PALOMAR COMMUNITY COLLEGE DISTRICT

SAN DIEGO COUNTY

REPORT ON
AUDIT OF FINANCIAL STATEMENTS
AND SUPPLEMENTARY INFORMATION
INCLUDING REPORTS ON COMPLIANCE
June 30, 2005

PALOMAR COMMUNITY COLLEGE DISTRICT

AUDIT REPORT
June 30, 2005

CONTENTS

VICENTI ♦ LLOYD ♦ STUTZMAN LLP
BUSINESS CONSULTANTS AND CPAs

INDEPENDENT AUDITORS' REPORT

The Board of Trustees
Palomar Community College District
1140 W. Mission Road
San Marcos, CA 92069-1487

We have audited the accompanying basic financial statements of the Palomar Community College District, as of and for the year ended June 30, 2005 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 and the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the basic financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall basic financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the basic financial statements listed in the aforementioned table of contents present fairly, in all material respects, the financial position of the Palomar Community College District as of June 30, 2005, and the results of its operations, changes in net assets and cash flows for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued our report dated November 2, 2005 on our consideration of the Palomar Community College District's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

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Board of Trustees
Palomar Community College District

The management's discussion and analysis is not a required part of the basic financial statements, but is supplementary information required by accounting principles generally accepted in the United States of America. 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.

Our audit was conducted for the purpose of forming an opinion on the Palomar Community College District's financial statements. The management's discussion and analysis section and supplementary section are presented for purposes of additional analysis and are not a required part of the basic financial statements. The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, <u>Audits of States, Local Governments, and Non-Profit Organizations</u>, and is also not a required part of the basic financial statements. The supplementary information, including the Schedule of Expenditures of Federal Awards have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The management's discussion and analysis section has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on it.

Vicenti, Lloyd & Stutzman LLP
VICENTI, LLOYD & STUTZMAN LLP

November 2, 2005

PALOMAR COMMUNITY COLLEGE DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2005

Introduction

The following discussion and analysis provides an overview of the financial position and activities of the Palomar Community College District (the "District") for the year ended June 30, 2005. This discussion has been prepared by college administration and should be read in conjunction with the financial statements and notes thereto which follow this section.

The District was required to implement the reporting standards of Governmental Accounting Standards Board Statements No. 34 and 35 during fiscal year 2002-03 using the Business Type Activity (BTA) model. The California Community College Chancellor's Office, through its Fiscal Standards and Accountability Committee, recommended that all community college districts implement the new reporting standards under the BTA model. To comply with the recommendation of the Chancellor's Office and to report in a manner consistent with other California Community College Districts, the District has adopted the BTA reporting model for these financial statements.

As required by the GASB reporting standards, the annual report consists of three basic financial statements that provide information on the District as a whole:

- The Statement of Net Assets
- The Statement of Revenue, Expenses and Changes in Net Assets
- The Statement of Cash Flows

The College

Palomar College is one of 108 colleges in the California Community Colleges system and eight in San Diego County. In addition to our main campus in San Marcos, we operate an educational center in Escondido, and seven smaller centers throughout north San Diego County, in Rancho Peñasquitos, Poway, Fallbrook, Ramona, Pauma Valley, Borrego Springs, and Camp Pendleton.

Palomar College serves more than 26,000 full-time and part-time students each fall and spring semester, while about 18,000 students attend during summer semester. About 28 percent of our students are enrolled full-time, while about 61 percent are enrolled part-time in credit classes, and 11 percent are enrolled in non-credit classes. About 61 percent of our students are aged 18 through 24, while 39 percent are 24 through 60+.

PALOMAR COMMUNITY COLLEGE DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2005

Palomar College offers more than 250 Associates Degree and certificate programs, as well as not-for-credit community development and personal enrichment classes for life-long learning. Palomar College is accredited through the Accrediting Commission for Community and Junior Colleges, Western Association of Schools and Colleges. We have transfer agreements with the California State University and University of California systems, and our high-level coursework in transferable classes fully prepares our students for success at four-year colleges and universities.

The California Community College system offers the most affordable education among community colleges through the United States. California residents pay an enrollment fee of only $26 per credit. Out-of-state residents pay the enrollment fee plus tuition fees of $151 per credit.

Financial Highlights

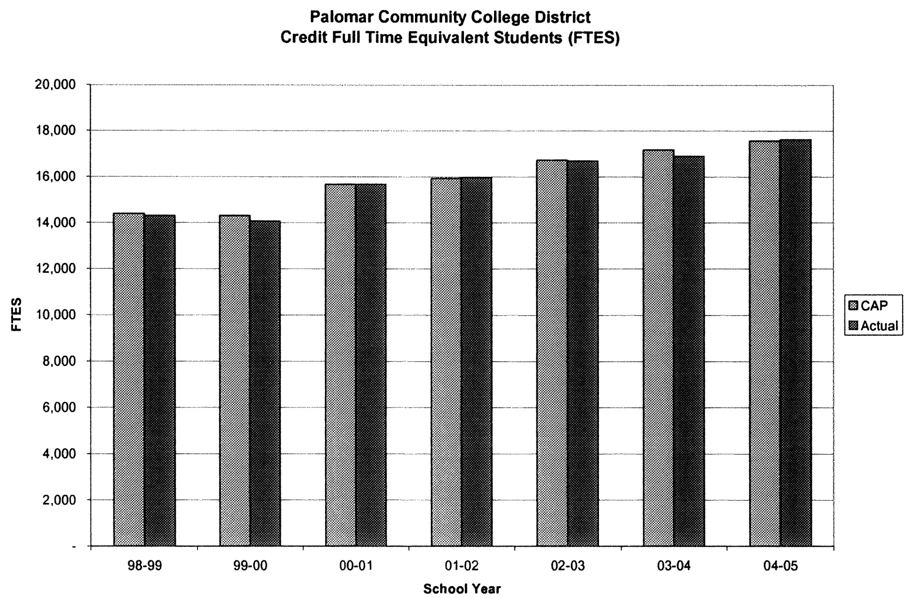
This section is to provide an overview of the District's financial activities. This is the third year of the new GASB reporting format of information presented in Management's Discussion and Analysis and in the accompanying audited financial statements. A comparative analysis is now provided for years in which we have this new format.

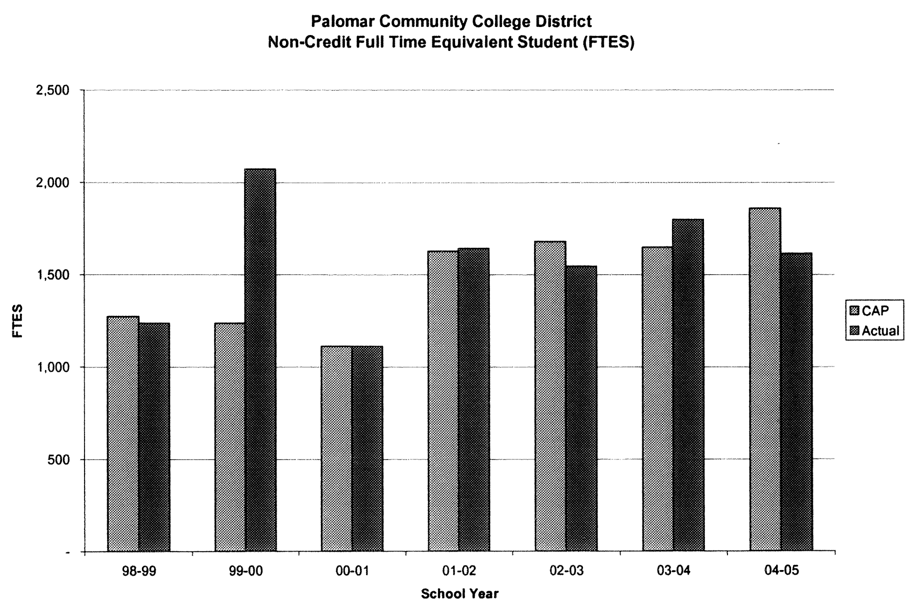
Selected Highlights

Total full-time equivalent students (FTES) increased approximately 4.24% for credit and decreased 10.24% for non-credit courses for an overall increase of 2.85%. The District exceeded its capped funding for credit by 59.21 FTES. Credit and non-credit FTES, along with other workload measures, are the basis for the District's state apportionment.

PALOMAR COMMUNITY COLLEGE DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2005





The District's net assets exceeded liabilities by $53.4 million.

Overall revenues were $115 million, which exceeded expenses by $4.2 million.

The District started construction on the new High Technology building in 2004-05. The scheduled completion date is fall of 2006.

Statement of Net Assets

The Statement of Net Assets presents the assets, liabilities and net assets of the District as of the end of the fiscal year and is prepared using the accrual basis of accounting, which is similar to the accounting basis used by most private-sector organizations. The Statement of Net Assets is a point of time financial statement whose purpose is to present to the readers a fiscal snapshot of the District. The Statement of Net Assets presents end-of-year data concerning assets (current and non-current), liabilities (current and non-current), and net assets (assets minus liabilities).

From the data presented, readers of the Statement of Net Assets are able to determine the assets available to continue the operations of the District. Readers are also able to determine how much the District owes vendors and employees. Finally, the Statement of Net Assets provides a picture of the net assets and their availability for expenditure by the District.

The difference between total assets and total liabilities (net assets) is one indicator of the current financial condition of the District; the change in net assets is an indicator of whether the overall financial condition has improved or worsened during the year. Assets and liabilities are generally measured using current values. One notable exception is capital assets, which are stated at historical cost less an allocation for depreciation expense.

The Net Assets are divided into three major categories. The first category, invested in capital assets, provides the equity amount in property, plant, and equipment owned by the District. The second category is expendable restricted net assets; these net assets are available for expenditure by the District, but must be spent for purposes as determined by external entities and/or donors that have placed time or purpose restrictions on the use of the assets. The final category is unrestricted net assets that are available to the District for any lawful purpose of the District.

PALOMAR COMMUNITY COLLEGE DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2005

A Statement of Net Assets as of June 30, 2005 is summarized below:

	(In Millions of Dollars) 2004	2005
ASSETS		
Current assets		
Cash and cash equivalents	$ 39.8	$ 33.3
Receivables	5.5	8.2
Prepaid expenses	0.5	0.5
Total current assets	45.8	42.0
Non-Current assets		
Restricted cash and cash equivalents	2.2	0.3
Capital assets, net	25.5	29.8
Total noncurrent assets	27.7	30.1
TOTAL ASSETS	$ 73.5	$ 72.1
LIABILITIES		
Current liabilities		
Accounts payable	$ 11.4	$ 6.2
Deferred revenue	2.0	1.1
Compensated absences	2.3	2.3
Long-term liabilities	0.5	0.4
Total current liabilities	16.2	10.0
Non-current liabilities		
Long-term liabilities less current portion	8.8	8.6
Total non-current liabilities	8.8	8.6
TOTAL LIABILITIES	25.0	18.6
NET ASSETS		
Invested in capital assets, net of related debt	16.2	20.8
Restricted	10.3	17.6
Unrestricted	22.0	15.1
TOTAL NET ASSETS	48.5	53.5
TOTAL NET ASSETS AND LIABILITIES	$ 73.5	$ 72.1

PALOMAR COMMUNITY COLLEGE DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2005

- Over 90% of the cash balance is cash deposited in the San Diego County Treasury, and approximately 2% is in other various investments related to the Certificates of Participation and Revenue Bonds. The remaining amounts are deposits with various financial institutions.

