NEW ISSUE – BOOK-ENTRY-ONLY

INSURED RATINGS:	UNDERLYING RATINGS:
Moody's: "Aaa"	*Moody's: "A1"*
Fitch: "AAA"	*Fitch: "AA-"*
S&P: "AAA"	*S&P: "AA-"*

In the opinion of Orrick, Herrington & Sutcliffe LLP, Special Counsel to the County, based upon an analysis of existing laws, regulations, rulings and court decisions, and assuming, among other matters, the accuracy of certain representations and compliance with certain covenants, interest evidenced by the Series 2006 Certificates is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986 and is exempt from State of California personal income taxes. In the further opinion of Special Counsel, interest evidenced by the Series 2006 Certificates is not a specific preference item for purposes of the federal individual or corporate alternative minimum taxes, although Special Counsel observes that such interest is included in adjusted current earnings when calculating corporate alternative minimum taxable income. Special Counsel expresses no opinion regarding any other tax consequences related to the ownership of, or accrual or receipt of interest evidenced by, the Series 2006 Certificates. See "Tax Matters" herein.

$42,390,000
COUNTY OF SAN DIEGO
Certificates of Participation
(2006 Edgemoor Completion Project)
Evidencing and Representing Proportionate Undivided Interest of the Owners Thereof in Base Rental Payments to be Made by the County of San Diego to the San Diego County Capital Asset Leasing Corporation

Dated: Date of Delivery **Due:** February 1, as shown on the inside cover

The County of San Diego Certificates of Participation (2006 Edgemoor Completion Project) (the "Series 2006 Certificates") are being executed and delivered pursuant to a Trust Agreement, dated as of February 1, 2005, as amended and supplemented by a First Supplemental Trust Agreement, dated as of December 1, 2006 (collectively, the "Trust Agreement"), each by and among Zions First National Bank, as trustee (the "Trustee"), the County of San Diego (the "County") and the San Diego County Capital Asset Leasing Corporation (the "Corporation"). The Series 2006 Certificates evidence proportionate undivided interests in additional base rental payments (together with the base rental payments presently made by the County under the hereinafter defined Sublease, the "Project Base Rental Payments") to be made by the County pursuant to that certain Project Sublease, dated as of February 1, 2005, as amended by that certain First Amendment to Project Sublease, dated as of December 1, 2006 (collectively, the "Project Sublease"), each by the County and the Corporation, pursuant to which the County subleases from the Corporation certain real property and all the improvements thereon or to be located thereon, as more particularly described herein (the "Project Property"). The Series 2006 Certificates are secured on a parity with the County's Certificates of Participation (2005 Edgemoor Project and 1996 Regional Communications System Refunding) executed and delivered pursuant to the Trust Agreement and evidencing proportionate undivided interests in Base Rental Payments made by the County pursuant to the Project Sublease and that certain Refunding Sublease, dated as of February 1, 2005 (the "Refunding Sublease" and, together with the Project Sublease, the "Subleases"), by the County and the Corporation, pursuant to which the County subleases from the Corporation certain real property and all the improvements thereon or to be located thereon, as more particularly described therein (the "Refunding Property" and, together with the Project Property, the "Properties"). See "Security and Sources of Payment for the Series 2006 Certificates – Base Rental Payments" herein. The proceeds of the Series 2006 Certificates will be applied to (i) finance the completion of a skilled nursing facility to replace the existing skilled nursing facility in Santee, California, (ii) purchase a reserve fund surety for the Certificate Reserve Fund, (iii) pay capitalized interest on a portion of the Series 2006 Certificates and a portion of the County's Certificates of Participation (2005 Edgemoor Project and 1996 Regional Communications System Refunding) through March 1, 2009, and (iv) pay certain costs of issuance incurred in connection with the Series 2006 Certificates. See "The Property and the Project" herein.

Interest represented by the Series 2006 Certificates is payable on February 1 and August 1 of each year, commencing on August 1, 2007. The Series 2006 Certificates will be issued in book-entry form only and, when delivered, will be registered in the name of Cede & Co., as nominee of The Depository Trust Company, New York, New York ("DTC"), which will act as securities depository for the Series 2006 Certificates. Individual purchases of the Series 2006 Certificates will be made in book-entry form only. Purchasers of the Series 2006 Certificates will not receive certificates representing their ownership interests in the Series 2006 Certificates purchased. Principal and interest payments represented by the Series 2006 Certificates are payable directly to DTC by the Trustee from Base Rental Payments. Upon receipt of payments of principal and interest, DTC will in turn distribute such payments to the beneficial owners of the Series 2006 Certificates. See Appendix D – "Book-Entry System" attached hereto.

Payment of principal and interest with respect to the Series 2006 Certificates when due will be insured by a financial guaranty insurance policy to be issued by Ambac Assurance Corporation simultaneously with the delivery of the Series 2006 Certificates. See "Certificate Insurance" herein and Appendix F – "Specimen of Financial Guaranty Insurance Policy" attached hereto.

Ambac

The Series 2006 Certificates are subject to optional and extraordinary prepayment, as described herein. See "The Series 2006 Certificates – Prepayment" herein.

THE OBLIGATION OF THE COUNTY TO MAKE BASE RENTAL PAYMENTS AND TO PAY ADDITIONAL RENTAL UNDER THE SUBLEASES DOES NOT CONSTITUTE AN OBLIGATION OF THE COUNTY FOR WHICH THE COUNTY IS OBLIGATED TO LEVY OR PLEDGE ANY FORM OF TAXATION OR FOR WHICH THE COUNTY HAS LEVIED OR PLEDGED ANY FORM OF TAXATION. NEITHER THE SERIES 2006 CERTIFICATES NOR THE OBLIGATION OF THE COUNTY TO MAKE BASE RENTAL PAYMENTS OR TO PAY ADDITIONAL RENTAL UNDER THE SUBLEASES CONSTITUTES AN INDEBTEDNESS OF THE COUNTY, THE STATE OF CALIFORNIA OR ANY OF ITS POLITICAL SUBDIVISIONS WITHIN THE MEANING OF ANY CONSTITUTIONAL OR STATUTORY DEBT LIMITATION OR RESTRICTION.

This cover page contains information for quick reference only. It is not a summary of this issue. Investors must read the entire Official Statement to obtain information essential to making an informed investment decision.

The Series 2006 Certificates will be offered when, as and if executed and delivered, and received by the Underwriters, subject to the approval as to their legality by Orrick, Herrington & Sutcliffe LLP, Special Counsel to the County, and certain other conditions. Certain legal matters will be passed upon for the Underwriters by their counsel, Hawkins Delafield & Wood LLP, Los Angeles, California, and for the County and the Corporation by the County Counsel. It is anticipated that the Series 2006 Certificates in definitive form will be available for delivery through the facilities of DTC in New York, New York, on or about December 13, 2006.

Banc of America Securities LLC **LEHMAN BROTHERS**

Dated: November 30, 2006

$42,390,000
COUNTY OF SAN DIEGO
CERTIFICATES OF PARTICIPATION
(2006 EDGEMOOR COMPLETION PROJECT)

MATURITY SCHEDULE

BASE CUSIP No.[†]: 797391

$19,485,000 Serial Series 2006 Certificates

Maturity (February 1)	Principal Amount	Interest Rate	Yield	CUSIP Suffix[†]
2010	$1,275,000	4.000%	3.450%	G86
2011	1,325,000	4.000	3.470	G94
2012	1,375,000	4.000	3.500	H28
2013	1,430,000	4.000	3.550	H36
2014	1,490,000	4.000	3.610	H44
2015	1,550,000	5.000	3.670	H51
2016	1,625,000	5.000	3.720	H69
2017[(1)]	1,705,000	5.000	3.810	H77
2018[(1)]	1,795,000	5.000	3.860	H85
2019[(1)]	1,885,000	5.000	3.900	H93
2020	1,975,000	4.000	4.160	J26
2021	2,055,000	4.000	4.210	J34

$11,645,000 4.250% Term Bonds Due February 1, 2026, Price: 97.942%, CUSIP No.[†] 797391J42
$11,260,000 4.450% Term Bonds Due February 1, 2030, Price: 100%, CUSIP No.[†] 797391J59

(1) Priced to call on February 1, 2016.

[†] CUSIP data, copyright 2006, American Bankers Association. CUSIP data herein is set forth for convenience of reference only. The Corporation, the County and the Underwriters assume no responsibility for its accuracy.

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This Official Statement does not constitute an offer to sell or the solicitation of an offer to buy nor shall there be any sale of the Series 2006 Certificates by any person in any jurisdiction in which it is unlawful for such person to make such an offer, solicitation or sale. No dealer, broker, salesperson or other person has been authorized to give any information or to make any representations other than those contained in this Official Statement. If given or made, such other information or representations must not be relied upon as having been authorized by the County, the Corporation, or the Underwriters.

This Official Statement is not to be construed as a contract with the purchasers of the Series 2006 Certificates. Statements contained in this Official Statement which involve estimates, projections, forecasts or matters of opinion, whether or not expressly so described herein, are intended solely as such and are not to be construed as representations of facts.

The information set forth herein has been provided by the County and other sources that are believed by the County to be reliable. The Underwriters have provided the following sentence for inclusion in this Official Statement. The Underwriters have reviewed the information in this Official Statement in accordance with, and as part of, their responsibility to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Underwriters do not guarantee the accuracy or completeness of such information.

The information and expressions of opinion herein are subject to change without notice and neither delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the County or the Corporation since the date hereof. This Official Statement is submitted with respect to the sale of the Series 2006 Certificates referred to herein and may not be reproduced or used, in whole or in part, for any other purpose, unless authorized in writing by the County. All summaries of the documents and laws are made subject to the provisions thereof and do not purport to be complete statements of any or all such provisions. Preparation of this Official Statement and its distribution have been duly authorized and approved by the County and the Corporation.

In connection with the offering of the Series 2006 Certificates, the Underwriters may over-allot or effect transactions which stabilize or maintain the market price of the Series 2006 Certificates at a level above that which might otherwise prevail in the open market. Such stabilizing, if commenced, may be discontinued at any time. The Underwriters may offer and sell the Series 2006 Certificates to certain dealers, institutional investors and others at prices lower than the public offering prices stated on the cover page hereof and such public offering prices may be changed from time to time by the Underwriters.

COUNTY OF SAN DIEGO, STATE OF CALIFORNIA

COUNTY OF SAN DIEGO
BOARD OF SUPERVISORS

Greg Cox	First District
Dianne Jacob	Second District
Pam Slater-Price	Third District
Ron Roberts, Vice-Chairman	Fourth District
Bill Horn, Chairman	Fifth District

******

Walter F. Ekard, *Chief Administrative Officer*
Dan McAllister, *Treasurer – Tax Collector*
Donald F. Steuer, *Chief Financial Officer*
Tracy M. Sandoval, *Auditor & Controller*
John J. Sansone, *County Counsel*

******

SPECIAL SERVICES

Special Counsel
Orrick, Herrington & Sutcliffe LLP
Los Angeles, California

Trustee
Zions First National Bank
Los Angeles, California

Financial Advisor
RBC Capital Markets

$42,390,000
COUNTY OF SAN DIEGO
Certificates of Participation
(2006 Edgemoor Completion Project)
Evidencing and Representing Proportionate Undivided Interests of the Owners Thereof in Base Rental Payments to be Made by the County of San Diego to the San Diego County Capital Asset Leasing Corporation

INTRODUCTION

This introduction contains only a brief summary of certain of the terms of the Series 2006 Certificates being offered, and a brief description of the Official Statement. All statements contained in this introduction are qualified in their entirety by reference to the entire Official Statement. References to, and summaries of, provisions of the Constitution and laws of the State of California and any documents referred to herein do not purport to be complete and such references are qualified in their entirety by reference to the complete provisions. All capitalized terms used in this Official Statement and not otherwise defined herein have the meanings set forth in the Trust Agreement and the Subleases (herein defined). See Appendix C – "Summary of Principal Legal Documents – Definitions" attached hereto.

General

This Official Statement, including the cover page and the Appendices attached hereto (the "Official Statement"), provides certain information concerning the sale and delivery of the County of San Diego Certificates of Participation (2006 Edgemoor Completion Project) in an aggregate principal amount of $42,390,000 (the "Series 2006 Certificates"). The Series 2006 Certificates are being executed and delivered pursuant to a Trust Agreement, dated as of February 1, 2005, as amended and supplemented by a First Supplemental Trust Agreement, dated as of December 1, 2006 (collectively, the "Trust Agreement"), each by and among Zions First National Bank, as trustee (the "Trustee"), the County of San Diego (the "County") and the San Diego County Capital Asset Leasing Corporation (the "Corporation") to (i) finance the completion of a skilled nursing facility to replace the existing skilled nursing facility in Santee, California (the "Project"), (ii) purchase a reserve fund surety for the Certificate Reserve Fund, (iii) pay capitalized interest on a portion of the Series 2006 Certificates and a portion of the County's Certificates of Participation (2005 Edgemoor Project and 1996 Regional Communications System Refunding) (the "Series 2005 Certificates") through March 1, 2009, and (iv) pay certain costs of issuance incurred in connection with the Series 2006 Certificates. See "The Project Property and the Project" herein.

The County leases certain real property and all improvements thereon or to be located thereon, as more particularly described herein (the "Project Property"), to the Corporation pursuant to a Project Lease, dated as of February 1, 2005 (the "Project Lease"), by and between the County and the Corporation. The County subleases the Project Property from the Corporation pursuant to a Project Sublease, dated as of February 1, 2005, as amended by that certain First Amendment to Project Sublease, dated as of December 1, 2006 (collectively, the "Project Sublease"), each by and between the County and the Corporation. The County also leases certain real property and all improvements thereon or to be located thereon, as more particularly described therein (the "Refunding Property", together with the Project Property, the "Properties" and, individually, a "Property") to the Corporation pursuant to a Refunding Lease, dated as of February 1, 2005 (the "Refunding Lease", together with the Project Lease, the "Leases" and, individually, a "Lease"), by and between the County and the Corporation. The County subleases the Refunding Property from the Corporation pursuant to a Refunding Sublease, dated as of February 1, 2005 (the "Refunding Sublease", together with the Project Sublease, the "Subleases" and, individually, a "Sublease"), by and between the County and the Corporation The Series 2006 Certificates evidence proportionate undivided interests in additional base rental payments (together with the base rental payments presently made by the County under the hereinafter defined

Sublease, the "Project Base Rental Payments") to be made by the County as the rental for the Project Property under and pursuant to the Project Sublease. The County is not obligated under the Refunding Sublease to pay Project Base Rental Payments or under the Project Sublease to pay base rental payments under the Refunding Sublease (the "Refunding Base Rental Payments and, together with the Project Base Rental Payments, the "Base Rental Payments"). The rights and obligations under each Sublease are independent and an Event of Default or abatement under one Sublease will not in and of itself result in an Event of Default or abatement under the other Sublease. See "Security and Sources of Payment for the Series 2006 Certificates" herein. The Series 2006 Certificates are secured on a parity with the Series 2005 Certificates executed and delivered pursuant to the Trust Agreement and, together with the Series 2005 Certificates, are secured by Base Rental Payments made by the County pursuant to the Project Sublease and the Refunding Sublease.

Security and Source of Payment for the Series 2006 Certificates

Under the Subleases, in consideration for the use and occupancy of the Properties, the County has agreed to make certain payments designated as Base Rental Payments and certain other payments designated as Additional Rental with respect to each of the Properties (collectively, the "Additional Rental"), in the amounts, at the times and in the manner set forth in the Subleases. Base Rental Payments are scheduled to be sufficient to pay, when due, amounts designated as principal and interest represented by the Series 2005 Certificates and the Series 2006 Certificates. The County has covenanted in the Subleases to take such action as may be necessary to include all Base Rental Payments and the Additional Rental due thereunder in its operating budget for each fiscal year commencing after the date of the Subleases, and to make all necessary appropriations for such Base Rental Payments and Additional Rental.

