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County of San Diego

AUDITOR AND CONTROLLER
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October 8, 1999

The Honorable Board of Supervisors
County of San Diego
San Diego County Administration Center
San Diego, California 92101

The annual financial report of the County of San Diego for the fiscal year ended June 30, 1999, has been prepared by the Chief Financial Officer/Auditor and Controller and is submitted in compliance with Section 25253 of the Government Code of the State of California. Responsibility for both the accuracy of the presented data and the completeness and fairness of the presentation, including all disclosures, rests with County staff. The report has been prepared in accordance with generally accepted accounting principles and is organized into three major sections. The introductory section consists of this letter and the organizational structure of the County. The financial section provides the financial statements for the fund types and account groups of the County. Within this section, the general purpose statements and notes thereto for all fund types and account groups are presented first, followed by statements and schedules for individual fund types and account groups. The statistical section is the final section of the report and consists of various tables and schedules depicting trends and miscellaneous relevant data concerning County finances and demographics.

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the County for its Comprehensive Annual Financial Report for the fiscal year ended June 30, 1998. In order to be awarded a Certificate of Achievement, a government unit must publish an easily readable and efficiently organized comprehensive annual financial report, whose contents conform to program standards. Such a report must satisfy both generally accepted accounting principles and applicable legal requirements. A Certificate of Achievement is valid for a period of one-year only. We believe our current report continues to conform to the Certificate of Achievement program requirements, and we are submitting it to GFOA.

The general purpose financial statements include the activities of the various fund types and account groups of the County and certain other entities for which the Board of Supervisors are financially accountable as defined by the Governmental Accounting Standards Board. Accordingly, all fund types and account groups of the County are reported herein as well as the operations of the following entities:

County Service Areas
Flood Control Districts
Lighting Maintenance Districts
Air Pollution Control District
County of San Diego Housing Authority
Sanitation Districts
San Diego County Redevelopment Agency
San Diego County Capital Asset Leasing Corporation (SANCAL)
San Diego County Employees' Retirement Association (SDCERA)

GOVERNMENTAL STRUCTURE, LOCAL ECONOMIC CONDITION AND OUTLOOK

The County was incorporated on February 18, 1850, and functions under a Charter adopted in 1933, as subsequently amended. A five-member Board of Supervisors elected to four-year terms in district nonpartisan elections governs the County. There are 18 incorporated cities in the County and a large number of unincorporated communities. The County provides a full range of public services including public assistance, judicial, police protection, detention and correction, health and sanitation, recreation and others.

The San Diego Economic Research Bureau indicates that the regional economy is expected to grow at a projected growth rate of 3.7% in Gross Regional Product (GRP), net of inflation, through December 1999 as compared to a 4.5% change in 1999. Although the rate of growth for GRP has slowed from the previous year, economic expansion has continued for a sixth straight year. The forecasted GRP growth rate for 1999 will also be more than the 2.6% growth rate projected for the nation's Gross Domestic Product. The gains in GRP have been the result of increases in industries relating to high tech, entertainment, foreign trade, tourism and professional services. San Diego County has emerged as one of the nation’s leading telecommunications technology centers due primarily to locally headquartered Qualcomm, which recently joined the ranks of the Standard & Poor’s index of the 500 most commonly held stocks. Other growth areas include computers and software, biotechnology and medical instruments. Additionally, San Diego still maintains a strong military presence and is currently the Navy’s principal location for West Coast operations. Defense spending accounts for approximately 10.7% of GRP. New housing construction is expected to increase to approximately 13,500 units, as compared to 12,434 units in 1998. This projected increase will accommodate approximately one-half the demand needed for current population growth with the result that housing prices for existing homes have increased. Housing prices are projected to increase 8.2% in 1999, after adjusting for inflation, compared to 6.0% in 1998. The population is expected to increase by 3.3% or 58,000 persons in 1999. This compares with previous gains of 65,731 in 1997 and an estimated 60,000 in 1998. Employment for 1999 is expected to rise 1.6% compared to a 1.7% increase in 1998. The unemployment rate at the end of fiscal year 1998/99 was 3.4% as compared to 3.6% the previous fiscal year. Per the County Assessor, property tax assessed valuation in fiscal year 1998/99 increased 7.4% from fiscal year 1997/98 and is more than the previous year’s increase of 2.9%.

MAJOR INITIATIVES

County operations in the last fiscal year were driven by the related financial tenets of (1) structurally balanced revenues and expenditures and (2) the use of one-time resources for one-time expenditures. Over the last few years, these guidelines, under the umbrella of the General Management System, have been utilized throughout the County planning process and resulted in the first-time adoption of a Five-Year Strategic Plan and a Two-Year Operational Plan.