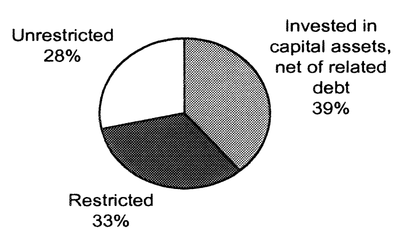
- The majority of the accounts receivable balance is from federal and state sources for grant and entitlement programs.

- Prior to 2001-02, Palomar College did not maintain records of the historical cost of capital assets. To comply with the new reporting requirement, the District contracted with an outside valuation company to obtain a complete listing of the historical cost and accumulated depreciation information for all capital assets within the capitalization policy established by the District. Depreciation expense net of retired assets of approximately $2.8 million was recognized during 2004-05. The capital asset section of this discussion and analysis provides greater detail.

- Accounts payable are amounts due as of the fiscal year end for goods and services received as of June 30, 2005. Total accounts payable are $6.2 million. Total current liabilities of approximately $10 million consist of amounts payable to or on behalf of employees for wages, benefits, accrued vacation, or load banking earned but not yet paid.

- The District currently has two debt issues outstanding that amount to $8.8 million; $5.9 million of this total is related to Certificates of Participation and $2.9 million is related to Revenue Bonds. Long-term debt also includes capital leases of $0.3 million. Additional information regarding long-term debt is included in the Debt Administration section of this discussion and analysis.

Net Assets
June 30, 2005



PALOMAR COMMUNITY COLLEGE DISTRICT

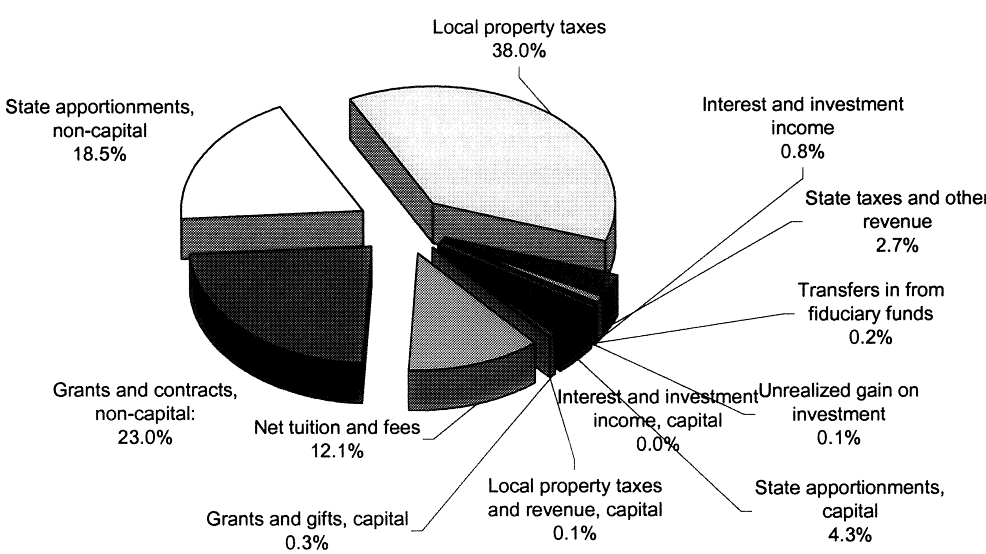
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2005

Statement of Revenues, Expenses, and Changes in Net Assets

Changes in total net assets as presented on the Statement of Net Assets are based on the activity presented in the Statement of Revenues, Expenses, and Changes in Net Assets. The purpose of this statement is to present the operating and non-operative revenues earned, whether received or not, by the District, the operating and non-operating expenses incurred, whether paid or not, by the District, and any other revenues, expenses, gains and/or losses earned or incurred by the District. Thus, this Statement presents the District's results of operations.

Generally, operating revenues are earned for providing goods and services to the various customers and constituencies of the District. Operating expenses are those expenses incurred to acquire or produce the goods and services provided in return for the operating revenues and to fulfill the mission of the District. Non-operating revenues are those received or pledged for which goods and services are not provided; for example, state appropriations are non-operating because they are provided by the legislature to the District without the legislature directly receiving commensurate goods and services for those revenues.

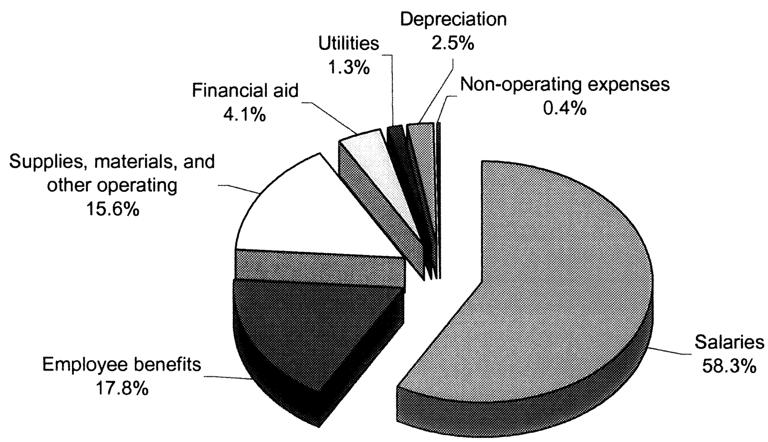
Palomar Community College District
Revenues
For the Year Ended June 30, 2005



PALOMAR COMMUNITY COLLEGE DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2005

Palomar Community College District
Expenses
For the Year Ended June 30, 2005



PALOMAR COMMUNITY COLLEGE DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2005

Statement of Revenues, Expenses and Changes in Net Assets for year ended
As of June 30 Each Year

	(In Millions of Dollars) 2004	2005
Operating Revenue		
Net tuition and fees	$ 10.7	$ 13.9
Grants and contracts, non-capital	23.3	26.4
Total operating revenues	34.0	40.3
Operating Expenses		
Salaries and benefits	74.9	84.2
Supplies and other expenses	16.6	18.8
Financial aid	3.5	4.6
Depreciation	2.8	2.8
Total operating expenses	97.8	110.4
Operating Loss	(63.8)	(70.1)
Non-operating revenues (expenses)		
State apportionments, non-capital	21.5	21.3
Local property taxes	38.6	43.6
State taxes and other revenues	3.4	3.1
Investment income, net	0.4	1.0
Transfers, net	0.1	0.0
Other non-operating expenses, net	(0.3)	(0.1)
Total non-operating revenues (expenses)	63.7	68.9
Other revenues, expenses, gains or losses		
State apportionments, capital	0.3	4.9
Local property taxes, capital	0.0	0.1
Grants and gifts, capital	0.0	0.4
Total other revenues, expenses, gains or losses	0.3	5.4
Change in Net Assets	0.2	4.2
Net assets, beginning of year	48.3	48.5
Adjustment for restatement		0.7
Net assets, end of year	$ 48.5	$ 53.4

- Tuition and fees are generated by the resident, non-resident, and foreign fees paid by students attending Palomar College, including fees such as health fees, parking fees, community services classes and other related fees.

- Non-capital grants and contracts are primarily those received from federal and state sources and used in the instructional program. This has remained fairly flat.

- Personnel costs make up 76% of total operating expenses. The balance of operating expenses is for supplies, other services, and capital outlay items below the capitalization threshold, insurance, utilities, and depreciation expense. There were several salary settlements this year, along with a COLA increase which accounts for the increase in salaries and benefits.

- State apportionment is generated based on the workload measures reported to the state by the District. The District has experienced a slight decrease in apportionment.

- Local property taxes are received through the Auditor-Controller's Office for San Diego County. The amount received for property taxes is deducted from the total state general apportionment amount calculated by the state for the District. The housing market has remained strong in the San Diego area. Home sales are starting to slow down, but valuations remain high.

- State apportionments, capital are the amount of capital outlay, scheduled maintenance, architectural barrier removal and hazardous substance funding received from the state through the Department of Finance. Capital outlay projects are typically funded 100% percent by the state while the other programs are funded at 50% to 90%.

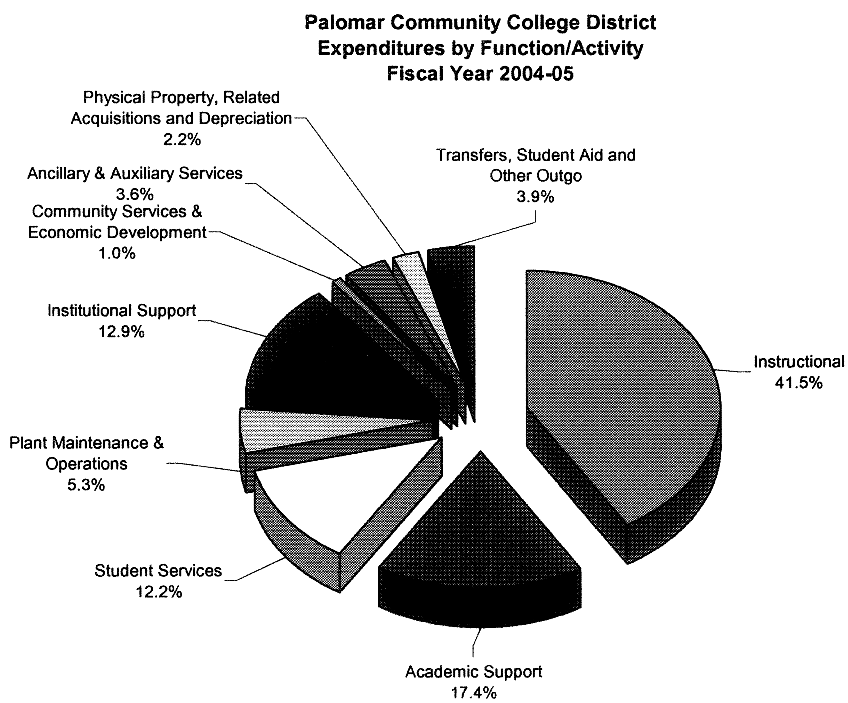
- Functional expenses are presented below. Governmental funds included are General Fund, Debt Service Fund, Child Development, Capital Outlay, Energy Conservation, Escondido Tenancies, Retiree Benefits, and Student Financial Aid. More detail on objects for fiscal year 2004-05 is included in Note 14 of the financial statements.

PALOMAR COMMUNITY COLLEGE DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2005

Expenditures by Function (Activity/Program)
Fiscal Year Comparison

Activity	Code	2002-03 Total	% of Total	2003-04 Total	% of Total	2004-05 Total	% of Total
Instructional	01-59	$ 38,127,102	38.34%	$ 39,553,644	40.16%	$ 45,804,671	41.50%
Academic Support	60-62	$ 19,246,779	19.35%	$ 19,191,890	19.48%	$ 19,251,522	17.44%
Student Services	63-64	$ 9,367,476	9.42%	$ 9,829,498	9.98%	$ 13,513,185	12.24%
Plant Maintenance & Operations	65	$ 4,850,755	4.88%	$ 5,207,412	5.29%	$ 5,894,459	5.34%
Institutional Support	66-67	$ 13,519,982	13.60%	$ 13,349,731	13.55%	$ 14,197,037	12.86%
Community Services & Economic Development	68	$ 593,353	0.60%	$ 955,741	0.97%	$ 1,065,421	0.97%
Ancillary & Auxiliary Services	69-70	$ 3,619,099	3.64%	$ 3,824,561	3.88%	$ 3,926,123	3.56%
Physical Property and Related Acquisitions	71	$ 3,617,579	3.64%	$ 2,921,115	2.97%	$ 2,416,330	2.19%
Transfers, Student Aid and Other Outgo	72-73	$ 6,494,477	6.53%	$ 3,659,402	3.72%	$ 4,309,451	3.90%
Total		$ 99,436,602	100.00%	$ 98,492,994	100.00%	$ 110,378,199	100.00%



Statement of Cash Flows

The Statement of Cash Flows provides information about cash receipts and cash payments during the fiscal year. This Statement also helps users assess the District's ability to generate positive cash flows, meet obligations as they come due and the need for external financing.