The County has no obligation to pay Base Rental Payments under the Project Sublease until the Project (as herein defined) is substantially completed. A portion of the proceeds of the Series 2006 Certificates will be set aside and used to pay Base Rental Payments due under the Project Sublease through March 1, 2009 ("Capitalized Base Rental Payments"). See table captioned "Base Rental Payments" under the heading "Security and Sources of Payment for the Series 2006 Certificates – Base Rental Payments" herein for a description of the amounts due under the Project Sublease. If completion of the Project is delayed beyond this date, Base Rental Payments due under the Project Sublease would not be payable by the County except from funds in the Certificate Reserve Fund.

Pursuant to an Assignment Agreement, dated as of February 1, 2005, as amended by a First Amendment to Assignment Agreement, dated as of December 1, 2006 (collectively, the "Assignment Agreement"), by and between the Trustee and the Corporation, the Corporation assigned to the Trustee, for the benefit of the Owners of the Series 2005 Certificates and the Series 2006 Certificates all of its right, title and interest in and to the Subleases, including the right to receive Base Rental Payments under the Subleases. See Appendix C – "Summary of Principal Legal Documents – The Subleases," and "– Trust Agreement" attached hereto.

THE OBLIGATION OF THE COUNTY TO MAKE BASE RENTAL PAYMENTS AND TO PAY ADDITIONAL RENTAL UNDER THE SUBLEASES DOES NOT CONSTITUTE AN OBLIGATION OF THE COUNTY FOR WHICH THE COUNTY IS OBLIGATED TO LEVY OR PLEDGE ANY FORM OF TAXATION OR FOR WHICH THE COUNTY HAS LEVIED OR PLEDGED ANY FORM OF TAXATION. NEITHER THE SERIES 2006 CERTIFICATES NOR THE OBLIGATION OF THE COUNTY TO MAKE BASE RENTAL PAYMENTS OR TO PAY ADDITIONAL RENTAL UNDER THE SUBLEASES CONSTITUTES AN INDEBTEDNESS OF THE COUNTY, THE STATE OF CALIFORNIA OR ANY OF ITS POLITICAL SUBDIVISIONS WITHIN THE MEANING OF ANY CONSTITUTIONAL OR STATUTORY DEBT LIMITATION OR RESTRICTION.

The County's obligation to pay Base Rental Payments is subject to abatement. However, during periods of abatement, any moneys in the Base Rental Payment Fund or in the Certificate Reserve Fund and amounts, if any, received from rental interruption insurance are available to pay Base Rental Payments. See "Security and Sources of Payment for the Series 2006 Certificates – Base Rental Payments" and "– Abatement" herein.

The Series 2006 Certificates

The Series 2006 Certificates will be executed and delivered in the form of fully registered certificates in principal amounts of $5,000 each or any integral multiple thereof. The Series 2006 Certificates will be dated their date of delivery and mature on February 1 in the years set forth on the cover page hereof. The interest represented by the Series 2006 Certificates will represent the sum of the portions of the Base Rental Payments designated as interest components coming due on the Interest Payment Dates in each year. The principal represented by the Series 2006 Certificates will represent the sum of the portions of the Base Rental Payments designated as principal components coming due on the Principal Payment Date in each year. Interest represented by the Series 2006 Certificates is payable on February 1 and August 1 of each year, commencing on August 1, 2007.

The Series 2006 Certificates will be issued in book-entry form only and, when delivered, will be registered in the name of Cede & Co., as nominee of The Depository Trust Company, New York, New York ("DTC"), which will act as securities depository for the Series 2006 Certificates. Individual purchases of the Series 2006 Certificates will be made in book-entry form only. Purchasers of the Series 2006 Certificates will not receive certificates representing their ownership interests in the Series 2006 Certificates purchased. Principal and interest payments represented by the Series 2006 Certificates are payable directly to DTC by the Trustee. Upon receipt of payments of principal and interest, DTC will in turn distribute such payments to the beneficial owners of the Series 2006 Certificates. See "The Series 2006 Certificates – General" herein and Appendix D – "Book-Entry System" attached hereto.

Bond Insurance

Payment of principal and interest with respect to the Series 2006 Certificates when due will be insured by a financial guaranty insurance policy (the "Insurance Policy") to be issued concurrently with the delivery of the Series 2006 Certificates by Ambac Assurance Corporation (the "Insurer"). See "Certificate Insurance" herein and Appendix F – "Specimen Financial Guaranty Insurance Policy" attached hereto.

Tax Matters

In the opinion of Orrick, Herrington & Sutcliffe LLP, Special Counsel, based upon an analysis of existing laws, regulations, rulings and court decisions, and assuming, among other matters, the accuracy of certain representations and compliance with certain covenants, interest evidenced by the Series 2006 Certificates is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986 and is exempt from State of California personal income taxes. In the further opinion of Special Counsel, interest evidenced by the Series 2006 Certificates is not a specific preference item for purposes of the federal individual or corporate alternative minimum taxes, although Special Counsel observes that such interest is included in adjusted current earnings when calculating corporate alternative minimum taxable income. Special Counsel expresses no opinion regarding any other tax consequences related to the ownership of, or accrual or receipt of interest evidenced by, the Series 2006 Certificates. See "Tax Matters" herein.

Continuing Disclosure

The County has agreed to provide, or cause to be provided, to each nationally recognized municipal securities information repository and any public or private repository or entity designated by the State as a state repository for purposes of Rule 15c2-12(b)(5) (the "Rule") adopted by the Securities and Exchange Commission (each, a "Repository") certain annual financial information and operating data and, in a timely manner, notice of certain material events. These covenants have been made in order to assist the Underwriters in complying with the Rule. See "Continuing Disclosure" herein for a description of the specific nature of the annual report and notices of material events and a summary description of the terms of the disclosure agreement pursuant to which such reports are to be made.

Forward-Looking Statements

Certain statements included or incorporated by reference in the Official Statement constitute "forward-looking statements." Such statements are generally identifiable by the terminology used such as "plan," "expect," "estimate," "budget" or other similar words. The achievement of certain results or other expectations contained in such forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause actual results, performance or achievements described to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Although such expectations reflected in such forward-looking statements are reasonable, there can be no assurance that such expectations will prove to be correct. The County is not obligated to issue any updates or revisions to the forward-looking statements if or when its expectations, or events, conditions or circumstances on which such statements are based occur.

Miscellaneous

The Series 2006 Certificates will be offered when, as and if executed and delivered, and received by the Underwriters, subject to the approval as to their legality by Special Counsel and certain other conditions.

The description herein of the Trust Agreement, the Subleases and the Assignment Agreement and any other agreements relating to the Series 2006 Certificates are qualified in their entirety by reference to such documents, and the descriptions herein of the Series 2006 Certificates are qualified in their entirety by the form thereof and the information with respect thereto included in the aforementioned documents. See Appendix C – "Summary of Principal Legal Documents" attached hereto. Copies of the documents are on file and available for inspection at the Corporate Trust Office of the Trustee at Zions First National Bank, 550 South Hope Street, Suite 2650, Los Angeles, California 90071.

The information and expressions of opinion herein speak only as of their date and are subject to change without notice. Neither the delivery of this Official Statement nor any sale made hereunder nor any future use of this Official Statement shall, under any circumstances, create any implication that there has been no change in the affairs of the County since the date hereof.

The presentation of information, including tables of receipt of revenues, is intended to show recent historical information and is not intended to indicate future or continuing trends in the financial position or other affairs of the County. No representation is made that past experience, as it might be shown by such financial and other information, will necessarily continue or be repeated in the future.

THE PROJECT PROPERTY AND THE PROJECT

The Project Property

The County subleases the Project Property from the Corporation pursuant to the Project Sublease. The Project Property consists of the Project, which is the construction and equipping of a County-owned and operated skilled nursing facility. The Project is located in the City of Santee, California on approximately 12.55 acres of the County's 326-acre Edgemoor property. The Project was initially financed by a portion of the proceeds of the Series 2005 Certificates and will be further financed by substantially all of the proceeds of the Series 2006 Certificates.

The Project

General. Substantially all of the proceeds of the Series 2006 Certificates will be used to finance the completion of the Project. The Project is a skilled nursing facility located on a two-story, 180,300 square feet complex and is expected to include 192 beds. The Project consists of three residential buildings and a central plant that houses certain utility pipes and drains for the entire Project. The Project is being constructed to replace an existing skilled nursing facility on another portion of the Edgemoor property. Construction of the Project began in February 2005 and has been subject to various delays and certain additional, unanticipated costs. See "– Project Schedule Delays and Construction Cost Increase" for a description of the factors contributing to the delays and additional costs experienced with respect to the Project. The Project has not been expanded as a result of the changes described herein. The Project is expected to be substantially completed in August 2008, with occupancy anticipated in December 2008, subject to extension because of force majeure events or changes to the Construction Contract (as herein defined) requested by the County (the "Completion Date").

As of October 2006, the total estimated cost of the Project was approximately $118.8 million, which is $35 million above the estimated Project costs at the time of issuance of the Series 2005 Certificates. Of the total Project costs, $79 million was funded from a portion of the proceeds of the Series 2005 Certificates, $4.78 million was appropriated by the County from its General Fund and $35 million will be funded from substantially all of the proceeds of the Series 2006 Certificates and other contributions from the County. See "– Project Schedule Delays and Construction Cost Increase" for a description of the factors contributing to the additional costs experienced with respect to the Project.

Project Status. As of October 2006, approximately $33.4 million of the proceeds of the Series 2005 Certificates had been expended on the Project and approximately $47.5 million remained available for the Project. Through such date, Sundt Construction, Inc. (the "Contractor") had completed approximately 39% of the Project, including excavations and grading completions, completion of the foundations, steel structures, cooling tower walls and ring roadway grading. In addition, concrete decks on residential buildings 1 and 2 had been poured, 90% of the paving had been completed and significant progress was made for roof concrete pouring. The framing of the Project complex is expected to start at the beginning of 2007.

Project Schedule Delays and Construction Cost Increase. The Project delays and increased costs are primarily related to a change in soil conditions, design problems associated with fireproofing the buildings' structural steel frames and design and construction conflicts associated with the fireproofing of the steel. Remediation of the soil condition and resolution of the design problems and associated conflicts will delay completion of the Project by approximately two years and resulted in approximately $35 million in increased Project costs, which amounts consist of $3 million in soil remediation, $10 million in design and fabrication of steel, and $13 million in remediation of the fireproofing issues associated with the steel redesign. In addition to these costs, there are approximately $9 million of other costs associated with the two year delay, including construction management, inspectors and reserves.

Saturated Soils. The County received an unusually high amount of winter rains in 2004 and 2005. The moisture from the rain was retained by the native clay soils and resulted in saturated subsurface soil conditions. The saturated soils initially prevented the excavation and compaction of the foundation beneath the building pads. Remediation consisting of permanent subsurface drains and cement treatment of the wet soils was completed upon the recommendation of a registered soils engineer. The cement treated soil provided a stabilized foundation to complete the construction of the building pads and slabs. The soil condition and remediation activities resulted in the addition of two months to the expected date of completion of the Project.

Steel Fireproofing. Design problems associated with steel fireproofing delayed fabrication and erection of the structural steel frames of the buildings. Although the Project plans were reviewed and approved by the Office of Statewide Health Planning and Development ("OSHPD") in December 2004, it was subsequently determined by OSHPD that the Underwriters Laboratory ("UL") assembly included in the architect's plans for fire proofing structural tube steel beams had not been tested and approved by UL for a beam application. In light of the pervasive use of tube steel throughout the design, OSHPD directed that the fabrication and erection of steel be halted until the architect could provide a code-compliant solution to fireproofing the tube steel. Approximately 40% of the steel had been fabricated for Buildings 1 and 2 at the time fabrication was stopped.

Based on a UL engineering judgment opinion, the architect submitted and obtained approval of a revised fireproofing assembly for tube steel beams that involved the application of wire mesh and an additional two inches of fireproofing material. OSHPD approval was finalized in December 2005 and the Contractor was directed to resume erection of the steel frame. Correction of the design error resulted in the addition of two months to the expected date of completion of the Project.

Shortly after steel fabrication was halted, the Contractor notified the County that its steel subcontractor was closing the local plant. An alternate fabrication shop was secured in January 2006 and delivery of steel began in late March 2006. This second steel fireproofing-related delay resulted in the addition of four months to the expected date of completion of the Project.

Impact of the Fireproofing of the Steel. Because of the pervasive use of tube steel throughout the design, the addition of several inches of fireproofing material per rolled steel beam as described above rippled throughout the Project design and resulted in approximately 6,000 mechanical, electrical and plumbing conflicts throughout the structure. Revisions to the designs and change orders relating to such revisions accounted for the remaining 13 months of delay. Accordingly, each of these events resulted in the addition of approximately two years to the expected date of completion of the Project.

The Contractor; Construction Contract. The changes to the Project described under "– Project Schedule Delays and Construction Cost Increase" were effected through change orders to the existing Construction Contract, which has been amended to reflect, among other things, all changes in design construction through August 15, 2006 affecting the Contractor and its subcontractors. The amendment to the Construction Contract also provides for an increase in the contract price from $66.231 million to $92.2 million, an extension of the construction schedule to reflect Project completion in August 2008, and liquidated damages payable to the County in the event the Project is not completed by October 2008. The Construction Contract does not provide for a release of the Contractor with respect to its performance under the Contract to date.

In 2005, the County conducted a competitive bidding process with respect to the Project and received two bids from bidders pre-qualified by the County. The Contractor submitted the lowest bid for the Project. The County entered into a construction agreement with the Contractor in connection with the Project in February 2005 and amended such contract in November 2006 (as amended, the "Construction Contract").

The Construction Contract is in the aggregate amount of approximately $92.2 million. The Contractor is a diversified construction company that provides general contracting, construction management and design-build services to private and public sector clients. The Contractor has completed projects in approximately 21 states and 11 foreign countries since its inception in 1890. In accordance with the terms of the Construction Contract, the Contractor posted a performance bond in the amount of 100% of the contract price and posted a payment bond in the amount of 100% of the contract price. No financial rating is required for such payment bonds; however, the payment bonds must be provided by a reputable surety company satisfactory to the County under the Construction Contract.

The Construction Contract is a "fixed price" contract. The County is not obligated to pay for increased costs of the Project above those addressed by the Construction Contract amendment unless such increased costs are the result of changes under the Construction Contract approved by the County or are caused by the gross negligence or willful act of the County as described in the next paragraph or as a result of federal, State or local agency review, approval, licensing, commissioning or inspection requirements. The Construction Contract provides that any unforeseeable delay of completion of the services and materials to be provided under the Construction Contract (the "Work") that is after the Completion Date caused by conditions beyond the control and without the fault or negligence of either the Contractor or the County (*e.g.*, "force majeure" events) may entitle the Contractor to an extension of the Construction Contract, but will not entitle the Contractor to any adjustment in the contract sum. The County cannot predict what force majeure events may occur in the future. The budget for the Project completion includes approximately $6 million for contingencies. This amount is 8.6% of the cost of work remaining to be completed under the Construction Contract, as amended.

The Construction Contract also provides that any unforeseeable delay of the completion of the Work beyond the Completion Date caused by the gross negligence or willful acts of the County, such as County-directed changes, differing site conditions, or suspension of the Work, and which delay is unreasonable under the circumstances involved and not within the contemplation of the parties, the Contractor may be entitled to an extension of Construction Contract and/or an adjustment of the contract sum. There can be no assurance that the County will be able to provide funds to complete the Project under circumstances in which the Contractor is entitled to an adjustment of the contract sum. The Construction Contract provides that the parties may, but are not required, to agree to submit disputes under the contract to binding arbitration and that the sureties of the Contractor are bound by the results of the arbitration and may join as parties to the arbitration. The Contractor is not entitled under the Construction Contract to either an extension of time or an adjustment of the contract sum for any foreseeable delay of the completion of the Work beyond the Completion Date caused by conditions within the control of the Contractor, including performance of the Contractor and subcontractors, timely material delivery, financial inability of the Contractor or any subcontractors, and any default of any subcontractor without limitation.

