premiums for workers' compensation could have a significant effect on the future financial health of the District. The District is working diligently on a workplace safety program in order to reduce workplace injuries, and the ensuing impact on the District's insurance rates. Currently, the District's Health JPA is struggling with a potential increase to the annual cost. The situation is under review and changes are expected. It is still unclear as to the final impact on the District. The PERS rate increased dramatically in the 2003/2004 year.

CONTACTING THE DISTRICT'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, parents, participants, investors and creditors with a general overview of the District's finances and to demonstrate the District's accountability for the money it receives. If you have questions about this report, or need additional financial information, contact Judy Murray at Post Office Box 87, Point Arena, California 95468, (707) 882-2803.

FINANCIAL SECTION

ARENA UNION ELEMENTARY SCHOOL DISTRICT
STATEMENT OF NET ASSETS
JUNE 30, 2004

		Governmental Activities
ASSETS		
Cash in county treasury	$	1,228,569
Cash on hand and in banks		17,327
Cash in revolving fund		1,210
Accounts receivable		292,492
Capital assets:		
Non-depreciable		1,012,205
Depreciable, net of accumulated depreciation		226,256
Total Assets	$	2,778,059
LIABILITIES		
Accounts payable	$	168,633
Deferred revenue		19,502
Long-term debt:		
Due within one year		8,578
Total Liabilities	$	196,713
NET ASSETS		
Invested in capital assets, net of related debt	$	1,238,461
Restricted for:		
Capital projects		794,493
Educational programs		20,439
Other purposes (expendable)		41,951
Unrestricted		486,002
Total Net Assets	$	2,581,346

The accompanying notes are an integral part of these financial statements.

ARENA UNION ELEMENTARY SCHOOL DISTRICT
STATEMENT OF ACTIVITIES
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

		Program Revenues			Net (Expense) Revenue and Changes in Net Assets
Functions	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities
GOVERNMENTAL ACTIVITIES					
Instruction	$ 1,450,340	$ 36,154	$ 469,290	$ 851,589	$ (93,307)
Instruction-related services:					
Supervision of instruction	11,562	218	7,445	-	(3,899)
Instructional library, media and technology	41,092	-	32,711	-	(8,381)
School site administration	209,080	1,190	23,805	-	(184,085)
Other instructional resources	2,230	-	-	-	(2,230)
Pupil services:					
Home-to-school transportation	99,424	-	99,424	-	-
Food services	95,958	8,968	85,836	-	(1,154)
All other pupil services	160,516	1,107	65,484	-	(93,925)
General administration:					
Data processing	22,674	-	765	-	(21,909)
All other general administration	215,103	25,418	5,176	-	(184,509)
Plant services	272,493	-	13,711	-	(258,782)
Ancillary services	29,085	-	22,704	-	(6,381)
Community services	52,839	-	52,839	-	-
Enterprise services	1,146	105	1,026	-	(15)
Transfers between agencies	370,952	-	-	-	(370,952)
Total Governmental Activities	$ 3,034,494	$ 73,160	$ 880,216	$ 851,589	(1,229,529)
GENERAL REVENUES					
Taxes and subventions:					
Property taxes levied for general purposes					1,541,326
Federal and state aid not restricted to specific purposes					226,646
Interest and investment earnings					7,326
Interagency revenues					8,122
Miscellaneous					123,815
Total General Revenues					1,907,235
Change in Net Assets					677,706
Net Assets - Beginning					1,903,640
Net Assets - Ending					$ 2,581,346

The accompanying notes are an integral part of these financial statements.

ARENA UNION ELEMENTARY SCHOOL DISTRICT
GOVERNMENTAL FUNDS
BALANCE SHEET
JUNE 30, 2004

	General Fund	Capital Facilities Fund	County School Facilities Fund	Other Governmental Funds	Total Governmental Funds
ASSETS					
Cash in county treasury	$ 289,604	$ 162,476	$ 693,996	$ 49,265	$ 1,195,341
Cash in banks	-	-	-	17,327	17,327
Cash in revolving fund	1,200	-	-	10	1,210
Accounts receivable	271,659	-	-	20,833	292,492
Due from other funds	849	-	-	9,342	10,191
Total Assets	$ 563,312	$ 162,476	$ 693,996	$ 96,777	$ 1,516,561
LIABILITIES AND FUND BALANCE					
Liabilities:					
Accounts payable	$ 104,386	$ -	$ 61,979	$ 2,268	$ 168,633
Due to other funds	9,426	-	-	765	10,191
Deferred revenue	19,502	-	-	-	19,502
Total Liabilities	133,314	-	61,979	3,033	198,326
Fund Balance:					
Reserved for:					
Cash in revolving fund	1,200	-	-	10	1,210
Unreserved:					
Designated for:					
Economic uncertainties	200,000	-	-	-	200,000
Other	107,268	-	-	41,951	149,219
Undesignated, reported in:					
General fund	121,530	-	-	-	121,530
Special revenue funds	-	-	-	51,783	51,783
Capital project funds	-	162,476	632,017	-	794,493
Total Fund Balance	429,998	162,476	632,017	93,744	1,318,235
Total Liabilities and Fund Balance	$ 563,312	$ 162,476	$ 693,996	$ 96,777	$ 1,516,561

The accompanying notes are an integral part of these financial statements.

ARENA UNION ELEMENTARY SCHOOL DISTRICT
RECONCILIATION OF THE GOVERNMENTAL FUNDS
BALANCE SHEET TO THE STATEMENT OF NET ASSETS
JUNE 30, 2004

Total fund balances - governmental funds	$	1,318,235
Amounts reported for governmental activities in the Statement of Net Assets differ from amounts reported in governmental funds as follows:		
Capital Assets used in governmental activities are not financial resources and, therefore, are not reported in the governmental funds. The historical cost of the capital assets is $1,607,614, and the accumulated depreciation is $369,153.		1,238,461
Long-term liabilities are not due and payable in the current period and, therefore, are not reported as liabilities in the governmental funds. Long-term liabilities, net of unamortized premiums, discounts, and deferred charges, are included in governmental activities in the statement of net assets.		(8,578)
The District uses an internal service fund to charge the costs of certain activities to individual funds. The assets and liabilities of the internal service fund are reported with governmental activities in the statement of net assets.		33,228
Total net assets, governmental activities	$	2,581,346

The accompanying notes are an integral part of these financial statements.

ARENA UNION ELEMENTARY SCHOOL DISTRICT
GOVERNMENTAL FUNDS
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

	General Fund	Capital Facilities Fund	County School Facilities Fund	Other Governmental Funds	Total Governmental Funds
REVENUES					
Revenue limit sources:					
State	$ 14,205	$ -	$ -	$ -	$ 14,205
Local	1,547,536	-	-	-	1,547,536
Federal	329,471	-	-	81,339	410,810
Other state	355,441	-	840,949	18,657	1,215,047
Other local	341,885	80,362	10,639	91,716	524,602
Total revenues	2,588,538	80,362	851,588	191,712	3,712,200
EXPENDITURES					
Instruction	1,421,297	-	-	18,224	1,439,521
Instruction related services:					
Supervision of instruction	11,562	-	-	-	11,562
Instructional library, media, and technology	41,092	-	-	-	41,092
School site administration	209,080	-	-	-	209,080
Other instructional resources	2,230	-	-	-	2,230
Pupil services:					
Home-to-school transportation	99,424	-	-	-	99,424
Food services	-	-	-	95,958	95,958
All other pupil services	158,110	-	-	2,406	160,516
General administration:					
Data processing	22,674	-	-	-	22,674
All other general administration	189,685	-	-	25,418	215,103
Plant services	192,526	12,000	-	67,967	272,493
Facility acquisition and construction	-	-	785,545	-	785,545
Ancillary services	7,115	-	-	21,970	29,085
Community services	52,839	-	-	-	52,839
Enterprise services	-	-	-	1,146	1,146
Transfers between agencies	370,952	-	-	-	370,952
Total expenditures	2,778,586	12,000	785,545	233,089	3,809,220
Excess (deficiency) of revenues over (under) expenditures	(190,048)	68,362	66,043	(41,377)	(97,020)
OTHER FINANCING SOURCES (USES)					
Operating transfers in	-	-	-	8,470	8,470
Operating transfers out	(8,470)	-	-	-	(8,470)
Total other financing sources (uses)	(8,470)	-	-	8,470	-
Excess of revenues and other financing sources over (under) expenditures and other financing sources (uses)	(198,518)	68,362	66,043	(32,907)	(97,020)
Fund Balance - Beginning	628,516	94,114	565,974	126,651	1,415,255
Fund Balance - Ending	$ 429,998	$ 162,476	$ 632,017	$ 93,744	$ 1,318,235

The accompanying notes are an integral part of these financial statements.

ARENA UNION ELEMENTARY SCHOOL DISTRICT
RECONCILIATION OF THE GOVERNMENTAL FUNDS STATEMENT
OF REVENUES, EXPENDITURES, AND CHANGES IN
FUND BALANCES TO THE STATEMENT OF ACTIVITIES
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

Total change in fund balances - governmental funds	$	(97,020)
Amounts reported for governmental activities differ from amounts reported in governmental funds as follows:		
Capital Outlays are reported as expenditures in governmental funds. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount by which capital outlay ($785,545) exceeds depreciation expense (11,908).		773,637
Increases in the liability for compensated absences are not recorded as expenditures in governmental funds because they are not expected to be liquidated with current financial resources. In the statement of activities, compensated absences are recognized as expenses when earned by employees.		(1,851)
The District uses an internal service fund to charge the costs of certain activities to individual funds. The change in net assets of the internal service fund are reported with governmental activities in the statement of net assets.		2,940
Change in net assets of governmental activities	$	677,706

The accompanying notes are an integral part of these financial statements.

ARENA UNION ELEMENTARY SCHOOL DISTRICT
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE – BUDGET AND ACTUAL
GENERAL FUND
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

	Budgeted Amounts		Actual
	Original	Final	Amounts
REVENUES			
Revenue limit sources:			
State	$ 33,327	$ 14,205	$ 14,205
Local	1,375,027	1,547,536	1,547,536
Federal	332,249	329,471	329,471
Other state	350,738	355,441	355,441
Other local	276,818	341,885	341,885
Total Revenues	2,368,159	2,588,538	2,588,538
EXPENDITURES			
Certificated salaries	957,104	1,015,603	1,015,603
Classified salaries	404,916	382,330	382,330
Employee benefits	441,603	514,572	514,572
Books and supplies	87,257	114,122	114,122
Services, other operating expenses	336,943	383,071	383,071
Capital outlay	6,530	-	-
Other outgo	315,717	370,952	370,952
Transfers of indirect/direct support costs	(3,330)	(2,064)	(2,064)
Total Expenditures	2,546,740	2,778,586	2,778,586
Excess (deficiency) of revenues over expenditures before other financing Sources (uses)	(178,581)	(190,048)	(190,048)
OTHER FINANCING SOURCES (USES)			
Transfers out	(1,938)	(8,470)	(8,470)
Total Other Financing Sources (Uses)	(1,938)	(8,470)	(8,470)
Net Increase (Decrease) in Fund Balance	(180,519)	(198,518)	(198,518)
Fund Balance - Beginning	628,516	628,516	628,516
Fund Balance - Ending	$ 447,997	$ 429,998	$ 429,998

The accompanying notes are an integral part of these financial statements.

ARENA UNION ELEMENTARY SCHOOL DISTRICT
STATEMENT OF FUND NET ASSETS
PROPRIETARY FUNDS
JUNE 30, 2004

	Governmental Activities
	Vision Insurance Fund
ASSETS	
Cash in county treasury	$ 33,228
Total Assets	$ 33,228
LIABILITIES	
Total Liabilities	$ -
FUND NET ASSETS	
Undesignated reported in:	
Internal service funds	$ 33,228
Total Fund Net Assets	$ 33,228

The accompanying notes are an integral part of these financial statements.

ARENA UNION ELEMENTARY SCHOOL DISTRICT
STATEMENT OF CHANGES IN FUND NET ASSETS
PROPRIETARY FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

	Governmental Activities
	Vision Insurance Fund
OPERATING REVENUES	
Premium contributions	$ 5,045
Total operating revenues	5,045
OPERATING EXPENSES	
Benefit expense	2,474
Total operating expenses	2,474
Operating income (loss)	2,571
NON-OPERATING REVENUES (EXPENSES)	
Interest income	369
Total non-operating revenue (expenses)	369
Income before contributions and transfers	2,940
Change in Net Assets	2,940
Fund Net Assets - Beginning	30,288
Fund Net Assets - Ending	$ 33,228

The accompanying notes are an integral part of these financial statements.

ARENA UNION ELEMENTARY SCHOOL DISTRICT
STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

	Governmental Activities
	Vision Insurance Fund
CASH FLOWS FROM OPERATING ACTIVITIES	
Payments to/on behalf of employees	$ 5,045
Payments for benefits	(2,474)
Net cash provided (used) by operating activities	2,571
CASH FLOWS FROM INVESTING ACTIVITIES	
Interest on investments	369
Net cash provided (used) by investing activities	369
Net increase (decrease) in cash and cash equivalents	2,940
Cash Balance - Beginning	30,288
Cash Balance - Ending	$ 33,228
Reconciliation of net operating revenues (expenses) to net cash provided (used) by operating activities:	
Operating income (loss)	$ 2,571
Net cash provided (used) by operating activities	$ 2,571

NON CASH TRANSACTIONS
There were no non-cash investing, capital, or financing activities.

ARENA UNION ELEMENTARY SCHOOL DISTRICT
STATEMENT OF FUND NET ASSETS
FIDUCIARY FUNDS
JUNE 30, 2004

	Fiduciary Funds	
	Staywell Foundation Emloyee Health Benefit Expendable Trust Fund	
ASSETS		
Cash in county treasury	$	32,540
Total Assets	$	32,540
LIABILITIES		
Total Liabilities	$	-
FUND NET ASSETS		
Reserved for:		
Vested benefits	$	23,062
Unreserved:		
Designated for:		
Potentially vested benefits		3,822
Undesignated, reported in:		
Expendable trust funds		5,656
Total Fund Net Assets	$	32,540

The accompanying notes are an integral part of these financial statements.

ARENA UNION ELEMENTARY SCHOOL DISTRICT
STATEMENT OF CHANGES IN FUND NET ASSETS
FIDUCIARY FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

	Fiduciary Funds Staywell Foundation Emloyee Health Benefit Expendable Trust Fund
ADDITIONS	
Contributions:	
Premium Contributions	$ 17,001
Interest	325
Total Additions	17,326
DEDUCTIONS	
Services and other operating expenditures	13,720
Total Deductions	13,720
Change in net assets	3,606
Net Assets - Beginning	28,934
Net Assets - Ending	$ 32,540

The accompanying notes are an integral part of these financial statements.

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES

A. Accounting Policies

The Arena Union Elementary School District (District) accounts for its financial transactions in accordance with the policies and procedures of the Department of Education's *California School Accounting Manual.* The accounting policies of the District conform to generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB) and the American Institute of Certified Public Accountants (AICPA).

B. Reporting Entity

The District has reviewed criteria to determine whether other entities with activities that benefit the District should be included within its financial reporting entity. The criteria include, but are not limited to, whether the entity exercises oversight responsibility (which includes financial interdependency, selection of governing authority, designation of management, ability to significantly influence operations, and accountability for fiscal matters), the scope of public service, and a special financing relationship.

The District has determined that no outside entity meets the above criteria, and therefore, no agency has been included as a component unit in the District's basic financial statements. In addition, the District is not aware of any entity that would exercise such oversight responsibility that would result in the District being considered a component unit of that entity.

C. Implementation of New Accounting Pronouncements

For the fiscal year ended June 30, 2004, the District was required to adopt GASB Statement No. 34 (GASB 34), *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments,* GASB Statement No. 37 (GASB 37), *Basic Financial Statements and Management's' Discussion and Analysis for State and Local Governments: Omnibus,* GASB Statement No. 38 (GASB 38), *Certain Financial Statement Note Disclosures,* and GASB Statement No. 39 (GASB 39), *Determining Whether Certain Organizations are Component Units.* GASB 34 significantly changes the way state and local governments report their financial information to the public. As a result of GASB 34, state and local governments are required to report financial information using both fund-based and government-wide financial statement presentations. Fund-based statements continue to use the modified accrual basis of accounting, but the government-wide statement uses full accrual basis of accounting. In addition to the change in the financial statement presentation, GASB 34 requires the reporting of capital assets and long-term obligations on the government-wide financial statements. The preparation of a *Management Discussion and Analysis* to clarify the District's financial activities is also required by GASB 34. Furthermore, the District's notes to the financial statements incorporate modifications as required under GASB 38. The effect of implementing GASB 34 resulted in a conversion of fund balance to net assets for an increase of $1,263,111, for net asset balance of $2,581,346 at June 30, 2004 on the government-wide financial statements.