The Statement of Cash Flows is divided into five parts. The first part reflects operating cash flows and shows the net cash provided by the operating activities of the District. The second part details cash received for non-operating, non-investing, and non-capital financing purposes. The third part shows cash flows from capital and related financing activities. This part deals with the cash used for the acquisition and construction of capital and related items. The fourth part provides information from investing activities and the amount of interest received. The last section reconciles the net cash provided by operating activities to the operating loss reflected on the Statement of Revenues, Expenses, and Changes in Net Assets.

A Statement of Cash Flows for the fiscal year ended June 30, 3004 and 2005 is summarized below:

Statement of Cash Flows
As of June 30 each year

	(In Millions of Dollars) 2004	2005
Cash Provided by (Used in)		
Operating activities	$ (58.0)	$ (73.9)
Non-capital financing activities	60.5	67.9
Capital and related financing activities	(0.9)	(3.3)
Investing activities	0.3	0.7
Net increase/(decrease) in cash and cash equivalents	1.9	(8.6)
Cash balance, beginning of year	39.4	41.3
Cash balance, end of year	$ 41.3	$ 32.7

- Cash receipts from operating activities are from student tuition and from federal, state, and local grants. Uses of cash are payments to employees, vendors and students related to the instructional program. Salary settlements, including retroactive increases, along with step and column increases made up the majority of the increase in cash used for operating activities.

- State apportionment received based on the workload measures generated by the District accounts for 31% of non-capital financing. Cash received from property taxes accounts for 64% of the cash generated in this section. The increase in property tax was indicative of the strong property valuations and sales that continue in the San Diego area.

- The primary use included in capital and related financing activities is the purchase of capital assets (building improvements and equipment). The new High Tech building represented most of the increase in costs in this area.

- Cash from investing activities is interest earned on cash in bank and cash invested though the San Diego County pool and on investments with LAIF and other various investments.

District's Fiduciary Responsibility

The District is the trustee, or fiduciary, for certain amounts held on behalf of students, clubs, and donors for student loans and scholarships. The District's fiduciary activities are reported in separate Statements of Fiduciary Net Assets and Changes in Fiduciary Net Assets. These activities are excluded from the District's other financial statements because we cannot use these assets to finance operations. The District is responsible for ensuring that the assets reported in these funds are used for their intended purposes.

Capital Asset and Debt Administration

Capital Assets

As of June 30, 2005, the District had over $29.8 million invested in net capital assets. Total capital assets of $60.8 million consist of land, buildings, and building improvements, construction in progress, vehicles, data processing equipment, and other office equipment. Accumulated depreciation related to these assets is $31 million. Depreciation expense of $2.8 million was recorded for the fiscal year, however due to adjustments concerning some asset acquisition year corrections the overall accumulated depreciation decreased.

Capital additions primarily comprise replacement, renovation, and new construction of facilities, as well as significant investments in equipment, including information technology. Current year additions were primarily continuing construction on the new High Tech building.

Construction in progress of approximately $7.7 million at June 30, 2005 consists mainly of a capital outlay project for construction of the new High Technology building. The High Technology building was in the planning phase during 2001-02 and 2002-03. Construction started in earnest in 2004-05 and is reflected in the increased expenditures for construction in progress.

Note 5 to the financial statements provides additional information on capital assets. A summary of capital assets, net of depreciation, is presented below:

Capital Assets, net of Depreciation
As of June 30 Each Year

	(In Millions of Dollars)	
	2004	2005
Land	$ 8.2	$ 7.3
Site and Site Improvement	11.3	12.2
Equipment	3.8	2.6
Construction in Progress	2.2	7.7
Net Capital Assets	$ 25.5	$ 29.8

Debt

At June 30, 2005, the District had $9.1 million in debt; $0.3 million from capital lease obligations, $5.9 million from certificates of participation and $2.9 million in revenue bonds payable.

These financial statements do not include the actuarially determined liability for retiree benefits. Current GASB pronouncements do not allow inclusion of this liability in the financial statements. GASB pronouncements 45 will address the financial statement presentation related to this liability. Note 12 provides additional information.

Note 10 to the financial statements provides additional information on long-term liabilities. A summary of long-term debt is presented below:

Summary of Long-Term Debt
As of June 30 Each Year

	(In Millions of Dollars)	
	2004	2005
Long Term Debt		
Capital leases	$ 0.2	$ 0.3
COP payable	6.1	5.9
Revenue bonds payable	3.0	2.9
Total long-term debt	9.3	9.1
Less current portion	0.5	0.4
Long term Portion	$ 8.8	$ 8.7

Economic Factors that May Affect the Future

The economic position of the District is closely tied to that of the State of California. We are concerned for fiscal year 2005-06 due to the economy and budget for the State of California. In addition to reductions in funding, all industries, including education, in California are experiencing increased costs for services and especially increased costs for employee benefits, insurance, and utilities. Declines in enrollment are a concern for community colleges statewide.

The District recognizes that the current budgets identify an on-going operational deficit. The Strategic Planning Council initiated the Fiscal Stability Task Force (FSTF) charged with adjusting the 2004-05 budget to a reasonable deficit level and "right-sizing" the budget for 2005-06 and beyond. The FSTF initiated processes which resulted in identifying and capturing over budgeted amounts. Fiscal year 2005-06 was the first year that the District built its budget for all departmental discretionary accounts based on past experience and projected needs rather than continuing to roll over the budget amounts.

GASB 45 will have a major impact as it requires Districts to develop and implement a plan for funding future retiree benefits. Palomar College has already undertaken two actuarial studies and has begun setting aside money to fund the unfunded liability. However, this will continue to have a major financial impact in the future.

Other than the items discussed above, the District is not aware of any currently known facts, decisions or conditions that are expected to have a significant effect on the financial position or results of operations during this fiscal year beyond those unknown variations having a global effect on virtually all types of business operations. Management will maintain a close watch over resources to maintain our ability to react to internal and external issues if and when they arise.

BASIC FINANCIAL STATEMENTS

PALOMAR COMMUNITY COLLEGE DISTRICT

STATEMENT OF NET ASSETS
June 30, 2005

ASSETS	
Current assets:	
Cash and cash equivalents	$ 32,494,572
Investments	722,069
Accounts receivable, net	8,227,005
Due from fiduciary funds	2,100
Prepaid expenses	525,609
Total current assets	41,971,355
Non-current assets:	
Restricted cash and cash equivalents	249,500
Capital assets, net of accumulated depreciation	29,836,937
Total non-current assets	30,086,437
TOTAL ASSETS	$ 72,057,792
LIABILITIES	
Current liabilities:	
Accounts payable	$ 2,677,638
Accrued liabilities	3,402,586
Deferred revenue	1,083,177
Due to fiduciary funds	141,754
Compensated absences	2,259,739
Capital leases - current portion	76,474
COP payable - current portion	290,000
Revenue bonds payable - current portion	60,000
Total current liabilities	9,991,368
Non-current liabilities:	
Capital leases	209,258
COP payable	5,595,000
Revenue bonds payable	2,830,000
Total non-current liabilities	8,634,258
TOTAL LIABILITIES	18,625,626
NET ASSETS	
Invested in capital assets, net of related debt	20,776,205
Restricted for:	
Capital projects	6,704,517
Debt service	722,069
Other special services	10,099,473
Unrestricted	15,129,902
TOTAL NET ASSETS	53,432,166
TOTAL LIABILITIES AND NET ASSETS	$ 72,057,792

See the accompanying notes to the financial statements.

PALOMAR COMMUNITY COLLEGE DISTRICT

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
For the Fiscal Year Ended June 30, 2005

OPERATING REVENUES	
Tuition and fees (gross)	$ 16,498,853
Less: scholarship discounts & allowances	(2,623,101)
Net tuition and fees	13,875,752
Grants and contracts, non-capital:	
Federal	6,316,608
State	13,887,772
Local	6,190,480
TOTAL OPERATING REVENUES	40,270,612
OPERATING EXPENSES	
Salaries	64,614,886
Employee benefits	19,572,216
Supplies, materials, and other operating expenses and services	17,383,993
Financial aid	4,572,744
Utilities	1,466,864
Depreciation	2,767,496
TOTAL OPERATING EXPENSES	110,378,199
OPERATING LOSS	(70,107,587)
NON-OPERATING REVENUES (EXPENSES)	
State apportionments, non-capital	21,260,239
Local property taxes	43,647,692
State taxes and other revenue	3,114,104
Interest and investment income	939,309
Transfers in from fiduciary funds	191,157
Unrealized gain on investment	165,566
Loss on disposal of capital assets	(5,394)
Transfers out to fiduciary funds	(185,254)
Debt service	(186,911)
TOTAL NON-OPERATING REVENUES (EXPENSES)	68,940,508
LOSS BEFORE OTHER REVENUES, EXPENSES, GAINS AND LOSSES	(1,167,079)
OTHER REVENUES, EXPENSES, GAINS AND LOSSES	
State apportionments, capital	4,887,221
Grants and gifts, capital	370,000
Local property taxes and revenue, capital	73,996
Interest and investment income, capital	42,031
TOTAL OTHER REVENUES, EXPENSES, GAINS AND LOSSES	5,373,248
INCREASE IN NET ASSETS	4,206,169
NET ASSETS - BEGINNING OF YEAR	48,501,929
ADJUSTMENT FOR RESTATEMENT (Note 10)	724,068
NET ASSETS, BEGINNING OF YEAR - AS ADJUSTED	49,225,997
NET ASSETS - END OF YEAR	$ 53,432,166

See the accompanying notes to the financial statements.

PALOMAR COMMUNITY COLLEGE DISTRICT

STATEMENT OF CASH FLOWS

For the Fiscal Year Ended June 30, 2005

CASH FLOWS FROM OPERATING ACTIVITIES	
Tuition and fees	$ 14,154,534
Federal grants and contracts	6,477,408
State grants and contracts	11,082,570
Local grants and contracts	4,873,645
Payments to suppliers	(16,997,933)
Payments to/on-behalf of employees	(89,303,176)
Payments to/on-behalf of students	(4,069,045)
Payments for other uses	(506,501)
Net amounts due from fiduciary funds	396,282
Net cash used by operating activities	(73,892,216)
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES	
State apportionments and receipts	21,161,869
Property taxes	43,594,828
Grants and gifts for other than capital purposes	3,126,993
Net cash provided by non-capital financing activities	67,883,690
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES	
State apportionment for capital purposes	2,985,917
Interest on capital investments	180,240
Property taxes - capital	370,000
Purchase of capital assets	(6,093,092)
Principal paid on capital debt	(335,000)
Interest paid on capital debt	(412,480)
Net cash used by capital and related financing activities	(3,304,415)
CASH FLOWS FROM INVESTING ACTIVITIES	
Interest on investments	721,180
Purchase of investments	(743,344)
Sale of investments	747,480
Net cash provided by investing activities	725,316
NET DECREASE IN CASH AND CASH EQUIVALENTS	(8,587,625)
CASH BALANCE - BEGINNING OF YEAR	41,331,697
CASH BALANCE - END OF YEAR	$ 32,744,072

See the accompanying notes to the financial statements.