The Contractor carries, from an insurance carrier rated A VII by Best Ratings, Commercial General Liability ("CGL") insurance in the amount of $5 million per occurrence for bodily injury and property damage. In addition, the Contractor carries products and completed operations insurance with a limit of not less than $5 million per occurrence to be maintained for three years following acceptance of the work by the County. The general aggregate limit shall be $5 million and shall be a project specific aggregate. The Contractor's commercial general liability policy names the County as an additional insured. The Contractor also carries automobile liability in the amount of $1 million for each accident for bodily injury and property damage covering all owned, non-owned and hired vehicles. The Contractor carries State worker's compensation and employer's liability insurance providing $1 million for each accident for bodily injury or disease. The worker's compensation-employers liability insurance includes a waiver of subrogation endorsement in favor of the County. The Contractor has obtained professional errors and omissions insurance in an amount of $2 million per claim with an aggregate limit of not less than $2 million. Any self retained limit over $50,000 must be approved by the County's Risk Manager. Professional errors and omissions

insurance must be maintained for a minimum of two years following submission of a Certificate of Completion.

The Contractor has obtained builder's risk insurance for the full replacement value of the property at the time of loss on an "all-risk" or special form perils, including flood and theft of building materials, which perils do not include an earthquake. The policy provides coverage for collapse resulting from design errors. This policy also includes $3 million in coverage for County furnished/Contractor installed equipment. There is no insurance required under the Construction Contract, or being sought, to cover possible delays in completion of the construction of the Project due to perils covered by the builder's risk insurance policy. If such insurance were obtained, it would cover some of or all of the Base Rental Payments payable under the Project Sublease after Capitalized Base Rental Payments are no longer available due to delays in completion of the Project if due to a peril covered by the builder's risk policy. See "Risk Factors – Seismic Events; Force Majeure" herein.

If the Contractor fails to deliver the Project to the County by August 29, 2008 or such later date as is extended by excusable delays such as force majeure events or changes in the Construction Contract or as a result of federal, State or local agency review, approval, licensing, commissioning or inspection requirements, and performance has not otherwise been excused, then the Contractor must pay the County liquidated damages in the amount of $5,000 per day for each day beyond the Completion Date until October 29, 2008, or such later date which is 120 days following the scheduled Completion Date, and an additional $15,000 per day for each day thereafter until the Project is substantially completed. The County's rights in and to all of these liquidated damages accruing from and after March 1, 2009 will be assigned to the Corporation (which then assigns those rights to the Trustee for the benefit of the Owners under the Assignment Agreement) and any payments of liquidated damages received by the Trustee will be deposited in the Base Rental Payment Fund and will be available to pay the principal components of Base Rental Payments with respect to the Series 2005 Certificates and the Series 2006 Certificates on a pro rata basis. Payments of liquidated damages, if any, are not available to pay the interest components of Base Rental Payments with respect to the Series 2005 Certificates or the Series 2006 Certificates. If the Contractor were to default in its obligation to pay these liquidated damages, County Counsel is of the opinion that the surety on the performance bond would be bound to pay the liquidated damages; however, the surety would not be so bound to the extent that these liquidated damages, when combined with all other amounts paid by the surety, exceed the penal sum of the bond. The Contractor may be entitled to raise certain contractual defenses, setoffs and counterclaims with respect to the payment of liquidated damages.

The Architect. The County has informed Anshen and Allen ("Anshen"), the original architect of record, that a significant portion of the cost and schedule increases are a direct result of Anshen's design. Anshen has chosen not to complete the Project as the architect of record. The County has identified and is in the process of contracting with an alternative firm, Carrier Johnson ("Carrier Johnson"), to complete the Project. Carrier Johnson is a local architectural firm that has assembled a team that includes the architectural firm of Leary, Childs, Mascari and Warner and the structural engineering firm of KPFF, Inc. Both of these additional sub-consultants were added to the team because of their significant experience with OSHPD projects. The collective team has built several hospitals in the San Diego area. Carrier Johnson has informed the County in writing that they have adequate resources onboard to ensure continued architectural and design support to the Project in order for the Project to be completed in accordance with the revised schedule. OSHPD approved the change to the architect of record for the Project on November 17, 2006.

See "Risk Factors - Risk of Further Delay in Completion of the Project" for a description of the County's obligation to pay Base Rental Payments if there are further delays in the completion of the Project.

Reimbursement. The County believes that approximately 46% of the total Base Rental Payments due under the Project Sublease will be reimbursed under Section 14105.26 of the California Welfare and

Institutions Code providing reimbursement to certain facilities that serve Medicaid patients. However, no assurance is made by the County in this regard. Notwithstanding, the County is required under the Project Sublease to make Base Rental Payments from legally available funds and has covenanted in the Project Sublease to take such action as may be necessary to include all Base Rental Payments and Additional Rental due under the Project Sublease in its operating budget for each fiscal year commencing after the date of the Project Sublease and to make the necessary appropriations for such Base Rental Payments and Additional Rental, except to the extent such payments are abated in accordance with the Project Sublease. See "Security and Sources of Payment for the Series 2006 Certificates – Base Rental Payments" herein.

ESTIMATED SOURCES AND USES OF FUNDS

The proceeds of the Series 2006 Certificates and certain other amounts are expected to be applied approximately as follows:

Sources:	
Principal Amount of Certificates	$42,390,000.00
Net Original Issue Premium	606,313.90
Contribution from the County	6,995,556.00
Total Sources	$49,991,869.90
Uses:	
Construction Fund	$36,291,069.39
Capitalized Interest Account within the Interest Fund[(1)]	10,582,029.12
Principal Fund[(2)]	2,210,000.00
Costs of Issuance[(3)]	908,771.39
Total Uses	$49,991,869.90

(1) Capitalized interest for a portion of the Series 2005 Certificates and a portion of the Series 2006 Certificates for the period from the date of delivery of the Series 2006 Certificates through March 1, 2009.

(2) Amount attributable to payment of the principal portion of the Base Rental Payment for the Series 2005 Certificates becoming due and payable in Fiscal Year 2007-08.

(3) Includes underwriters' discount, rating agencies fees, bond insurance premium, reserve fund surety premium, financial advisor fees, title insurance fees, legal fees, trustee fees and printing costs and other costs of issuance.

THE SERIES 2006 CERTIFICATES

The following is a summary of certain provisions of the Series 2006 Certificates. Reference is made to the Series 2006 Certificates for the complete text thereof and to the Trust Agreement for a more detailed description of such provisions. The discussion herein is qualified by such reference. See Appendix C – "Summary of Principal Legal Documents" attached hereto.

General

The Series 2006 Certificates will be dated their date of delivery and principal with respect to the Series 2006 Certificates will be payable on the dates set forth on the inside cover page of this Official Statement. The interest represented by the Series 2006 Certificates will represent the sum of the portions of the Base Rental Payments designated as interest components coming due on the Interest Payment Dates in each year. The principal represented by the Series 2006 Certificates will represent the sum of the portions of the Base Rental Payments designated as principal components coming due on the Principal Payment Date in each year. Interest with respect to the Series 2006 Certificates will be payable semiannually on each February 1 and August 1 of each year, commencing on August 1, 2007 (each, an "Interest Payment Date") and will be computed on the basis of a 360-day year of twelve 30-day months.

Book-Entry System

The Series 2006 Certificates will be executed and delivered in the form of fully registered certificates in principal amounts of $5,000 each or any integral multiple thereof. The Series 2006 Certificates will be issued in book-entry form only and, when delivered, will be registered in the name of Cede & Co., as nominee of DTC, which will act as securities depository for the Series 2006 Certificates. Individual purchases of the Series 2006 Certificates will be made in book-entry form only. Purchasers of the Series 2006 Certificates will not receive certificates representing their ownership interests in the Series 2006 Certificates purchased. Principal and interest payments represented by the Series 2006 Certificates are payable directly to DTC by the Trustee. Upon receipt of payments of principal and interest, DTC will in turn distribute such payments to the beneficial owners of the Series 2006 Certificates. See Appendix D – "Book-Entry System" attached hereto.

Prepayment

Optional Prepayment. The Series 2006 Certificates maturing on and after February 1, 2017 are subject to optional prepayment prior to their stated Principal Payment Dates, on any date on or after February 1, 2016, in whole or in part, in Authorized Denominations, from and to the extent of prepaid Base Rental Payments paid pursuant to the Leases, any such prepayment to be at a price equal to the principal evidenced by the Series 2006 Certificates to be prepaid, plus accrued interest evidenced thereby to the date fixed for prepayment, without premium.

Mandatory Sinking Fund Prepayment. The Series 2006 Certificates with a stated Principal Payment Date of February 1, 2026 are subject to prepayment prior to such stated Principal Payment Date, in part, from Mandatory Sinking Account Payments, on each February 1 specified below, at a prepayment price equal to the principal evidenced thereby, plus accrued interest evidenced thereby to the date fixed for prepayment, without premium. The principal evidenced by such Series 2006 Certificates to be so prepaid and the dates therefor shall be as follows:

Prepayment Date (February 1)	Principal Component To Be Prepaid
2022	$2,140,000
2023	2,230,000
2024	2,325,000
2025	2,425,000
2026*	2,525,000

* Stated Principal Payment Date

The Series 2006 Certificates with a stated Principal Payment Date of February 1, 2030 are subject to prepayment prior to such stated Principal Payment Date, in part, from Mandatory Sinking Account Payments, on each February 1 specified below, at a prepayment price equal to the principal evidenced thereby, plus accrued interest evidenced thereby to the date fixed for prepayment, without premium. The principal evidenced by such Series 2006 Certificates to be so prepaid and the dates therefor shall be as follows:

Prepayment Date (February 1)	**Principal Component To Be Prepaid**
2027	$2,635,000
2028	2,750,000
2029	2,875,000
2030*	3,000,000

* Stated Principal Payment Date

The amount of each such prepayment shall be reduced proportionately in the event and to the extent of any and all prepayments of Series 2006 Certificates with a stated Principal Payment Date of February 1, 2026 or February 1, 2030, pursuant to any provision of the Trust Agreement other than optional prepayments as described above.

Extraordinary Prepayment. The Series 2006 Certificates are subject to prepayment on any date prior to their respective maturity dates, as a whole, or in part, at the written direction of the County, from the net proceeds of any insurance or condemnation award with respect to the Property or portions thereof, at a prepayment price equal to the sum of the principal amount represented thereby plus accrued interest represented thereby to the date fixed for prepayment, without premium.

Notice of Prepayment. When prepayment is authorized pursuant to the Trust Agreement the Trustee shall give notice, at the expense of the County, of the prepayment of the Series 2006 Certificates. The notice of prepayment shall specify: (a) the Series 2006 Certificates or designated portions thereof (in the case of prepayment of the Series 2006 Certificates in part but not in whole) which are to be prepaid, (b) the date of prepayment, (c) the place or places where the prepayment will be made, including the name and address of any paying agent, (d) the prepayment price, (e) the CUSIP numbers assigned to the Series 2006 Certificates to be prepaid, (f) the numbers of the Series 2006 Certificates to be prepaid in whole or in part (if less than all of the Series 2006 Certificates of a maturity are to be prepaid) and, in the case of any Certificates to be prepaid in part only, the amount of such Certificates to be prepaid, and (g) the stated Principal Payment Date of each Series 2006 Certificate to be prepaid in whole or in part. Such notice of prepayment shall further state that on the specified date there shall become due and payable upon each Series 2006 Certificate or portion thereof being prepaid the prepayment price, together with interest accrued to the prepayment date thereon, and that from and after such date interest represented thereby shall cease to accrue and be payable. A notice of prepayment may provide (a) that the prepayment is conditioned upon the occurrence of one or more events specified in the notice and (b) that such notice may be revoked, without any cause, at any time prior to the prepayment date. The Trustee shall give the foregoing notice at least 30 but not more than 60 days before to the prepayment date to the respective Owners of Certificates designated for prepayment by first class mail, postage prepaid, at their addresses appearing on the registration books of the Trustee as of the close of business on the day before such notice of prepayment is given.

SECURITY AND SOURCES OF PAYMENT FOR THE SERIES 2006 CERTIFICATES

Base Rental Payments

General. The Series 2006 Certificates, together with the Series 2005 Certificates, represent the aggregate principal components of the Base Rental Payments under the Refunding Sublease and the Project Sublease. The Series 2006 Certificates evidence proportionate undivided interests in an amount of Project Base Rental Payments equal to additional Project Base Rental Payments to be made by the County pursuant to the Project Sublease. The County is required under the Subleases to make Base Rental Payments subject to the provisions of the Subleases related to abatement. Until such time as a Certificate of Completion has been delivered to the Trustee, the County's obligation to pay Base Rental Payments and Additional Rental under the Subleases will be limited solely, in the case of Base Rental Payments under the Subleases, to amounts on deposit in the Interest Fund (including, without limitation, the Capitalized Interest Account established therein) established pursuant to the Trust Agreement, and, if there are no funds remaining in the Interest Fund, the Certificate Reserve Fund, and, in the case of Additional Rent, the Cost of Issuance Fund, and the County will have no obligation to make any Base Rental Payments or Additional Rental under the Subleases from any other source. The County has covenanted in the Subleases to take such action as may be necessary to include all Base Rental Payments and Additional Rental with respect to the Properties in its operating budget for each fiscal year commencing after the date of the Subleases and to make the necessary appropriations for such Base Rental Payments and Additional Rental. Base Rental Payments are scheduled to be paid as set forth herein. The County is not obligated under the Refunding Sublease to pay Project Base Rental Payments or under the Project Sublease to pay Refunding Base Rental Payments. The rights and obligations under each Sublease are independent and an Event of Default or abatement under one Sublease will not in and of itself result in an Event of Default or abatement under the other Sublease.

THE OBLIGATION OF THE COUNTY TO MAKE BASE RENTAL PAYMENTS AND TO PAY ADDITIONAL RENTAL UNDER THE SUBLEASES DOES NOT CONSTITUTE AN OBLIGATION OF THE COUNTY FOR WHICH THE COUNTY IS OBLIGATED TO LEVY OR PLEDGE ANY FORM OF TAXATION OR FOR WHICH THE COUNTY HAS LEVIED OR PLEDGED ANY FORM OF TAXATION. NEITHER THE SERIES 2006 CERTIFICATES NOR THE OBLIGATION OF THE COUNTY TO MAKE BASE RENTAL PAYMENTS OR TO PAY ADDITIONAL RENTAL UNDER THE SUBLEASES CONSTITUTES AN INDEBTEDNESS OF THE COUNTY, THE STATE OF CALIFORNIA OR ANY OF ITS POLITICAL SUBDIVISIONS WITHIN THE MEANING OF ANY CONSTITUTIONAL OR STATUTORY DEBT LIMITATION OR RESTRICTION.

The Trustee, pursuant to the Trust Agreement, will receive Base Rental Payments for the benefit of the Owners. Base Rental Payments are scheduled to be sufficient to pay, when due, amounts designated as principal and interest represented by the Series 2005 Certificates and the Series 2006 Certificates. Except as expressly provided in the Trust Agreement, the Trustee will not have any obligation or liability to the Owners with respect to the payment when due of the Base Rental Payments by the County, or with respect to the performance by the County or the Corporation of the other agreements and covenants required to be performed by them, respectively contained in the Leases or the Subleases or in the Trust Agreement. Additional Rental payable by the County under the Subleases include, among others, amounts sufficient to pay certain taxes and assessments and insurance premiums, and certain administrative costs.