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES (Continued)

D. Basis of Presentation

Government-wide Financial Statements:

The government-wide financial statements (i.e., the statement of net assets and the statement of changes in net assets) report information on all of the nonfiduciary activities of the District and its component units.

The government-wide statements are prepared using the economic resources measurement focus. This is the same approach used in the preparation of the proprietary fund and fiduciary fund financial statements but differs from the manner in which governmental fund financial statements are prepared. Governmental fund financial statements, therefore, include reconciliations with brief explanations to better identify the relationship between the government-wide statements and the statements for the governmental funds.

The government-wide statement of activities presents a comparison between direct expenses and program revenues for each function or program of the District's governmental activities. Direct expenses are those that are specifically associated with a service, program, or department and are therefore clearly identifiable to a particular function. The District does not allocate indirect expenses to functions in the statement of activities. Program revenues include charges paid by the recipients of goods or services offered by a program, as well as grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues which are not classified as program revenues are presented as general revenues of the District, with certain exceptions. The comparison of direct expenses with program revenues identifies the extent to which each governmental function is self-financing or draws from the general revenues of the District.

Fund Financial Statements:

Fund financial statements report detailed information about the District. The focus of governmental fund financial statements is on major funds rather than reporting funds by type. Each major governmental fund is presented in a separate column, and all non-major funds are aggregated into one column. The Proprietary Fund statements also focus on major funds, with each major proprietary enterprise fund presented in a separate column and all non-major enterprise funds aggregated into one column. Fiduciary Fund statements report on a fund type basis.

The accounting and financial treatment applied to a fund is determined by its measurement focus. All governmental funds are accounted for using a flow of current financial resources measurement focus. With this measurement focus, only current assets and current liabilities are generally included on the balance sheet. The Statement of Revenues, Expenditures, and Changes in Fund Balances for these funds present increases (i.e., revenues and other financing sources) and decreases (i.e., expenditures and other financing uses) in net current assets.

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES (Continued)

All proprietary fund types are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operation of these funds are included on the proprietary fund's Statement of Fund Net Assets. The Statement of Revenues, Expenses, and Changes in Fund Net Assets for proprietary funds presents increases (i.e., revenues) and decreases (i.e. expenditures) in net total assets. The statement of cash flows provides information about how the District finances and meets the cash flow needs of its proprietary activities.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the internal service fund are charges to other funds for self insurance costs. Operating expenses for internal service funds include the costs of insurance premiums and claims related to self-insurance.

Fiduciary funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operation of these funds are included on the fiduciary fund's Statement of Fund Net Assets. The Statement of Changes in Fund Net Assets for fiduciary funds presents additions (i.e. revenues) and deductions (i.e. expenses) in net total assets.

E. Basis of Accounting

Basis of accounting refers to when revenues and expenditures are recognized in the accounts and reported in the financial statements. Government-wide financial statements are prepared using the accrual basis of accounting. Governmental funds use the modified accrual basis of accounting. Proprietary and fiduciary funds use the accrual basis of accounting.

Revenues - Exchange and Non-exchange Transactions:

Revenue resulting from exchange transactions, in which each party gives and receives essentially equal value, is recorded under the accrual basis when the exchange takes place. On a modified accrual basis, revenue is recorded in the fiscal year in which the resources are measurable and become available. "Available" means the resources will be collected within the current fiscal year or are expected to be collected soon enough thereafter to be used to pay liabilities of the current fiscal year.

Non-exchange transactions, in which the District receives value without directly giving equal value in return, include property taxes, grants, and entitlements. Under the accrual basis, revenue from property taxes is recognized in the fiscal year for which the taxes are levied. Revenue from grants and entitlements is recognized in the fiscal year in which all eligibility requirements have been satisfied. Eligibility requirements include timing requirements, which specify the year when the resources are to be used or the fiscal year when use is first permitted; matching requirements, in

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES (Continued)

which the District must provide local resources to be used for a specific purpose; and expenditure requirements, in which the resources are provided to the District on a reimbursement basis. Under the modified accrual basis, revenue from non-exchange transactions must also be available before it can be recognized.

Deferred revenue:

Deferred revenue arises when assets are received before revenue recognition criteria have been satisfied. Grants and entitlements received before eligibility requirements are met are recorded as deferred revenue. On governmental fund financial statements, receivables associated with non-exchange transactions that will not be collected within the availability period have also been recorded as deferred revenue.

Expenses/Expenditures:

On the accrual basis of accounting, expenses are recognized at the time a liability is incurred. On the modified accrual basis of accounting, expenditures are generally recognized in the accounting period in which the related fund liability is incurred, as under the accrual basis of accounting. However, under the modified accrual basis of accounting, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due. Allocations of cost, such as depreciation and amortization, are not recognized in the governmental funds.

When both restricted and unrestricted resources are available for use, it is the District's policy to use restricted resources first, then unrestricted resources as they are needed.

F. Fund Accounting

The accounts of the District are organized on the basis of funds, each of which is considered to be a separate accounting entity. The operations of each fund are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, fund equity or retained earnings, revenues, and expenditures or expenses, as appropriate. District resources are allocated to and accounted for in individual funds based upon the purpose for which they are to be spent and the means by which spending activities are controlled. The District's accounts are organized into major, non-major, proprietary, and fiduciary funds as follows:

Major Governmental Funds:

The *General Fund* is the general operating fund of the District. It is used to account for all financial resources except those required to be accounted for in another find.

The *Capital Facilities Fund* is used to account for resources received from developer impact fees assessed under provisions of the California Environmental Quality Act (CEQA).

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES (Continued)

The *County School Facilities Fund* is also used to account for the accumulation of resources from State Facility Program funding and the expenditures relating to the acquisition, construction, or renovation of approved capital facilities projects.

Non-major Governmental Funds:

Special Revenue Funds are used to account for the proceeds of specific revenue sources that are legally restricted to expenditures for specific purposes. The District maintains the following non-major special revenue fund(s):

1. The Child Development Fund is used to account for resources committed to child development programs maintained by the District.

2. The Cafeteria Fund is used to account for revenues and expenditures associated with the District's food service program.

3. The Deferred Maintenance Fund is used for the purpose of major repair or replacement of District property.

4. The Foundation Fund is used to account for special projects, some of which may be restricted in nature.

5. The Student Body Fund is used to account for the proceeds of Board approved student activities and student body approved expenditures.

Proprietary Funds:

Internal Service Funds are used to account for services rendered on a cost-reimbursement basis with in the District. The District maintains the following internal service fund:

1. The Self-Insurance Fund is used to separate moneys received for vision self-insurance activities from other operating funds of the District. This fund was previously reported as a special revenue type fund, but has been reclassified in the implementation of GASB 34.

Fiduciary Funds:

Fiduciary funds are used to account for resources that are required to be held in trust for individuals, private organizations, other governments and/or other funds. The District maintains the following expendable trust fund:

1. The Staywell Foundation Employee Health Benefit Expendable Trust Fund is used to account for an employee side-benefit fund in which the employee may earn a vested interest. This fund was previously reported as a special revenue type fund, but has been reclassified in the implementation of GASB 34.

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES (Continued)

G. Budgets and Budgetary Accounting

Annual budgets are adopted on a basis consistent with generally accepted accounting principles for all governmental funds. By state law, the District's governing board must adopt a final budget no later than July 1. A public hearing must be conducted to receive comments prior to adoption. The District's governing board satisfied these requirements.

These budgets are revised by the District's governing board and District superintendent during the year to give consideration to unanticipated income and expenditures. The original and final revised budgets are presented for the General Fund in the financial statements.

Formal budgetary integration was employed as a management control device during the year for all budgeted funds. The District employs budget control by minor object and by individual appropriation accounts. Expenditures cannot legally exceed appropriations by major object account.

H. Encumbrances

Encumbrance accounting is used in all budgeted funds to reserve portions of applicable appropriations for which commitments have been made. Encumbrances are recorded for purchase orders, contracts, and other commitments when they are written. Encumbrances are liquidated when the commitments are paid. All encumbrances are liquidated on June 30.

I. Assets, Liabilities, and Equity

1. Deposits and Investments

Cash balances held in banks and in revolving funds are insured to $100,000 by the Federal Deposit Insurance Corporation.

In accordance with *Education Code* Section 41001, the District maintains substantially all of its cash in the County Treasury. The County pools these funds with those of other District's in the county and invests the cash. These pooled funds are carried at cost, which approximates market value. Interest earned is deposited quarterly into participating funds. Any investment losses are proportionately shared by all funds in the pool.

The County is authorized to deposit cash and invest excess funds by California *Government Code* Section 53648 et seq. The funds maintained by the County are either secured by federal depository insurance or are collateralized.

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES (Continued)

2. Stores Inventories and Prepaid Expenditures

Inventories are recorded using the consumption method, in that inventory acquisitions are initially recorded in inventory (asset) accounts, and are charged as expenditures when used. Reported inventories are equally offset by a fund balance reserve, which indicates that these amounts are not "available for appropriation and expenditure" even though they are a component of net current assets.

The District has the option of reporting an expenditure in governmental funds for prepaid items either when purchased or during the benefiting period. The District has chosen to report the expenditure when incurred.

3. Capital Assets

Capital assets are those purchased or acquired with an original cost of $50,000 or more and are reported at historical cost or estimated historical cost. Contributed assets are reported at fair market value as of the date received. Additions, improvements, and other capital outlays that significantly extend the useful life of an asset are capitalized. The costs of normal maintenance and repairs that do not add to the value of the assets or materially extend the asset's lives are not capitalized, but are expensed as incurred. Depreciation on all capital assets is computed using a straight-line basis over the following estimated useful lives (in years):

Land improvements	20
Buildings and improvements	50

4. Deferred Revenue

Cash received for federal and state special projects and programs is recognized as revenue to the extent that qualified expenditures have been incurred. Deferred revenue is recorded to the extent that cash received on specific projects and programs exceeds qualified expenditures.

5. Compensated Absences

All vacation pay is accrued when incurred in the government-wide financial statements. A liability for these amounts is reported in the governmental funds only if they have matured, for example, as a result of employee resignations and retirements.

Accumulated sick leave benefits are not recognized as liabilities of the District. The District's policy is to record sick leave as an operating expense in the period taken, since such benefits do not vest, nor is payment probable; however, unused sick leave is added to the creditable service period for calculation of retirement benefits when the employee retires.

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES (Continued)

6. Long-Term Obligations

In the government-wide financial statements, long-term debt and other long-term obligations are reported as liabilities in the Statement of Net Assets.

7. Fund Balance Reserves and Designations

Reservations of the ending fund balance indicate the portions of fund balance not appropriable for expenditure or amounts legally segregated for a specific future use. The reserve for revolving fund and reserve for stores inventory reflects the portions of fund balance represented by revolving fund cash and stores inventory, respectively. These amounts are not available for appropriation and expenditure at the balance sheet date.

Designations of the ending fund balance indicate tentative plans for financial resource utilization in a future period.

8. Revenue Limit/Property Tax

The District's revenue limit is received from a combination of local property taxes, state apportionments, and other local sources. The County is responsible for assessing, collecting, and apportioning property taxes. Taxes are levied for each fiscal year on taxable real and personal property in the county. The levy is based on the assessed values as of the preceding January 1, which is also the lien date. Property taxes on the secured roll are due on November 1 and February 1, and taxes become delinquent after December 10 and April 10, respectively. Property taxes on the unsecured roll are due on the lien date and become delinquent if unpaid by August 31.

Secured property taxes are recorded as revenue when apportioned, in the fiscal year of the levy. The County apportions secured property tax revenue in accordance with the alternate method of distribution prescribed by Section 4705 of the California *Revenue and Taxation Code*. This alternate method provides for crediting each applicable fund with its total secured taxes upon completion of the secured tax roll, approximately October 1 of each year.

The County Auditor reports the amount of the District's allocated property tax revenue to the California Department of Education. Property taxes are recorded as local revenue limit sources by the District.

The California Department of Education reduces the District's entitlement by the District's local property tax revenue. The balance is paid from the state General Fund, and is known as the State Apportionment.

The District's base revenue limit is the amount of general purpose tax revenue, per average daily attendance (ADA), that the District is entitled to by law. This amount is multiplied by the second period ADA to derive the District's total entitlement.

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES (Continued)

J. Risk Management

The District maintains self-insurance for negotiated employee vision benefits as described in Note 10 and participates in four joint power agreements as described in Note 13 for the various other insurance and risk management needs that have been identified.

NOTE 2. CASH

Cash balances held in banks and in revolving funds are insured up to $100,000 by the Federal Depository Insurance Corporation. All cash held by the financial institutions is fully insured or collateralized.

In accordance with Education Code Section 41001, the District maintains substantially all of its cash in the Mendocino County Treasury. The County pools these funds with those of other District's in the county and invests the cash. These pooled funds are carried at cost that approximates market value. Interest earned is deposited quarterly into participating funds.

NOTE 3. ACCOUNTS RECEIVABLE

Accounts Receivable at June 30, 2004, consists of the following:

	General Fund	All Other Governmental Funds	Total Governmental Funds
Federal	$ 120,077	$ 11,572	$ 131,649
State	56,443	9,261	65,704
Other	95,139	-	95,139
Totals	$ 271,659	$ 20,833	$ 292,492

NOTE 4. INTERFUND TRANSACTIONS AND OTHER TRANSFERS

Interfund transactions are reported either as loans, services provided, reimbursements, or transfers. Loans are reported as interfund receivables and payables, as appropriate, and are subject to elimination upon consolidation. Services provided, deemed to be at market or near market rates, are treated as revenues and expenditures/expenses. Reimbursements occur when one fund incurs a cost, charges the appropriate benefiting fund, and reduces its related cost as a reimbursement. All other interfund transactions are treated as transfers. Transfers among governmental or proprietary finds are netted as part of the reconciliation to the government wide financial statements.

NOTE 4. INTERFUND TRANSACTIONS AND OTHER TRANSFERS (Continued)

Interfund Receivables/Payables (Due From/Due To)

As of June 30, 2004, interfund receivables and payables were as follows:

	Due from Other Funds	Due to Other Funds
General Fund	$ 849	$ 9,426
Other Governmental Funds	9,342	765
Total	$ 10,191	$ 10,191

Interfund Transfers

Interfund transfers consist of nonreciprocal operating movements of net assets from funds receiving revenue to funds through which the resources are to be expended.

	Transfers In	Transfers Out
General Fund	$ -	$ 8,470
Other Governmental Funds	8,470	-
Total	$ 8,470	$ 8,470

NOTE 5. CAPITAL ASSETS

The changes in capital assets for the year ended June 30, 2004, are shown below:

Governmental Activities:	Balance July 1, 2003	Additions	Deductions	Balance June 30, 2004
Capital Assets Not Being Depreciated:				
Land	$ 50,000	$ -	$ -	$ 50,000
Construction in progress	176,660	785,545	-	962,205
Total Capital Assets Not Being Depreciated	226,660	785,545	-	1,012,205
Capital Assets Being Depreciated:				
Buildings and improvements	595,409	-	-	595,409
Total Capital Assets Being Depreciated	595,409	-	-	595,409
Less Accumulated Depreciation for:				
Buildings and improvements	(357,245)	(11,908)	-	(369,153)
Total Accumulated Depreciation	(357,245)	(11,908)	-	(369,153)
Total Capital Assets Being Depreciated, Net	238,164	(11,908)	-	226,256
Total Governmental Activities Capital Assets, Net	$ 464,824	$ 773,637	$ -	$ 1,238,461

The above deductions may include reclassifications of completed construction in progress.

Depreciation expense was charged to governmental activities as follows:

Governmental Activities:	
Instruction	$ 11,908
Total Depreciation Expense	$ 11,908

NOTE 6. COMPENSATED ABSENCES

Accumulated vacation is not accrued in governmental funds. It must be paid to an employee upon termination, but it is generally applied in the year earned or a succeeding year. The estimated value of vacation pay liabilities of $8,578 has been included in the District's financial statements.