In FY 1998/99, as a result of countywide cost control, resource management, and the healthy local economy, the County General Fund revenues exceeded operating expenditures. Consequently, financial reserves increased and plans initiated to use them for one-time requirements, such as office automation and technology upgrades, deferred major maintenance, and new and ongoing capital projects. One use of these reserves is the restoration of the County Administration Center, a nationally registered historical building, to include new stucco and interior modernization. Also, this year the County developed a comprehensive Capital Improvement Plan (CIP), a two-year plan to improve existing infrastructure and provide seed money for new projects. Plans for new libraries and for a new Central Animal Shelter have been included in the CIP, along with substantial improvements to Sheriff Department facilities.

The major non-financial initiative of this fiscal year has been the improvement of services to the residents and taxpayers of San Diego County. All business and support functions were charged by the Board of Supervisors to improve services with no increases in net costs. In support of this effort, the Health and Human Services Agency underwent a massive reorganization to deliver fully integrated health and social services in a regional structure. Other examples of improved service levels include the County Library System, which is staying open nearly 7,000 additional hours annually, and the Registrar of Voters that was staffed on weekends prior to elections. Additionally, service delivery improvement has occurred as a result of the automation of various County functions, such as the use of the Internet for Property Tax payments and recorded document requests.

Competition and reengineering of County functions were also a focus of the County's Agency/Groups. Departments were reorganized to reallocate resources from line to staff functions and to cut overhead in general. For example, the Probation Department cut management and overhead costs in order to hire 55 new probation officers. Also, General Services Fleet staff successfully competed against private companies to retain the vehicle repair and maintenance functions in-house.

In addition to the initiative for CIP, future initiatives include outsourcing the County's Information Technology (IT) functions such as telecommunications, IT hardware components, systems maintenance, and financial systems. The County expects to finalize a comprehensive IT contract by the end of 1999.

FINANCIAL INFORMATION

Accounting System and Budgetary Control

The County of San Diego maintains its principal fund accounting records using a modified accrual basis of accounting, as explained in the Notes to Financial Statements, and follows the accounting practices for governmental units which have been recommended by the Governmental Accounting Standards Board.

Using the County's automated accounting system, the Chief Financial Officer/Auditor and Controller restricts each department's expenditures at the object level to the amount of that department's budgeted appropriations for the year. Changes in appropriations must be approved by the Board of Supervisors as a transfer from contingency reserve, transfer from another budgeted unit, or as an appropriation of unanticipated or overrealized revenue identified to a specific source. No budget unit is permitted to spend more than its available appropriations. Any appropriations remaining at the end of the fiscal year, which have not been specifically committed, automatically lapse to the unreserved fund balance. The fund balance along with projected revenues become available for appropriation the following year.

Internal Accounting Controls

The Chief Financial Officer/Auditor and Controller is charged with maintaining adequate systems of internal control sufficient to ensure reliability and validity of financial reporting in accordance with generally accepted accounting principles and general law. This is accomplished through the application of a series of automated accounting controls and administrative procedures designed to ensure the integrity of County transactions and to safeguard County assets. This internal control structure is subject to periodic evaluation by the internal audit staff of the County. Accordingly, the Chief Financial Officer/Auditor and Controller represents that the current systems of internal control adequately safeguard County assets and provide reasonable assurance over the fairness of presentation of this report.

General Government Functions

The following schedules present a summary of revenues and other financing sources and a summary of expenditures and other financing uses for the County's General, Special Revenue, Debt Service, and Capital Projects funds. Amounts are stated in millions of dollars.

SUMMARY OF REVENUES AND OTHER FINANCING SOURCES:

	YEAR ENDED JUNE 30 1999 AMOUNT	1999 PERCENT	1998 AMOUNT	1998 PERCENT	PERCENT INCREASE (DECREASE) 1999 OVER 1998
Taxes	$ 338.5	14.3	$ 306.2	11.8	10.5
Licenses and Permits	31.1	1.3	28.3	1.1	9.9
Fines, Forfeitures and Penalties	27.0	1.2	29.4	1.1	(8.2)
Use of Money and Property	41.0	1.7	49.0	1.9	(16.3)
Aid From Other Governmental Agencies:					
State	944.7	40.0	933.9	35.9	1.2
Federal	416.1	17.6	512.0	19.7	(18.7)
Other	57.2	2.4	35.3	1.3	62.0
Charges for Current Services	211.3	9.0	196.4	7.5	7.6
Other Revenues	31.1	1.3	18.8	0.7	65.4
TOTAL REVENUES	2,098.0	88.8	2,109.3	81.0	(0.5)
Sale of Fixed Assets	0.5		0.9	0.1	(44.4)
Long-Term Debt Proceeds	73.0	3.1	77.9	3.0	(6.3)
Issuance of Lease Purchases	3.9	0.2	4.2	0.2	(7.1)
Operating Transfers In	186.3	7.9	247.2	9.5	(24.6)
Residual Equity In			161.3	6.2	(100.0)
TOTAL	$ 2,361.7	100	$ 2,600.8	100	(9.2)