The lease payments under the Subleases are absolutely net to the Corporation so that the Subleases will yield to the Corporation the lease payments, free of any charges, assessments or impositions of any kind charged, assessed or imposed on or against the Properties, and without counterclaim, deduction, defense, deferment or set-off by the County except as specifically otherwise provided in the Subleases. The Subleases provide that the covenants of the County thereunder are deemed to be duties imposed by law, and it further provides that it will be the duty of each and every public official of the County to take such action and do

such things as are required by law in the performance of the official duty of such officials to enable the County to carry out and perform the covenants and agreements of the County contained in the Subleases.

Upon the occurrence of an Event of Default under the Project Sublease or the Refunding Sublease, the Trustee must thereafter maintain the Project Sublease or the Refunding Sublease, as applicable, in full force and effect and may only recover rent and other monetary charges as they become due, all without terminating the County's right to possession of the Project Property or the Refunding Property, as applicable, regardless of whether or not the County has abandoned the Property, as applicable; THIS IS THE SOLE AND EXCLUSIVE REMEDY AVAILABLE AGAINST THE COUNTY UNDER THE SUBLEASES OR OTHERWISE. The Trustee may not exercise any right of entry upon or repossession of the Properties and there is no remedy of acceleration of Base Rental Payments over the term of the Subleases.

THE OBLIGATION OF THE COUNTY TO MAKE BASE RENTAL PAYMENTS AND TO PAY ADDITIONAL RENTAL UNDER THE SUBLEASES DOES NOT CONSTITUTE AN OBLIGATION OF THE COUNTY FOR WHICH THE COUNTY IS OBLIGATED TO LEVY OR PLEDGE ANY FORM OF TAXATION OR FOR WHICH THE COUNTY HAS LEVIED OR PLEDGED ANY FORM OF TAXATION. NEITHER THE SERIES 2006 CERTIFICATES NOR THE OBLIGATION OF THE COUNTY TO MAKE BASE RENTAL PAYMENTS OR TO PAY ADDITIONAL RENTAL UNDER THE SUBLEASES CONSTITUTES AN INDEBTEDNESS OF THE COUNTY, THE STATE OF CALIFORNIA OR ANY OF ITS POLITICAL SUBDIVISIONS WITHIN THE MEANING OF ANY CONSTITUTIONAL OR STATUTORY DEBT LIMITATION OR RESTRICTION. SEE APPENDIX C – "SUMMARY OF PRINCIPAL LEGAL DOCUMENTS – THE PROJECT SUBLEASE – RENTAL PAYMENTS – RENTAL ABATEMENT" AND "REFUNDING SUBLEASE-RENTAL PAYMENTS – RENTAL ABATEMENT" ATTACHED HERETO.

In addition, the County's rights in and to all of these liquidated damages accruing from and after March 1, 2009 will be assigned to the Corporation (which then assigns those rights to the Trustee for the benefit of the Owners under the Assignment Agreement) and any payments of liquidated damages received by the Trustee will be deposited in the Base Rental Payment Fund and will be available to pay the principal components of Base Rental Payments with respect to the Series 2005 Certificates and the Series 2006 Certificates on a pro rata basis. Payments of liquidated damages, if any, are not available to pay the interest components of Base Rental Payments with respect to the Series 2005 Certificates or the Series 2006 Certificates.

Base Rental Payments Schedules. The Project Sublease requires that each year's semi-annual Base Rental Payments thereunder be deposited with the Trustee, as assignee of the Corporation, on or before each July 5 of such fiscal year (or the next Business Day if July 5 does not fall on a Business Day), commencing on the July 5 (or the next Business Day if July 5 does not fall on a Business Day) following the date of delivery of the Certificate of Completion to the Trustee, through the term of the Project Sublease; provided, however, that if a Certificate of Completion is delivered after July 5, 2008 on any date in a Fiscal Year of the County after July 5 (or the next Business Day if July 5 does not fall on a Business Day) and before February 1 of that same Fiscal Year, the County will make the scheduled Base Rental Payments due on any Interest Payment Date in that Fiscal Year following the date of the delivery of the Certificate of Completion. The Refunding Sublease requires that each year's semi-annual Base Rental Payments thereunder be deposited with the Trustee, as assignee of the Corporation, on or before each July 5 of such fiscal year (or the next Business Day if July 5 does not fall on a Business Day) through the term of the Refunding Sublease.

A table of annual debt service payments under the Subleases is set forth below.

BASE RENTAL PAYMENTS

Payment Date (Year Ending)[1]	Series 2005 Certificates		Series 2006 Certificates Principal[1]	Series 2006 Certificates Interest[1]	Subtotal 2006 Base Rental Payments	Total Base Rental Payments[2]
	Refunding Component	Edgemoor Component[1]				
2/1/2006	$5,736,112.12	$3,919,095.80				$ 9,655,207.92
2/1/2007	2,984,637.50	3,930,012.50				6,914,650.00
2/1/2008	2,978,587.50	6,140,012.50		$2,109,113.50	$2,109,113.50	11,227,713.50
2/1/2009	2,985,887.50	6,138,712.50		1,860,982.50	1,860,982.50	10,985,582.50
2/1/2010	2,981,087.50	6,140,462.50	$1,275,000.00	1,860,982.50	3,135,982.50	12,257,532.50
2/1/2011	2,969,487.50	6,140,112.50	1,325,000.00	1,809,982.50	3,134,982.50	12,244,582.50
2/1/2012	2,961,237.50	6,137,662.50	1,375,000.00	1,756,982.50	3,131,982.50	12,230,882.50
2/1/2013	2,960,350.00	6,136,900.00	1,430,000.00	1,701,982.50	3,131,982.50	12,229,232.50
2/1/2014	2,962,350.00	6,136,150.00	1,490,000.00	1,644,782.50	3,134,782.50	12,233,282.50
2/1/2015	1,433,400.00	6,139,600.00	1,550,000.00	1,585,182.50	3,135,182.50	10,708,182.50
2/1/2016	1,427,750.00	6,140,750.00	1,625,000.00	1,507,682.50	3,132,682.50	10,701,182.50
2/1/2017	1,429,000.00	6,138,000.00	1,705,000.00	1,426,432.50	3,131,432.50	10,698,432.50
2/1/2018	1,427,250.00	6,138,000.00	1,795,000.00	1,341,182.50	3,136,182.50	10,701,432.50
2/1/2019	1,417,500.00	6,140,250.00	1,885,000.00	1,251,432.50	3,136,432.50	10,694,182.50
2/1/2020		6,139,250.00	1,975,000.00	1,157,182.50	3,132,182.50	9,271,432.50
2/1/2021		6,139,750.00	2,055,000.00	1,078,182.50	3,133,182.50	9,272,932.50
2/1/2022		6,136,250.00	2,140,000.00	995,982.50	3,135,982.50	9,272,232.50
2/1/2023		6,138,500.00	2,230,000.00	905,032.50	3,135,032.50	9,273,532.50
2/1/2024		6,135,750.00	2,325,000.00	810,257.50	3,135,257.50	9,271,007.50
2/1/2025		6,137,750.00	2,425,000.00	711,445.00	3,136,445.00	9,274,195.00
2/1/2026		6,138,750.00	2,525,000.00	608,382.50	3,133,382.50	9,272,132.50
2/1/2027		6,138,250.00	2,635,000.00	501,070.00	3,136,070.00	9,274,320.00
2/1/2028		6,135,750.00	2,750,000.00	383,812.50	3,133,812.50	9,269,562.50
2/1/2029		6,140,750.00	2,875,000.00	261,437.50	3,136,437.50	9,277,187.50
2/1/2030		6,137,250.00	3,000,000.00	133,500.00	3,133,500.00	9,270,750.00

(1) Until the Certificate of Completion is delivered to the Trustee, the County's obligation to make Base Rental Payments under the Project Sublease is limited to amounts on deposit in the Interest Fund (including the Capitalized Interest Account) and the Certificate Reserve Fund.

(2) Amounts reflect the aggregate amount of scheduled Base Rental Payments under the Subleases on August 1 of any calendar year and the February 1 of the immediately following calendar year.

Certificate Reserve Fund

The Certificate Reserve Fund shall be held by the Trustee and shall be kept separate and apart from all other funds held by the Trustee. The Certificate Reserve Fund must be funded in the amount of the Certificate Reserve Fund Requirement and must be used and withdrawn by the Trustee solely for the purposes and at the times specified in the Trust Agreement. The "Certificate Reserve Fund Requirement" is, as of any date of calculation, the lesser of (i) an amount equal to the largest Annual Debt Service for all future Lease Years beginning the Lease Year in which the calculation is made, (ii) 10% of the proceeds of the Series 2005 Certificates, the Series 2006 Certificates and any Additional Certificates, in accordance with the Tax Certificate to be made by the County under the Subleases until the final maturity of the Outstanding Series 2005 Certificates, Series 2006 Certificates and any Additional Certificates, or (iii) 125% of the average of the Annual Debt Service for all Lease Years, including the Lease Year in which the calculation is made. "Lease Year" means the period from each February 1 to and including the following January 31. "Annual Debt Service" means, for each Lease Year, an amount equal to the sum of all Base Rental Payments due in such Lease Year.

At the option of the County, one or more letter of credit, line of credit, surety bond, insurance policy or similar facility (each a "Reserve Fund Credit Facility") may be substituted for the funds held by the Trustee

in the Certificate Reserve Fund such that the amount available to be drawn under such Reserve Fund Credit Facilities together with funds remaining in the Certificate Reserve Fund satisfies the Certificate Reserve Fund Requirement.

The County will initially fund the Certificate Reserve Fund with a Reserve Fund Credit Facility. See Appendix C – "Summary of Principal Legal Documents – Trust Agreement – Proceeds of the Certificates – Certificate Reserve Fund" attached hereto.

Ambac Assurance Surety Bond

The Trust Agreement requires the establishment of a Certificate Reserve Fund in an amount equal to the Certificate Reserve Requirement with respect to the Series 2005 Certificates and the Series 2006 Certificates. The Trust Agreement authorizes the Obligor (as such term is defined in the hereinafter described Surety Bond) to obtain a Reserve Fund Credit Facility, which may be a surety bond (the "Surety Bond"), in lieu of funding the Certificate Reserve Fund with cash. Accordingly, application has been made to the Insurer for the issuance of a Surety Bond for the purpose of funding the Certificate Reserve Fund. See Appendix C – "Summary of the Principal Legal Documents – Trust Agreement – Proceeds of the Certificates – Certificate Reserve Fund" attached hereto. The Series 2006 Certificates will only be delivered upon the issuance of such Surety Bond. The premium on the Surety Bond is to be fully paid at or prior to the execution and delivery of the Series 2006 Certificates. The Surety Bond provides that upon the later of (i) one (1) day after receipt by the Insurer of a demand for payment executed by the Trustee certifying that provision for the payment of principal of or interest on the Series 2006 Certificates when due has not been made or (ii) the interest payment date specified in the Demand for Payment submitted to the Insurer, the Insurer will promptly deposit funds with the Trustee sufficient to enable the Trustee to make such payments due on the Series 2006 Certificates, but in no event exceeding the Surety Bond Coverage, as defined in the Surety Bond.

Pursuant to the terms of the Surety Bond, the Surety Bond Coverage is automatically reduced to the extent of each payment made by the Insurer under the terms of the Surety Bond and the Obligor is required to reimburse the Insurer for any draws under the Surety Bond with interest at a market rate. Upon such reimbursement, the Surety Bond is reinstated to the extent of each principal reimbursement up to but not exceeding the Surety Bond Coverage. The reimbursement obligation of the Obligor is subordinate to the Obligor's obligations with respect to the Series 2006 Certificates.

In the event the amount on deposit, or credited to the Certificate Reserve Fund with respect to the Series 2006 Certificates, exceeds the amount of the Surety Bond, any draw on the Surety Bond shall be made only after all the funds in the Certificate Service Reserve Fund with respect to the Series 2006 Certificates have been expended. In the event that the amount on deposit in, or credited to, the Certificate Reserve Fund with respect to the Series 2006 Certificates, in addition to the amount available under the Surety Bond, includes amounts available under a letter of credit, insurance policy, Surety Bond or other such funding instrument (the "Additional Funding Instrument"), draws on the Surety Bond and the Additional Funding Instrument shall be made on a pro rata basis to fund the insufficiency. The Trust Agreement provides that the Certificate Reserve Fund shall be replenished in the following priority: (i) principal and interest on the Surety Bond and on the Additional Funding Instrument shall be paid from first available Base Rental Payments on a pro rata basis and (ii) after all such amounts are paid in full, amounts necessary to fund the Certificate Reserve Fund to the required level, after taking into account the amounts available under the Surety Bond shall be deposited from next available Base Rental Payments.

The Surety Bond does not insure against nonpayment caused by the insolvency or negligence of the Trustee.

In the event that the Insurer were to become insolvent, any claims arising under the Surety Bond would be excluded from coverage by the California Insurance Guaranty Association, established pursuant to the laws of the State of California.

Insurance

The Subleases provides that the County will secure and maintain, or cause to be secured and maintained, insurance against the risks and in the amounts set forth in the Subleases. Such insurance includes "all risk" insurance against loss or damage to the Project Property or the Refunding Property, as applicable, which must be maintained at any time in an amount per occurrence (the "Per Occurrence Amount") at least equal to the lesser of (1) the cumulative replacement values of the Project Property or the Refunding Property, as applicable, and, in the case of a policy covering more than the Project Property or the Refunding Property, as applicable, as permitted by the Subleases, any other property which is the subject of a lease, installment purchase agreement or other financing arrangement for which bonds, certificates of participation or other obligations shall have been issued or (2) the aggregate amount of the principal component of the then-remaining Base Rental Payments under the Project Sublease or the Refunding Sublease, as applicable. This insurance may include a deductible clause providing for a deductible not to exceed $100,000 for any one loss (except for flood, in which case the deductible may not exceed $250,000 for any one loss). With respect to the Project, the foregoing insurance provisions apply from and after the completion of the Project. The County may obtain such "all risk" coverage as a joint insured with one or more other public agencies located within or outside of the County which may be limited in an amount per occurrence in the aggregate for insureds in amount at least equal to the Per Occurrence Amount and which may be limited in a cumulative amount of claims during a 12-month period in the aggregate for all insureds in an amount not less than $500,000,000. The County anticipates that it will secure and maintain "all risk" insurance covering the Project Property and the Refunding Property through an insurance policy described in the immediately preceding sentence. As a consequence, Project Property and the Refunding the Property will not be covered through stand-alone insurance policies and will rather be covered through an insurance policy that covers multiple properties owned by varying public agencies throughout the State. If there occurs one or more losses or damages to the properties covered by that insurance policy in a fiscal year that exceeds the annual cumulative limit provided therein and there were also to occur a loss or damage to the Project Property or the Refunding Property in the same fiscal year, then the County and the Trustee may be unable to make a claim under such insurance policy for such loss or damage and there may not otherwise be any other insurance covering such loss or damage to the Project Property or the Refunding Property, as applicable.

The County will also obtain rental interruption insurance with respect to the Project Property or the Refunding Property, as applicable, in an amount sufficient at all times to pay the total rent payable under the Project Sublease and the Refunding Sublease, as applicable, for a period of not less than two years' of Base Rental Payments for the Project Property or the Refunding Property, as applicable.

The Subleases provide that, with consent of the Insurer, the amount of coverage required may be reduced to a smaller amount if an insurance consultant or insurance broker retained by the County provides written advice to the Trustee that, based upon its evaluation of the County's maximum foreseeable loss in the event of a major conflagration, windstorm, explosion, riot flood or similar event, a specified smaller amount is believed to be reasonable given the nature of the risks insured and the proximity of the insured properties to each other. The County is under no obligation to provide insurance against loss or damage occasioned by the perils of earthquake. **Under the Project Sublease, the County is under no obligation to secure or maintain any insurance policies covering the risks described above until the Certificate of Completion has been delivered to the Trustee.**

For additional information regarding the County's risk management programs, see Appendix A - "County of San Diego Financial, Economic and Demographic Information – County Financial Information -

Risk Management" and "– Insurance Coverage Respecting Lease Obligations and Long-Term Loans" and Appendix C - "Summary of Principal Legal Documents - The Project Sublease - Maintenance; Taxes; Insurance and Other Charges - Insurance" and "- The Refunding Sublease - Maintenance; Taxes; Insurance and Other Charges - Insurance" attached hereto.