Accumulated employee sick leave benefits are not recognized as liabilities of the District, as the rights to these benefits do not vest with the employee. Therefore, sick leave benefits are recorded as expenditures in the period that sick leaves are taken and have not been included in the long-term debt.

NOTE 7. GENERAL LONG-TERM DEBT – SCHEDULE OF CHANGES

A schedule of changes in long-term debt for the year ended June 30, 2004 is shown below:

	Balance July 1, 2003	Additions	Deductions	Balance June 30, 2004
Compensated absences	$ 6,727	$ 1,851	$ -	$ 8,578
Totals	$ 6,727	$ 1,851	$ -	$ 8,578

NOTE 8. STATE AND FEDERAL ALLOWANCES, AWARDS, AND GRANTS

The District has received State and Federal funds for specific purposes that are subject to review and audit by the grantor agencies. Although such audits could generate expenditure disallowances under terms of the grants, it is believed that any required reimbursements will not be material.

NOTE 9. STAYWELL FOUNDATION EMPLOYEE HEALTH EXPENDABLE TRUST FUND

The purpose of the Staywell Foundation Employee Health Expendable Trust Fund is to provide a side fund as a benefit to employees for use in reimbursing eligible medical expenses. The plan establishes a set amount of money per year for each covered employee to be deposited into this fund.

The employee is entitled to have insurance claims paid from his/her portion of the fund. Any fund net assets remaining at the end of the year is credited to the employee's account. The District retains the interest on the fund and pays all operating costs of the fund. When an employee terminates employment, that employee is entitled to the balance in the respective account if he or she meets additional collectively-agreed upon criteria.

The June 30, 2004 fund net assets have been allocated as follows:

Vested benefits that are recorded as a reservation to fund net assets	$ 23,062
Potentially vested - Designated fund net assets	3,822
Undesignated fund net assets	5,656
Total Fund net assets	$ 32,540

The undesignated and potentially vested fund balances are due to interest earned and the amount contributed for terminated employees who terminated prior to the end of the policy year then in force, and 2003/2004 amounts which are scheduled for-transfer to the employees vested balance prior to June 30, 2005.

NOTE 10. VISION SELF-INSURANCE FUND

The District maintains self-insurance for negotiated employee vision benefits. These activities are accounted for in a self-insurance fund, the sole purpose of which is to service the other governmental funds. The assets, liabilities, and net assets of this fund are included in the District's government wide financial statements, however revenues and expenditures are eliminated to prevent duplication. The District made contributions to the fund in the amount of $5,045 during the 2003/2004 year and incurred expenses of $2,474. The ending balance at June 30, 2004 was in the amount of $33,228.

NOTE 11. STUDENT ORGANIZATIONS

The amount reported for student body funds represent the combined totals of all accounts regarding the various student body clubs and activities of all schools within the District. Individual totals, both by school and club, are maintained within the District's accounting system.

The student body clubs often utilize students in off-campus revenue-generating activities that involve cash transactions. These transactions are not subject to adequate internal accounting control prior to deposits being recorded at the individual school sites. It has been determined on a cost benefit basis that providing increased internal control in this area does not justify the additional costs that would be necessary to control receipts prior to the point of deposit.

NOTE 12. INTER-DISTRICT AGREEMENTS

Arena Union Elementary School and Point Arena Joint Union High School District have entered into agreements to share personnel and facilities when feasible. The District Office administration costs are prorated between the Districts based on use.

NOTE 13. JOINT POWERS AGREEMENTS

The District participates in the following four Joint Powers Agreements (JPA):

The Northern California Schools Insurance Group arranges for and provides property and liability insurance for its member School Districts. The District pays a premium commensurate with the level of coverage requested. This is a partial self-insurance program.

The JPA is governed by an Executive Committee consisting of a representative from each member District and County. The Governing Board controls the operations of its JPA independent of any influence by the District beyond the District's representation on the Governing Board.

The JPA is independently accountable for its fiscal matters. The Insurance Group maintains its own accounting records. The budget is not subject to any approval other than that of the Executive Committee.

NOTE 13. JOINT POWERS AGREEMENTS (Continued)

The District also participates in Schools Insurance Group Northern Alliance which is a Joint Powers Authority organized in accordance with Title 1, Division 7, Chapter 5, Article 1 of the California Government Code. The purpose of the organization is to jointly provide for a self-insurance plan and system for workers' compensation claims against the member public educational agencies. The Alliance is under the control and direction of a Board of Directors consisting of representatives of the twenty member Districts.

Member contributions are based on rates established by the Joint Powers Authority's Board of Directors. The Board sets member contribution rates based on actual historical loss experience statistics. Experience modification factors are computed for each member based on the Workers' Compensation Insurance Rating Bureau of California guidelines.

In addition, the District also participates in the Schools Excess Liability Fund (SELF), a State Joint Powers Agency established as a cooperative program of self-funding and risk management for excess liability for California public educational agencies.

District's commit to a three-year participation in SELF, but those withdrawing after three years may be entitled to a partial refund five years after withdrawal, under certain conditions.

Member District's may be required to make additional contributions in the event excess liability claims against SELF exceed available resources.

The Mendocino County Youth Project (MCYP) is a Joint Powers Agency created by schools and cities of Mendocino County to provide a variety of services to children, youth, and their families throughout the County. Services are provided from a network of seven area centers located in Ukiah, Willits, Fort Bragg/Mendocino, Point Arena, Boonville, Laytonville and Covelo.

The relationship between the District and these JPAs is such that none of them are a component unit of the District for financial reporting purposes. Condensed financial information relating to these JPAs is not available.

NOTE 14. CHARTER SCHOOLS

The District granted and approved one Charter School pursuant to Education Code 47605 as follows:

1. The Pacific Community Charter (Charter) was approved in May, 1999 and began operations in August of 1999. The Charter is organized as a non-profit public benefit corporation under IRC Section 501(C)(3). The Charter is governed by an independent board of directors and issues audited financial statements annually. The Charter provides sites-based instruction in grades K-8 to approximately 65 students. The District has determined that the Charter does not meet sufficient criterion for inclusion in the financial reporting entity as a component unit.

NOTE 15. EMPLOYEE RETIREMENT SYSTEMS

Qualified employees are covered under multiple-employer defined benefit pension plans maintained by agencies of the State of California. Certified employees are members of the State Teachers' Retirement System (STRS), and classified employees are members of the California Public Employees' Retirement System (CalPERS).

STRS:

Plan Description and Provisions

The District contributes to the STRS, a cost-sharing multiple-employer public employee retirement system defined benefit pension plan administered by STRS. The plan provides retirement, disability, and survivor benefits to beneficiaries. Benefit provisions are established by state statutes, as legislatively amended, within the State Teachers' Retirement Law. STRS issues a separate comprehensive annual financial report that includes financial statements and required supplementary information. Copies of the STRS annual financial report may be obtained from the STRS, 7667 Folsom Boulevard, Sacramento, California 95826.

Funding Policy

Active plan members are required to contribute 8.0% of their salary and the District is required to contribute an actuarially determined rate. The actuarial methods and assumptions used for determining the rate are those adopted by the STRS Teachers' Retirement Board. The required employer contribution rate for fiscal year 2003/2004 was 8.25% of annual payroll. The contribution requirements of the plan members are established by state statute. The District's contribution to STRS for the fiscal year ending June 30, 2004, 2003, and 2002 were $82,844, $86,709 and $75,445 respectively, and equal 100% of the required contributions for each year.

CalPERS:

Plan Description

The District contributes to the School Employer Pool under the CalPERS, a cost-sharing multiple-employer public employee retirement system defined benefit pension plan administered by CalPERS. The plan provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Benefit provisions are established by State statutes, as legislatively amended, within the Public Employees' Retirement Law. CalPERS issues a separate comprehensive annual financial report that includes financial statements and required supplementary information. Copies of the CalPERS' annual financial report may be obtained from the CalPERS Executive Office, 400 P Street, Sacramento, CA 95814.

NOTE 15. EMPLOYEE RETIREMENT SYSTEMS (Continued)

Funding Policy

Active plan members are required to contribute 7.0% of their salary and the District is required to contribute an actuarially determined rate. The actuarial methods and assumptions used for determining the rate are those adopted by the CalPERS Board of Administration. The required employer contribution rate for fiscal 2003/2004 was 10.42% of annual payroll. The contribution requirements of the plan members are established by State statute. The District's contributions to CalPERS for the fiscal year ending June 30, 2004, 2003 and 2002 were $36,757, $12,402 and $0, respectively and equal 100% of the required contributions for each year.

NOTE 16. CONTINGENT LIABILITIES

As of June 30, 2004, there are no known uninsured material contingent liabilities pending in the District.

NOTE 17. SUBSEQUENT EVENTS

- The District has received State approval for the 2004/2005 school year to submit one budget and one SACS Financial Report in combination with the Point Arena Joint Union High School District with whom they share common Governing Boards and administration.

- During the 2004/2005 year the District was the recipient of proceeds relating to a $2,810,000 general obligation proposition 39 bond. The purpose of the bond is to finance specific construction and modernization projects approved by the voters. Principal payments commence during the 2005/2006 year and continue on a prorate basis until the final payment of $335,000 is made during the 2029/2030 year.

SUPPLEMENTARY INFORMATION SECTION

ARENA UNION ELEMENTARY SCHOOL DISTRICT
OTHER GOVERNMENTAL FUNDS
COMBINING BALANCE SHEET
JUNE 30, 2004

	Special Revenue Funds					
	Child Development	Cafeteria	Deferred Maintenance	Foundation	Student Body	Total Other Governmental
ASSETS						
Cash in county treasury	$ 1	$ (9,235)	$ 33,825	$ 24,674	$ -	$ 49,265
Cash in banks	-	-	-	-	17,327	17,327
Cash in revolving fund	-	10	-	-	-	10
Accounts receivable	-	12,363	8,470	-	-	20,833
Due from other funds	872	-	8,470	-	-	9,342
Total Assets	$ 873	$ 3,138	$ 50,765	$ 24,674	$ 17,327	$ 96,777
LIABILITIES AND FUND BALANCE						
Liabilities:						
Accounts payable	$ 33	$ -	$ 2,185	$ 50	$ -	$ 2,268
Due to other funds	765	-	-	-	-	765
Total Liabilities	798	-	2,185	50	-	3,033
Fund Balance:						
Reserved for:						
Cash in revolving fund	-	10	-	-	-	10
Unreserved:						
Designated for:						
Other	-	-	-	24,624	17,327	41,951
Undesignated, reported in:						
Special revenue funds	75	3,128	48,580	-	-	51,783
Total Fund Balance	75	3,138	48,580	24,624	17,327	93,744
Total Liabilities and Fund Balance	$ 873	$ 3,138	$ 50,765	$ 24,674	$ 17,327	$ 96,777

See accompanying notes to supplementary information.

ARENA UNION ELEMENTARY SCHOOL DISTRICT
OTHER GOVERNMENTAL FUNDS
COMBINING SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

	Special Revenue Funds					
	Child Development	Cafeteria	Deferred Maintenance	Foundation	Student Body	Total Other Governmental
REVENUES						
Federal	$ -	$ 81,339	$ -	$ -	$ -	$ 81,339
Other state	-	5,524	13,133	-	-	18,657
Other local	43,860	8,855	577	17,795	20,629	91,716
Total Revenues	43,860	95,718	13,710	17,795	20,629	191,712
EXPENDITURES						
Certificated salaries	1,488	-	-	-	-	1,488
Classified salaries	26,465	-	-	-	-	26,465
Employee benefits	5,401	-	-	-	-	5,401
Books and supplies	1,930	1,130	12,564	2,355	-	17,979
Services, other operating expenses	6,512	95,757	55,403	50	21,970	179,692
Transfers of indirect/direct support costs	2,064	-	-	-	-	2,064
Total Expenditures	43,860	96,887	67,967	2,405	21,970	233,089
Excess (deficiency) of revenues over expenditures before other financing sources (uses)	-	(1,169)	(54,257)	15,390	(1,341)	(41,377)
OTHER FINANCING SOURCES (USES)						
Transfers in	-	-	8,470	-	-	8,470
Total Other Financing Sources (Uses)	-	-	8,470	-	-	8,470
Net Increase (Decrease) in Fund Balance	-	(1,169)	(45,787)	15,390	(1,341)	(32,907)
Fund Balance - Beginning	75	4,307	94,367	9,234	18,668	126,651
Fund Balance - Ending	$ 75	$ 3,138	$ 48,580	$ 24,624	$ 17,327	$ 93,744

See accompanying notes to supplementary information.

ARENA UNION ELEMENTARY SCHOOL DISTRICT
SCHEDULE OF AVERAGE DAILY ATTENDANCE
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

	Second Period Report	Annual Report
Elementary:		
Kindergarten	14	14
Grades One Through Three	69	68
Grades Four Through Six	82	82
Grades Seven and Eight	44	44
Average Daily Attendance Totals	209	208

	Hours of Attendance
Summer School:	
Elementary	8,138

See accompanying notes to supplementary information.

ARENA UNION ELEMENTARY SCHOOL DISTRICT
SCHEDULE OF INSTRUCTIONAL TIME
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

Grade Level	1986/1987 Minutes Requirement	1982/1983 Actual Minutes	2003/2004 Actual Minutes	Number of Days Traditional Calendar [1]	Status
Kindergarten	36,000	31,500	40,500	180	In Compliance
Grades One Through Three	50,400	47,250	51,100	180	In Compliance
Grades Four Through Five	54,000	47,250	60,620	180	In Compliance
Grades Six Through Eight	54,000	50,750	60,620	180	In Compliance

[1] The District did not utilize a multitrack calendar during the 2003/2004 year.

ARENA UNION ELEMENTARY SCHOOL DISTRICT
SCHEDULE OF FINANCIAL TRENDS AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

General Fund:	(Budgeted) 2004/2005	2003/2004	2002/2003	2001/2002
Revenues and Other Financing Sources	$ 2,522,487	$ 2,588,538	$ 2,788,259	$ 2,795,972
Expenditures	2,575,594	2,778,586	2,572,167	2,381,441
Other Uses and Transfers Out	-	8,470	334,584	295,809
Total Outgo	2,575,594	2,787,056	2,906,751	2,677,250
Change in Fund Balance	(53,107)	(198,518)	(118,492)	118,722
Ending Fund Balance	$ 376,891	$ 429,998	$ 628,516	$ 747,008
Available Reserves	$ 323,360	$ 428,797	$ 627,316	$ 745,808
Designated for Economic Uncertainties	$ 322,160	$ 200,000	$ 200,000	$ 146,257
Undesignated Fund Balance	$ 130,000	$ 121,530	$ 35,758	$ -
Available Reserves as a percentage of Total Outgo	12.6%	15.4%	21.6%	27.9%
Total Long-Term Debt	$ 2,818,578	$ 8,578	$ 6,727	$ 8,448
Average Daily Attendance at P-2	209	209	222	248

The District is in compliance with all State guidelines relative to their available reserve.

See accompanying notes to supplementary information.

ARENA UNION ELEMENTARY SCHOOL DISTRICT
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

Federal Grantor/Pass-Through Grantor/Program or Cluster Title	Federal CFDA Number	Pass-Through Entity Identifying Number	Federal Expenditures
Federal Programs:			
U.S. Department of Education:			
Title I - Part A - Basic Grants Low-Income and Neglected	84.010	****	$ 111,234
Special Ed - Basic Local Assistance Entitlement	84.027	****	45,780
Special Ed - Local Staff Development Grant - Part B - Sec 611	84.027	****	1,526
Title IV - Part A - Drug Free Schools	84.186	****	3,173
Title II - Part A - Teacher Quality	84.367	****	23,073
Title II - Part D - Enhancing Education Through Technology	84.318	****	1,204
Title V - Part A - Innovative Education Strategies	84.298	****	3,112
Title IV - Part B - Rural and Low Income School Program	84.358	****	11,835
Title III - Limited English Proficiency Student Program	84.365	****	52
21st Century After School Program	84.287A	****	59,902
Impact Aid	84.041	****	53,027
Total U.S. Department of Education			318,790
U.S. Department of Health and Human Services:			
Medi-Cal Billing Option	93.778	****	10,681
Total U.S.Department of Health and Human Services			10,681
Department of Agriculture:			
Child Nutrition - School Programs	10.553	****	81,339
Total Department of Agriculture			81,339
Total Federal Categorical Aid Programs			$ 410,810

**** The District does not assign identifying numbers to pass through funds.

See accompanying notes to supplementary information.