PALOMAR COMMUNITY COLLEGE DISTRICT

STATEMENT OF CASH FLOWS
For the Fiscal Year Ended June 30, 2005

Reconciliation of Operating Loss to
Net Cash Used by Operating Activities

CASH USED BY OPERATING ACTIVITIES

Operating loss	$ (70,107,587)
Adjustments to reconcile net loss to net cash used by operating activities:	
Depreciation expense	2,767,496
Changes in assets and liabilities:	
Receivables, net	(708,146)
Due to fiduciary funds (net)	78,116
Prepaid expenses	(11,307)
Accounts payable and accrued liabilities	(5,005,359)
Deferred revenue	(887,720)
Compensated absences	(17,709)
Net cash used by operating activities	$ (73,892,216)

See the accompanying notes to the financial statements.

PALOMAR COMMUNITY COLLEGE DISTRICT

STATEMENT OF FIDUCIARY NET ASSETS
June 30, 2005

ASSETS		
Cash in county treasury	$	1,139,236
Cash on hand and in banks		130,462
Accounts receivable:		
Miscellaneous		24,784
Due from governmental funds		141,754
TOTAL ASSETS	$	1,436,236
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Accounts payable	$	7,119
Due to governmental funds		2,100
Deferred revenue		35,354
Amounts held for others		67,524
TOTAL LIABILITIES		112,097
NET ASSETS		
Undesignated		1,324,139
TOTAL NET ASSETS		1,324,139
TOTAL LIABILITIES AND NET ASSETS	$	1,436,236

See the accompanying notes to the financial statements.

PALOMAR COMMUNITY COLLEGE DISTRICT

STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS
For the Fiscal Year Ended June 30, 2005

ADDITIONS	
Interest and investment income	$ 31,125
Other local revenues	466,863
TOTAL ADDITIONS	497,988
DEDUCTIONS	
Classified salaries	7,284
Supplies and materials	47,117
Other operating expenses and services	140,180
Capital outlay	19,645
Other transfers out	8,262
TOTAL DEDUCTIONS	222,488
Excess of additions over deductions	275,500
OTHER SOURCES (USES)	
Transfers in from governmental funds	185,254
Transfers out to governmental funds	(191,157)
TOTAL OTHER SOURCES (USES)	(5,903)
CHANGE IN NET ASSETS	269,597
NET ASSETS - BEGINNING OF YEAR	1,054,542
NET ASSETS - END OF YEAR	$ 1,324,139

See the accompanying notes to the financial statements.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

A. REPORTING ENTITY

The District is the level of government primarily accountable for activities related to public education. The governing authority consists of elected officials who, together, constitute the Board of Trustees.

The District considered its financial and operational relationships with potential component units under the reporting entity definition of GASB Statement No. 14, The Financial Reporting Entity. The basic, but not the only, criterion for including another organization in the District's reporting entity for financial reports is the ability of the District's elected officials to exercise oversight responsibility over such agencies. Oversight responsibility implies that one entity is dependent on another and that the dependent unit should be reported as part of the other.

Oversight responsibility is derived from the District's power and includes, but is not limited to: financial interdependency; selection of governing authority; designation of management; ability to significantly influence operations; and accountability for fiscal matters.

Based upon the requirements of GASB Statement No. 14, and as amended by GASB Statement No. 39, Determining Whether Certain Organizations are Component Units, certain organizations warrant inclusion as part of the financial reporting entity because of the nature and significance of their relationship with the District, including their ongoing financial support to the District or its other component units. A legally separate, tax-exempt organization should be reported as a component unit of the District if all of the following criteria are met:

1. The economic resources received or held by the separate organization are entirely or almost entirely for the direct benefit of the District, its component units, or its constituents.

2. The District, or its component units, is entitled to, or has the ability to otherwise access, a majority of the economic resources received or held by the separate organization.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (continued)

A. REPORTING ENTITY (continued)

3. The economic resources received or held by an individual organization that the District, or its component units, is entitled to, or has the ability to otherwise access, are significant to the District.

Based upon the application of the criteria listed above, the following potential component unit has been excluded from the District's reporting entity:

Palomar College Foundation - The Foundation is a separate not-for-profit corporation. The Foundation is not included as a Component unit because the third criterion above was not met.

Separate financial statements for the Foundation may be obtained through the District.

B. FINANCIAL STATEMENT PRESENTATION

The accompanying financial statements have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB), including Statement No. 34, Basic Financial Statements and Management's Discussion and Analysis – for State and Local Governments and including Statement No. 35, Basic Financial Statements and Management's Discussion and Analysis of Public College and Universities, issued in June and November 1999 and Audits of State and Local Governmental Units issued by the American Institute of Certified Public Accountants. The financial statement presentation required by GASB No. 34 and No. 35 provides a comprehensive, entity-wide perspective of the District's financial activities. The entity-wide perspective replaces the fund-group perspective previously required. Fiduciary activities, with the exception of the Student Financial Aid Fund and the Retiree Benefits Fund, are excluded from the basic financial statements.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (continued)

C. BASIS OF ACCOUNTING

Basis of accounting refers to when revenues and expenditures or expenses are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of measurement made, regardless of the measurement focus applied.

For financial reporting purposes, the District is considered a special-purpose government engaged in business-type activities. Accordingly, the District's basic financial statements have been presented using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred. All significant intra-agency transactions have been eliminated.

For internal accounting purposes, the budgetary and financial accounts of the District have been recorded and maintained in accordance with the Chancellor's Office of the California Community College's Budget and Accounting Manual.

To ensure compliance with the California Education Code, the financial resources of the District are divided into separate funds for which separate accounts are maintained for recording cash, other resources and all related liabilities, obligations and equities.

By State law, the District's Governing Board must approve a budget no later than September 15. A public hearing must be conducted to receive comments prior to adoption. The District's Governing Board satisfied these requirements. Budgets for all governmental funds were adopted on a basis consistent with generally accepted accounting principles (GAAP).

These budgets are revised by the District's Governing Board during the year to give consideration to unanticipated income and expenditures. Formal budgetary integration was employed as a management control device during the year for all budgeted funds. Expenditures cannot legally exceed appropriations by major object account.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (continued)

C. BASIS OF ACCOUNTING (continued)

In accordance with GASB Statement No. 20, the District follows all GASB statements issued prior to November 30, 1989 until subsequently amended, superseded or rescinded. The District also applies all Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989 unless FASB conflicts with GASB.

1. Cash and Cash Equivalents

Cash in the County Treasury is recorded at fair value, in accordance with the requirements of GASB Statement No. 31. The District's cash and cash equivalents, are considered to be cash on hand, demand deposits and short-term investments with original maturities of three months or less from the date of acquisition.

2. Accounts Receivable

Accounts receivable consists primarily of amounts due from the Federal government, State and local governments, or private sources, in connection with reimbursement of allowable expenditures made pursuant to the District's grant and contracts. Accounts receivable are recorded net of estimated uncollectible amounts.

3. Prepaid Expenses

Payments made to vendors for services that will benefit periods beyond June 30, 2005, are recorded as prepaid items using the consumption method. A current asset for the prepaid amount is recorded at the time of the purchase and an expenditure/expense is reported in the year in which services are consumed.

4. Restricted Cash and Cash Equivalents

Restricted cash and cash equivalents are those amounts externally restricted as to use pursuant to the requirements of the District's grants, contracts and debt service requirements.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (continued)

C. BASIS OF ACCOUNTING (continued)

5. Capital Assets

Capital assets are recorded at cost at the date of acquisition. Donated capital assets are recorded at their estimated fair value at the date of donation. For equipment, the District's capitalization policy includes all items with a unit cost of $5,000 or more and an estimated useful life of greater than one year. Buildings, renovations to building and infrastructure with a unit cost of $100,000 or more, and land and site improvements, with a unit cost of $50,000 or more, that significantly increase the value or extend the useful life of the structure, are capitalized. Interest incurred during construction is not capitalized.

The cost of normal maintenance and repairs that does not add to the value of the asset or materially extend the asset's life is recorded in operating expense in the year in which the expense was incurred. Depreciation is computed using the straight-line method with a half-year convention over the estimated useful lives of the assets, generally 50 years for buildings and certain major building and site improvements, 15 years for modular buildings and land improvements, 5 to 8 years for equipment and 3 years for technology.

6. Accounts Payable

Accounts payable consists of amounts due to vendors and accrued interest.

7. Accrued Liabilities

Accrued liabilities consist of salaries and benefits payable.

8. 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 cash received on specific projects and programs exceed qualified expenditures.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (continued)

C. BASIS OF ACCOUNTING (continued)

9. Compensated Absences

In accordance with GASB Statement No. 16, accumulated unpaid employee vacation benefits are recognized as liabilities of the District as compensated absences in the Statement of Net Assets.

The District has accrued a liability for the amounts attributable to load banking hours within accounts payable. Load banking hours consist of hours worked by instructors in excess of a full-time load for which they may carryover for future paid time off.

Sick leave benefits are accumulated without limit for each employee. The employees do not gain a vested right to accumulated sick leave.

Accumulated employee 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 and within the constraints of the appropriate retirement systems.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (continued)

C. BASIS OF ACCOUNTING (continued)

10. Net Assets

Invested in capital assets, net of related debt: This represents the District's total investment in capital assets, net of outstanding debt obligations related to those capital assets. To the extent debt has been incurred but not yet expended for capital assets, such amounts are not included as a component of invested in capital assets, net of related debt.

Restricted net assets – expendable: Restricted expendable net assets include resources in which the District is legally or contractually obligated to spend resources in accordance with restrictions imposed by external third parties.

Restricted net assets – non-expendable: Non-expendable restricted net assets consist of endowment and similar type funds in which donors or other outside sources have stipulated, as a condition of the gift instrument, that the principal is to be maintained inviolate and in perpetuity, and invested for the purpose of producing present and future income, which may either be expended or added to principal. The District had no restricted net assets – non-expendable.

Unrestricted net assets: Unrestricted net assets represent resources available to be used for transactions relating to the general operations of the District, and may be used at the discretion of the governing board, as designated, to meet current expenses for specific future purposes.

11. State Apportionments

Certain current year apportionments from the State are based upon various financial and statistical information of the previous year.

Any prior year corrections due to the recalculation in February of 2006 will be recorded in the year computed by the State.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (continued)

C. BASIS OF ACCOUNTING (continued)

12. Property Taxes

Secured property taxes attach as an enforceable lien on property as of January 1. Taxes are payable in two installments on November 15 and March 15. Unsecured property taxes are payable in one installment on or before August 31.

Real and personal property tax revenues are reported in the same manner in which the County auditor records and reports actual property tax receipts to the Department of Education. This is generally on a cash basis. A receivable has not been recognized in the General Fund for property taxes due to the fact that any receivable is offset by a payable to the State for apportionment purposes. Property taxes for debt service purposes have not been accrued in the basic financial statements as the amount is not material.