Abatement

Except to the extent of (i) amounts held by the Trustee in the Base Rental Payment Fund or the Certificate Reserve Fund with respect to the Series 2006 Certificates; (ii) amounts received in respect of rental interruption insurance; and (iii) amounts, if any, otherwise legally available to the Trustee for payments in respect of the Series 2005 Certificates, the Series 2006 Certificates or Additional Certificates, during any period in which, by reason of material damage, destruction, title defect, or condemnation, there is substantial interference with the use and possession by the County of any portion of the Project or the Refunding Property, as applicable, rental payments due under the Project Sublease or the Refunding Sublease, as applicable, will be abated to the extent that the annual fair rental value of the portion of the Project Property or Refunding Property, applicable, in respect of which there is no substantial interference is less than the annual Base Rental Payments and Additional Rental, in which case rental payments will be abated only by an amount equal to the difference. In the event the County will assign, transfer or sublease any or all of the Project Property or the Refunding Property, as applicable, or other rights under the Project Sublease or the Refunding Sublease, as applicable, as permitted by the Project Sublease or the Refunding Sublease, as applicable, for purposes of determining the fair rental value available to pay Base Rental Payments and Additional Rental, annual fair rental value of the Project Property or the Refunding Property, as applicable, will first be allocated to the Project Sublease, or the Refunding Sublease, as applicable, as provided in the Project Sublease or the Refunding Sublease, as applicable. Any abatement of rental payments will not be considered an Event of Default under the Project Sublease or the Refunding Sublease, as applicable. Such abatement will continue for the period commencing with the date of such damage, destruction, title defect or condemnation and ending with the substantial completion of the work of repair or replacement of the portions of the Project Property or the Refunding Property, as applicable, so damaged, destroyed, rendered defective or condemned.

In the event that rental is abated, in whole or in part, pursuant to the Project Sublease or the Refunding Sublease, as applicable, due to damage, destruction, title defect or condemnation of any part of the Project Property or the Refunding Property, as applicable, and the County is unable to repair, replace or rebuild either of the Project Property or the Refunding Property, as applicable, from the proceeds of insurance, if any, the County agrees to apply for and to use its best efforts to obtain any appropriate state and/or federal disaster relief to obtain funds to repair, replace or rebuild the Project Property or the Refunding Property, as applicable.

Substitution

The County may amend the Subleases to substitute other real property and/or improvements (the "Substituted Property") for any of the existing Properties and/or to remove real property (including undivided interests therein) and/or improvements from the definition of Project Property or Refunding Property, as applicable, and upon compliance with all of the conditions set forth in the Project Sublease or the Refunding Sublease, as applicable. After a Substitution or Removal, the part of the Project Property or Refunding Property, as applicable, for which the Substitution or Removal has been effected shall be released from the leasehold created under the Project Sublease or the Refunding Sublease, as applicable. See Appendix C - "Summary of Principal Legal Documents – The Project Sublease – The Project Property – Substitution or Removal of Project Property" and "– The Refunding Sublease – The Refunding Property – Substitution or Removal of the Refunding Property" attached hereto.

Additional Certificates

In addition to the Series 2005 Certificates and the Series 2006 Certificates, the County, the Corporation and the Trustee may, by execution of a Supplemental Trust Agreement without the consent of the Owners, but with the consent of the Insurer (which consent will not be unreasonably withheld) provide for the execution and delivery of Additional Certificates representing additional Base Rental Payments. The Trustee may execute and deliver to or upon the request of the County such Additional Certificates, in such principal amount as shall reflect the additional principal components and interest components of the Base Rental Payments, and the proceeds of such Additional Certificates may be applied to any lawful purposes of the County or the Corporation, but such Additional Certificates may only be executed and delivered upon compliance by the County with the provisions set forth in the Trust Agreement and subject to the specific conditions set forth in the Trust Agreement, which are made conditions precedent to the execution and delivery of any such Additional Certificates, including, but not limited to, prior to or concurrently with the execution and delivery of the either the Project Lease and the Project Sublease or the Refunding Lease and the Refunding Sublease, providing for an increase in the Base Rental Payments to be made thereunder subject to the limitations set forth therein. See Appendix C - "Summary of Principal Legal Documents – Trust Agreement – Additional Certificates" attached hereto.

CERTIFICATE INSURANCE

The following information has been furnished by the Insurer for use in this Official Statement. The County and the Underwriters cannot and do not make any representation as to the accuracy or completeness of such information or the absence of material adverse changes in such information subsequent to the date hereof. Reference is made to Appendix F for a specimen of the Financial Guaranty Insurance Policy attached hereto.

Payment Pursuant to Financial Guaranty Insurance Policy

The Insurer has made a commitment to issue the Financial Guaranty Insurance Policy relating to the Series 2006 Certificates, effective as of the date of execution and delivery of the Series 2006 Certificates. Under the terms of the Financial Guaranty Insurance Policy, the Insurer will pay to The Bank of New York, in New York, New York, or any successor thereto (the "Insurance Trustee"), that portion of the principal of and interest on the Series 2006 Certificates that shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Obligor (as such terms are defined in the Financial Guaranty Insurance Policy). The Insurer will make such payments to the Insurance Trustee on the later of the date on which such principal and/or interest becomes Due for Payment or within one business day following the date on which the Insurer shall have received notice of Nonpayment from the Trustee. The insurance will extend for the term of the Series 2006 Certificates and, once issued, cannot be canceled by the Insurer.

The Financial Guaranty Insurance Policy will insure payment only on stated maturity dates and on mandatory sinking fund installment dates, in the case of principal, and on stated dates for payment, in the case of interest. If the Series 2006 Certificates become subject to mandatory redemption and insufficient funds are available for redemption of all outstanding Series 2006 Certificates, the Insurer will remain obligated to pay the principal of and interest on outstanding Series 2006 Certificates on the originally scheduled interest and principal payment dates, including mandatory sinking fund redemption dates. In the event of any acceleration of the principal of the Series 2006 Certificates, the insured payments will be made at such times and in such amounts as would have been made had there not been an acceleration, except to the extent that the Insurer elects, in its sole discretion, to pay all or a portion of the accelerated principal and interest accrued thereon to the date of acceleration (to the extent unpaid by the Obligor). Upon payment of all such accelerated principal and interest accrued to the acceleration date, the Insurer's obligations under the Financial Guaranty Insurance Policy shall be fully discharged.

In the event the Trustee has notice that any payment of principal of or interest on a Series 2006 Certificate that has become Due for Payment and that is made to a holder by or on behalf of the Obligor has been deemed a preferential transfer and theretofore recovered from its registered owner pursuant to the United States Bankruptcy Code in accordance with a final, non-appealable order of a court of competent jurisdiction, such registered owner will be entitled to payment from the Insurer to the extent of such recovery if sufficient funds are not otherwise available.

The Financial Guaranty Insurance Policy does **not** insure any risk other than Nonpayment (as set forth in the Financial Guaranty Insurance Policy). Specifically, the Financial Guaranty Insurance Policy does **not** cover:

1. payment on acceleration, as a result of a call for redemption (other than mandatory sinking fund redemption) or as a result of any other advancement of maturity;

2. payment of any redemption, prepayment or acceleration premium; and

3. nonpayment of principal or interest caused by the insolvency or negligence of the Trustee, Paying Agent or Bond Registrar, if any.

If it becomes necessary to call upon the Financial Guaranty Insurance Policy, payment of principal requires surrender of the Series 2006 Certificates to the Insurance Trustee together with an appropriate instrument of assignment so as to permit ownership of such Series 2006 Certificates to be registered in the name of the Insurer to the extent of the payment under the Financial Guaranty Insurance Policy. Payment of interest pursuant to the Financial Guaranty Insurance Policy requires proof of holder entitlement to interest payments and an appropriate assignment of the holder's right to payment to the Insurer.

Upon payment of the insurance benefits, the Insurer will become the owner of the Series 2006 Certificate, appurtenant coupon, if any, or right to payment of the principal of or interest on such Series 2006 Certificate and will be fully subrogated to the surrendering holder's rights to payment.

In the event that the Insurer were to become insolvent, any claims arising under the Financial Guaranty Insurance Policy would be excluded from coverage by the California Insurance Guaranty Association, established pursuant to the laws of the State of California.

Ambac Assurance Corporation

The Insurer is a Wisconsin-domiciled stock insurance corporation regulated by the Office of the Commissioner of Insurance of the State of Wisconsin, and is licensed to do business in 50 states, the District of Columbia, the Territory of Guam, the Commonwealth of Puerto Rico and the U.S. Virgin Islands, with admitted assets of approximately **$9,699,000,000** (unaudited) and statutory capital of approximately **$6,223,000,000** (unaudited) as of **September 30, 2006**. Statutory capital consists of the Insurer's policyholders' surplus and statutory contingency reserve. Standard & Poor's Ratings Services, a division of The McGraw-Hill Companies, Inc., Moody's Investors Service, Inc. and Fitch Ratings have each assigned a triple-A financial strength rating to the Insurer.

The Insurer has obtained a ruling from the Internal Revenue Service to the effect that the insuring of an obligation by the Insurer will not affect the treatment for federal income tax purposes of interest on such obligation and that insurance proceeds representing maturing interest paid by the Insurer under policy provisions substantially identical to those contained in the Financial Guaranty Insurance Policy shall be treated for federal income tax purposes in the same manner as if such payments were made by the Obligor. No representation is made by the Insurer regarding the federal income tax treatment of payments that are

made by the Insurer under the terms of the Financial Guaranty Insurance Policy due to non-appropriation of funds by the Lessee.

The Insurer makes no representation regarding the Series 2006 Certificates or the advisability of investing in the Series 2006 Certificates and makes no representation regarding, nor has it participated in the preparation of, this Official Statement other than the information supplied by the Insurer and presented under the heading "Certificate Insurance".

Available Information

The parent company of the Insurer, Ambac Financial Group, Inc. (the "Company"), is subject to the informational requirements of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and in accordance therewith files reports, proxy statements and other information with the Securities and Exchange Commission (the "SEC"). These reports, proxy statements and other information can be read and copied at the SEC's public reference room at 100 F Street, N.E., Room 1580, Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the public reference room. The SEC maintains an internet site at http://www.sec.gov that contains reports, proxy and information statements and other information regarding companies that file electronically with the SEC, including the Company. These reports, proxy statements and other information can also be read at the offices of the New York Stock Exchange, Inc., 20 Broad Street, New York, New York 10005.

Copies of the Insurer's financial statements prepared in accordance with statutory accounting standards are available from the Insurer. The address of the Insurer's administrative offices is One State Street Plaza, 19th Floor, New York, New York 10004, and its telephone number is (212) 668-0340.

Incorporation of Certain Documents by Reference

The following documents filed by the Company with the SEC (File No. 1-10777) are incorporated by reference in this Official Statement:

1. The Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2005 and filed on March 13, 2006;

2. The Company's Current Report on Form 8-K dated and filed on April 26, 2006;

3. The Company's Quarterly Report on Form 10-Q for the fiscal quarterly period ended March 31, 2006 and filed on May 10, 2006;

4. The Company's Current Report on Form 8-K dated July 25, 2006 and filed on July 26, 2006;

5. The Company's Current Report on Form 8-K dated and filed on July 26, 2006; and

6. The Company's Quarterly Report on Form 10-Q for the fiscal quarterly period ended June 30, 2006 and filed on August 9, 2006.

7. The Company's Current Report on Form 8-K dated and filed on October 25, 2006; and

8. The Company's Quarterly Report on Form 10-Q for the fiscal quarterly period ended September 30, 2006 and filed on November 8, 2006.

All documents subsequently filed by the Company pursuant to the requirements of the Exchange Act after the date of this Official Statement will be available for inspection in the same manner as described above in **"Available Information"**.

THE CORPORATION

The Corporation was organized on June 12, 1984, as a nonprofit public benefit corporation pursuant to the Nonprofit Public Corporation Law of the State of California. The Corporation's purpose is to render assistance to the County in its acquisition of Property, real property and improvements on behalf of the County. Under its articles of incorporation, the Corporation has all powers conferred upon nonprofit public benefit corporations by the laws of the State of California, provided that it will not engage in any activity other than that which is necessary or convenient for, or incidental to the purposes for which it was formed. The Corporation has no taxing authority. The Corporation has no liability to the Owners of the Series 2006 Certificates and has pledged none of its moneys, funds or assets toward the Base Rental Payments or Additional Rental under the Subleases, or toward the payment of any amount due in connection with the Series 2006 Certificates.

The Corporation is a separate legal entity from the County. It is governed by a five-member Board of Directors (the "Board of Directors") appointed by the Board of Supervisors of the County. The Corporation has no employees. All staff work is performed by employees of the County. The members of the Corporation's Board of Directors are Michel Anderson, Timothy Considine, Jeff Kane, Barry I. Newman and David Devol.

The County's Chief Financial Officer, Treasurer-Tax Collector, the County Counsel, and other County employees are available to provide staff support to the Corporation.

The Corporation has not entered into any material financing arrangements with respect to the Series 2006 Certificates other than those referred to in this Official Statement. Further information concerning the Corporation may be obtained from the San Diego County Capital Asset Leasing Corporation office at 1600 Pacific Highway, Room 166, San Diego, California 92101.

RISK FACTORS

The following factors, along with all other information in this Official Statement, should be considered by potential investors in evaluating the Series 2006 Certificates.

Not a Pledge of Taxes

The obligation of the County to pay the Base Rental Payments or Additional Rental does not constitute an obligation of the County for which the County is obligated to levy or pledge any form of taxation or for which the County has levied or pledged any form of taxation. The obligation of the County to pay Base Rental Payments or Additional Rental does not constitute a debt or indebtedness of the County, the State of California or any of its political subdivisions within the meaning of any constitutional or statutory debt limitation or restriction.

Although the Subleases do not create a pledge, lien or encumbrance upon the funds of the County, the County is obligated under the Subleases to pay Base Rental Payments from any source of legally available funds (subject to certain exceptions) and the County has covenanted in the Subleases that, for as long as the Properties are available for its use and possession, it will make the necessary annual appropriations within its budget for all Base Rental Payments. The County is currently liable on other obligations payable from general revenues.

Additional Obligations of the County

The County has the capability to enter into other obligations which may constitute additional charges against its revenues. To the extent that additional obligations are incurred by the County, the funds available to make Base Rental Payments may be decreased.

The Base Rental Payments and other payments due under the Subleases (including payment of costs of repair and maintenance of the Properties, taxes and other governmental charges levied against the Properties) are payable from funds lawfully available to the County. In the event that the amounts which the County is obligated to pay in a fiscal year exceed the County's revenues for such year, the County may choose to make some payments rather than making other payments, including Base Rental Payments, based on the perceived needs of the County. The same result could occur if, because of California Constitutional limits on expenditures, the County is not permitted to appropriate and spend all of its available revenues.