ARENA UNION ELEMENTARY SCHOOL DISTRICT
RECONCILIATION OF ANNUAL FINANCIAL AND
BUDGET REPORT (SACS) WITH AUDITED FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

	Capital Assets
June 30, 2004 Annual Financial and Budget Report (SACS)	
Capital Assets	$ -
Adjustments and Reclassifications:	
Capital Assets:	
Land	50,000
Construction in progress	962,205
Buildings and improvements	595,409
Depreciation:	
Buildings and improvements	(369,153)
June 30, 2004 Audited Financial Statement Balance	$ 1,238,461

See accompanying notes to supplementary information.

ARENA UNION ELEMENTARY SCHOOL DISTRICT
EARLY RETIREMENT INCENTIVE PROGRAM
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

Retiree Information

			Retired Employee		Replacement Employee (If Applicable)	
Position Vacated	Age	Service Credit	Salary	Benefits	Salary	Benefits
Behavior Specialist	60	34	$ 62,154	$ 8,540	$ 36,020	$ 4,812
Totals			$ 62,154	$ 8,540	$ 36,020	$ 4,812

As a result of this early retirement incentive program, the District expects to incur additional costs as follows:

Additional Costs	
Retirement costs	$ 36,961
Postemployment health benefit costs	-
Administrative costs	360
Total additional costs	$ 37,321

ARENA UNION ELEMENTARY SCHOOL DISTRICT
SCHEDULE OF CHARTER SCHOOLS
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

Charter School	Status	Included in Audit Report
Pacific Community	Active	No

See accompanying notes to supplementary information.

ARENA UNION ELEMENTARY SCHOOL DISTRICT
NOTES TO SUPPLEMENTARY INFORMATION
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

NOTE 1. PURPOSE OF SCHEDULES

A. Other Governmental Funds Financial Schedules

These schedules provide information on the Arena Union Elementary School District's (District) Governmental non-major funds, by object.

B. Schedule of Average Daily Attendance

Average daily attendance is a measurement of the number of pupils attending classes of the District. The purpose of attendance accounting from a fiscal standpoint is to provide the basis on which apportionments of state funds are made to the District. This schedule provides information regarding the attendance of students at various grade levels and in different programs.

C. Schedule of Instructional Time

Districts must maintain their instructional minutes at either the 1982/1983 actual minutes or the 1986/1987 requirement, whichever is greater, as required by Education Code Section 46201.

The District has received incentive funding for increasing instructional time as provided by the Incentives for Longer Instructional Day. This schedule presents information on the amount of instruction time offered by the district and whether the district complied with the provisions of Education Code Sections 46201 through 46206.

D. Schedule of Financial Trends and Analysis

This schedule discloses the District's financial trends by displaying past years' data along with current year budget information. These financial trend disclosures are used to evaluate the District's ability to continue as a going concern for a reasonable period of time.

E. Schedule of Expenditures of Federal Awards

The California State Controller's Office requires disclosure of the financial activities of all federally funded programs. This schedule was prepared to comply with the state requirements.

F. Reconciliation of Annual Financial and Budget Report (SACS) with Audited Financial Statements

This schedule provides the information necessary to reconcile the fund balances of all funds and the total balances of capital assets and general long-term debt as reported on the SACS to the audited financial statements.

NOTE 1. PURPOSE OF SCHEDULES (Continued)

G. Schedule of Overstated Apportionments

The information in this schedule is presented in accordance with the requirements of the California State Controller's Office. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the general-purpose financial statements. There is no overstatement of apportionment; therefore, this schedule has not been included for 2003/2004.

H. Early Retirement Incentive Program

The District may adopt an early retirement incentive program, pursuant to *Education Code* Sections 22714 and 44929, whereby the service credit to eligible employees is increased by two years. Eligible employees must have five or more years of service under the State Teachers' Retirement System and retire during a period of not more that 120 days or less than 60 days from the date of the formal action taken by the District.

I. Schedule of Charter Schools

This schedule represents a complete listing of all charter schools authorized by the District and indicates whether their financial activities and balances have been included in the District's annual audited financial statements for the fiscal year ended June 30, 2004.

NOTE 2. BASIS OF PRESENTATION

A. Schedule of Expenditures of Federal Awards

The accompanying Schedule of Expenditures of Federal Awards is presented using the modified accrual basis of accounting, which is described in Note 1 to the District's financial statements.

OTHER INDEPENDENT AUDITOR'S REPORTS

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REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

Board of Education
Arena Union Elementary School District
Point Arena, California

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Arena Union Elementary School District (District) as of and for the fiscal year ended June 30, 2004, which collectively comprise the District basic financial statements and have issued our report thereon dated February 19, 2005. 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.

Compliance

As part of obtaining reasonable assurance about whether the District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the District's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions

In planning and performing our audit, we considered the District's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider being reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the District's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying schedule of findings and questioned costs as items 2004-4.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe none of the reportable conditions described above is a material weakness.

This report is intended solely for the information and use of the Governing Board, management, and Federal and State awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than the specified parties.

Robertson, Cahill & Associates, CPAs

Lakeport, California
February 19, 2005

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AUDITOR'S REPORT ON STATE COMPLIANCE

Board of Education
Arena Union Elementary School District
Point Arena, California

We have audited the financial statements of the Arena Union Elementary School District (District) as of and for the year ended June 30, 2004, and have issued our report thereon dated February 19, 2005. Our audit was made in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the State Controller's *Standards and Procedures for Audits of California K-12 Local Educational Agencies*. 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 opinion.

The District's management is responsible for the District's compliance with laws and regulations. In connection with the audit referred to above, we selected and tested transactions and records to determine the District's compliance with the State laws and regulations applicable to the following items:

Description	Procedures in Controller's Audit Guide	Procedures Performed
Attendance Reporting	6	Yes
Kindergarten Continuance	3	Yes
Independent Study	22	No, see below
Continuation Education	10	Not applicable
Adult Education	9	Not applicable
Regional Occupational Centers and Program	6	Not applicable
Instructional Time and Staff Development Reform Program	7	Yes
Instructional Time (School Districts)	4	Yes
Instructional Time (County Offices of Education)	3	Not applicable
Community Day Schools	9	Not applicable
Class Size Reduction General Requirements	7	Yes
Option One	3	Yes
Option Two	4	Not applicable
Districts or Charter Schools with only one school serving K-3	4	Yes
Program to Reduce Class Size in Two Courses in Grade 9 (Morgan-Hart Class Size Reduction Program)	7	Not applicable
Instructional Materials General Requirements	9	Yes
K-8 only	1	Yes
Grades 9-12 only	1	Not applicable
Ratios of Administrative Employees to Teachers	1	Yes
Early Retirement Incentive Program	4	Yes
Gann Limit Calculation	1	Yes

We did not perform testing for independent study because the independent study ADA was under the level that requires testing.

Based on our audit, we found that, for the items tested, the Arena Union Elementary School District complied with the State laws and regulations referred to above, except as described in the Findings and Recommendations section of this report. Further, based on our examination, for items not tested, nothing came to our attention to indicate that the Arena Union Elementary School District had not complied with the State laws and regulations.

This report is intended solely for the information and use of the Governing Board, management, State awarding agencies, and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

Robertson, Cahill & Associates, CPAs

Lakeport, California
February 19, 2005

FINDINGS AND RECOMMENDATIONS SECTION

Financial Statement Findings

2004-1 <u>Longitudinal Budgeting Process / State Code 30000</u>

A. General Background Information

Since 1972 with the Serrano decision and 1978 with Proposition 13 and thereafter, School Districts have had a growing need for longitudinal budgeting, primarily for the following reasons:

(l) Because of the Serrano decision, revenues per ADA are, or eventually will be, more or less equal regardless of historic local spending patterns.

(2) By reason of Proposition 13, property taxes, the traditional method of securing school support, can no longer be raised.

(3) On account of the above two factors, the State has increased its funding role. School Districts, therefore, are no longer as financially independent as they once were, as State funding is far more contingent upon cyclical economic and unpredictable political factors than local. Cyclical economic conditions often result in unbudgeted deficit factors being applied to final State apportionments, while political factors can create mandated programs without providing an adequate or continuing funding base for such programs.

B. Meaning of "Longitudinal Budgeting"

In its most common interpretation, the budgeting capacity could be defined as a District's ability to meet current obligations as they become due. However, this is primarily a short-term emergency oriented explanation. A long-term or chronic budgeting problem can exist if a District has not internally developed the capacity or systems that will enable it to become aware that a potential short-term crisis may suddenly develop. This is particularly true in public education because while revenues are not always predictable, the bulk of school expenditures are often committed very early in the school year.

At the conclusion of the 2003/2004 school term, a State study indicated that several School Districts were in a financial status such that a going concern problem had arisen.

2004-1 Longitudinal Budgeting Process / State Code 30000 (continued)

C. Audit Procedures

In such an environment, it is particularly desirable for school boards and District administrative personnel to conduct periodic internal assessments of the District's longitudinal budgeting capacity.

Taking the above factors into consideration, we decided to review the District's previous longitudinal budgeting process and to inform the school board and administration of the results of this review in the following three specific areas:

(1) The audited General Fund balance was examined for the past eight years, and a trend analysis schedule was developed.

(2) The Average Daily Attendance (ADA) for the past eight years, which is the major source of school funding, was similarly scheduled with particular attention being paid to the impact of declining enrollment.

(3) The total of year-end unrestricted cash reserves was compared to one month's average expenditures, and the audited year-end General Fund balance was compared to the subsequent year's General Fund budget.

The results of these procedures are as follows:

Fund Balance

June 30	Fund Balance
1997	$ 115,455
1998	237,499
1999	273,630
2000	418,031
2001	628,286
2002	747,008
2003	628,516
2004	429,998

The District's available balance declined to approximate the 2000 year fund balance.

2004-1 Longitudinal Budgeting Process / State Code 30000 (continued)

Average Daily Attendance

June 30	P2-ADA
1997	337
1998	330
1999	299
2000	254
2001	254
2002	248
2003	222
2004	209

Average daily attendance has declined by 128 ADA during the period under review.

Cash Balance

Cash June 30, 2004	Average Cash Outlay One Month 2003/2004 Year
$ 290,804	$ 232,255

Cash availability at the 2003/2004 year end was approximately equal to thirty-eight days of average cash outlay.

Fund Balance

Fund Balance June 30, 2004	Budgeted General Fund Total Outlay 2004/2005
$ 429,998	$ 2,575,594

The year-end available fund balance was approximately equal to two months of budgeted total outlay for the ensuing period.

2004-1 Longitudinal Budgeting Process / State Code 30000 (continued)

Conclusion and Recommendation

In the past, the District has been able to utilize its budget as an information tool that enables it to exercise the restraint necessary to maintain a viable fund balance; and it should especially continue to do so until the current State and general economic climate with its potential impact on school funding has been clarified.

District Response and Action Plan

We are continuing to monitor our ending balance to ensure that it does not decline below Board established levels.

2004-2 GASB 34 Financial Reporting Model / State Code 30000

The Governmental Accounting Standards Board (GASB) has issued a new accounting and reporting standard, GASB 34, which has been incorporated into the California School District reporting model. GASB 34 represents the most fundamental change in governmental accounting ever in that the new statements encompass full accrual accounting including depreciation of fixed assets, and the recognition of long-term debt as a liability within the statements. While the governmental fund type, modified accrual basis statements have not been completely abandoned, there are significant reporting changes augmented by a reconciliation between the modified accrual basis and the full accrual basis reports.

At the District the GASB34 financial statements represent the consolidated activities of all governmental activities conducted, which has meant that the District has had to redefine, for reporting purposes, certain funds that were previously classified as internal service type activities. This accounting was performed manually as the funds have not yet been redefined in the State Standardized Account Code Structure (SACS) in use at the District Office.

The year-end conversion process from the modified accrual basis to the full accrual basis required in the government-wide statements would be facilitated by reclassifying the Staywell Foundation Employee Health Fund as a Fiduciary, Expendable Trust type fund within the Standard Account Code Structure. This fund is currently classified as an internal service type fund that consolidates with the District's Self Insurance Fund for Vision benefits to report a combined total in the SACS reporting system.

The year-end conversion process from the modified accrual basis to the full accrual basis required in the government-wide statements would be further facilitated by the development of additional reviews of the fund accounting being performed. For example, a regular review and reconciliation of the amounts expended to object codes in the 6000 series and to function 8500 against the additions to capital assets would greatly enhance the ease with which this conversion can be made.

Recommendation

Additional accounting procedures as described above, including the redefinition of the SACS fund structure utilized at the District, should be developed in order to facilitate the conversion of the District's financial data from a modified accrual, fund accounting basis to a full accrual, government-wide basis.

District Response and Action Plan

We intend to fully implement this recommendation.

2004-3 Internal Controls – Student Body Accounting / State Code 30000

The District maintains an Associated Student Body that generates local revenues and contributions that are deposited to and disbursed from a local bank account. These amounts must then be compiled for inclusion in the District's annual financial statements.

In the past, prior to the implementation of the GASB 34 financial reporting model, the Student Body financial statements were not included in the SACS financial reporting system. The implementation of GASB 34, however, requires the District to aggregate all governmental fund activities and make additional accrual entries in order to provide government-wide reporting. The Student Body financial statements therefore have become an integral part of the Districts financial reporting system.

Recommendation

Prior to the submission of the unaudited financial data (SACS) to the Department of Education in September of each year, the District should consider recording the transactions and balances associated with the Associated Student Body account in such a manner that they are included with the SACS reporting system.

District Response and Action Plan

We intend to implement this recommendation.

2004-4 Internal Controls – Expenditure Reimbursements / State Code 30000

Internal Controls over expenditure reimbursements relating to administrative personnel are strengthened whenever two administrative approvals are required prior to processing. At the District a few such reimbursements were processed with only one approval.

Recommendation

While we were able to determine that all such expenditures were proper, two administration approvals should be required prior to processing administrative personnel reimbursements.

District Response and Action Plan

This recommendation has been implemented.

Federal Award Findings and Questioned Costs

There were no findings or questioned costs relative to federal awards or programs.

State Award Findings and Questioned Costs

There were no findings or questioned costs relative to State awards or programs.

ARENA UNION ELEMENTARY SCHOOL DISTRICT
CORRECTIVE ACTION PLAN
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

A Corrective Action Plan is not available and has not been submitted with the audited financial statements. If required, the District will prepare its Corrective Action Plan and will submit it to all recipients of the audit report within sixty days of the issue date of the report.

ARENA UNION ELEMENTARY SCHOOL DISTRICT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

Finding/Recommendation	Current Status	District Explanation, If Not Implemented
1. The District should provide GASB 34 implementation training.	Implemented	
2. The District should set a capitalization threshold consistent with GASB 34.	Implemented	
3. The District should maintain an adequate fund balance.	Implemented	
4. The District should update its fixed asset accounting records.	Implemented	

APPENDIX C

PROPOSED FORM OF OPINION OF BOND COUNSEL

[Delivery Date]

Board of Trustees
Arena Union Elementary School District
Point Arena, California

Arena Union Elementary School District
General Obligation Bonds, Election of 2003, Series 2005
(Final Opinion)

Ladies and Gentlemen:

We have acted as bond counsel in connection with the issuance by the County of Mendocino, California (the "County"), on behalf of the Arena Union Elementary School District (the "District"), which is located in the County, of $889,062.35 aggregate principal amount of bonds designated as "Arena Union Elementary School District General Obligation Bonds, Election of 2003, Series 2005" (the "Bonds"). The Bonds are issued under and pursuant to a resolution of the Board of Trustees of the District adopted on May 19, 2005 (the "Resolution").

In such connection, we have reviewed the Resolution, the tax certificate of the District dated the date hereof (the "Tax Certificate"), certificates of the District, the County, and others, and such other documents and matters to the extent we deemed necessary to render the opinions set forth herein.

Certain agreements, requirements and procedures contained or referred to in the Resolution, the Tax Certificate and other relevant documents may be changed and certain actions (including, without limitation, the defeasance of Bonds) may be taken or omitted under the circumstances and subject to the terms and conditions set forth in such documents. No opinion is expressed herein as to any Bond or the interest thereon if any such change occurs or action is taken or omitted upon the advice or approval of counsel other than ourselves.