SUMMARY OF EXPENDITURES AND OTHER FINANCING USES:

	YEAR ENDED JUNE 30 1999 AMOUNT	1999 PERCENT	1998 AMOUNT	1998 PERCENT	PERCENT INCREASE (DECREASE) 1999 OVER 1998
General Government	$ 185.4	8.0	$ 184.5	7.6	0.5
Public Protection	575.8	25.0	544.6	22.4	5.7
Public Ways and Facilities	80.1	3.5	66.5	2.7	20.5
Health and Sanitation	319.5	13.9	294.9	12.1	8.3
Public Assistance	703.1	30.5	816.6	33.6	(13.9)
Education	11.3	0.5	10.1	0.4	11.9
Recreation and Cultural	11.2	0.5	9.3	0.4	20.4
Capital Outlay	47.1	2.0	91.1	3.8	(48.3)
Debt Service	103.5	4.5	98.2	4.0	5.4
TOTAL EXPENDITURES	2,037.0	88.4	2,115.8	87.0	(3.7)
Operating Transfers Out	185.1	8.1	241.2	9.9	(23.2)
Transfers to Escrow Agent	70.8	3.1	71.2	2.9	(0.6)
Equity Conveyed to Other Entities	0.6				
Residual Equity Out	9.3	0.4	5.7	0.2	63.2
TOTAL	$ 2,302.8	100	$ 2,433.9	100	(5.4)

Revenue for general County functions remained approximately the same as the prior year although there were variances between categories of revenues. Property taxes increased $32 million from the previous year due primarily to increases in assessed valuation and increased resales of existing homes. Use of Money and Property decreased $8 million due to a one-time lease payment for the East Mesa Detention Facility received in the prior year and lower interest revenue earned on smaller Tax and Revenue Anticipation Notes' cash balances. Federal Aid decreased $96 million from the previous year primarily reflecting reductions in food stamps and decreased welfare case loads in assistance programs relating to Federal welfare reform. Other governmental aid revenue increased $22 million primarily reflecting revenues relating to juvenile dependency received from independent trial courts. Other revenue increased $12 million from the previous year. The major part of this increase was due to the employee personal computer loan program revenue and the contributions from trial courts resulting from the enactment of the Trial Court Funding Act of 1997. Operating transfers in and residual equity transfers in declined significantly from the previous fiscal year due to prior year completion of capital projects, e.g., central detention facility, and one time transfers relating to the sale of the Solid Waste System in fiscal year 1997/98. The major sources of funding to the County continued to be the State and Federal governments, collectively providing 64.9% of all revenue as compared to 68.5% in the previous year. Long-term debt proceeds are explained under "Debt Administration."

Expenditures and encumbrances for FY 1998/99 showed a slight decrease from the previous year. Public protection expenditures increased $31 million primarily because of salary increases and increased staffing and other costs required to staff the new detention facility, a new communications center and increased child support enforcement activities. Public ways and facility expenditures increased $14 million from the previous year due to increased road construction and maintenance. Health and Sanitation expenditures increased $25 million due primarily to a $3 million increase in inmate medical costs, a $6 million increase for mental health programs and a $16 million cost shift to the health services function as a result of the merger of the Department of Social Services with the Department of Health Services. Public Assistance decreased $113 million from the previous year which reflects the elimination of federal food stamp pass through funds, decreased public assistance spending resulting from State and Federal welfare reform measures and a shift in program-related costs to the health services function as previously described. Capital project expenditures decreased $44 million due to completion of construction improvements to County regional centers in the prior year.

General Fund unreserved fund balance amounted to approximately $210 million at June 30, 1999, an increase of $54 million from the previous year. This increase was primarily attributable to an increase in discretionary revenues, e.g. property taxes, which offset revenue losses in Federal assistance, coupled with a reduction in public assistance related costs.

Results Of Operations - Enterprise Funds

During fiscal year 1998/99, these funds received total revenue and net operating transfers of $41 million and incurred expenses of $38 million resulting in a net gain of $3 million. At June 30, 1999, these funds had a $82 million balance in retained earnings. The major share of this balance included $70 million in six sanitation districts and $12 million in the Airport Enterprise Fund.

Results Of Operations - Pension Trust Fund

Contributions to the SDCERA for fiscal year 1998/99 totaled $44 million, while income from investment was $396 million, making total additions of $440 million. After payments of retirement benefits and investment expenses of $136 million, net assets were increased by $304 million over that of the previous fiscal year. The total net assets held in trust for pension benefits as of June 30, 1999 was $3,810 million.