Default; Remedies Upon Default; No Right of Relet

Upon the occurrence of an Event of Default under the Project Sublease or the Refunding Sublease, the Trustee must thereafter maintain the Project Sublease or the Refunding Sublease, as applicable, in full force and effect and may only recover rent and other monetary charges as they become due, all without terminating the County's right to possession of the Project Property or the Refunding Property, as applicable, regardless of whether or not the County has abandoned the Project Property or the Refunding Property, as applicable; THIS IS THE SOLE AND EXCLUSIVE REMEDY AVAILABLE AGAINST THE COUNTY UNDER THE SUBLEASES OR OTHERWISE IN THE EVENT OF A DEFAULT UNDER THE PROJECT SUBLEASES. There is no remedy of acceleration of the total Base Rental Payments due over the term of the Subleases, nor is the Trustee empowered to sell the Project Property or the Refunding Property, as applicable, and use the proceeds of such sale to prepay the Series 2005 Certificates and the Series 2006 Certificates or pay debt service thereon. The County shall remain liable and agrees to keep or perform all covenants and conditions contained in the Subleases to be kept or performed by the County and, to pay the rent to the end of the term of the Subleases and further agrees to pay such rent and/or rent deficiency punctually at the same time and in the same manner as provided in the Subleases for the payment of rent hereunder (without acceleration). The Trustee would be required to seek a separate judgment each year for that year's defaulted Base Rental Payments. Any such suit for money damages would be subject to limitations on legal remedies against counties in the State, including a limitation on enforcement of judgments against funds of a fiscal year other than the fiscal year in which the Base Rental Payments were due and against funds needed to serve the public welfare and interest.

Limitations on Remedies

The rights of the Owners of the Series 2006 Certificates are subject to the limitations on legal remedies against counties in the State, including a limitation on enforcement of judgments against funds needed to serve the public welfare and interest. Additionally, enforceability of the rights and remedies of the owners of the Series 2006 Certificates, and the obligations incurred by the County, may become subject to the federal bankruptcy code and applicable bankruptcy, insolvency, reorganization, moratorium, or similar laws relating to or affecting the enforcement of creditors' rights generally, now or hereafter in effect, equity principles which may limit the specific enforcement under State law of certain remedies, the exercise by the United States of America of the powers delegated to it by the Constitution, the reasonable and necessary exercise, in certain exceptional situations, of the police powers inherent in the sovereignty of the State and its governmental bodies in the interest of serving a significant and legitimate public purpose and the limitations on remedies against counties in the State. Bankruptcy proceedings, or the exercise of powers by the federal or State government, if initiated, could subject the owners of the Series 2006 Certificates to judicial discretion

and interpretation of their rights in bankruptcy or otherwise, and consequently may entail risks of delay, limitation, or modification of their rights.

Under Chapter 9 of the Bankruptcy Code (Title 11, United States Code) (the "Bankruptcy Code"), which governs the bankruptcy proceedings for public agencies such as the County, there are no involuntary petitions in bankruptcy. If the County were to file a petition under Chapter 9 of the Bankruptcy Code, the owners of the Series 2006 Certificates could be prohibited from taking certain steps to enforce their rights under the Trust Agreement. In a decision dated March 8, 1995, the United States Bankruptcy Court for the Central District of California ruled that a pledge granted by Orange County pursuant to a resolution adopted by that county in connection with the issuance of tax and revenue anticipation notes ("TRANs") was not effective with respect to general revenues accruing to the County after the filing of a petition in bankruptcy. The resolution obligated Orange County to set aside a specified amount of revenues in certain months in order to secure the payment of its TRANs. On July 12, 1995, the United States District Court for the Central District of California reversed the order of the Bankruptcy Court and held that the obligation created under the resolution adopted by Orange County is a statutory lien which survived the filing of Orange County's bankruptcy petition.

On January 24, 1996, the United States Bankruptcy Court for the Central District of California held in the case of *County of Orange v. Merrill Lynch* that a State statute providing for a priority of distribution of property held in trust conflicted with, and was preempted by, federal bankruptcy law. In that case, the court addressed the priority of the disposition of moneys held in a county investment pool upon bankruptcy of the county, but was not required to directly address the state statute that provides for the lien in favor of holders of tax and revenue anticipation notes. The County may invest, and direct the Trustee to invest, amounts held in the Certificate Reserve Fund, the Base Rental Payment Fund and the Administrative Expense Fund in the Treasury Pool, which amounts are pledged to repay the Series 2006 Certificates. In the event of a petition for the adjustment of County debts under Chapter 9 of the Bankruptcy Code, a court might hold that the Owners of the Series 2006 Certificates do not have a valid and/or prior lien on the Base Rental Payments where such amounts are deposited in the Treasury Pool and may not provide the Owners of the Series 2006 Certificates with a priority interest in such amounts. In that circumstance, unless the Owners could "trace" the funds that have been deposited in the Treasury Pool, the owners would be unsecured (rather than secured) creditors of the County. There can be no assurance that the Owners could successfully so "trace" the pledged taxes and other revenues.

Risk of Further Delay in Completion of the Project

The Project was originally scheduled to be substantially completed by October 2006 and was expected to cost approximately $83.8 million. The Project is currently scheduled to be substantially completed by August 2008 and is expected to cost approximately $118.8 million. The County has experienced various delays and certain additional, unanticipated costs as described herein. The County has no obligation to pay Base Rental Payments under the Project Sublease until the Project is substantially completed. A portion of the proceeds of the Series 2006 Certificates will be set aside and used to pay Capitalized Base Rental Payments through March 1, 2009. If completion of the Project is delayed beyond March 1, 2009, the date through which capitalized interest is funded, Base Rental Payments due under the Project Sublease would not be payable by the County except from funds in the Certificate Reserve Fund.

Until the Project is substantially completed, the County's obligation to pay Base Rental Payments under the Project Sublease will be limited solely to Capitalized Base Rental Payments and, when such Capitalized Base Rental Payments are no longer available, the Certificate Reserve Fund. Thus, if the Contractor delivers the Project to the County later than March 1, 2009, there could be an interruption of Base Rental Payments under the Project Sublease and consequently the payment of principal and interest on the Series 2006 Certificates. If the delay results from a circumstance in which the Contractor is excused from

performance and the Contractor is entitled to an adjustment of the Contract sum, there can be no assurance that the County will have available resources to pay the adjusted Contract sum or that accordingly the Project will be completed. See "The Project Property and the Project – The Project – The Contractor; Construction Contract" herein. If the delay results from an event for which the Contractor has no excuse under the Construction Contract, such as a force majeure event or a change in the Construction Contract requested by the County or as a result of Federal, State or local agency review, approval, licensing, commissioning or inspection requirements, the Contractor may be liable for liquidated damages in an amount that the County estimates will be sufficient to pay Base Rental Payments under the Project Sublease until the Project is substantially completed. No assurances can be given that the Contractor will make such payments of liquidated damages or that, if the Contractor does make such payments, that they will be in an amount sufficient to pay Base Rental Payments under the Project Sublease. However, if the delay is a result of an event for which the Contractor has an excuse under the Construction Contract, such as a force majeure event, then the Contractor will not be liable under the Construction Contract to pay any liquidated damages. If the Contractor is excused from a delay under the Construction Contract only amounts in the Certificate Reserve Fund would be available after March 1, 2009 to pay Base Rental Payments under the Project Sublease. The County has no obligation to make Base Rental Payments under the Project Sublease from any other source in such circumstance. See "The Project Property and the Project" herein.

Abatement

Except to the extent of (i) amounts held by the Trustee in the Base Rental Payment Fund or the Certificate Reserve Fund, (ii) amounts received in respect of rental interruption insurance, and (iii) amounts, if any, otherwise legally available to the Trustee for payments in respect of the Series 2006 Certificates or Additional Certificates, during any period in which, by reason of material damage, destruction, title defect, or condemnation, there is substantial interference with the use and possession by the County of any portion of the Project Property or the Refunding Property, as applicable, rental payments due under the Project Sublease or the Refunding Sublease, as applicable, shall be abated to the extent that the annual fair rental value of the portion of the Project Property or the Refunding Property, as applicable, in respect of which there is no substantial interference is less than the annual Base Rental Payments and Additional Rental, in which case rental payments shall be abated only by an amount equal to the difference. Any abatement of rental payments shall not be considered an Event of Default under the Project Sublease or the Refunding Sublease, as applicable. Such abatement will continue for the period commencing with the date of such damage, destruction, title defect or condemnation and ending with the substantial completion of the work of repair or replacement of the portions of the Project Property or the Refunding Property, as applicable, so damaged, destroyed, rendered defective or condemned.

Seismic Events; Force Majeure

The Properties are located within a seismically active area, and damage from an earthquake could be substantial. There is no builders risk insurance for losses relating to earthquakes during construction of the Project. Further, the County is not obligated under the Subleases to procure and maintain, or cause to be procured and maintained, earthquake insurance on the Properties and no assurance can be made that the County will procure and maintain, or cause to be procured and maintained, such insurance. There can be no assurance that earthquake insurance on the Properties, if any, can be renewed or will be maintained by the County in the future, or will be available to pay Base Rental Payments or debt service on the Series 2006 Certificates. If there is no earthquake insurance on the Properties are damaged in an earthquake, the Base Rental Payments would be subject to abatement. See "Risk Factors – Abatement" herein.

Operation of the Project may also be at risk from other events of force majeure, such as damaging storms, floods, fires and explosions, strikes, sabotage, riots and spills of hazardous substances, among other events. The County cannot predict what force majeure events may occur in the future. The County does not

presently anticipate any impact on the availability of materials for the Project as a result of the recent tsunami in the Indian Ocean. For additional information regarding the County's risk management programs, see Appendix A – "County of San Diego Financial, Economic and Demographic Information – County Financial Information – Risk Management" and Appendix C – "Summary of Principal Legal Documents – The Project Sublease – Maintenance; Taxes; Insurance and Other Charges – Insurance" attached hereto.

TAX MATTERS

In the opinion of Orrick, Herrington & Sutcliffe LLP, ("Special Counsel"), special counsel to the County, based upon an analysis of existing laws, regulations, rulings and court decisions, and assuming, among other matters, the accuracy of certain representations and compliance with certain covenants, interest evidenced by the Series 2006 Certificates is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986 (the "Code") and is exempt from State of California personal income taxes. Special Counsel is of the further opinion that interest evidenced by the Series 2006 Certificates is not a specific preference item for purposes of the federal individual or corporate alternative minimum taxes, although Special Counsel observes that such interest is included in adjusted current earnings when calculating corporate alternative minimum taxable income. A complete copy of the proposed form of opinion of Special Counsel is set forth in Appendix E hereto.

To the extent the issue price of any maturity of the Series 2006 Certificates is less than the amount to be paid at maturity of such Series 2006 Certificates (excluding amounts stated to be interest and payable at least annually over the term of such Series 2006 Certificates), the difference constitutes "original issue discount," the accrual of which, to the extent properly allocable to each Beneficial Owner thereof, is treated as interest evidenced by the Series 2006 Certificates which is excluded from gross income for federal income tax purposes and State of California personal income taxes. For this purpose, the issue price of a particular maturity of the Series 2006 Certificates is the first price at which a substantial amount of such maturity of the Series 2006 Certificates is sold to the public (excluding bond houses, brokers, or similar persons or organizations acting in the capacity of underwriters, placement agents or wholesalers). The original issue discount with respect to any maturity of the Series 2006 Certificates accrues daily over the term to maturity of such Series 2006 Certificates on the basis of a constant interest rate compounded semiannually (with straight-line interpolations between compounding dates). The accruing original issue discount is added to the adjusted basis of such Series 2006 Certificates to determine taxable gain or loss upon disposition (including sale, prepayment, or payment on maturity) of such Series 2006 Certificates. Beneficial Owners of the Series 2006 Certificates should consult their own tax advisors with respect to the tax consequences of ownership of Series 2006 Certificates with original issue discount, including the treatment of Beneficial Owners who do not purchase such Series 2006 Certificates in the original offering to the public at the first price at which a substantial amount of such Series 2006 Certificates is sold to the public.

Series 2006 Certificates purchased, whether at original execution and delivery or otherwise, for an amount higher than their principal evidenced thereby payable at maturity (or, in some cases, at their earlier prepayment date) ("Premium Certificates") will be treated as having amortizable premium. No deduction is allowable for the amortizable premium in the case of obligations, like those evidenced by the Premium Certificate, the interest with respect to which is excluded from gross income for federal income tax purposes. However, the amount of tax-exempt interest received, and a Beneficial Owner's basis in a Premium Certificates, will be reduced by the amount of amortizable premium properly allocable to such Beneficial Owner. Beneficial Owners of Premium Certificates should consult their own tax advisors with respect to the proper treatment of amortizable premium in their particular circumstances.

The Code imposes various restrictions, conditions and requirements relating to the exclusion from gross income for federal income tax purposes of interest evidenced by obligations such as the Series 2006 Certificates. The County has made certain representations and covenanted to comply with certain restrictions,

conditions and requirements designed to ensure that interest evidenced by the Series 2006 Certificates will not be included in federal gross income. Inaccuracy of these representations or failure to comply with these covenants may result in interest evidenced by the Series 2006 Certificates being included in gross income for federal income tax purposes, possibly from the date of original execution and delivery of the Series 2006 Certificates. The opinion of Special Counsel assumes the accuracy of these representations and compliance with these covenants. Special Counsel has not undertaken to determine (or to inform any person) whether any actions taken (or not taken), or events occurring (or not occurring), or any other matters coming to Special Counsel's attention after the date of execution and delivery of the Series 2006 Certificates may adversely affect the value of, or the tax status of interest evidenced by, the Series 2006 Certificates.

Certain requirements and procedures contained or referred to in the Trust Agreement, the Project Sublease, the Tax Certificate to be entered into by the County on the date of execution and delivery of the Series 2006 Certificates, and other relevant documents may be changed and certain actions (including, without limitation, prepayment of the Series 2006 Certificates) may be taken or omitted under the circumstances and subject to the terms and conditions set forth in such documents. Special Counsel expresses no opinion as to any Series 2006 Certificate or the interest thereon if any such change occurs or action is taken or omitted upon the advice or approval of special counsel other than Orrick, Herrington & Sutcliffe LLP.

Although Special Counsel is of the opinion that interest evidenced by the Series 2006 Certificates is excluded from gross income for federal income tax purposes and is exempt from State of California personal income taxes, the ownership or disposition of, or the accrual or receipt of interest evidenced by, the Series 2006 Certificates may otherwise affect a Beneficial Owner's federal, state or local tax liability. The nature and extent of these other tax consequences depend upon the particular tax status of the Beneficial Owner or the Beneficial Owner's other items of income or deduction. Special Counsel expresses no opinion regarding any such other tax consequences.

Future legislation, if enacted into law, or clarification of the Code may cause interest evidenced by the Series 2006 Certificates to be subject, directly or indirectly, to federal income taxation, or otherwise prevent Beneficial Owners from realizing the full current benefit of the tax status of such interest. The introduction or enactment of any such future legislation or clarification of the Code may also affect the marker price for, or marketability of, the Series 2006 Certificates. Prospective purchasers of the Series 2006 Certificates should consult their own tax advisers regarding any pending or proposed federal tax legislation, as to which Special Counsel expresses no opinion.

The opinion of Special Counsel is based on current legal authority, covers certain matters not directly addressed by such authorities, and represents Special Counsel's judgment as to the proper treatment of the Series 2006 Certificates for federal income tax purposes. It is not binding on the Internal Revenue Service ("IRS") or the courts. Furthermore, Special Counsel cannot give and has not given any opinion or assurance about the future activities of the County, or about the effect of future changes in the Code, the applicable regulations, the interpretation thereof or the enforcement thereof by the IRS. The County has covenanted, however, to comply with the requirements of the Code.

Special Counsel's engagement with respect to the Series 2006 Certificates ends with the execution and delivery of the Series 2006 Certificates, and, unless separately engaged, Special Counsel is not obligated to defend the County or the Beneficial Owners regarding the tax-exempt status of the Series 2006 Certificates in the event of an audit examination by the IRS. Under current procedures, parties other than the County and their appointed counsel, including the Beneficial Owners, would have little, if any, right to participate in the audit examination process. Moreover, because achieving judicial review in connection with an audit examination of tax-exempt bonds is difficult, obtaining an independent review of IRS positions with which the County legitimately disagrees may not be practicable. Any action of the IRS, including but not limited to

selection of the Series 2006 Certificates for audit, or the course or result of such audit, or an audit of obligations presenting similar tax issues may affect the market price for, or the marketability of, the Series 2006 Certificates, and may cause the County or the Beneficial Owner to incur significant expense.