13. On-Behalf Payments

GASB Statement No. 24 requires that direct on-behalf payments for fringe benefits and salaries made by one entity to a third party recipient for the employees of another, legally separate entity be recognized as revenue and expenditures by the employer government. The State of California makes direct on-behalf payments for retirement benefits to the State Teachers Retirement System on behalf of all Community Colleges in California. However, a fiscal advisory was issued by the California Department of Education instructing districts not to record revenue and expenditures for these on-behalf payments. The amount of on-behalf payments made for the District is estimated at $678,800 for STRS.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (continued)

C. BASIS OF ACCOUNTING (continued)

14. Classification of Revenues

The District has classified its revenues as either operating or non-operating revenues according to the following criteria:

Operating revenues: Operating revenues include activities that have the characteristics of exchange transactions, such as student fees, net of scholarship discounts and allowances, and Federal and most State and local grants and contracts.

Non-operating revenues: Non-operating revenues include activities that have the characteristics of non-exchange transactions, such as State apportionments, taxes, and other revenue sources that are defined as non-operating revenues by GASB No. 9, Reporting Cash Flows of Proprietary and Non-expendable Trust Funds and Governmental Entities that use Proprietary Fund Accounting, and GASB No. 33, such as investment income.

15. Scholarship Discounts and Allowances

Student tuition and fee revenues, and certain other revenues from students, are reported net of scholarship discounts and allowances in the statement of revenues, expenses, and changes in net assets. Scholarship discounts and allowances are the difference between the stated charge for goods and services provided by the District, and the amount that is paid by students and/or third parties making payments on the students' behalf. Certain governmental grants, such as Pell grants, and other Federal, State or non-governmental programs, are recorded as operating revenues in the District's financial statements. To the extent that revenues from such programs are used to satisfy tuition and fees and other student charges, the District has recorded a scholarship discount and allowance.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (continued)

C. BASIS OF ACCOUNTING (continued)

16. Estimates

The preparation of the financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Some of the more common estimates would relate to year end accruals for receivables and payables, and useful lives of capital assets. Actual results may differ from those estimates.

NOTE 2 - DEPOSITS AND INVESTMENTS:

A. Custodial Credit Risk - Deposits

Custodial credit risk is the risk that in the event of a bank failure, the District's deposits may not be returned to it. The District does not have a deposit policy for custodial risk. As of June 30, 2005, $ 1,430,043 of the District's bank balance of $1,530,043 was exposed to credit risk as follows:

Collateral held by pledging bank's trust department but not specifically in the District's name	$1,430,043

In accordance with the Budget and Accounting Manual, the District maintains substantially all of its cash in the San Diego County Treasury as part of the common investment pool. These pooled funds are carried at cost which approximates fair value. The fair market value of the District's deposits in this pool as of June 30, 2005, as provided by the pool sponsor, was $32,084,933. Interest earned is deposited monthly into participating funds. Any investment losses are proportionately shared by all funds in the pool.

NOTE 2 - DEPOSITS AND INVESTMENTS: (continued)

B. Investments

Under provisions of California Government Code Sections 53601 and 53602 and District Board Policy Section 6006, the District may invest in the following types of investments:

- State of California Local Agency Investment Fund (LAIF)
- San Diego County Investment Pools
- U.S. Treasury notes, bonds, bills or certificates of indebtedness
- U.S. Government Agency guaranteed instruments
- Fully insured or collateralized certificates of deposit
- Prime Commercial Paper having an "AA" rating or better

Investments and Investments with Fiscal Agent at June 30, 2005 are presented below:

Investment	Maturities	Fair Value
MBIA Investment Agreement	10/1/2019	$527,982
First American Treasury Obligation		131
Bayerische Landesbank	4/1/2031	193,956
Total		$722,069

The investments in MBIA Investment Agreement and Bayerische Landesbank are Guaranteed Investment Contracts (GIC), therefore no risk is disclosed.

Interest Rate Risk

The District does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates

NOTE 3 - ACCOUNTS RECEIVABLE:

The accounts receivable balance as of June 30, 2005 consists of the following:

Federal and State	$7,009,287
Miscellaneous	1,217,718

NOTE 4 - INTERFUND TRANSACTIONS:

Interfund transfers consist of operating transfers from funds receiving resources to funds through which the resources are to be expended. Interfund receivables and payables result when the interfund transfer is transacted after the close of the fiscal year. Interfund activity between governmental funds has been eliminated in the basic financial statements.

NOTE 5 - CAPITAL ASSETS:

The following provides a summary of changes in capital assets for the year ended June 30, 2005:

	Balance July 1, 2004	Additions	Adjustments	Deletions	Balance June 30, 2005
Capital Assets					
Land and improvements	$15,622,795	$	$	$	$15,622,795
Site and site improvements	23,764,291	616,976			24,381,267
Equipment	15,131,265	843,601	(2,655,201)	156,986	13,162,679
Construction in progress	2,171,981	5,585,153	515,180	615,846	7,656,468
Total cost	56,690,332	7,045,730	(2,140,021)	772,832	60,823,209
Accumulated Depreciation					
Land improvements	7,412,570	878,926			8,291,496
Site and site improvements	12,405,179	473,502	(754,937)		12,123,744
Equipment	11,416,708	1,415,068	(2,109,152)	151,592	10,571,032
Total accumulated depreciation	31,234,457	2,767,496	(2,864,089)	151,592	30,986,272
Net capital assets	$25,455,875	$ 4,278,234	$ 724,068	$ 621,240	$29,836,937

NOTE 5 - CAPITAL ASSETS: (continued)

During the 2004-05 fiscal year the District reviewed its capitalization policy and its listing of capitalized assets. The result of this process identified some assets which did not meet the capitalization policy and assets with incorrect acquisition dates. The following schedule identifies the changes made:

	Net Value
Deletion of software	$ (609,375)
Corrections to equipment inventory	63,326
Addition of construction in progress from 2003-04	515,180
Change in acquisition date	754,937
Total adjustment	$ 724,068

NOTE 6 - LEASES:

A. Capital Leases

The District leases equipment valued at approximately $1,129,000 under agreements which provide for title to pass upon expiration of the lease period. Future minimum lease payments are as follows:

Year Ended June 30	Principal	Interest	Total
2005-06	$ 76,474	$ 11,410	$ 87,884
2006-07	67,042	7,612	74,654
2007-08	69,720	4,935	74,655
2008-09	72,496	2,159	74,655
Total	$ 285,732	$ 26,116	$ 311,848

The District will receive no sublease rental revenues nor pay any contingent rentals for this equipment.

NOTE 6 - LEASES: (continued)

B. Operating Leases

The District has entered into various operating leases for land, buildings, and equipment with lease terms in excess of one year. None of these agreements contain purchase options. Future minimum lease payments under these agreements are as follows:

Fiscal Year	Lease Payment
2005-06	$ 234,853

Current year expenditures for operating leases is approximately $270,000. The District will receive no sublease rental revenues nor pay any contingent rentals for these properties.

NOTE 7 - CERTIFICATES OF PARTICIPATION:

A. The agreement dated January 13, 1999, is between the Palomar Community College District as the "lessee" and the California Community College Corporation as the "lessor" or "corporation". The Corporation is a legally separate entity which was formed for the purpose of capital improvement and then leasing such items to the participating district and to refinance the 1994 Certificates of Participation.

The Corporation's funds for acquiring these items were generated by the issuance of $7,480,000 of Certificates of Participation (COPs). COPs are long-term debt instruments which are tax exempt and therefore issued at interest rates below current market levels for taxable investments.

Lease Payments - Lease payments are required to be made by the District under the lease agreement on each April 1 and October 1 for use and possession of the equipment for the period commencing April 1, 1999 and terminating October 1, 2019. Lease payments will be funded in part from the proceeds of the Certificates. Interest rates range from 3.5% to 5.0% for the length of the issuance.

NOTE 7 - CERTIFICATES OF PARTICIPATION: (continued)

The lease requires that lease payments be deposited in the lease payment fund maintained by the trustee. Any amount held in the lease payment fund will be credited towards the lease payment due and payable. The trustee will pay from the lease payment fund the required principal and interest payments as follows:

Lease Payment Date	Principal	Interest	Total Payments
October 1, 2005	$ 290,000	$ 129,768	$ 419,768
April 1, 2006		124,331	124,331
October 1, 2006	300,000	124,331	424,331
April 1, 2007		118,556	118,556
October 1, 2007	310,000	118,556	428,556
April 1, 2008		112,356	112,356
October 1, 2008	325,000	112,356	437,356
April 1, 2009		105,856	105,856
October 1, 2009	340,000	105,856	445,856
April 1, 2010		98,886	98,886
10/1/2010 – 4/1/2015	1,915,000	786,262	2,701,262
10/1/2015 – 4/1/2020	2,405,000	287,792	2,692,792
Total	$ 5,885,000	$ 2,224,906	$ 8,109,906

B. In October 1994, the Palomar Community College District Financing Corporation issued Certificates of Participation in the amount of $6,875,000 with interest rates ranging from 4.30% to 6.50%. These certificates were refinanced in January 1999 and have been in-substance defeased. At June 30, 2004, $5,260,000 of the 1994 Certificates of Participation were outstanding. On October 1, 2004 the 1994 Certificates of Participation liability was repaid.

NOTE 8 - REVENUE BONDS:

The District issued Revenue Bonds on July 18, 2001 in the amount of $3,095,000 to be used to remodel and expand the Student Center. Interest rates on the bonds range from 5.0% to 5.625% for the length of the issuance. The bonds will mature on April 1, 2031. The source of revenue to pay off the debt will come from the Student Center Fee Fund. Future principal and interest payments are as follows:

Lease Payment Date	Principal	Interest	Total Payments
October 1, 2005	$	$ 72,167	$ 72,167
April 1, 2006	60,000	72,167	132,167
October 1, 2006		71,042	71,042
April 1, 2007	60,000	71,042	131,042
October 1, 2007		69,842	69,842
April 1, 2008	65,000	69,842	134,842
October 1, 2008		68,542	68,542
April 1, 2009	65,000	68,542	133,542
October 1, 2009		67,242	67,242
April 1, 2010	70,000	67,242	137,242
10/1/2010 – 4/1/2015	395,000	625,569	1,020,569
10/1/2015 – 4/1/2020	500,000	522,775	1,022,775
10/1/2020 – 4/1/2025	645,000	380,032	1,025,032
10/1/2025 – 4/1/2030	835,000	183,457	1,018,457
10/1/2030 – 4/1/2031	195,000	9,994	204,994
Total	$ 2,890,000	$ 2,419,497	$ 5,309,497

NOTE 9 - LONG-TERM DEBT:

A schedule of changes in long-term debt for the year ended June 30, 2005 is shown below:

	Balance July 1, 2004	Additions	Deductions	Balance June 30, 2005
Capital leases	$ 171,329	$ 336,792	$ 222,389	$ 285,732
Certificates of participation (COP)	6,160,000		275,000	5,885,000
Revenue bonds	2,950,000		60,000	2,890,000
Totals	$ 9,281,329	$ 336,792	$ 557,389	$ 9,060,732

NOTE 10 – ADJUSTMENT FOR RESTATEMENT

As identified in Note 5, the value of capital assets was evaluated during the 2004-05 fiscal year. The process identified asset values which required adjustment. The cumulative effect of these adjustments was a net increase in capital assets of $724,068. This amount is reported as an adjustment for restatement on the Statement of Revenues, Expenses and Changes in Net Assets.