Debt Administration

The County has no outstanding general obligation or revenue bonds, although in accordance with generally accepted accounting principles, in particular Governmental Accounting Standards Board Statement No. 14, the County "reporting entity" as reflected in this financial report has the following outstanding bonded debt:

Proprietary Fund Revenue Bonds	$ 65,000
Pension Obligation Bonds	373,220,000
Redevelopment Agency Revenue Bonds	4,960,000
Certificates of Participation (COPs)	473,818,000
Total	$ 852,063,000

Proprietary fund revenue bonds are legal obligations of various sanitation districts. The Pension Obligation Bonds represent obligations of the County to fund the prior years' unfunded actuarial accrued liability of the SDCERA pension trust fund. The Redevelopment Agency revenue bonds are obligations of the Agency used to finance the Agency's capital improvements, while the COPs are legal obligations of a non-profit corporation formed for the sole purpose of financing the acquisition or construction of County facilities. Interest expense to maturity on bonded debt is projected at $346 million. Short-term financings consisted of Tax and Revenue Anticipation Notes (TRANS) for $175 million and an outstanding balance of $56 million in short-term Teeter Obligation Commercial Paper Notes. The Teeter Obligation notes are secured by future collections of delinquent property taxes and were used to provide various taxing agencies the amount of their property taxes without regard to such delinquencies. Credit ratings for the County's long-term COPs and Pension Obligation Bonds remained unchanged during fiscal year 1998/99.

However, these ratings were upgraded in the subsequent fiscal year to A1 and Aa3, respectively, from Moody's and to A+ and AA-, respectively from Standard & Poor's. Short-term Tax and Revenue Anticipation Notes continued to receive the highest ratings from both Moody's and Standard & Poor's Corporation.

On January 1, 1999, SANCAL issued $73 million in COPs with an average interest rate of 4.6% to advance refund $72 million of lease revenue bonds issued by the San Diego Regional Building Authority in July 1993. The lease revenue bonds of the Authority were secured by capital leases between the County and the Authority. The refunding resulted in a debt payment reduction of $2 million over the next 24 years.

Certain buildings and equipment are being acquired under various long-term capital leases (lease-purchases). Excluding those leases represented by the COPs noted above, the outstanding obligation for these leases at June 30, 1999, totaled $86 million. Assuming all such capital leases are held to full term, the total projected interest expense would be an additional $48 million.

Cash Management

Under a pooled-money concept, the County invests all idle cash in various securities with maturities planned to coincide with projected needs while attempting to maximize yield. The portfolio during the year was as follows: Government Securities, 30%; Repurchase Agreements, 12%; Negotiable Certificates of Deposit, 31%; Commercial Paper, 14%; Medium Term Notes, 8%; Bank Notes, 3%; Mutual Funds, 2%. Time deposits in various depositories were fully collateralized in accordance with State statutes which require depositories having public funds on deposit to maintain a pool of securities with the agent of the depository having a market value of at least 10% in excess of the total amount of all public funds on deposit.

The average yield rate on pooled cash investments was 4.25%.

Risk Management

The County is self-insured for premises liability at medical facilities, medical malpractice, errors and omissions, false arrest, forgery, general liability and workers' compensation. The County purchases insurance for property damage, certain casualty claims, and loss of money up to $10,000 per selected site locations. The County's uninsured risk management activities are accounted for in an Internal Service Fund (ISF). During FY 1998/99, fund equity increased $19 million in the Public Liability Insurance ISF while fund equity for the Workers' Compensation Fund increased $12 million. The liability for unpaid claims decreased by $11 million in the Public Liability ISF and by $8 million in the Workers' Compensation ISF. These amounts included estimates for claims incurred but not yet reported and are based on actuarial reviews conducted in 1999. Funding these liabilities must remain a priority if the County is to be truly self-insured. In addition, there is a potential gross liability of $67 million to $123 million which could result if unfavorable adjudication were rendered for pending legal actions. At June 30, 1999, there are 39 litigation cases representing the probable and potential public liabilities discussed above. The range of litigation cases is from $100 thousand to $100 million.

OTHER INFORMATION

Independent Audit

An independent auditors' report on the general purpose financial statements and combining and individual fund financial statements and schedules by the independent certified public accounting firm of KPMG LLP is included in the financial section of this report.

Acknowledgment

The preparation of the Comprehensive Annual Financial Report can only be accomplished through the dedicated and coordinated efforts of the accounting staffs of County departments and the staff of the Chief Financial Officer/Auditor and Controller. I applaud their contribution to ensuring that this report meets the highest reporting standards. I would also like to thank the members of the Board of Supervisors, the Chief Administrative Officer, Group Agency General Managers and their staffs for their continued emphasis on conducting the financial operations of the County in accordance with sound business practices to achieve planned objectives.

Respectfully,

WILLIAM J. KELLY
Chief Financial Officer