The opinions expressed herein are based on an analysis of existing laws, regulations, rulings and court decisions and cover certain matters not directly addressed by such authorities. Such opinions may be affected by actions taken or omitted or events occurring after the date hereof. We have not undertaken to determine, or to inform any person, whether any such actions are taken or omitted or events do occur or any other matters come to our attention after the date hereof. Our engagement with respect to the Bonds has concluded with their issuance, and we disclaim any obligation to update this letter. We have assumed the genuineness of all documents and signatures presented to us (whether as originals or as copies) and the due and legal execution and delivery thereof by, and validity against, any parties other than the District and the County. We have assumed, without undertaking to verify, the accuracy of the factual matters represented, warranted or certified in the documents referred to in the second paragraph hereof. Furthermore, we have assumed compliance with all covenants and agreements contained in the Resolution and the Tax Certificate, including (without limitation) covenants and agreements compliance with which is necessary to ensure that future actions, omissions or events will not cause interest on the Bonds to be included in gross income for federal income tax purposes. We call attention to the fact that the rights and obligations under the Bonds, the Resolution and the Tax Certificate and their enforceability may be subject to bankruptcy, insolvency, reorganization, arrangement, fraudulent conveyance, moratorium and other laws relating to or affecting creditors' rights, to the application of equitable principles, to the exercise of judicial discretion in appropriate cases and to the limitations on legal remedies against school districts or counties in the State of California. We express no opinion with respect to any indemnification, contribution, penalty, choice of law, choice of forum, waiver or severability provisions contained in the documents mentioned in the preceding sentence. Finally, we undertake no responsibility for the accuracy, completeness or fairness of the Official Statement or other offering materials relating to the Bonds and express no opinion with respect thereto.

Based on and subject to the foregoing and in reliance thereon, as of the date hereof, we are of the following opinions:

1. The Bonds constitute valid and binding obligations of the District.

2. The Resolution has been duly and legally adopted and constitutes a valid and binding obligation of the District.

3. The Board of Supervisors of the County has power and is obligated to levy ad valorem taxes without limitation as to rate or amount upon all property within the District's boundaries subject to taxation by the District (except certain personal property which is taxable at limited rates) for the payment of the Bonds and the interest thereon.

4. Interest on the Bonds is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986 and is exempt from State of California personal income taxes. Interest on the Bonds is not a specific preference item for purposes of the federal individual or corporate alternative minimum taxes, although we observe that interest on the Bonds is included in adjusted current earnings in calculating corporate alternative minimum taxable income. We express no opinion regarding any other tax consequences related to the ownership or disposition of, or the accrual or receipt of interest on, the Bonds.

Faithfully yours,

ORRICK, HERRINGTON & SUTCLIFFE LLP

per

APPENDIX D

FORM OF CONTINUING DISCLOSURE CERTIFICATE

This Continuing Disclosure Certificate (the "Disclosure Certificate") is executed and delivered by the Arena Union Elementary School District (the "District") in connection with the issuance of $889,062.35 aggregate initial principal (denominational) amount of Arena Union Elementary School District General Obligation Bonds, Election of 2003, Series 2005 (the "Bonds"). The Bonds are being issued pursuant to a resolution (the "Resolution") adopted by the Board of Trustees of the District by its resolution adopted on May 19, 2005. The District covenants and agrees as follows:

SECTION 1. Purpose of the Disclosure Certificate. This Disclosure Certificate is being executed and delivered by the District for the benefit of the Holders and Beneficial Owners of the Bonds and in order to assist the Participating Underwriters in complying with Securities and Exchange Commission ("S.E.C.") Rule 15c2-12(b)(5).

The District is not an obligated person with respect to more than $10,000,000 in aggregate principal amount of outstanding municipal securities, including the Bonds. The offering of the Bonds is therefore exempt from S.E.C. Rule 15c2-12(b)(5) pursuant to Section (d)(2) of said Rule.

SECTION 2. Definitions. In addition to the definitions set forth in the Resolution, which apply to any capitalized term used in this Disclosure Certificate unless otherwise defined in this Section, the following capitalized terms shall have the following meanings:

"Annual Report" shall mean any Annual Report provided by the District pursuant to, and as described in, Sections 3 and 4 of this Disclosure Certificate.

"Beneficial Owner" shall mean any person which has or shares the power, directly or indirectly, to make investment decisions concerning ownership of any Bonds (including persons holding Bonds through nominees, depositories or other intermediaries).

"Dissemination Agent" shall mean the District, or any successor Dissemination Agent designated in writing by the District and which has filed with the District a written acceptance of such designation.

"Holder" shall mean the person in whose name any Bond shall be registered.

"Listed Events" shall mean any of the events listed in Section 5(a) of this Disclosure Certificate.

"National Repository" shall mean any Nationally Recognized Municipal Securities Information Repository for purposes of the Rule. The National Repositories currently approved by the Securities and Exchange Commission are set forth at http://www.sec.gov/info/municipal/nrmsir.htm.

"Participating Underwriter" shall mean any of the original underwriters of the Bonds required to comply with the Rule in connection with offering of the Bonds.

"Repository" shall mean each National Repository and the State Repository.

"Rule" shall mean Rule 15c2-12(b)(5) adopted by the Securities and Exchange Commission under the Securities Exchange Act of 1934, as the same may be amended from time to time.

"State Repository" shall mean any public or private repository or entity designated by the State of California as the state repository for the purpose of the Rule and recognized as such by the Securities and Exchange Commission, as listed at http://www.sec.gov/info/municipal/nrmsir.htm.

SECTION 3. Provision of Annual Reports.

(a) The District shall, or shall cause the Dissemination Agent to, not later than nine months after the end of the District's fiscal year (currently ending June 30), commencing with the report for the 2004-05 Fiscal Year (which is due no later than April 1, 2006, provide to any person upon written request an Annual Report which is consistent with the requirements of Section 4 of this Disclosure Certificate. The Annual Report may be submitted as a single document or as separate documents comprising a package, and may cross-reference other information as provided in Section 4 of this Disclosure Certificate. If the District's fiscal year changes, it shall give notice of such change in the same manner as for a Listed Event under Section 5(c).

Written request shall be made to:
Arena Union Elementary School District
45 Lake Street
Point Arena, CA 95468
Attn: Superintendent
Tel: (707) 882-2803

SECTION 4. Content of Annual Reports. The District's Annual Report shall contain or include by reference the following:

* Audited financial statements of the District for the preceding fiscal year, prepared in accordance with the laws of the State of California and including all statements and information prescribed for inclusion therein by the Controller of the State of California. If the District's audited financial statements are not available by the time the Annual Report is required to be made available pursuant to Section 3(a), the Annual Report shall contain unaudited financial statements in a format similar to the financial statements contained in the final Official Statement, and the audited financial statements shall be made available in the same manner as the Annual Report when they become available.

Any or all of the items listed above may be included by specific reference to other documents, including official statements of debt issues of the District or related public entities, which have been submitted to each of the Repositories or the S.E.C.. If the document included by reference is a final official statement, it must be available from the Municipal Securities Rulemaking Board. The District shall clearly identify each such other document so included by reference.

SECTION 5. Reporting of Significant Events.

(a) Pursuant to the provisions of this Section 5, the District shall give, or cause to be given, notice of the occurrence of any of the following events with respect to the Bonds, if material:

1. Principal and interest payment delinquencies;

2. Non-payment related defaults;

3. Unscheduled draws on debt service reserves reflecting financial difficulties;

4. Unscheduled draws on credit enhancements reflecting financial difficulties;

5. Substitution of credit or liquidity providers, or their failure to perform;

6. Adverse tax opinions or events affecting the tax-exempt status of the Bonds;

7. Modifications to rights of Bond holders;

8. Optional, unscheduled or contingent Bond calls;

9. Defeasances;

10. Release, substitution, or sale of property securing repayment of the Bonds;

11. Rating changes.

(b) Whenever the District obtains knowledge of the occurrence of a Listed Event, the District shall as soon as possible determine if such event would be material under applicable federal securities laws.

(c) If the District determines that knowledge of the occurrence of a Listed Event would be material under applicable federal securities laws, the District shall promptly file a notice of such occurrence with each National Repository or with the Municipal Securities Rulemaking Board, and with the State Repository. Notwithstanding the foregoing, notice of Listed Events described in subsections (a)(4) and (5) need not be given under this subsection any earlier than the notice (if any) of the underlying event is given to Holders of affected Bonds pursuant to the Resolution.

SECTION 6. Electronic Filing. Submission of Annual Reports and notices of Listed Events to DisclosureUSA.org or another "Central Post Office" designated and accepted by the S.E.C. shall constitute compliance with the requirement of filing such reports and notices with each National Repository and any State Repository hereunder.

SECTION 7. Termination of Reporting Obligation. The District's obligations under this Disclosure Certificate shall terminate upon the legal defeasance, prior redemption or payment in full of all of the Bonds. If such termination occurs prior to the final maturity of the Bonds, the District shall give notice of such termination in the same manner as for a Listed Event under Section 5(c).

SECTION 8. Dissemination Agent. The District may, from time to time, appoint or engage a Dissemination Agent to assist it in carrying out its obligations under this Disclosure Certificate, and may discharge any such Agent, with or without appointing a successor Dissemination Agent. The Dissemination Agent shall not be responsible in any manner for the content of any notice or report prepared by the District pursuant to this Disclosure Certificate. The initial Dissemination Agent shall be the District.

SECTION 9. Amendment; Waiver. Notwithstanding any other provision of this Disclosure Certificate, the District may amend this Disclosure Certificate, and any provision of this Disclosure Certificate may be waived, provided that the following conditions are satisfied:

(a) If the amendment or waiver relates to the provisions of Sections 3(a), 4, or 5(a), it may only be made in connection with a change in circumstances that arises from a change in legal requirements, change in law, or change in the identity, nature or status of an obligated person with respect to the Bonds, or the type of business conducted;

(b) The undertaking, as amended or taking into account such waiver, would, in the opinion of nationally recognized bond counsel, have complied with the requirements of the Rule at the time of the original issuance of the Bonds, after taking into account any amendments or interpretations of the Rule, as well as any change in circumstances; and

(c) The amendment or waiver either (i) is approved by the Holders of the Bonds in the same manner as provided in the Resolution for amendments to the Resolution with the consent of Holders, or (ii) does not, in the opinion of nationally recognized bond counsel, materially impair the interests of the Holders or Beneficial Owners of the Bonds.

In the event of any amendment or waiver of a provision of this Disclosure Certificate, the District shall describe such amendment in the next Annual Report, and shall include, as applicable, a narrative explanation of the reason for the amendment or waiver and its impact on the type (or in the case of a change of accounting principles, on the presentation) of financial information or operating data being presented by the District. In addition, if the amendment relates to the accounting principles to be followed in preparing financial statements, (i) notice of such change shall be given in the same manner as for a Listed Event under Section 5(c), and (ii) the Annual Report for the year in which the change is made should present a comparison (in narrative form and also, if feasible, in quantitative form) between the financial statements as prepared on the basis of the new accounting principles and those prepared on the basis of the former accounting principles.

SECTION 10. Additional Information. Nothing in this Disclosure Certificate shall be deemed to prevent the District from disseminating any other information, using the means of dissemination set forth in this Disclosure Certificate or any other means of communication, or including any other information in any Annual Report or notice of occurrence of a Listed Event, in addition to that which is required by this Disclosure Certificate. If the District chooses to include any information in any Annual Report or notice of occurrence of a Listed Event in addition to that which is specifically required by this Disclosure Certificate, the District shall have no obligation under this Certificate to update such information or include it in any future Annual Report or notice of occurrence of a Listed Event.

SECTION 11. Default. In the event of a failure of the District to comply with any provision of this Disclosure Certificate any Holder or Beneficial Owner of the Bonds may take such actions as may be necessary and appropriate, including seeking mandate or specific performance by court order, to cause the District to comply with its obligations under this Disclosure Certificate; provided, that any such action may be instituted only in Superior Court of the State of California in and for the County of Mendocino or in U.S. District Court in or nearest to the County. A default under this Disclosure Certificate shall not be deemed an Event of Default under the Resolution, and the sole remedy under this Disclosure Certificate in the event of any failure of the District to comply with this Disclosure Certificate shall be an action to compel performance.

SECTION 12. Beneficiaries. This Disclosure Certificate shall inure solely to the benefit of the District, the Dissemination Agent, the Participating Underwriters and Holders and Beneficial Owners from time to time of the Bonds, and shall create no rights in any other person or entity.

Date: ______________.

ARENA UNION ELEMENTARY SCHOOL DISTRICT

By ____
Superintendent

CONTINUING DISCLOSURE EXHIBIT A

FORM OF NOTICE TO REPOSITORIES OF FAILURE TO FILE ANNUAL REPORT

Name of District:	ARENA UNION ELEMENTARY SCHOOL DISTRICT
Name of Bond Issue:	ARENA UNION ELEMENTARY SCHOOL DISTRICT GENERAL OBLIGATION BONDS, ELECTION OF 2003, SERIES 2005
Date of Issuance:	______________

NOTICE IS HEREBY GIVEN that the District has not provided an Annual Report with respect to the above-named Bonds as required by Section 4 of the Continuing Disclosure Certificate of the District, dated the Date of Issuance. [The District anticipates that the Annual Report will be filed by _____________.]

Dated:_______________

ARENA UNION ELEMENTARY SCHOOL DISTRICT

By ____________[to be signed only if filed]___________

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APPENDIX E

MENDOCINO COUNTY
INVESTMENT POLICIES AND PRACTICES

DESCRIPTION OF INVESTMENT POOL

The following information has been furnished by the Office of the Treasurer-Tax Collector, County of Mendocino. It describes (i) the policies applicable to investment of District funds, including bond proceeds and tax levies, and funds of other agencies held by the County Treasurer and (ii) the composition, carrying amount, market value and other information relating to the investment pool. Further information may be obtained directly from the Treasurer-Tax Collector, 501 Low Gap Road, Ukiah, CA 95482, phone number (707) 463-4321.

MENDOCINO COUNTY
STATEMENT OF INVESTMENT POLICY

March, 2005

As designated by the Board of Supervisors under the laws of the State of California, it is the responsibility of the County Treasurer, to secure and protect the public funds of the County, and to establish proper safeguards, controls, and procedures to maintain these funds in a lawful, rational and auspicious manner. Said maintenance shall include the prudent and secure investment of those funds that are not immediately required for daily operations, in a manner anticipated to provide additional benefit to the people of the County of Mendocino. In addition, the County Treasurer acts as the Treasurer, cash manager, and investor for a sizable number of public agencies within the County, instead of each entity having to locate and hire a knowledgeable person to handle the entity's banking, investments and other financial duties separately. This pooling of public funds not only eliminates duplication of jobs, but also smoothes out cash flow differences, permits cost savings through higher volume, and attracts more professional service providers.

This Statement of Investment Policy will be provided annually for review by a sitting Treasury Oversight Committee and the approval of the Board of Supervisors after discussion in an open public meeting. Upon request, it will also be provided to participants in the County Investment Pool; to securities dealers, banks and brokers, currently approved for conducting investment transactions with the County Treasurer's office in the ongoing effort to manage the excess cash portfolio; to other involved persons or entities; and to any member of the electorate wishing to review this document. The Treasurer reserves the right to provide these documents on a cost basis.

SCOPE

This Statement of Investment Policy pertains to those temporarily surplus funds under the control of the Treasurer, designated for the daily ongoing operations of the County and pool participants; and concerns the deposit, maintenance, and safekeeping of all such funds, and the investments made with these funds. This Policy does not apply to pension moneys, delayed compensation funds, trustee, and certain other non-operating funds not participating in the County Investment Pool. Percentage limitations noted within this Policy shall apply to all money considered to be within the County Investment Pool. Any investments existing outside the Pool shall be subject to the local agency's individual percentages.

PURPOSE OF POLICY STATEMENT

The purpose of this Statement of Investment Policy is to provide the Board of Supervisors, a Treasury Oversight Committee, those entities invested in the County Investment Pool, those involved in servicing the investment requirements of the County, and any other interested party, a clear understanding of the regulations and internal guidelines that will be observed in maintaining and investing those pooled funds to not be required for immediate cash flow needs.