NOTE 11 - EMPLOYEE RETIREMENT PLANS:

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

State Teachers' Retirement System (STRS)

Plan Description

The District contributes to the State Teachers' Retirement System (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 STRS, 7667 Folsom Boulevard, Sacramento, CA 95826.

NOTE 11 - EMPLOYEE RETIREMENT PLANS: (continued)

State Teachers' Retirement System (STRS) (continued)

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 2004-05 was 8.25% of annual payroll. The contribution requirements of the plan members are established and may be amended by State statute.

Public Employees' Retirement System (PERS)

Plan Description

The District contributes to the School Employer Pool under the California Public Employees' Retirement System (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 required supplementary information. Copies of the CalPERS' annual financial report may be obtain from the CalPERS Executive Office, 400 P Street, Sacramento, CA 95814.

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 average required employer contribution for fiscal year 2004-05 was 9.952% of annual payroll. The contribution requirements of the plan members are established and may be amended by State statute.

NOTE 11 - EMPLOYEE RETIREMENT PLANS: (continued)

Contributions to STRS and PERS

The District's contributions to STRS and PERS for each of the last three fiscal years is as follows:

	STRS		PERS	
Year Ended June 30,	Required Contribution	Percent Contributed	Required Contribution	Percent Contributed
2003	$2,580,601	100%	$ 566,774	100%
2004	2,458,564	100%	1,993,349	100%
2005	2,776,507	100%	2,029,623	100%

NOTE 12 - RETIREE BENEFITS:

The District currently provides retiree dental, medical or Medicare supplement coverage for employees that have rendered at least ten years of service for the District and have reached the age of 50 for PERS retirees or the age of 55 for STRS retirees. These benefits provide for both the employee and their spouse until death. For all new hires, after March, 1994, medical benefits are provided only to age 65 and dental benefits are provided for life. The estimated total gross liability, based upon an actuarial study dated June 9, 2005 is approximately $85.5 million; this actuarial liability is as of March 1, 2005 and is not reflected in these financial statements as long-term debt awaiting implementation of Governmental Accounting Standards Board Statement No. 45. In 2004-05, the District paid approximately $2,450,500 for retiree benefits. In addition, the District contributed approximately $536,200 toward the payment of the actuarial liability. The District has budgeted $2,658,238 for these benefits in 2005-06.

NOTE 13 - JOINT POWERS AGREEMENT:

The Palomar Community College District participates in three joint powers agreement (JPA) entities; the San Diego County Schools Fringe Benefits Consortium (SDCSFBC); the Statewide Association of Community Colleges (SWACC); and the Schools Excess Liability Fund (SELF). The relationship between the District and the JPAs is such that none of the JPAs are a component unit of the District for financial reporting purposes, as explained below.

The San Diego County Schools Fringe Benefits Consortium provides employee fringe benefits to various school districts and community college districts throughout San Diego County. The San Diego County Schools Fringe Benefits Consortium's governing board is made up of one representative from each member district.

The Statewide Association of Community Colleges provides property and liability coverage to various community college districts throughout California. SWACC is governed by a board consisting of one representative from each member district.

SELF arranges for and provides a self-funded or additional insurance for excess liability fund for approximately 1,100 public educational agencies. SELF is governed by a board of 16 elected voting members, elected alternates, and two ex-officio members. The board controls the operations of SELF, including selection of management and approval of operating budgets, independent of any influence by the members beyond their representation on the board. Each member pays an annual contribution based upon that calculated by SELF's board of directors and shares surpluses and deficits proportionately to its participation in SELF.

Previously the District participated in the San Diego County Schools Risk Management JPA (SDCRM-JPA). Currently they continue to make payments for on-going claims processed by the JPA.

NOTE 13 - JOINT POWERS AGREEMENT: (continued)

Condensed financial information of SDCSFBC, SWACC, and SELF for the most current information available is as follows:

	SDCSFBC 6/30/2004 (Audited)	SWACC 6/30/2005 (Unaudited)	SELF 6/30/2005 (Unaudited)
Total assets	$12,303,895	$28,208,879	$180,614,745
Total liabilities	6,175,323	17,248,919	174,685,047
Retained earnings	$ 6,128,572	$ 10,959,960	$ 5,929,698
Total revenues	$42,836,360	$ 9,373,188	$ 42,044,244
Total expenditures	41,993,895	4,837,422	61,979,691
Net increase/(decrease) in retained earnings	$ 842,465	$ 4,535,766	$ (19,935,447)

NOTE 14 - FUNCTIONAL EXPENSE:

	Salaries	Employee Benefits	Supplies, Materials, Utilities Other Expenses and Services	Financial Aid and Other Outgo	Depreciation	Total
Instructional	$ 32,848,380	$ 9,829,676	$ 3,126,615	$ -	$ -	$ 45,804,671
Academic Support	11,121,260	2,991,850	5,138,412			19,251,522
Student Services	8,634,274	2,322,799	2,524,602	31,510		13,513,185
Operation & Maintenance of Plant	2,600,240	699,519	2,594,700			5,894,459
Institutional Support	6,833,831	3,033,814	4,206,938	122,454		14,197,037
Community Services and Economic Development	352,762	95,679	616,979			1,065,421
Ancillary Services and Auxiliary Operations	2,224,138	598,879	993,777	109,329		3,926,123
Physical Property and Related Acquisitions			(351,166)			(351,166)
Transfers, Student Aid and Other Outgo				4,309,451		4,309,451
Depreciation Expense					2,767,496	2,767,496
Total	$ 64,614,886	$ 19,572,216	$ 18,850,857	$ 4,572,744	$ 2,767,496	$ 110,378,199

NOTE 15 - COMMITMENTS AND CONTINGENCIES:

A. State and Federal Allowances, Awards and Grants

The District has received State and Federal funds for specific purposes, including reimbursement of mandated costs, 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 reimbursement will not be material.

B. Ground Lease and Lease-Back Purchase Agreement

The District entered into a ground lease and lease back purchase of 1.8 acres for a parking lot at the Escondido Center in December of 1991 with the Community Development Commission of the City of Escondido (CDC). The debt service of the structure totaled $4,480,000 that is to be paid from a tax sharing agreement with the CDC. The tax sharing agreement provides direct funding to the CDC from the County from property tax for servicing the debt that was issued in their name. The outstanding debt as of June 30, 2005, including principal and interest, is $2,958,816.

C. Purchase Commitments

As of June 30, 2005, the District was committed under various capital expenditure purchase agreements for construction and modernization projects totaling approximately $27,000,000. Projects will be funded through Capital Outlay Funds.

NOTE 16 - SUBSEQUENT EVENT:

A. GASB Statement No. 45

The Governmental Accounting Standards Board (GASB) has recently issued GASB Statement No. 45 outlining new accounting standards for governmental agencies regarding other post-employment benefits. The statement will be effective for phase two GASB Statement No. 34 implementers in fiscal year 2008-09. The statement requires governmental agencies to record the actuarially determined cost based on the benefits expected to be earned by employees in the future, as well as those benefits the employees have already earned. Annual required contributions shall include the employer's normal cost and a provision(s) for amortizing the total unfunded actuarial accrued liability for a period not to exceed 30 years. The statement also requires that an actuarial valuation be performed every two years for a plan with more than 200 members and every three years for plans with fewer than 200 members.

B. Provisional Purchase of Passerelle Property

The District has entered into an agreement for the purchase of 80 acres located east of Fallbrook near the intersection of I-15 and Highway 76. The purchase is contingent on the successful passage of a General Obligation Bond measure on the ballot in November 2006. At June 30, 2005, the District had deposited $200,000 toward the purchase. The total cost of this undeveloped property will be $8 million.

SUPPLEMENTARY INFORMATION

PALOMAR COMMUNITY COLLEGE DISTRICT

HISTORY AND ORGANIZATION
June 30, 2005

The Palomar Community College District was established in January 1945, to provide higher education to the communities of North San Diego County. The first classes were held in September 1946. The College is located in San Marcos and draws students from the communities of Escondido, San Marcos, Poway, Vista, Ramona and surrounding areas. Classes are currently held on the main campus in San Marcos as well as satellite campus centers in Escondido, Ramona, Poway, Mt. Carmel, Pauma Valley, Borrego Springs, Fallbrook and Camp Pendleton.

GOVERNING BOARD

Member	Office	Term Expires
Nancy C. Chadwick, M.S.W., M.P.A.	President	2008
Michele T. Nelson, Ph.D.	Vice President	2006
Mark R. Evilsizer, M.A.	Secretary	2006
Darrell L. McMullen, M.B.A.	Trustee	2008
Ruth Larson	Trustee	2008
Neill Kivrig	Student Trustee	2006

DISTRICT EXECUTIVE OFFICERS

Robert P. Deegan	Superintendent/President
Berta Cuaron	Assistant Superintendent/Vice President, Instruction
Joseph Madrigal	Assistant Superintendent/Vice President, Student Services
Joe Newmyer	Interim Assistant Superintendent/Vice President, Finance and Administrative Services
Carmen Fernandez, DBA	Interim Assistant Superintendent/Vice President, Financial and Administrative Services (effective October 24, 2005)
Jack Miyamoto, Ph.D.	Interim Assistant Superintendent/Vice President, Human Resources and Affirmative Action
Patrick Schwerdtfeger	Dean, Arts, Media, Business and Computing Systems
Wilma Owens	Dean, Career, Technical and Extended Education
Katheryn Garlow	Dean, Languages and Literature
Sara Thompson	Dean, Math and the Natural and Health Sciences
Mark Vernoy	Dean, Social and Behavioral Sciences
Lynda Halttunen	Dean, Counseling Services

PALOMAR COMMUNITY COLLEGE DISTRICT

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

For the Fiscal year Ended June 30, 2005

Program Name	Federal Catalog Number	Pass-Through Entity Identifying Number *	Total Program Expenditures and Encumbrances
U.S. Department of Education			
SEOG	84.007	N/A	$ 222,600
Federal Work Study administrative allowance	84.007	N/A	22,428
Pell Grant administrative allowance	84.063	N/A	7,066
Pell Grant	84.063	N/A	2,830,281
Higher Education Act:			
Federal Work Study	84.033	N/A	152,290
Veterans Education	N/A	N/A	4,908
TRIO Educational Opportunity Centers	84.066	N/A	213,817
TRIO Student Support Services	84.042A	N/A	233,453
TRIO Upward Bound	84.047A	N/A	275,021
Gear-Up	84.334A	N/A	1,226,115
Vocational Technology Education Act:			
Leadership IIC	84.048	13920	251,787
ROP	84.048	N/A	77,442
Tech Prep	84.243	13929	65,587
Direct Loans	84.268	N/A	557,866
U.S. Department of Justice			
Department of Justice/ COPS	16.710	N/A	49,935
U.S. Department of Health and Human Services			
Temporary Assistance for Needy Families (TANF)	93.558	N/A	59,741
Child Development Training Consortium	93.575	13967	22,985
U.S. Department of Agriculture			
Child Nutrition	10.555	03755	43,286
Total Federal Programs			**$ 6,316,608**

* N/A - Pass through number either not available or not applicable.

See the accompanying notes to the supplementary information.