CERTAIN LEGAL MATTERS

The validity of the Certificates and certain other legal matters are subject to the approval of Orrick, Herrington & Sutcliffe LLP, Special Counsel, and certain other conditions. A complete copy of the proposed form of opinion of Special Counsel is contained in Appendix E hereto. Certain legal matters will be passed upon for the Underwriters by their counsel, Hawkins Delafield & Wood LLP, Los Angeles, California and for the County by the County Counsel.

FINANCIAL STATEMENTS

The general purpose financial statements of the County for fiscal year 2004-05, pertinent sections of which are included in Appendix B to this Official Statement, have been audited by Macias Gini & Company LLP, independent certified public accountants, as stated in their report appearing in Appendix B. Macias Gini & Company LLP has not consented to the inclusion of its report as Appendix B and has not undertaken to update its report or to take any action intended or likely to elicit information concerning the accuracy, completeness or fairness of the statements made in this Official Statement, and no opinion is expressed by Macias Gini & Company LLP with respect to any event subsequent to its report dated December 19, 2005.

LITIGATION

No litigation is pending or threatened against the County or the Corporation concerning the validity of the Series 2006 Certificates. The County is not aware of any litigation pending or threatened questioning the political existence of the County or the Corporation or contesting the County's ability to execute and delivery the Series 2006 Certificates or pay the Base Rental Payments pursuant to the Project Sublease. There are a number of lawsuits and claims pending against the County. Other than as described in this section and in Appendix A, the County does not believe that any of these proceedings could have a material adverse impact upon the financial condition of the County.

RATINGS

Standard & Poor's Ratings Services, a Division of The McGraw-Hill Companies, Inc. ("S&P"), Moody's Investors Service, Inc. ("Moody's") and Fitch Ratings ("Fitch") have assigned the Series 2006 Certificates their ratings of "AAA," "Aaa" and "AAA," respectively, with the understanding that, upon the execution and delivery of the Series 2006 Certificates, the Financial Guaranty Insurance Policy will be issued by the Insurer. S&P has assigned the Series 2006 Certificates an underlying rating of "AA-," Moody's has assigned the Series 2006 Certificates an underlying rating of "A1" and Fitch has assigned the Series 2006 Certificates an underlying rating of "AA-." In addition, S&P has assigned the County a Debt Derivative Profile ("DDP") score of "1.5" S&P's DDP scale ranges from "1" to "5," with "5" representing the lowest risk and "5" representing the highest risk assigned by S&P. Such ratings reflect only the views of such organizations and explanations of the significance of such ratings may be obtained only from the organizations at: Standard and Poor's Ratings Services, 55 Water Street, New York, New York 10041, telephone number (212) 438-2000; Moody's Investors Service, Inc. 99 Church Street, New York, New York 10007-2796, telephone number (212) 553-0317. There is no assurance that such ratings will continue for any given period of time or that they will not be revised downward or withdrawn entirely by the respective rating agencies, if in the judgment of such rating agency circumstances so warrant. Any such downward revision or withdrawal of such ratings may have an adverse effect on the market price of the Series 2006 Certificates.

UNDERWRITING

The Series 2006 Certificates are being purchased by Banc of America Securities LLC, on behalf of itself and Lehman Brothers Inc. (collectively the "Underwriters"), pursuant to a Purchase Contract with the County (the "Purchase Contract"). The Underwriters have agreed, subject to certain conditions, to purchase the Series 2006 Certificates at a price of $$42,717,680.45 (representing the principal amount of the Series 2006 Certificates, plus a net original issue premium of $606,313.90, less an Underwriters' discount of $278,633.45). The Purchase Contract relating to the Series 2006 Certificates provides that the Underwriters will purchase all of the Series 2006 Certificates if any are purchased, the obligation to make such purchase being subject to certain terms and conditions set forth in the Purchase Contract, the approval of certain legal matters by counsel and certain other conditions. The Underwriters may offer and sell the Series 2006 Certificates to certain dealers and others at prices lower than the offering prices stated on the cover page. The offering prices may be changed from time to time by the Underwriters.

FINANCIAL ADVISOR

RBC Capital Markets served as the Financial Advisor to the County in connection with the execution and delivery of the Series 2006 Certificates. RBC Capital Markets is the name under which RBC Dain Rauscher Inc., a broker-dealer, conducts investment banking business.

CONTINUING DISCLOSURE

Material Events Undertaking

Pursuant to a Continuing Disclosure Agreement with the Trustee (the "Disclosure Agreement"), the County has agreed to provide, or cause to be provided, with respect to each fiscal year of the County, commencing with fiscal year 2005-06, by no later than eight months after the end of the respective fiscal year, to each Repository the audited financial statements, if available, or unaudited financial statements, and the annual financial information and operating data with respect to the County, for each fiscal year of the County, as described in Appendix A – "County of San Diego Financial, Economic and Demographic Information" attached hereto. In addition, the County has agreed to provide, or cause to be provided, to each Repository in a timely manner notice of the following "Listed Events" if determined by the County to be material: (1) principal and interest payment delinquencies; (2) non-payment related defaults; (3) unscheduled draws on the debt service reserves reflecting financial difficulties; (4) unscheduled draws on credit enhancements reflecting financial difficulties; (5) substitution of credit or liquidity providers, or their failure to perform; (6) adverse tax opinions or events affecting the tax-exempt status of the security; (7) modifications to rights of security holders; (8) bond calls; (9) defeasances; (10) release, substitution, or sale of property securing repayment of the securities; and (11) rating changes. These covenants have been made in order to assist the Underwriters in complying with Rule 15c2-12(b)(5).

Additional Information

The County agreed to provide, or cause to be provided, to each Repository annual reports, including its financial statements with respect to each fiscal year of the County, in connection with the issuance of certain of its outstanding debt obligations. The annual report for Fiscal Year 2001-02 with respect to the County's Taxable Pension Obligation Bonds, Series 2002, including financial statements, was not submitted by the required deadline. In addition, the County did not provide financial statements with respect to Fiscal Years 2001-02 and 2002-03 for its outstanding obligations which are identified in the following table when it filed its annual reports by their respective required filing dates, most of which are December 27 and the latest of which is January 26 of each year, because the County's financial statements were not available by such dates. The County filed notices of failure to provide required annual financial information as required by Rule

15c2-12 for each of these instances. The County subsequently provided to each Repository its unaudited and audited financial statements with respect to these fiscal years for these annual reports. The County has otherwise complied in all material respects in the last five years with each of its previous undertakings with regard to Rule 15c2-12 to provide annual reports or notices of material events.

Obligations for which the County Failed to Timely File Complete Annual Reports in Fiscal Years 2001-02 and 2002-03

$737,340,000 County of San Diego Taxable Pension Obligation Bonds, Series 2002
$26,060,000 Certificates of Participation (2002 Motorola Refunding)[1]
$40,000,000 Certificates of Participation (2001 MTS Tower Refunding)
$51,620,000 Certificates of Participation (2000 Information Technology System Financing)
$15,010,000 Certificates of Participation (1999 East Mesa Refunding)
$73,115,000 Certificates of Participation (1998 Downtown Courthouse Refunding)
$80,675,000 Certificates of Participation (1997 Central Jail Refunding)
$28,035,000 Certificates of Participation (1997 Master Refunding)
$37,580,000 Certificates of Participation (1996 North County Regional Center Expansion and East County Courthouse Detention Facility Conversion)
$52,230,000 Certificates of Participation (1996 Regional Communication System)
Teeter Obligation Tax-Exempt Commercial Paper Notes, Series B
$21,755,000 Reassessment District No. 97-1 (4-S Ranch) Limited Obligation Improvement Bonds
$5,100,000 Redevelopment Agency of the County of San Diego Revenue Bonds, Series 1995 (Gillespie Field Project)

[1] The continuing disclosure obligation requirement for the Annual Report for this obligation began for Fiscal Year 2002-03. Accordingly, the County was late with respect to this Annual Report only for Fiscal Year 2002-03.

MISCELLANEOUS

Included herein are brief summaries of certain documents and reports, which summaries do not purport to be complete or definitive, and reference is made to such documents and reports for full and complete statements of the contents thereof. This Official Statement is not to be construed as a contract or agreement between the County and the purchasers or owners of any of the Series 2006 Certificates. Any statements made in this Official Statement involving matters of opinion, whether or not expressly so stated, are intended merely as an opinion and not as representations of fact. The information and expressions of opinion herein are subject to change without notice and neither the delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in affairs in the County since the date hereof.

The execution and delivery of this Official Statement have been duly authorized by the County.

COUNTY OF SAN DIEGO

By: /s/ Donald F. Steuer
Chief Financial Officer

APPENDIX A

COUNTY OF SAN DIEGO FINANCIAL, ECONOMIC AND DEMOGRAPHIC INFORMATION

APPENDIX A

COUNTY OF SAN DIEGO FINANCIAL, ECONOMIC AND DEMOGRAPHIC INFORMATION

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THE COUNTY

General

The County of San Diego (the "County") is the southernmost major metropolitan area in the State of California (the "State"). The County covers 4,255 square miles, extending 70 miles along the Pacific Coast from the Mexican border to Orange County, and inland 75 miles to Imperial County. Riverside and Orange Counties form the northern boundary. The County is approximately the geographic size of the State of Connecticut. The County's Fiscal Year 2006-07 Adopted General Fund budget is $3.289 billion.

The County was incorporated on February 18, 1850, and functions under a charter adopted in 1933, as subsequently amended from time to time. The County is governed by a five-member Board of Supervisors (the "Board") elected to four-year terms in district nonpartisan elections. The Board appoints the Chief Administrative Officer and the County Counsel. The Chief Administrative Officer appoints the Chief Financial Officer and the Auditor and Controller. Elected officials include the Assessor/Recorder/County Clerk, the District Attorney, the Sheriff and the Treasurer-Tax Collector.

Many of the County's functions are required under County ordinances or by State or federal mandate. State and federally mandated programs, primarily in the social and health services areas, are directed to be maintained at certain minimum levels, which may, under some conditions, limit the County's ability to control its budget. However, under designated State and federal programs, eligible costs are subject to reimbursement according to specific guidelines.

The County is the delivery system for federal, State and local programs. The County supports a wide range of services to its residents, including, regional services such as medical examiner, jails, elections and public health; health, welfare and human services such as mental health, senior citizen and child welfare services; basic local services such as planning, parks, libraries and Sheriff's patrol to the unincorporated area, and law enforcement by contract and libraries by city's request to incorporated cities; and infrastructure such as roads, waste disposal and flood control to the unincorporated area of the County.

County of San Diego Employees

Table 1 below sets forth the number of County employees for the years 1998 through 2006:

TABLE 1

TOTAL COUNTY EMPLOYEES[1]

Year	Total Employees
1998	17,790
1999	16,390
2000	16,617
2001	17,057
2002	18,208
2003	17,835
2004	16,949
2005	16,418
2006	16,195

Source: The County.
(1) Excludes temporary employees of the County.

County employees are represented by eight unions representing 24 bargaining units. The unions represent approximately 88% of the County's approximately 16,195 employees and include the Deputy Sheriffs' Association of San Diego County; Social Services Union, SEIU, Local 535, CLC; Deputy District Attorneys Association; San Diego County Probation Officers' Association SEIU, Local 2028, CLC; District Attorney Investigators Association; the Service Employees International Union, Local 2028, CLC; San Diego Deputy County Counsels Association; and the Public Defender Association of San Diego County.

The County has negotiated new labor agreements, effective June 23, 2006 through June 18, 2009, with the Social Services Union, SEIU, Local 535, CLC; San Diego County Probation Officers' Association SEIU, Local 2028, CLC; Service Employees International Union, Local 2028, CLC; San Diego Deputy County Counsels Association and the Public Defender Association of San Diego County. The County negotiated a new labor agreement, effective October 13, 2006 through June 18, 2009, with the Deputy District Attorneys Association. The Deputy Sheriffs' Association and the District Attorney Investigators Association have agreements that are effective through June 21, 2007. The remaining employees are unrepresented.

COUNTY FINANCIAL INFORMATION

The following is a summary of certain financial information with respect to the County, including the County's property tax collections, General Fund Balance Sheet and Statement of Revenues, Expenditures and Changes in Fund Balance, adopted General Fund budgets for Fiscal Years 2004-05, 2005-06 and 2006-07, pension plan, risk management program, pending litigation and outstanding indebtedness.

Assessed Valuations

The assessed valuation of property in the County is established by the County Assessor, except for public utility property which is assessed by the State Board of Equalization. Assessed valuations are

reported in compliance with the requirements of Proposition 13. Generally, property can only be reappraised to market value upon a change in ownership or completion of new construction. Pursuant to Article XIIIA of the State Constitution, the assessed value of property that has not incurred a change of ownership or new construction shall be adjusted annually to reflect inflation at a rate not to exceed 2% per year based on the California consumer price index. In the event of declining property value caused by substantial damage, destruction, economic or other factors, Article XIIIA of the State Constitution allows the assessed value to be reduced temporarily to reflect the lower market value. For the definition of full cash value and more information on property tax limitations and adjustments, see "Constitutional and Statutory Limitations on Taxes, Revenues and Appropriations – Article XIIIA" herein.

The County Assessor determines and enrolls a value for each parcel of taxable real property in the County every year. The value review may result in the reinstatement of the indexed base value after a temporary reduction or it may result in a reduction in value. Taxpayers in the County also may appeal the determination of the County Assessor with respect to the assessed value of their property. In Fiscal Year 2005-06, the County Assessor received and processed approximately 2,500 appeals.

Ad Valorem Property Taxation

Table 2 below sets forth the assessed valuation of property within the County subject to taxation for Fiscal Years 1997-98 through 2006-07:

TABLE 2

ASSESSED VALUATION OF PROPERTY
SUBJECT TO AD VALOREM TAXATION
Fiscal Years 1997-98 through 2006-07
(In Thousands)

Fiscal Year	Land	Improvements	Personal Property	Gross Assessed Valuation	Exemption[1]	Net Assessed Valuation for Tax Purposes[2]
1997-98	59,965,573	87,226,803	10,222,561	157,414,937	4,512,558	152,902,379
1998-99	63,633,576	94,172,901	10,577,494	168,383,971	4,655,381	163,728,590
1999-00	70,120,054	105,048,079	10,221,397	185,389,530	4,840,799	180,548,731
2000-01	76,745,341	112,696,091	11,598,968	201,040,400	5,322,920	195,717,480
2001-02	84,852,228	122,629,979	12,675,787	220,157,994	5,674,325	214,483,669
2002-03	93,104,455	133,459,423	11,773,210	238,337,088	5,474,711	232,862,377
2003-04	103,818,122	145,973,945	11,949,627	261,741,694	6,742,042	254,999,652
2004-05	117,332,258	159,013,240	11,804,416	288,149,914	7,332,153	280,817,761
2005-06	137,276,347	175,791,219	12,807,092	325,874,658	7,916,172	317,958,485
2006-07	158,460,301	192,889,631	13,201,802	364,551,734	8,553,542	355,998,192

Source: County of San Diego Auditor and Controller.
(1) Exemption figures include veterans, church, welfare, religious, college and cemetery exemptions.
(2) Net Assessed Valuation for Tax Purposes figures include local secured, unsecured, state unitary and redevelopment valuation.

Table 3 below sets forth the approximate tax levied against the ten largest taxpayers in the County for Fiscal Year 2006-07. These tax payments represent approximately 2.8% of the total secured property tax levied by the County for Fiscal Year 2006-07, which amount is $3,964,281,859.

TABLE 3

TEN LARGEST TAXPAYERS
Fiscal Year 2006-07

Property Owners	Business Area	Approximate Tax
San Diego Gas & Electric Company	Gas and Electric Utility	38,537,523
Southern California Edison Co.	Electric Utility	19,431,900
Irvine Co.	Real Estate	8,564,865
Qualcomm Inc.	Telecommunication	8,404,072
Kilroy Realty LP	Real Estate	8,302,918
Pacific Bell Telephone Company	Telecommunication	7,948,754
San Diego Family Housing LLC	Real Estate	5,365,592
Fashion Valley Mall LLC	Retail	5,002,506
Pfizer Inc.	Pharmaceutical	4,651,676
Sea World Inc.	Amusement	4,108,849

Source: County of San Diego Auditor and Controller.