TREASURY OBJECTIVES

The primary and overriding objective of the Treasurer is to protect the safety of the principal of the Investment Pool through the judicious purchase of those legal investments permitted to local agencies, as defined in the State of California Government Codes, consistent with current conditions and the other dominant objectives pursuant to managing a local agency portfolio, namely:

Safety: It is the primary responsibility of the Treasurer to maintain the safe return of all principal placed in investments by avoiding decisions that might result in losses through either fraud, default, or adverse market conditions. Import is also accorded the protection of accrued interest earned on any investment instrument.

Liquidity: It is imperative that a vast majority of all investments be in items that are immediately negotiable, as the portfolio is a cash management fund. It shall always be assumed that all investments could require immediate liquidation in order to meet unexpected cash calls.

Availability: Due to the nature of a public funds portfolio, it is mandatory that moneys be available to meet the monetary requirements inherent to operating a public entity. Thus funds need to be invested in such a manner that money will always be available, without risk of trading loss, to pay normal cash requirements. A vast majority of the moneys invested by the Treasurer should never require the realization of immoderate losses should a unforeseen cash demand require the sale of investments prior to maturity. A sufficient portion of all funds shall be invested in securities providing a high degree of availability, that is, in securities easily sold or converted to cash in a timely manner, with little or no loss of interest earnings.

Yield: While it is considered desirable to obtain a yield, commensurate to current conditions, yield shall not be the driving force in determining which investments are to be selected for purchase. Yield is definitely considered to be of much lessor importance than either safety, liquidity or availability.

The Treasurer places investments with the objective of obtaining a respectable rate of return, not attempting to maximize yield at the expense of either safety, liquidity, or availability, yet not totally ignoring those factors within the marketplace that may be indicative of either favorable or hazardous conditions. The portfolio will be managed very conservatively, but actively enough to avert avoidable losses due to adverse market conditions.

PRUDENCE

The Treasurer is subject to the "Prudent Person Rule" whenever making a decision regarding the investment of the County's funds. This rule states, in principle:

> *"In investing property for the benefit of others, a trustee shall exercise the judgment and care, under circumstances then prevailing, that persons of prudence, discretion and intelligence, would exercise in the management of their own affairs - not in regard to speculation, but in regard to the permanent disposition of their funds, considering the probable safety of, as well as the probable income from, their capital."*

The Treasurer, and those acting for the Treasurer, are considered to have a fiduciary, trustee, relationship with the public for the public funds, and all investment decisions will be made in a manner sustaining this responsibility.

DELEGATION OF AUTHORITY

While the Treasurer has final responsibility for all investment decisions, other Treasury personnel may aid in the day to day operations. Those staff members, in addition to the Treasurer, currently authorized to act on behalf of the County, as of the date entered on this Policy, are listed below. This list is subject to change, and those parties newly involved in transactions with the Treasurer's department should always obtain a current Trading Authorization and Agreement form, and be verbally introduced by a known Treasury employee, prior to accepting unconfirmed verbal instructions from any previously unknown Treasury staff member.

Authorized Personnel	***Title***
Steve Duman	Property Tax Clerk
Shari Schapmire	Assistant Treasurer - Tax Collector

Other persons, both inside and outside County employment, may act in the role of assistant or advisor to aid in the timely and proper settlement of investment transactions. While these persons may provide information or aid in the expedient delivery of securities, they may not authorize, approve, or initiate any trading activities. **Only the persons listed on a current *Trading Authorization & Agreement,* and the Treasurer, may initiate trading activity.**

SECURITIES CUSTODY

The Treasurer has established a third party custody and safekeeping account to which all negotiable instruments shall be delivered upon purchase on a payment versus delivery basis. No negotiable, deliverable, securities or investments will be left in the custody of any brokerage firm or issuing party, including any collateral from Repurchase Agreements**.**

AUTHORIZED INVESTMENTS AND LIMITATIONS

The Government Codes of the State of California, primarily within sections 53600 et. seq., establish the legality of certain types of investment vehicles for a California local agency's portfolio. Thereby, under no circumstances is the Treasurer permitted to purchase an investment that is not specifically authorized for a local agency under these, or other code sections that may apply, or might later be enacted, pertaining to local agency investments. Securities brokers dealing with the County should possess a complete understanding of these Code sections.

An attached Addendum briefly describes the types of securities legal within the Government Code sections noted above and outlines the various limitations included in these sections. Except for the restrictions noted below in this section, all legally permitted investment options described in the Government Code are authorized at this time. Funds placed in the State's Local Agency Investment Fund (LAIF) shall follow the limitations placed on these deposits by the State and may change in accordance with these restrictions.

Though these Government Code sections define the investment types and terms permissible to the Treasurer under this Policy, various temporary and more restrictive constraints may at times be deemed beneficial due to transient conditions within the marketplace. These flexible constraints are not part of this Policy but may be obtained by requesting a current "Temporary Constraints and Restrictions on Investments", page which will change on an "as needed" basis. These constraints or restrictions may only be ***more*** restrictive than those of the Policy, but may ***not*** be ***less*** restrictive. Securities Brokers and Dealers should be aware of these temporary conditions in order to save time and best serve the County.

Though the Government Code sections define the investment types and terms permissible to the Treasurer, **the Treasurer will not:**

- Invest in any security or investment with a stated or potential final maturity longer than five years, unless the conditions of the security include terms that permit the purchaser to unconditionally "put", or sell back, to the original issuer the security prior to five years from the purchase date; or the Board of Supervisors has pre-approved as required by the Government Codes.
- Invest in any security or investment wherein, by the terms of the investment, interest might not be earned during any period the security or investment exists.
- Purchase any security wherein under terms inherent to the security, or the investment agreement under which the security is purchased, circumstances could result wherein the investment runs a risk of earning a rate of return substantially below other investments obtainable on a fixed rate basis at the time of purchase or drastically different than the prevailing rate during any time prior to the maturity of the issue.
- Enter into a reverse repurchase agreement.
- Purchase any Collateralized Mortgage Obligation.
- Lend securities.
- Invest in futures or options.

AUTHORIZED DEALER LIST

It is prohibited for a transaction to be entered into with any securities broker, dealer or bank investment department or subsidiary prior to that entity being designated an Authorized Dealer, and placed on the Authorized Dealer List. For a firm to become authorized it must first demonstrate that it will add value to the Treasurer's efforts to best manage the cash portfolio, as well as fulfill certain other minimum requirements. To qualify for Authorized Dealer status, a brokerage firm or bank must:

1) Be a dealer operation properly licensed to deal with local agencies in California, **and;**
2) Have a minimum of $10mm in capital, or, be a Primary Dealer of the Federal Reserve Bank of New York; **and;**
3) Be headquartered in the State of California, or, the City of New York, or be the direct issuer of a security type normally purchased by the Treasurer,

Or;

Be a department or subsidiary of an insured bank with minimum assets of $500mm that the County has comprehensive banking relationships with,

Or;

Be an established broker operation in New York or its environs, with a history of profitability that is properly licensed to deal with local agencies in California, that has capital of $500m and does not position securities for their own portfolio, but brokers securities for their established clients consisting primarily of traders for Primary Dealers and/or other major institutional fixed income brokerage operations, issuers and investors.

If meeting the above requirements, a salesperson may apply to become a Authorized Dealer by sending to the Treasurer their most recent annual and interim audited financial statements and a letter furnishing:

1) Their reasons for believing they would add value to the present coverage; **and,**
2) A general roster of those markets they participate in, and specifics on those types of securities they as a firm, regularly issue or regularly hold dealer trading positions in; [**or,** a list of those dealers they are able to represent, and the securities they regularly position;] **and,**
3) A list of five references, at least three being California local agency treasurers, including telephone numbers, that the Treasurer or his representative may contact.

The Treasurer will instigate an investigation of the applying salesperson and the firm through various sources, including the California Department of Corporations and the N.A.S.D., to determine market participation, knowledge, reputation, and financial stability. All salespeople and their supervisors will be expected to have a working knowledge of the appropriate sections of the State of California Government Code, sufficient experience in covering public entities, a willingness to well serve their customers, a complete and total understanding of this Investment Policy, and demonstrate an ongoing ability to work with the Treasurer and staff. The Treasurer will review all new requests at the end of each quarter, and if the decision is made that additional dealers would be beneficial to best service the portfolio's needs, those dealers selected will be informed of their addition to the Authorized Dealer List. All dealers are subject to removal from the Authorized Dealer List at any time, solely at the discretion of the Treasurer.

The Treasurer, or Treasury staff, are prohibited from dealing with a salesman, broker, or account executive from any broker, dealer or bank investment department or bank subsidiary until the Acknowledgment form found on the last page of the Trading Authorization and Agreement is signed by all parties and received by the Treasurer. The Trading Authorization and Agreement is sent out to all approved dealers, and is an integral addition to this Policy Statement for Brokers/ Dealers, etc. doing investment business with the County Treasurer or Treasury staff.

Similar restrictions and forms may be required of those firms doing business with the County through retained financial advisors or managers. Certain selected firms may be chosen or appointed by the Treasurer to render specific services the Treasurer determines they are uniquely qualified to provide, wherein some of the requirements of this section may be waived.

Neither the Treasurer, nor any member of the Treasurer's staff, may accept any gift, honoraria, gratuity or service of value in violation of the regulations set forth by the Fair Political Practices Commission, the Government Code, additional limitations set forth by County ordinance, or internal requirements of the Treasurer. The Treasurer and all members of the Treasury staff are prohibited from conducting any business with any broker, dealer, or securities firm that has made a political contribution within any consecutive 48 month period beginning January 1, 1996, in an amount exceeding the limitation contained in Rule G 37 of the Municipal Securities Rulemaking Board, to the County Treasurer or any member of the Board of Supervisors, or any candidate for these offices.

THE COUNTY TREASURY OVERSIGHT COMMITTEE

[Due to the current lack of State Mandate and funding for Oversight Committees, the terms, conditions and requirements of the following section will be temporarily held in abeyance.]

The Treasurer currently agrees that an Oversight Committee should be retained, despite discontinuance of the State Mandate. The requirements set forth with the Government Codes sections shall continue to provide the basis for this committee. After reinstatement of the State Mandate reimbursement program the Treasurer will nominate for approval by the Board, a County Treasury Oversight Committee. This committee will include from three to eleven members, as the Board of Supervisors, in consultation with the County Treasurer, shall determine is appropriate. Government Codes require that this Committee shall include selected persons only from the following categories:

a) The County Treasurer.
b) The County Auditor/Auditor-Controller/Finance Director.
c) An appointed representative of the Board of Supervisors.
d) The County Superintendent of Schools, or designee.
e) A representative selected by a majority of the presiding officers of the governing bodies of the school districts and community college districts of the County.
f) A representative selected by a majority of the presiding officers of the legislative bodies of the special districts within the County that are required or authorized to deposit money in the County Investment Pool.
g) One to five bipartisan members of the public that have expertise in public finance and come from diverse economic backgrounds.

Members of the Committee may not have contributed to the any election campaign for the position of Treasurer or for any candidate to the Board of Supervisors within the past three years. Members may not directly or indirectly raise money for any candidate for local treasurer or a candidate for member of the legislative body of any local agency with money in the County Pool while a member of the Committee, nor may the member secure employment with a bond underwriter, bond counsel, security brokerage or dealer firm, or financial services firm for three years after leaving the Committee. Committee members may not accept any gift, honoraria, gratuity or service of value in violation of the regulations set forth by the Fair Political Practices Commission, the Government Code, additional limitations set forth by County ordinance, or internal requirements of the Treasurer.

The Treasurer will annually provide a copy of the Investment Policy for review and monitoring by the Oversight Committee. The Treasurer will provide a report quarterly to the Board and the Oversight Committee, identifying all investments held in the County Investment Pool, or elsewhere by the Treasurer. or as required by the Board of Supervisors. The Oversight Committee shall, via this report and other appropriate means, monitor the activities of the Treasurer, and, if specifically requested by the Board of Supervisors, cause to be performed an annual audit to determine the Treasurer's compliance with the Investment Policy, and other appropriate regulations.

Committee meetings shall be open to the public and in compliance with the appropriate sections of the Ralph M. Brown Act. All costs related to the duties of the Oversight Committee will be considered normal charges against earnings of the Investment Pool.

The Oversight Committee shall have no authority to require discussion, attempt to direct, or in any way interfere with the process or daily operation of any portion of the Treasury department, nor shall the Committee attempt to play any role in determining which banks, firms or individuals the Treasurer does business with, nor shall the Committee be involved at all in determining which investments the Treasurer purchases, but shall act solely to review the actions of the Treasurer to determine that they are in accordance and compliance with the Investment Policy and all other legal requirements or regulations.

TERMS FOR FUNDS INVESTED WITH THE COUNTY INVESTMENT POOL

The Government Code requires the County Treasurer to define the limits and conditions under which local agencies having their money in the Investment Pool may deposit and withdraw their funds. The Government Codes confer upon the Treasurer the final authority as to how funds for which the Treasurer is held responsible for overseeing, are to be invested. The Treasurer must take into consideration the current financial condition of the sum total of the Pool's agencies, the conditions of the market place, as well as the cash flow projections and the potential for changes in the Pool's cash needs. The Treasurer must protect the earnings of each individual local agency in the Pool, and also see that no decision will reward a particular agency or group of agencies within the Pool at the expense of another or others within the Pool. If the Treasurer determines that a request for a withdrawal of funds for a specific or outside investment is not, in the Treasurer's opinion, in the best interest of a particular agency, or is overly detrimental to the pool as a whole, the Treasurer must legally deny the request, or find a means of neutralizing the harm to all others affected.

Any funds deposited in accounts that are consolidated into the County Investment Pool that are immediately required to meet cash flows of the Pool will be invested by the Treasurer or the Treasurer's staff. All Pool entities agree that by placing funds in such accounts that they agree to proportionately participate in all investments within the Investment Pool.

FUNDS OF AGENCIES REQUIRED TO INVEST WITHIN THE POOL

Funds will be accepted at all times, in the manner prescribed, from those local agencies where the County Treasurer is also the Treasurer for the local agency, or from any agencies that by statute must place their money in the County Pool. Funds will earn interest based on the average daily balance paid on a quarterly basis.

Should a legislative body of a local agency determine that certain funds will not be required by the local agency for a period of at least two years, the local agency may petition the County Treasurer to invest that portion of the local agency's excess funds in a specific investment under the control of the County Treasurer. Such a petition should state the nature of the funds the legislative body wishes to invest specifically, and the reasons why the legislative body believes a specific investment is a preferable and viable alternative to general Pool participation. Should the Treasurer determine that the request for a specific investment is valid and not counter-productive to the Pool as a whole, the Treasurer will consult with the local agency's legislative body, or its appointed representative, to suggest and determine exactly what investment(s) should be purchased to fulfill the needs of the local agency. The Treasurer will then purchase the specific investment(s) upon receipt of a written resolution, issued by the legislative body of the local agency, requesting the specific investment. The resolution must acknowledge that the local agency's legislative body takes full responsibility for the decision to purchase the specific investment(s), and that should conditions change requiring a sale prior to maturity of the specific investment(s), any loss that might be suffered as a result ,will be solely that of the local agency, and that this loss shall not be shared by the Pool as a whole, nor by the County.

Under language added to the Government Code in 1995, it is not permissible for local agency legislative bodies, required to have their funds within the Pool, to withdraw funds from the Pool in order to invest outside the County Pool in any manner, at any time, without the specific permission of the Treasurer. Any such investments shall either be terminated and all funds returned to the Pool, or the securities so purchased shall be transferred to the custody of the County Treasurer immediately. Upon receipt of any such securities by the Treasurer, the Treasurer shall at the Treasurer's option, place the investment in the Pool, terminate the investment at the current market value and credit the local agency with the proceeds, or place the security in the name of the local agency as a specific investment.

MONEY VOLUNTARILY INVESTED WITH THE COUNTY INVESTMENT POOL

By Code, the County Treasurer shall set conditions under which money from local agencies, not required to have their funds in the Investment Pool, may deposit and withdraw voluntarily invested funds. Local agencies from outside the County will not be permitted to deposit funds in the County Pool. Funds from local agencies within the County, voluntarily wishing to participant in the Pool, shall be accepted under the terms existing in this Policy. Voluntary money maybe withdrawn under conditions set forth in Sections 27133 and 27136 of the Government Codes. Specific investments are not normally permitted with voluntary funds, though on a cost recovery basis and under circumstances that dictate such activity, exceptions may be permitted. [Local agency legislators with surplus money involuntarily in the County Investment Pool wishing to withdraw funds from the Pool beyond those amounts needed for the normal operation of the agency, will send their **"Request for Withdrawal"** to the Treasurer for a decision as to the feasibility of the request.]