PALOMAR COMMUNITY COLLEGE DISTRICT

SCHEDULE OF STATE FINANCIAL ASSISTANCE
For the Fiscal Year Ended June 30, 2005

	Program Entitlements			Program Revenues				
Program Name	Current Year	Prior Year Carryover	Total	Cash Received	Accounts Receivable	Deferred Income	Total	Total Program Expenditures and Encumbrances
State Categorical Aid Programs:								
Associate Nursing Degree Grant	$ 54,218	$ 12,427	$ 66,645	$ 66,086	$ 559	$	66,645	$ 66,645
Apprentice Allowance	1,032,283		1,032,283	1,078,006			1,078,006	1,032,283
BFAP	499,388	40,842	540,230	540,230			540,230	540,230
Block Grant - Instructional Materials	865,893	148,270	1,014,163	1,011,109		76,860	934,249	934,249
Cal Works	279,471		279,471	278,786		13,204	265,582	265,582
CCC Satellite Network	1,355,536	140,320	1,495,856	734,196	727,451		1,461,647	1,461,647
Disabled Student Programs and Services	853,582		853,582	853,582		21,471	832,111	832,111
Education Network Grant		3,543	3,543	340			340	340
Cooperative Agencies Resources for Education	102,457		102,457	102,457		670	101,787	101,787
Extended Opportunity Programs & Services	1,017,570		1,017,570	1,017,570		11,614	1,005,956	1,005,956
Lottery Prop 20 - Instructional Materials	223,080	399,838	622,918	142,951	299,837		442,788	442,788
Matriculation	1,052,399	190,859	1,243,258	1,243,258			1,243,258	1,243,258
Part-Time Faculty	838,297		838,297	838,297			838,297	838,297
Partnership for Excellence	3,064,151		3,064,151	3,064,151			3,064,151	3,064,151
Department of Education Interpreters		110,915	110,915	76,802	31,417		108,219	108,219
Staff Diversity	20,676	31,366	52,042	37,381		4,466	32,915	32,915
Telecommunications and Technology	58,369	29,129	87,498	58,369		21,341	37,028	37,028
TTIP E-Conferencing	1,583,361	973,074	2,556,435	481,185	2,013,356		2,494,541	2,494,541
Total State Program Expenditures	**$ 12,900,731**	**$ 2,080,583**	**$ 14,981,314**	**$ 11,624,756**	**$ 3,072,620**	**$ 149,626**	**$ 14,547,750**	**$ 14,502,027**

See the accompanying notes to the supplementary information.

PALOMAR COMMUNITY COLLEGE DISTRICT

SCHEDULE OF WORKLOAD MEASURES FOR PROGRAM BASED FUNDING
For the Fiscal Year Ended June 30, 2005

Categories	
A. Credit Full-Time Equivalent Students (FTES)	
Weekly census	13,322.84
Daily census	1,094.44
Actual hours of attendance	489.62
Independent study/work experience	752.90
Summer intersession	1,954.15
Total	17,613.95
B. Non-Credit FTES	
Actual hours of attendance	1,292.62
Summer intersessions	321.40
Total	1,614.02
C. Basic Skills Courses	
Credit	673.81
Non-credit	967.14
Total	1,640.95
Gross Square Footage	
Existing Facilities	649,102
In-service Training Courses	109.27
FTES in Leased Facilities	1,679.40

See the accompanying notes to the supplementary information.

PALOMAR COMMUNITY COLLEGE DISTRICT

RECONCILIATION OF ANNUAL FINANCIAL AND BUDGET REPORT WITH AUDITED FINANCIAL STATEMENTS
For the Fiscal Year Ended June 30, 2005

	General Fund	Debt Service Fund	Capital Outlay Fund
June 30, 2005 Annual Financial and Budget Report Fund Balance (CCFS-311)	$15,372,882	$ 622,845	$7,260,232
Adjustments and Reclassifications:			
Understatement of Prepaid Expense			200,000
Cumulative Unrealized Loss on Investment	(141,450)		
Under-Statement of Beginning Balance		103,360	
Over-Statement of Revenues		(4,136)	
Net Adjustments and Reclassifications	(141,450)	99,224	200,000
June 30, 2005 Audited Fund Balance	$15,231,432	$ 722,069	$7,460,232

Notes:

Additional entries were made to comply with the GASB 34/35 reporting requirements. These entries are not considered audit adjustments for purposes of this reconciliation.

See the accompanying notes to the supplementary information.

PALOMAR COMMUNITY COLLEGE DISTRICT

SCHEDULE OF GENERAL FUND FINANCIAL TRENDS AND ANALYSIS
For the Fiscal Year Ended June 30,

	(Budget) 2006		2005		2004		2003	
	Amount	%	Amount	%	Amount	%	Amount	%
GENERAL FUND:								
Revenue								
Federal	$ 4,034,471	3.68	$ 2,662,575	2.64	$ 2,965,016	3.19	$ 2,560,776	2.76
State	38,854,103	35.44	37,543,509	37.21	36,179,657	38.91	40,751,461	43.96
County and local	64,651,720	58.96	61,171,666	60.62	54,087,420	58.17	49,619,613	53.53
Total revenue	107,540,294	98.08	101,377,750	100.47	93,232,093	100.27	92,931,850	100.25
Expenditures								
Academic salaries	40,301,471	36.76	40,052,472	39.70	35,637,975	38.33	36,714,332	39.61
Classified salaries	25,403,324	23.17	23,784,103	23.57	21,711,803	23.35	22,886,108	24.69
Employee benefits	20,936,994	19.10	16,913,521	16.76	16,502,218	17.75	14,124,853	15.23
Supplies and materials	2,143,067	1.95	1,780,357	1.76	1,466,810	1.58	1,777,935	1.92
Other operating expenses & services	12,809,389	11.68	11,225,015	11.12	10,964,403	11.79	11,802,448	12.73
Capital outlay	2,447,969	2.23	2,860,954	2.84	2,370,873	2.55	2,837,517	3.06
Other uses (net)	5,603,110	5.11	4,284,427	4.25	4,323,698	4.65	2,555,931	2.76
Total expenditures	109,645,324	100.00	100,900,849	100.00	92,977,780	100.00	92,699,124	100.00
Change in fund balance	$ (2,105,030)	(1.92)	$ 476,901	0.47	$ 254,313	0.27	$ 232,726	0.25
Ending fund balance	$ 13,126,402	11.97	$ 15,231,432	15.10	$ 14,754,531	14.62	$ 14,500,218	15.64
Full-Time Equivalent Students	19,853		19,853		18,696		18,495	
Total long-term debt	$ 8,622,848		$ 9,060,732		$ 9,281,329		$ 9,860,340	

IMPORTANT NOTES:

For 2003, 2004 and 2005 all percentages are of total expenditures excluding contingencies; for 2006, the expenditures include an amount budgeted for contingencies.

The California Community College Chancellor's Office has provided guidelines that recommend an ending fund balance of 3% of expenditures as a minimum, with a prudent ending fund balance being 5% of expenditures.

Total long-term debt for 2003, 2004, 2005 and Budget (2006) excludes the actuarially determined liability for retiree benefits as explained in Note 12.

See the accompanying notes to the supplementary information.

PALOMAR COMMUNITY COLLEGE DISTRICT

NOTES TO SUPPLEMENTARY INFORMATION
For the Fiscal Year Ended June 30, 2005

NOTE 1 - PURPOSE OF SCHEDULES:

A. **Schedules of Expenditures of Federal Awards and State Financial Assistance**

The audit of the Palomar Community College District for the year ended June 30, 2005 was conducted in accordance with OMB Circular A-133, which requires a disclosure of the financial activities of all federally funded programs. To comply with A-133 and state requirements, the Schedule of Federal Awards and the Schedule of State Financial Assistance was prepared for the Palomar Community College District on the modified accrual basis of accounting.

B. **Schedule of Workload Measures for Program-Based Funding**

The Schedule of Workload Measures for Program-Based Funding represents the basis of apportionment of the Palomar Community College District's annual source of funding.

C. **Reconciliation of Annual Financial and Budget Report with Audited Fund Balances**

This schedule reports any audit adjustments made to the fund balances of all funds as reported on the Form CCFS-311.

D. **Schedule of General Fund Financial Trends and Analysis**

This report is prepared to show financial trends of the General Fund over the past three fiscal years as well as the current year budget. This report is intended to identify if the District faces potential fiscal problems and if they have met the recommended available reserve percentages.

NOTE 2 – EXCESS OF EXPENDITURES OVER APPROPRIATIONS:

There were no excesses of expenditures over appropriations, by major object accounts.

VICENTI ♦ LLOYD ♦ STUTZMAN LLP
BUSINESS CONSULTANTS AND CPAs

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

The Board of Trustees
Palomar Community College District
1140 W. Mission Road
San Marcos, CA 92069-1487

We have audited the financial statements of Palomar Community College District (the District) as of and for the year ended June 30, 2005, and have issued our report thereon dated November 2, 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Palomar Community College 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 an opinion 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 to be 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 Palomar Community College 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 05-1 and 05-2.

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

A material weakness is a reportable 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 caused by error or fraud 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. We believe item 05-2 of the reportable conditions described above to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Palomar Community College District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, 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 instances of noncompliance and other matters that are required to be reported under Government Auditing Standards which are described in the accompanying schedule of findings and questioned costs as item 05-3.

This report is intended solely for the information and use of the Board, management, the California Department of Finance, the State Chancellor's Office and federal awarding agencies and pass-through entities and is not intended to be, and should not be, used by anyone other than these specified parties.

Vicenti, Lloyd & Stutzman LLP

VICENTI, LLOYD & STUTZMAN LLP

November 2, 2005

VICENTI ♦ LLOYD ♦ STUTZMAN LLP
BUSINESS CONSULTANTS AND CPAs

REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

The Board of Trustees
Palomar Community College District
1140 W. Mission Road
San Marcos, CA 92069-1487

Compliance

We have audited the compliance of the Palomar Community College District with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to each of its major federal programs for the year ended June 30, 2005. Palomar Community College District's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of Palomar Community College District's management. Our responsibility is to express an opinion on Palomar Community College District's compliance based on our audit.

We conducted our audit of compliance 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 OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Palomar Community College District's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on Palomar Community College District's compliance with those requirements.

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REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

In our opinion, the Palomar Community College District complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2005. However, the results of our auditing procedures disclosed an instance of noncompliance with those requirements, which is required to be reported in accordance with OMB Circular A-133 and which is described in the accompanying schedule of findings and questioned costs as item 05-4.

Internal Control Over Compliance

The management of Palomar Community College District is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered Palomar Community College District's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable 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 noncompliance with the applicable requirements of laws, regulations, contracts and grants caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the Board, management, the California Department of Finance, the State Chancellor's Office and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Vicenti, Lloyd & Stutzman LLP

VICENTI, LLOYD & STUTZMAN LLP

November 2, 2005

VICENTI ♦ LLOYD ♦ STUTZMAN LLP
BUSINESS CONSULTANTS AND CPAs

REPORT ON STATE COMPLIANCE

The Board of Trustees
Palomar Community College District
1140 W. Mission Road
San Marcos, CA 92069-1487

We have audited the basic financial statements of Palomar Community College District, as of and for the year ended June 30, 2005, and have issued our report thereon dated November 2, 2005.

Our examination was made in accordance with auditing standards generally accepted in the United States of America and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In connection with our audit, we performed an audit for compliance as required in Part II, State and Federal Compliance Requirements for those programs identified in the California Department of Finance's 2005 transmittal of audit requirements for community colleges. The objective of the examination of compliance applicable to the Palomar Community College District is to determine with reasonable assurance:

- Whether the District's salaries of classroom instructors equal or exceed 50 percent of the District's current expense of education in accordance with Section 84362 of the Education Code.