APPORTIONING OF COSTS AND INTEREST

All costs related to investing, maintaining and accounting for the investments purchased for the Investment Pool, as authorized by Section 27013, shall be apportioned equally on the average daily balance method quarterly to all participants with funds in the Investment Pool, including those held in specific investments. Interest earning shall be apportioned on the same basis and also distributed quarterly.

REPORTING

The Treasurer shall provide the Board of Supervisors this Statement of Investment Policy annually at the start of each calendar year for their approval, and will quarterly report the holdings, status and earnings of the portfolio. [The Oversight Committee shall be provided with the same reports for their perusal.] Should circumstances require revision of this policy during the year, the changes will be presented to the Board of Supervisors for approval prior to these alterations being adopted.

Policy effective upon approval of Board of Supervisors, submitted for approval March, 2005.

MENDOCINO COUNTY INVESTMENT POOL

Mendocino County Investment Pool
Summary of Assets Held
As of March 31, 2005

	Cost	Par Value	Market Value	Coupon Rate	Purchase Date	Maturity Date	Days to Maturity
INVESTMENT							
Local Agency Investment Fund	$9,000,000	$9,000,000	$9,000,000	2.54%	N/A	N/A	
Medium Term Notes	$27,023,530	$27,000,000	$27,005,480	2.89-3.45%	various	various	106-331
Mutual Funds	$7,573,379	$7,573,379	$7,252,261	3.09%	07/20/93	N/A	
Agencies	$5,007,4205	$5,075,786	$5,069,075	3.58-10%	various	various	714-4551
Certificates of Deposit	$25,000,249	$25,000,000	$25,000,385	2.36-2.61%	various	various	4-126
Commercial Paper	$20,915,002	$21,000,000	$20,940,680	2.42-2.90%	various	various	15-61
Total Investments	$94,584,4011	$94,649,166	$97,267,882	5.25%			

APPENDIX F

BOOK-ENTRY ONLY SYSTEM

The information in this appendix has been provided by DTC for use in securities offering documents, and the District takes no responsibility for the accuracy or completeness thereof. The District cannot and does not give any assurances that DTC, DTC Participants or Indirect Participants will distribute the Beneficial owners either (a) payments of interest, principal or premium, if any, with respect to the Bonds or (b) certificates representing ownership interest in or other confirmation of ownership interest in the Bonds, or that they will so do on a timely basis or that DTC, DTC Direct Participants or DTC Indirect Participants will act in the manner described in this Official Statement.

1. The Depository Trust Company ("DTC"), New York, NY, will act as securities depository for the Bonds (the "Securities"). The Securities will be issued as fully-registered securities registered in the name of Cede & Co. (DTC's partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered Security certificate will be issued for each maturity of the Securities, in the aggregate principal amount of such issue, and will be deposited with DTC. If, however, the aggregate principal amount of any issue exceeds $500 million, one certificate will be issued with respect to each $500 million of principal amount, and an additional certificate will be issued with respect to any remaining principal amount of such issue.

2. DTC, the world's largest depository, is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of the New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 2 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments from over 85 countries that DTC's participants ("Direct Participants") deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants' accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation ("DTCC"). DTCC, in turn, is owned by a number of Direct Participants of DTC and Members of the National Securities Clearing Corporation, Government Securities Clearing Corporation, MBS Clearing Corporation, and Emerging Markets Clearing Corporation, (NSCC, GSCC, MBSCC, and EMCC, also subsidiaries of DTCC), as well as by the New York Stock Exchange, Inc., the American Stock Exchange LLC, and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). DTC has Standard & Poor's highest rating: AAA. The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtcc.com.

3. Purchases of Securities under the DTC system must be made by or through Direct Participants, which will receive a credit for the Securities on DTC's records. The ownership interest of each actual purchaser of each Security ("Beneficial Owner")is in turn to be recorded on the Direct and Indirect Participants' records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Securities are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in Securities, except in the event that use of the book-entry system for the Securities is discontinued.

4. To facilitate subsequent transfers, all Securities deposited by Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of Securities with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Securities; DTC's records reflect only the identity of the Direct Participants to whose accounts such Securities are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

5. Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time.

6. Redemption notices shall be sent to DTC. If less than all of the Securities within an issue are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such issue to be redeemed.

7. Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to Securities unless authorized by a Direct Participant in accordance with DTC's Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the issuer as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts Securities are credited on the record date (identified in a listing attached to the Omnibus Proxy).

8. Redemption proceeds, distributions, and dividend payments on the Securities will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the issuer or the paying agent or bond trustee, on payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC nor its nominee, the paying agent or bond trustee, or the issuer, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of redemption proceeds, distributions, and dividend payments to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the issuer or the paying agent or bond trustee, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

9. DTC may discontinue providing its services as depository with respect to the Securities at any time by giving reasonable notice to the issuer or the paying agent or bond trustee. Under such circumstances, in the event that a successor depository is not obtained, Security certificates are required to be printed and delivered.

10. The issuer may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, Security certificates will be printed and delivered.

APPENDIX G

SPECIMEN MUNICIPAL BOND INSURANCE POLICY

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FINANCIAL SECURITY ASSURANCE®

MUNICIPAL BOND INSURANCE POLICY

ISSUER:

BONDS: $ in aggregate principal amount of

Policy No.: -N

Effective Date:

Premium: $

FINANCIAL SECURITY ASSURANCE INC. ("Financial Security"), for consideration received, hereby UNCONDITIONALLY AND IRREVOCABLY agrees to pay to the trustee (the "Trustee") or paying agent (the "Paying Agent") (as set forth in the documentation providing for the issuance of and securing the Bonds) for the Bonds, for the benefit of the Owners or, at the election of Financial Security, directly to each Owner, subject only to the terms of this Policy (which includes each endorsement hereto), that portion of the principal of and interest on the Bonds that shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Issuer.

On the later of the day on which such principal and interest becomes Due for Payment or the Business Day next following the Business Day on which Financial Security shall have received Notice of Nonpayment, Financial Security will disburse to or for the benefit of each Owner of a Bond the face amount of principal of and interest on the Bond that is then Due for Payment but is then unpaid by reason of Nonpayment by the Issuer, but only upon receipt by Financial Security, in a form reasonably satisfactory to it, of (a) evidence of the Owner's right to receive payment of the principal or interest then Due for Payment and (b) evidence, including any appropriate instruments of assignment, that all of the Owner's rights with respect to payment of such principal or interest that is Due for Payment shall thereupon vest in Financial Security. A Notice of Nonpayment will be deemed received on a given Business Day if it is received prior to 1:00 p.m. (New York time) on such Business Day; otherwise, it will be deemed received on the next Business Day. If any Notice of Nonpayment received by Financial Security is incomplete, it shall be deemed not to have been received by Financial Security for purposes of the preceding sentence and Financial Security shall promptly so advise the Trustee, Paying Agent or Owner, as appropriate, who may submit an amended Notice of Nonpayment. Upon disbursement in respect of a Bond, Financial Security shall become the owner of the Bond, any appurtenant coupon to the Bond or right to receipt of payment of principal of or interest on the Bond and shall be fully subrogated to the rights of the Owner, including the Owner's right to receive payments under the Bond, to the extent of any payment by Financial Security hereunder. Payment by Financial Security to the Trustee or Paying Agent for the benefit of the Owners shall, to the extent thereof, discharge the obligation of Financial Security under this Policy.

Except to the extent expressly modified by an endorsement hereto, the following terms shall have the meanings specified for all purposes of this Policy. "Business Day" means any day other than (a) a Saturday or Sunday or (b) a day on which banking institutions in the State of New York or the Insurer's Fiscal Agent are authorized or required by law or executive order to remain closed. "Due for Payment" means (a) when referring to the principal of a Bond, payable on the stated maturity date thereof or the date on which the same shall have been duly called for mandatory sinking fund redemption and does not refer to any earlier date on which payment is due by reason of call for redemption (other than by mandatory sinking fund redemption), acceleration or other advancement of maturity unless Financial Security shall elect, in its sole discretion, to pay such principal due upon such acceleration together with any accrued interest to the date of acceleration and (b) when referring to interest on a Bond, payable on the stated date for payment of interest. "Nonpayment" means, in respect of a Bond, the failure of the Issuer to have provided sufficient funds to the Trustee or, if there is no Trustee, to the Paying Agent for payment in full of all principal and interest that is Due for Payment on such Bond. "Nonpayment" shall also include, in respect of a Bond, any payment of principal or interest that is Due for Payment made to an Owner by or on behalf of the Issuer which has been recovered from such Owner pursuant to the

United States Bankruptcy Code by a trustee in bankruptcy in accordance with a final, nonappealable order of a court having competent jurisdiction. "Notice" means telephonic or telecopied notice, subsequently confirmed in a signed writing, or written notice by registered or certified mail, from an Owner, the Trustee or the Paying Agent to Financial Security which notice shall specify (a) the person or entity making the claim, (b) the Policy Number, (c) the claimed amount and (d) the date such claimed amount became Due for Payment. "Owner" means, in respect of a Bond, the person or entity who, at the time of Nonpayment, is entitled under the terms of such Bond to payment thereof, except that "Owner" shall not include the Issuer or any person or entity whose direct or indirect obligation constitutes the underlying security for the Bonds.

Financial Security may appoint a fiscal agent (the "Insurer's Fiscal Agent") for purposes of this Policy by giving written notice to the Trustee and the Paying Agent specifying the name and notice address of the Insurer's Fiscal Agent. From and after the date of receipt of such notice by the Trustee and the Paying Agent, (a) copies of all notices required to be delivered to Financial Security pursuant to this Policy shall be simultaneously delivered to the Insurer's Fiscal Agent and to Financial Security and shall not be deemed received until received by both and (b) all payments required to be made by Financial Security under this Policy may be made directly by Financial Security or by the Insurer's Fiscal Agent on behalf of Financial Security. The Insurer's Fiscal Agent is the agent of Financial Security only and the Insurer's Fiscal Agent shall in no event be liable to any Owner for any act of the Insurer's Fiscal Agent or any failure of Financial Security to deposit or cause to be deposited sufficient funds to make payments due under this Policy.

To the fullest extent permitted by applicable law, Financial Security agrees not to assert, and hereby waives, only for the benefit of each Owner, all rights (whether by counterclaim, setoff or otherwise) and defenses (including, without limitation, the defense of fraud), whether acquired by subrogation, assignment or otherwise, to the extent that such rights and defenses may be available to Financial Security to avoid payment of its obligations under this Policy in accordance with the express provisions of this Policy.

This Policy sets forth in full the undertaking of Financial Security, and shall not be modified, altered or affected by any other agreement or instrument, including any modification or amendment thereto. Except to the extent expressly modified by an endorsement hereto, (a) any premium paid in respect of this Policy is nonrefundable for any reason whatsoever, including payment, or provision being made for payment, of the Bonds prior to maturity and (b) this Policy may not be canceled or revoked. THIS POLICY IS NOT COVERED BY THE PROPERTY/CASUALTY INSURANCE SECURITY FUND SPECIFIED IN ARTICLE 76 OF THE NEW YORK INSURANCE LAW.

In witness whereof, FINANCIAL SECURITY ASSURANCE INC. has caused this Policy to be executed on its behalf by its Authorized Officer.

[Countersignature] FINANCIAL SECURITY ASSURANCE INC.

By ______________________ By ______________________
Authorized Officer

A subsidiary of Financial Security Assurance Holdings Ltd.
350 Park Avenue, New York, N.Y. 10022-6022 (212) 826-0100

Form 500NY (5/90)

FINANCIAL SECURITY ASSURANCE®

ENDORSEMENT NO. 1 TO MUNICIPAL BOND INSURANCE POLICY (California Insurance Guaranty Association)

ISSUER:

BONDS:

Policy No.:

Effective Date:

Notwithstanding the terms and provisions contained in this Policy, it is further understood that the insurance provided by this Policy is not covered by the California Insurance Guaranty Association established pursuant to Article 14.2 (commencing with Section 1063) of Chapter 1 of Part 2 of Division 1 of the California Insurance Code.

Nothing herein shall be construed to waive, alter, reduce or amend coverage in any other section of the Policy. If found contrary to the Policy language, the terms of this Endorsement supersede the Policy language.

In witness whereof, FINANCIAL SECURITY ASSURANCE INC. has caused this Endorsement to be executed on its behalf by its Authorized Officer.

FINANCIAL SECURITY ASSURANCE INC.

By: ______________________________
Authorized Officer

A subsidiary of Financial Security Assurance Holdings Ltd.
350 Park Avenue, New York, N.Y. 10022-6022

(212) 826-0100

Form 560NY (CA 1/91)

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APPENDIX H

ACCRETED VALUE TABLES FOR THE CAPITAL APPRECIATION BONDS

Accreted Values shown per $5,000 Maturity Value

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BOND ACCRETED VALUE TABLE

Date	Series B: Capital Appreciation Bond 08/01/2028 5%	Series B: Capital Appreciation Bond 08/01/2029 5.04%	Series B: Capital Appreciation Bond 08/01/2030 5.08%	Series B: Capital Appreciation Bond 08/01/2031 5.12%	Series B: Capital Appreciation Bond 08/01/2032 5.14%	Series B: Capital Appreciation Bond 08/01/2033 5.16%	Series B: Capital Appreciation Bond 08/01/2034 5.17%	Series B: Capital Appreciation Bond 08/01/2035 5.18%	Series B: Capital Appreciation Bond 08/01/2036 5.19%	Series B: Capital Appreciation Bond 08/01/2037 5.21%
06/22/2005	1,597.15	1,505.95	1,418.85	1,335.75	1,263.20	1,194.15	1,131.60	1,072.15	1,015.60	958.85
08/01/2005	1,605.70	1,514.10	1,426.60	1,343.10	1,270.15	1,200.75	1,137.90	1,078.10	1,021.25	964.20
02/01/2006	1,645.85	1,552.25	1,462.80	1,377.45	1,302.80	1,231.70	1,167.30	1,106.00	1,047.75	989.35
08/01/2006	1,687.00	1,591.35	1,499.95	1,412.75	1,336.30	1,263.50	1,197.45	1,134.65	1,074.95	1,015.10
02/01/2007	1,729.15	1,631.45	1,538.05	1,448.90	1,370.65	1,296.10	1,228.45	1,164.05	1,102.85	1,041.55
08/01/2007	1,772.40	1,672.55	1,577.15	1,486.00	1,405.85	1,329.55	1,260.20	1,194.20	1,131.45	1,068.70
02/01/2008	1,816.70	1,714.70	1,617.20	1,524.05	1,442.00	1,363.85	1,292.75	1,225.15	1,160.85	1,096.50
08/01/2008	1,862.15	1,757.95	1,658.30	1,563.05	1,479.05	1,399.05	1,326.20	1,256.85	1,190.95	1,125.10
02/01/2009	1,908.70	1,802.25	1,700.40	1,603.05	1,517.05	1,435.15	1,360.45	1,289.40	1,221.85	1,154.40
08/01/2009	1,956.40	1,847.65	1,743.60	1,644.10	1,556.05	1,472.15	1,395.65	1,322.80	1,253.55	1,184.45
02/01/2010	2,005.30	1,894.20	1,787.90	1,686.20	1,596.05	1,510.15	1,431.70	1,357.10	1,286.10	1,215.30
08/01/2010	2,055.45	1,941.95	1,833.30	1,729.35	1,637.05	1,549.10	1,468.70	1,392.25	1,319.45	1,247.00
02/01/2011	2,106.85	1,990.90	1,879.85	1,773.65	1,679.15	1,589.05	1,506.70	1,428.30	1,353.70	1,279.45
08/01/2011	2,159.50	2,041.05	1,927.60	1,819.05	1,722.30	1,630.05	1,545.65	1,465.30	1,388.85	1,312.80
02/01/2012	2,213.50	2,092.50	1,976.55	1,865.60	1,766.55	1,672.10	1,585.60	1,503.25	1,424.90	1,347.00
08/01/2012	2,268.85	2,145.20	2,026.75	1,913.35	1,811.95	1,715.25	1,626.55	1,542.15	1,461.85	1,382.10
02/01/2013	2,325.55	2,199.30	2,078.25	1,962.35	1,858.55	1,759.50	1,668.60	1,582.10	1,499.80	1,418.10
08/01/2013	2,383.70	2,254.70	2,131.05	2,012.60	1,906.30	1,804.90	1,711.75	1,623.10	1,538.70	1,455.05
02/01/2014	2,443.30	2,311.55	2,185.15	2,064.10	1,955.30	1,851.50	1,756.00	1,665.15	1,578.65	1,492.95
08/01/2014	2,504.35	2,369.80	2,240.70	2,116.95	2,005.55	1,899.25	1,801.40	1,708.25	1,619.60	1,531.85
02/01/2015	2,566.95	2,429.50	2,297.60	2,171.15	2,057.10	1,948.25	1,847.95	1,752.50	1,661.65	1,571.75
08/01/2015	2,631.15	2,490.70	2,355.95	2,226.75	2,109.95	1,998.50	1,895.75	1,797.90	1,704.75	1,612.70
02/01/2016	2,696.95	2,553.50	2,415.80	2,283.75	2,164.20	2,050.10	1,944.75	1,844.45	1,749.00	1,654.70
08/01/2016	2,764.35	2,617.85	2,477.15	2,342.20	2,219.80	2,102.95	1,995.00	1,892.25	1,794.40	1,697.80
02/01/2017	2,833.45	2,683.80	2,540.05	2,402.15	2,276.85	2,157.25	2,046.60	1,941.25	1,840.95	1,742.00
08/01/2017	2,904.30	2,751.45	2,604.60	2,463.65	2,335.35	2,212.90	2,099.50	1,991.50	1,888.75	1,787.40
02/01/2018	2,976.90	2,820.75	2,670.75	2,526.75	2,395.40	2,270.00	2,153.75	2,043.10	1,937.75	1,833.95
08/01/2018	3,051.35	2,891.85	2,738.60	2,591.40	2,456.95	2,328.55	2,209.45	2,096.00	1,988.00	1,881.75
02/01/2019	3,127.60	2,964.75	2,808.15	2,657.75	2,520.10	2,388.60	2,266.55	2,150.30	2,039.60	1,930.75
08/01/2019	3,205.80	3,039.45	2,879.50	2,725.80	2,584.85	2,450.25	2,325.15	2,206.00	2,092.55	1,981.05
02/01/2020	3,285.95	3,116.05	2,952.60	2,795.60	2,651.30	2,513.45	2,385.25	2,263.15	2,146.85	2,032.65
08/01/2020	3,368.10	3,194.55	3,027.60	2,867.15	2,719.45	2,578.30	2,446.90	2,321.75	2,202.55	2,085.60
02/01/2021	3,452.30	3,275.05	3,104.50	2,940.55	2,789.30	2,644.85	2,510.15	2,381.90	2,259.70	2,139.95
08/01/2021	3,538.60	3,357.60	3,183.35	3,015.85	2,861.00	2,713.05	2,575.05	2,443.55	2,318.35	2,195.70
02/01/2022	3,627.10	3,442.20	3,264.25	3,093.05	2,934.55	2,783.05	2,641.60	2,506.85	2,378.50	2,252.90
08/01/2022	3,717.75	3,528.95	3,347.15	3,172.20	3,009.95	2,854.85	2,709.90	2,571.80	2,440.25	2,311.60
02/01/2023	3,810.70	3,617.90	3,432.15	3,253.40	3,087.30	2,928.55	2,779.95	2,638.40	2,503.55	2,371.80
08/01/2023	3,905.95	3,709.05	3,519.35	3,336.70	3,166.65	3,004.10	2,851.80	2,706.75	2,568.55	2,433.60
02/01/2024	4,003.60	3,802.55	3,608.75	3,422.15	3,248.05	3,081.60	2,925.55	2,776.85	2,635.20	2,497.00
08/01/2024	4,103.70	3,898.35	3,700.40	3,509.75	3,331.50	3,161.10	3,001.15	2,848.75	2,703.55	2,562.05

BOND ACCRETED VALUE TABLE

Date	Series B: Capital Appreciation Bond 08/01/2028 5%	Series B: Capital Appreciation Bond 08/01/2029 5.04%	Series B: Capital Appreciation Bond 08/01/2030 5.08%	Series B: Capital Appreciation Bond 08/01/2031 5.12%	Series B: Capital Appreciation Bond 08/01/2032 5.14%	Series B: Capital Appreciation Bond 08/01/2033 5.16%	Series B: Capital Appreciation Bond 08/01/2034 5.17%	Series B: Capital Appreciation Bond 08/01/2035 5.18%	Series B: Capital Appreciation Bond 08/01/2036 5.19%	Series B: Capital Appreciation Bond 08/01/2037 5.21%
02/01/2025	4,206.30	3,996.60	3,794.40	3,599.60	3,417.15	3,242.65	3,078.75	2,922.55	2,773.75	2,628.75
08/01/2025	4,311.45	4,097.30	3,890.75	3,691.75	3,504.95	3,326.30	3,158.35	2,998.25	2,845.70	2,697.25
02/01/2026	4,419.25	4,200.55	3,989.60	3,786.25	3,595.05	3,412.15	3,239.95	3,075.90	2,919.55	2,767.50
08/01/2026	4,529.75	4,306.40	4,090.90	3,883.20	3,687.40	3,500.15	3,323.70	3,155.55	2,995.30	2,839.60
02/01/2027	4,642.95	4,414.95	4,194.85	3,982.60	3,782.20	3,590.50	3,409.65	3,237.30	3,073.05	2,913.60
08/01/2027	4,759.05	4,526.20	4,301.40	4,084.55	3,879.40	3,683.10	3,497.80	3,321.15	3,152.80	2,989.50
02/01/2028	4,878.00	4,640.25	4,410.65	4,189.10	3,979.10	3,778.15	3,588.20	3,407.15	3,234.60	3,067.35
08/01/2028	5,000.00	4,757.20	4,522.65	4,296.35	4,081.35	3,875.60	3,680.95	3,495.40	3,318.55	3,147.25
02/01/2029		4,877.05	4,637.55	4,406.35	4,186.25	3,975.60	3,776.10	3,585.95	3,404.65	3,229.25
08/01/2029		5,000.00	4,755.35	4,519.15	4,293.85	4,078.15	3,873.70	3,678.80	3,493.00	3,313.35
02/01/2030			4,876.10	4,634.85	4,404.20	4,183.40	3,973.85	3,774.10	3,583.65	3,399.70
08/01/2030			5,000.00	4,753.50	4,517.40	4,291.30	4,076.60	3,871.85	3,676.65	3,488.25
02/01/2031				4,875.15	4,633.45	4,402.05	4,181.95	3,972.10	3,772.05	3,579.10
08/01/2031				5,000.00	4,752.55	4,515.60	4,290.05	4,075.00	3,869.95	3,672.35
02/01/2032					4,874.70	4,632.10	4,400.95	4,180.55	3,970.35	3,768.00
08/01/2032					5,000.00	4,751.65	4,514.75	4,288.80	4,073.40	3,866.20
02/01/2033						4,874.20	4,631.45	4,399.90	4,179.10	3,966.90
08/01/2033						5,000.00	4,751.15	4,513.85	4,287.55	4,070.25
02/01/2034							4,874.00	4,630.75	4,398.80	4,176.25
08/01/2034							5,000.00	4,750.70	4,512.95	4,285.05
02/01/2035								4,873.75	4,630.10	4,396.70
08/01/2035								5,000.00	4,750.25	4,511.20
02/01/2036									4,873.50	4,628.75
08/01/2036									5,000.00	4,749.30
02/01/2037										4,873.05
08/01/2037										5,000.00
02/01/2038										
08/01/2038										
02/01/2039										
08/01/2039										
02/01/2040										
08/01/2040										
02/01/2041										
08/01/2041										
02/01/2042										
08/01/2042										
02/01/2043										
08/01/2043										

BOND ACCRETED VALUE TABLE

Date	Series B: Capital Appreciation Bond 08/01/2038 5.23%	Series B: Capital Appreciation Bond 08/01/2039 5.25%	Series B: Capital Appreciation Bond 08/01/2040 5.26%	Series B: Capital Appreciation Bond 08/01/2041 5.27%	Series B: Capital Appreciation Bond 08/01/2042 5.28%	Series B: Capital Appreciation Bond 08/01/2043 5.29%
06/22/2005	904.95	853.70	807.80	764.25	722.90	683.65
08/01/2005	910.00	858.50	812.35	768.55	727.00	687.50
02/01/2006	933.80	881.05	833.75	788.80	746.15	705.70
08/01/2006	958.20	904.15	855.65	809.60	765.85	724.35
02/01/2007	983.30	927.90	878.15	830.95	786.10	743.55
08/01/2007	1,009.00	952.25	901.25	852.85	806.85	763.20
02/01/2008	1,035.40	977.25	924.95	875.30	828.15	783.40
08/01/2008	1,062.45	1,002.90	949.30	898.35	850.00	804.10
02/01/2009	1,090.25	1,029.25	974.25	922.05	872.45	825.35
08/01/2009	1,118.75	1,056.25	999.90	946.35	895.50	847.20
02/01/2010	1,148.00	1,084.00	1,026.20	971.30	919.15	869.60
08/01/2010	1,178.00	1,112.45	1,053.15	996.85	943.40	892.60
02/01/2011	1,208.85	1,141.65	1,080.85	1,023.15	968.30	916.20
08/01/2011	1,240.45	1,171.60	1,109.30	1,050.10	993.85	940.45
02/01/2012	1,272.90	1,202.35	1,138.50	1,077.75	1,020.10	965.35
08/01/2012	1,306.15	1,233.95	1,168.40	1,106.15	1,047.05	990.85
02/01/2013	1,340.30	1,266.30	1,199.15	1,135.30	1,074.70	1,017.10
08/01/2013	1,375.35	1,299.55	1,230.70	1,165.25	1,103.05	1,044.00
02/01/2014	1,411.35	1,333.70	1,263.05	1,195.95	1,132.15	1,071.60
08/01/2014	1,448.25	1,368.70	1,296.25	1,227.45	1,162.05	1,099.95
02/01/2015	1,486.10	1,404.60	1,330.35	1,259.80	1,192.75	1,129.05
08/01/2015	1,525.00	1,441.50	1,365.35	1,293.00	1,224.25	1,158.90
02/01/2016	1,564.85	1,479.35	1,401.25	1,327.05	1,256.55	1,189.55
08/01/2016	1,605.80	1,518.15	1,438.10	1,362.05	1,289.70	1,221.00
02/01/2017	1,647.75	1,558.00	1,475.95	1,397.90	1,323.75	1,253.30
08/01/2017	1,690.85	1,598.90	1,514.75	1,434.75	1,358.70	1,286.45
02/01/2018	1,735.10	1,640.90	1,554.60	1,472.55	1,394.60	1,320.50
08/01/2018	1,780.45	1,683.95	1,595.50	1,511.35	1,431.40	1,355.40
02/01/2019	1,827.00	1,728.15	1,637.45	1,551.20	1,469.20	1,391.25
08/01/2019	1,874.80	1,773.50	1,680.50	1,592.05	1,508.00	1,428.05
02/01/2020	1,923.80	1,820.10	1,724.70	1,634.00	1,547.80	1,465.85
08/01/2020	1,974.10	1,867.85	1,770.05	1,677.10	1,588.65	1,504.60
02/01/2021	2,025.75	1,916.90	1,816.60	1,721.25	1,630.60	1,544.40
08/01/2021	2,078.70	1,967.20	1,864.40	1,766.65	1,673.65	1,585.25
02/01/2022	2,133.10	2,018.85	1,913.45	1,813.20	1,717.85	1,627.20
08/01/2022	2,188.85	2,071.85	1,963.75	1,860.95	1,763.20	1,670.25
02/01/2023	2,246.10	2,126.25	2,015.40	1,910.00	1,809.75	1,714.40
08/01/2023	2,304.85	2,182.05	2,068.40	1,960.30	1,857.50	1,759.75
02/01/2024	2,365.10	2,239.30	2,122.80	2,011.95	1,906.55	1,806.30
08/01/2024	2,426.95	2,298.10	2,178.65	2,065.00	1,956.90	1,854.10

BOND ACCRETED VALUE TABLE

Date	Series B: Capital Appreciation Bond 08/01/2038 5.23%	Series B: Capital Appreciation Bond 08/01/2039 5.25%	Series B: Capital Appreciation Bond 08/01/2040 5.26%	Series B: Capital Appreciation Bond 08/01/2041 5.27%	Series B: Capital Appreciation Bond 08/01/2042 5.28%	Series B: Capital Appreciation Bond 08/01/2043 5.29%
02/01/2025	2,490.40	2,358.45	2,235.95	2,119.40	2,008.55	1,903.10
08/01/2025	2,555.55	2,420.35	2,294.75	2,175.25	2,061.55	1,953.45
02/01/2026	2,622.35	2,483.90	2,355.10	2,232.55	2,116.00	2,005.15
08/01/2026	2,690.95	2,549.10	2,417.05	2,291.40	2,171.85	2,058.15
02/01/2027	2,761.30	2,616.00	2,480.60	2,351.80	2,229.20	2,112.60
08/01/2027	2,833.55	2,684.65	2,545.85	2,413.75	2,288.05	2,168.50
02/01/2028	2,907.65	2,755.15	2,612.80	2,477.35	2,348.45	2,225.85
08/01/2028	2,983.65	2,827.45	2,681.55	2,542.65	2,410.45	2,284.70
02/01/2029	3,061.70	2,901.70	2,752.05	2,609.65	2,474.10	2,345.15
08/01/2029	3,141.75	2,977.85	2,824.45	2,678.40	2,539.40	2,407.15
02/01/2030	3,223.90	3,056.00	2,898.70	2,748.95	2,606.45	2,470.85
08/01/2030	3,308.20	3,136.25	2,974.95	2,821.40	2,675.25	2,536.20
02/01/2031	3,394.70	3,218.55	3,053.20	2,895.75	2,745.90	2,603.30
08/01/2031	3,483.50	3,303.05	3,133.50	2,972.05	2,818.40	2,672.15
02/01/2032	3,574.60	3,389.75	3,215.90	3,050.35	2,892.80	2,742.80
08/01/2032	3,668.05	3,478.75	3,300.50	3,130.75	2,969.15	2,815.35
02/01/2033	3,764.00	3,570.05	3,387.30	3,213.25	3,047.55	2,889.85
08/01/2033	3,862.40	3,663.80	3,476.35	3,297.90	3,128.00	2,966.25
02/01/2034	3,963.40	3,759.95	3,567.80	3,384.80	3,210.60	3,044.75
08/01/2034	4,067.05	3,858.65	3,661.65	3,474.00	3,295.35	3,125.25
02/01/2035	4,173.40	3,959.95	3,757.95	3,565.55	3,382.35	3,207.90
08/01/2035	4,282.55	4,063.90	3,856.75	3,659.50	3,471.65	3,292.75
02/01/2036	4,394.55	4,170.55	3,958.20	3,755.90	3,563.30	3,379.85
08/01/2036	4,509.45	4,280.05	4,062.30	3,854.90	3,657.35	3,469.25
02/01/2037	4,627.40	4,392.40	4,169.15	3,956.45	3,753.90	3,561.05
08/01/2037	4,748.40	4,507.70	4,278.80	4,060.70	3,853.00	3,655.20
02/01/2038	4,872.55	4,626.05	4,391.35	4,167.70	3,954.75	3,751.90
08/01/2038	5,000.00	4,747.45	4,506.80	4,277.55	4,059.15	3,851.15
02/01/2039		4,872.10	4,625.35	4,390.25	4,166.30	3,953.00
08/01/2039		5,000.00	4,747.00	4,505.95	4,276.30	4,057.55
02/01/2040			4,871.85	4,624.65	4,389.20	4,164.90
08/01/2040			5,000.00	4,746.55	4,505.05	4,275.05
02/01/2041				4,871.60	4,624.00	4,388.10
08/01/2041				5,000.00	4,746.05	4,504.20
02/01/2042					4,871.35	4,623.30
08/01/2042					5,000.00	4,745.60
02/01/2043						4,871.15
08/01/2043						5,000.00

ARENA UNION ELEMENTARY SCHOOL DISTRICT • (MENDOCINO COUNTY, CALIFORNIA) • GENERAL OBLIGATION BONDS, ELECTION OF 2003, SERIES 2005 • BANK QUALIFIED

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