- Whether the District has the appropriate documentation to support the FTES, if any, that are claimed for instructional service agreements/contracts.

- Whether the District has the ability to support timely accurate and complete information for workload measures used in the calculation of State General Apportionment.

- Whether the District has acted to ensure that the residency of each student is properly classified and that only the attendance of California residents is claimed for apportionment purposes.

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REPORT ON STATE COMPLIANCE

- Whether District has complied with all requirements necessary to claim FTES for the attendance of concurrently enrolled K-12 pupils.

- Whether the District had local funds to support at least 75 percent of the credit matriculation activities and that all matriculation expenditures are consistent with the District's State approved matriculation plan.

- Whether the District's salaries of instructors teaching FTES generating classes, school counselors providing advisement, student services at the Dean level or above, and financial aid officers conducting need analysis, are not considered supportable charges against either Extended Opportunity Programs and Services (EOPS) or Disabled Student Program Services (DSP&S) accounts unless their activities require them to perform additional functions for the EOPS or DSP&S program which are beyond the scope of services provided to all students in the normal performance of the regular duty assignments.

- Whether the District contributed 100% of the salary and benefits for the EOPS Director/Administrator from funds other than EOPS. In addition, the District must employ a full-time 100% Director to manage the daily operations of the EOPS program unless a waiver has been obtained.

- Whether the Gann Limit Calculation was properly calculated and supported by adequate documentation.

- Whether the District is reporting the total amount that students should have paid for enrollment fees for the purpose of determining the District's share of annual apportionment.

- Whether the District spent an amount equal to or greater than the amount provided by the State for scheduled maintenance and special repairs. Funds provided by the State must be to supplement, not supplant, District scheduled maintenance funds. The amount expended for plant maintenance and operations during the base year of 1995-96 was $3,447,456.

- Whether all District courses that qualify for State apportionment are open to enrollment by the general public unless specifically exempted by statute.

- Whether the District has adopted regulations consistent with the "Standards of Scholarship" contained in the California Code of Regulations and has published statements of those regulations in the College catalog.

- Whether the District has adopted policies or regulations regarding the authority of the District to require students to provide various types of instructional materials.

REPORT ON STATE COMPLIANCE

In our opinion, except for finding 05-3 described in the accompanying Schedule of Findings and Questioned Costs, Palomar Community College District complied with the compliance requirements for the state programs listed and tested above. Nothing came to our attention as a result of the aforementioned procedures to indicate that Palomar Community College District had not complied with the terms and conditions of state assisted educational programs not selected for testing.

Our examination of compliance made for the purposes set forth in the preceding paragraph of this report would not necessarily disclose all instances of noncompliance.

This report is intended solely for the information and use of the Board, management, the California Department of Finance, and the State Chancellor's Office and is not intended to be, and should not be, used by anyone other than these specified parties.

Vicenti, Lloyd & Stutzman LLP

VICENTI, LLOYD & STUTZMAN LLP

November 2, 2005

PALOMAR COMMUNITY COLLEGE DISTRICT

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
SUMMARY OF AUDITOR RESULTS
June 30, 2005

Financial Statements

Type of auditor's report issued:	*Unqualified*
Internal control over financial reporting:	
Material weakness(es) identified?	X Yes ___ No
Reporting condition(s) identified not considered to be material weaknesses?	X Yes ___ None reported
Non-compliance material to financial statements noted?	___ Yes X No

Federal Awards

Internal control over major programs:	
Material weakness(es) identified?	___ Yes X No
Reporting condition(s) identified not considered to be material weaknesses?	X Yes ___ None reported
Type of auditor's report issued on compliance for major programs:	*Unqualified*
Any audit findings disclosed that are required to be Reported in accordance with Circular A-133, Section .510(a)	X Yes ___ No

Identification of Major Programs Tested

CFDA Number(s)	Name of Federal Program or Cluster
84.007, 84.033 and 84.063	Student Financial Assistance Cluster of Programs

Dollar threshold used to distinguish between Type A and Type B programs:	$ 300,000
Auditee qualified as low-risk auditee?	___ Yes X No

SCHEDULE OF FINDINGS AND QUESTIONED COSTS RELATED TO FINANCIAL STATEMENTS June 30, 2005

FINDING 05-1 – PAYROLL PROCEDURES

Original Finding No. 04-2

Finding: Current payroll procedures involve employees in the Payroll Department entering employees and pay rates into the payroll system for stipends and special duty assignments. Proper internal controls would call for Human Resources to enter all employees and pay rates into the payroll system. The Payroll Department's responsibilities should be limited to the actual preparation of pay checks, primarily the entry of hours worked and any special entries such as vacation or sick leave pay. The District has compensating controls that reduce the significance of the deficiency in internal control.

Recommendation: All responsibility for entering employees and pay rates into the payroll system should be turned over to the Human Resources Department. This will improve the effectiveness of internal controls and reduce the risk of fraud.

District Response: The District is in the process of hiring a permanent Vice President of Human Resources. Once this person is in place and has had a chance to review this comment, steps will be taken to address the situation.

FINDING 05-2 – INTERNAL CONTROLS

Finding: We noted the following weaknesses in the District's internal controls:

- Journal entry documentation for some entries tested was missing or incomplete (12 from a sample of 26). In addition we noted three entries which had not been approved.
- The passwords of the employees who approve "B" warrants are not changed because the computer system does not force employees to change passwords periodically.
- The District currently does not have a contingency plan for alternative processing in the event of loss or interruption of the IT function.
- The equipment inventory is not balanced to the general ledger expense account balance.

Recommendation: We recommend the following:

- District management should establish procedures for the journal entry process. These procedures should address the preparation, approval and recording of journal entries. In addition, a central filing system for journal entries should be implemented. These improvements would provide a clear trail for internal and audit purposes.
- The District should implement a process to require the periodic change of employee passwords.
- The IT department should investigate alternative data processing options that will allow the District to continue operations in the event of a major disruption.
- The equipment inventory should be reconciled to the equipment expenditures to verify the accuracy of the value of equipment added to the District's property and equipment.

District Response: The District will develop procedures to correct these weaknesses. The situation of the passwords changing periodically will need to wait until the PeopleSoft upgrade has been completed.

FINDING 05-3 – STATE COMPLIANCE (MATERIAL FEES)

Finding: Our testing disclosed the following areas of non-compliance concerning materials fees:

- Material fees were charged for two courses which did not provide tangible personal property to the students (Bowling and Field Study - trip to Santa Catalina)
- The District's records were not sufficient to determine the cost of materials provided by the District. We were, therefore, unable to determine if students were being charged more than the District's actual cost of the materials provided.

Recommendation: The District should implement a process which requires departments wishing to charge material fees to submit a request form. Information included on this form would be an itemization of items to be provided along with the cost to purchase those materials. The form should also address the Education Code requirements for material fees and provide justification for charging a material fee for the items provided. For courses, such as Bowling and Field Study, the fee designation should be changed to more accurately identify what the student is paying for.

District Response: The District will change the wording in the course catalog to read Activity Fee instead of Material Fee.

PALOMAR COMMUNITY COLLEGE DISTRICT

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
RELATED TO FEDERAL AWARDS
June 30, 2005

FINDING 05-4 – SINGLE COST OBJECTIVE EMPLOYEES

Federal Programs: VTEA Leadership IIC

Federal Catalog No.: 84.048

Original Finding No. 04-5

Finding: OMB Circular A-87 requires that a semi-annual certification be completed in addition to the maintenance of payroll records. The District maintains time records for employees whose positions are funded by Federal programs; however, the required semi-annual certification is not being prepared to support time and effort for employees whose salaries are charged to a single cost objective. Lack of adequate documentation, as required by OMB Circular A-87, could jeopardize the categorical funding related to salaries and benefits received by these programs.

Questioned Costs: The amount potentially at risk due to this issue of non-compliance is approximately $18,237 for VTEA Leadership IIC program.

Recommendation: Develop procedures to ensure that the semi-annual certification is completed for those employees whose salaries are charged to a single cost objective.

District Response: The State does not require the District to maintain these certifications. The amount is less than 10% of the total grant amount.

STATUS OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS
June 30, 2005

Original Finding No.	Finding	Recommendation	Current Status
04-1	**GANN LIMIT**		
	The District calculated the GANN Limit using the 2003-04 Second Period Factored FTES to arrive at the population factor. The calculation should be based on the 2003-04 Second Period Actual FTES.	The District should recalculate the GANN Limit using the Second Period Actual FTES and submit a revised form to the Chancellor's Office.	Implemented
04-2	**PAYROLL PROCEDURES**		
	Current payroll procedures involve employees in the Payroll Department entering employees and pay rates into the payroll system for stipends and special duty assignments. Proper internal controls would call for Human Resources to enter all employees and pay rates into the payroll system.	Segregate duties for entering employees and pay rates into the payroll system by assigning this responsibility to the Human Resources Department. Limit the Payroll Department's responsibilities to the actual preparation of pay checks; primarily the entry of hours worked and any special entries such as vacation or sick leave pay. This will improve the effectiveness of internal controls and reduce the risk of fraud.	Not implemented. See finding 05-1.

STATUS OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS
June 30, 2005

Original Finding No.	Finding	Recommendation	Current Status
04-3	**INTERNAL CONTROLS PERTAINING TO ACCESS TO ACCOUNTING DATA** There are weaknesses in internal controls related to the accounting process, including delays in deleting terminated employees from computer system functions. Numerous employees who do not need access to the purchasing system are able to make changes, additions or deletions to the District's approved vendor listing. In addition, changes can be made to purchase orders by employees in departments other than Purchasing. A few departments make purchases without contacting the Purchasing Department until after the transaction has been completed.	District management should review the accounting procedures in the areas of access to computer data and functions, and purchasing. Specifically, management needs to determine specific access needs for each position and then instruct the Information Systems Department to program those limitations into the system. Also, develop and follow District-wide procedures for purchasing materials and services. These procedures should identify responsibilities, specifically addressing purchasing procedures for various college departments. In addition, develop a procedure so that Human Resources immediately notifies Information Systems of all employee terminations.	Implemented.

Original Finding No.	Finding	Recommendation	Current Status
04-4	**CLOSING PROCEDURES** District management continued to make adjustments to the financial data after they had indicated the balances were final. The closing process included duplicate journal entries, as well as entries which had not been reviewed or approved.	Establish closing procedures which include designation of responsibilities, deadlines for completing various portions of the closing process and procedures for preparing, approving and entering journal entries. In addition, accounting records should be reviewed monthly so that errors may be located and corrected in a timely manner. This will reduce the amount of adjustments necessary at year-end to accurately reflect the District's financial information.	Implemented
04-5	**SINGLE COST OBJECTIVE EMPLOYEES** **Federal Programs: Gear-Up, VTEA Leadership IIC and TRIO Student Support Services** **Federal Catalog No.: 84.334A, 84.048 and 84.042A** OMB Circular A-87 requires that a semi-annual certification be completed in addition to the maintenance of payroll records. The District maintains time records for employees whose positions are funded by Federal programs; however, the required semi-annual certification is not being prepared to support time and effort for employees whose salaries are charged to a single cost objective. Lack of adequate documentation, as required by OMB Circular A-87, could jeopardize the categorical funding related to salaries and benefits received by these programs.	Develop procedures to ensure that the semi-annual certification is completed for those employees whose salaries are charged to a single cost objective.	Partially implemented. See finding 05-4.