Taxes are levied for each Fiscal Year on taxable real and personal property which is situated in the County as of the preceding January 1. However, upon a change in ownership of property or completion of new construction, State law permits an accelerated recognition and taxation of increases in real property assessed valuation. For assessment and collection purposes, property is classified either as "secured" or "unsecured" and is listed accordingly on separate assessment rolls. The "secured roll" is that assessment roll containing locally assessed property secured by a lien which is sufficient, in the opinion of the assessor, to secure payment of the taxes. Other property is assessed on the "unsecured roll."

The County levies a 1% property tax on behalf of all taxing agencies in the County. The taxes collected are allocated on the basis of a formula established by State law enacted in 1979. Under this formula, the County and all other taxing entities receive a base year allocation plus an allocation on the basis of growth in situs assessed value (new construction, change of ownership, inflation) prorated among the jurisdictions which serve the tax rate areas within which the growth occurs. Tax rate areas are specifically defined geographic areas which were developed to permit the levying of taxes for less than county-wide or less than city-wide special and school districts. In addition, the County levies and collects additional voter approved debt service and fixed charge assessments on behalf of any taxing agency and special districts within the County.

Property taxes on the secured roll are due in two installments, on November 1 and February 1. If unpaid, such taxes become delinquent after 5:00 p.m. on December 10 and April 10, respectively, and a ten percent penalty attaches. A ten dollar cost also applies to all delinquent second installments. Property on the secured roll with unpaid delinquent taxes is declared tax-defaulted after 5:00 p.m. on June 30th. Such property may thereafter be redeemed by payment of the delinquent taxes, the ten percent delinquency penalty, the ten dollar cost, a fifteen dollar per parcel redemption fee (from which the State receives five dollars), and redemption penalty of one and one half percent per month starting July 1 and continuing until date of redemption (collectively, the "Redemption Amount"). If taxes remain unpaid after five years on the default roll, the property becomes subject to a tax sale by the County Treasurer - Tax Collector.

Property taxes on the unsecured roll are due on the lien date being assessed (January 1). A Due Date, or date to pay by, is set based on the enrollment date of the bill. If not paid in full, a ten percent penalty is added to the bill on September 1st, or on the first business day of the second month following

the enrollment date and an additional penalty of one and one-half percent per month begins to accrue on November 1st, or on the first business day of the third month after the date of enrollment. Penalties are posted based on the type of Unsecured bill and the time of year it is enrolled. The taxing authority has a number of ways of collecting delinquent unsecured property taxes, which include: filing a Certificate of Tax Lien for recordation in the County Recorder's office, and/or other jurisdictions; a civil action against the taxpayer; and seizure and/or sale of assets belonging or assessed to the taxpayer.

In the 2005-06 Fiscal Year, the County collected $6,603,222 in property tax administrative fees from cities, special districts and redevelopment agencies. State law exempts school districts from paying such fees.

Secured Tax Rolls Statistics

Table 4 below sets forth information relating to the County's secured tax roll and assessed value of property for each of the last ten Fiscal Years, including an estimate for the Fiscal Year ending on June 30, 2007.

TABLE 4

SECURED TAX ROLL STATISTICS
Fiscal Years 1997-98 through 2006-07

Fiscal Year	Total Bills	Total Assessed Value[1]	Total Tax Amount[2]	Delinquent Tax Bills	Delinquent Tax Amount[3]	Delinquent Tax Amount as Percent of Total Tax Amount
1997-98	823,332	$149,611,690,276	$1,685,104,282	28,715	$31,933,378	1.90%
1998-99	831,497	160,102,387,349	1,791,871,717	33,484	32,513,581	1.60
1999-00	842,959	176,113,891,329	1,962,926,237	36,820	39,059,369	1.70
2000-01	857,777	191,194,756,333	2,126,737,380	33,817	38,805,254	1.82
2001-02	871,191	209,281,264,375	2,335,927,431	31,198	39,156,006	1.68
2002-03	885,452	227,376,419,310	2,552,212,549	29,769	39,156,463	1.53
2003-04	898,222	250,071,362,845	2,831,188,116	30,244	41,183,548	1.45
2004-05	912,850	276,651,738,142	3,141,818,961	38,065	64,556,967	2.05
2005-06	934,416	313,592,785,425	3,565,874,923	46,386	93,084,098	2.60
2006-07[4]	954,808	350,431,485,633	3,964,281,859	52,000	99,000,000	2.50

Source: County of San Diego Auditor and Controller.
(1) Total Assessed Value figures include local secured and state unitary valuation.
(2) Amount excludes penalties.
(3) Delinquent Tax Amounts represent the dollar value of tax due for delinquencies in the year shown that had not been collected as of June 30 of that year.
(4) Total Bills, Total Assessed Value and Total Tax Amount figures are actual, remaining columns are estimated.

Liens and Redemption

Properties may be redeemed under a five-year installment plan by paying current taxes plus a minimum annual payment of 20% of the original Redemption Amount. A delinquent taxpayer may enter into the installment plan at any time up to the June 30 occurring five years after the property becomes tax-defaulted. Redemption interest accrues at 1-1/2% per month on the unpaid balance of the Redemption Amount during the period of the installment plan. If taxes are unpaid after June 30 of the fifth year of default (or if an installment plan is in place, taxes are unpaid at the end of the plan), the property becomes subject to sale by the County Treasurer-Tax Collector.

Financial Statements

Table 5 below sets forth the audited General Fund Balance Sheet for Fiscal Year ended June 30, 2004 and for Fiscal Year ended June 30, 2005. Table 6 below sets forth the audited General Fund Statement of Revenues, Expenditures, and Changes in Fund Balance for Fiscal Years 2001-02 through 2004-05.

TABLE 5

COUNTY OF SAN DIEGO
GENERAL FUND BALANCE SHEET
June 30, 2004 and June 30, 2005
(In Thousands)

ASSETS	(Audited) 2004[3]	(Audited) 2005[3]
Equity in Pooled Cash and Investments	$310,870	$496,759
Cash with Fiscal Agent	10,090	43,902
Collections in Transit	7,334	5,362
Imprest Cash	299	298
Investments	2	2
Taxes Receivable, net	34,488	105,009
Accounts and Notes Receivable, net	218,662	224,527
Due from Other Funds[1]	178,321	172,209
Prepaid Items	10	5
Advances to Other Funds	948	928
Inventories of Materials and Supplies	6,941	8,795
Restricted Assets - Investments[2]	--	360,000
TOTAL ASSETS	$767,965	$1,417,796
LIABILITIES		
Accounts Payable	$ 57,300	$101,766
Accrued Payroll	57,152	55,366
Amount Due for Tax and Revenue Anticipation Notes[2]	--	369,280
Due to Other Funds[1]	24,744	21,342
Deferred Revenue[3]	77,769	--
Deferred Credits and Other Liabilities	--	44,624
Amount for Commercial Paper Notes	--	74,990
Unearned Revenue	--	82,970
TOTAL LIABILITIES	$216,965	$750,338
FUND BALANCE		
Reserved for Encumbrances	$ 84,031	$131,356
Reserved for Notes Receivable and Advances	7,555	7,295
Reserved for Inactive Landfill Closure	16,170	16,170
Reserved for Inventory of Materials and Supplies	6,941	8,795
Reserved for Other Purposes	98,595	128,216
Unreserved:		
Designated for Subsequent Years' Expenditures	122,334	111,448
Undesignated	215,374	264,178
TOTAL FUND BALANCE	$551,000	$ 667,458
TOTAL LIABILITIES AND FUND BALANCES	$767,965	$1,417,796

Source: County of San Diego Auditor and Controller.

(1) Amounts are receivables and payables between General Fund and other County funds based on actual or estimated claims outstanding.

(2) Includes the tax and revenue anticipation notes outstanding at June 30, 2004 and June 30, 2005, respectively. The tax and revenue anticipation notes for Fiscal Year 2003-04 were paid in full by June 30, 2004; no amount was outstanding as of such date. The tax and revenue anticipation notes for Fiscal Year 2004-05 matured in July 2005; the amount outstanding as of such date is reflected above. Consistent with National Council on Governmental Accounting Interpretation No. 9, the liability for tax and revenue anticipation notes outstanding at June 30 is displayed in the General Fund and offset by a corresponding asset recorded as Restricted Assets-Investments representing the pledged amounts.

(3) For Comprehensive Annual Financial Report reporting purposes to conform with Governmental Accounting Standards Board (GASB) Statements 33 and 34, activities from various Internal Agency Funds are included in the General Fund.

TABLE 6

COUNTY OF SAN DIEGO
GENERAL FUND
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE
For Fiscal Years 2001-02 through 2004-05
(In Thousands)

	(Audited) 2001-02	(Audited) 2002-03	(Audited) 2003-04	(Audited) 2004-05
Revenues:				
Taxes[1]	$ 369,199	$ 396,415	$ 457,062	$ 671,850
Licenses, Permits and Franchises	28,250	28,840	31,233	32,015
Fines, Forfeitures and Penalties	33,978	36,246	40,363	51,000
Revenue From Use of Money and Property	22,020	16,691	12,721	29,308
Aid From Other Governmental Agencies:				
State[1]	646,680	709,693	649,829	511,830
Federal	495,775	533,562	588,815	620,477
Other	43,150	49,853	57,442	60,415
Charges for Current Services	211,727	243,125	246,381	254,585
Other Revenue	37,092	25,389	32,058	38,057
Total Revenues	$1,887,871	$2,039,814	$2,115,904	$2,269,537
Expenditures:				
Current:				
General[2]	$ 148,326	$ 192,720	$ 207,600	$ 204,566
Public Protection[2]	788,698	1,123,518	1,172,110	928,375
Public Ways and Facilities[2]	3,185	21,855	23,983	4,348
Health and Sanitation[2]	524,974	569,914	552,035	499,471
Public Assistance[2]	755,737	945,562	948,165	858,487
Education[2]	473	6,649	5,798	597
Recreational and Cultural[2]	14,734	19,884	23,709	18,300
Debt service:				
Interest	5,495	12,735	5,776	12,310
Total Expenditures	$2,241,622	$2,892,837	$2,939,176	$2,544,382
Excess (Deficiency) of Revenues over (under) Expenditures	($ 353,751)	($853,023)	($ 823,272)	($ 274,845)
Other financing sources (uses):				
Sale of Capital Assets	—	$ 11	$ 7	—
Long Term Debt Proceeds[2]	—	560,450	454,113	—
Refunding Bonds Issued[2]	—	176,890	—	—
Payment to Refunded Bond Escrow Agent	—	(176,890)	—	—
Transfers In[3]	$ 465,910	$478,806	$ 483,333	$ 568,677
Transfers (Out)[4]	(159,825)	(156,879)	(162,035)	(179,228)
Total Other Financing Sources (Uses)	$ 306,085	$882,388	$ 775,418	$ 389,449
Net Change in Fund Balance	($ 47,666)	$ 29,365	($ 47,854)	$ 114,604

(Table continued from prior page.)

	(Audited) 2001-02	(Audited) 2002-03	(Audited) 2003-04	(Audited) 2004-05
Fund Balance - Beginning of Year	618,284	570,352	598,661	551,000
Residual Equity Transfers (Out)	—	—	—	—
Increase (Decrease) In:				
Reserve For Inventory of	—	—	—	—
Materials and Supplies	(266)	(1,056)	193	1,854
Fund Balance - End of Year	$570,352	$598,661	$551,000	$667,458

Source: Comprehensive Annual Financial Report of the County.

(1) The conversion of vehicle license fee revenues to property taxes in lieu of vehicle license fees resulted in a reclassification of such revenues from State aid to taxes. See "– Vehicle License Fee" herein.

(2) The respective amounts in 2002-03 reflect the issuance of the 2002 Pension Obligation Bonds and the escrow and pledge of funds for the 1994 Pension Obligation Bonds in September 2004. The respective amounts in 2003-04 reflect the issuance of 2004 Pension Obligation Bonds in June 2004. The proceeds of these Pension Obligation Bonds were deposited with the San Diego County Retirement Association and were accounted for in Fiscal Years 2002-03 and 2003-04, respectively, as having been expended by each of the seven functional areas noted based on the payrolls attributable to these functional areas.

(3) Beginning in Fiscal Year 2000-01, an accounting method change occurred creating the Special Revenue funds for the Safety Augmentation Sales Tax (Proposition 172), Health and Social Services' Realignment monies and the tobacco securitization proceeds. Revenues from these three sources are recognized in the Special Revenue funds and treated as operating transfers when moved to the General Fund to reimburse expenses incurred, and these three sources accounted for substantially all of the transfers.

(4) Represents contributions to capital funds for General Fund projects, County contributions to the library fund and other internal fund contributions.

General Fund Budget

The Board of Supervisors is required by State law to adopt a balanced annual budget no later than August 30 of each year. The County General Fund finances the legally authorized activities of the County not provided for in other restricted funds. General Fund revenues are derived from such sources as taxes, licenses, permits and franchises, fines, forfeitures and penalties, use of money and property, aid from other governmental agencies, charges for current services and other revenue. General Fund expenditures and encumbrances are classified by the functions of public safety, health and human services, land use and environment, community services, finance and general government and other. Increases in the aggregate appropriations based on actual or anticipated increases in available financing can be made after the final budget has been adopted upon approval by a four-fifths vote of the Board of Supervisors.

To ensure that the expenditures do not exceed authorized levels or available financing sources, quarterly reviews are made covering actual and projected receipts and expenditures. In the event of any shortfall in projected revenue, immediate steps are taken to freeze or reduce appropriations. Similarly, if expenditures are projected to exceed appropriations, steps are taken to freeze expenditures in other areas or to transfer available resources to offset the added expenditure requirement. California counties are not permitted by State law to impose fees to raise general revenue, but only to recover the costs of regulation or provision of services. The Chief Financial Officer is responsible for monitoring and reporting expenditures within budgeted appropriations.

2005-06 Budget and Financial Position of the County

The Fiscal Year 2005-06 Adopted Budget (the "2005-06 Adopted Budget") for the County's General Fund included expenditures of approximately $2.944 billion and revenues and other financing sources of approximately $2.944 billion. In accordance with the normal practice of the County, the 2005-06 Adopted Budget has been adjusted to reflect carry-over appropriations from the prior fiscal year and program needs not included in the 2005-06 Adopted Budget. As of March 31, 2006, the County's

Fiscal Year 2005-06 General Fund Adjusted Budget (the "2005-06 Adjusted Budget") included expenditures of $3.252 billion and revenues and other financing sources of $3.252 billion. As of March 31, 2006, as reported in the Fiscal Year 2005-06 Third Quarter Operational Plan Status Report and Budget Adjustments (the "Third Quarter Report") delivered to the Board of Supervisors from the County's Chief Administrative Officer, which was based on the first nine months of Fiscal Year 2005-06, the County projects that its General Fund expenditures for Fiscal Year 2005-06 will be below the 2005-06 Adjusted Budget by $252.5 million and its General Fund revenues and other financing sources will be below the 2005-06 Adjusted Budget by $7.1 million. The net variance is a projected savings to the County's General Fund of $245.4 million, which will be added to any remaining unreserved and undesignated General Fund Balance as of June 30, 2006.

The lower than budgeted, projected expenditures of the General Fund are primarily attributable to the following:

- Lower than budgeted salaries and employee benefit costs due to turnover in departments, controlled staffing, and ongoing recruitment challenges in select classifications;
- Savings in services and supplies due to projected savings in contracted services and the extension of certain grants;
- Savings in other charges are due to reduced caseloads and aid payments, and due to projected delays in carrying out grant funded activities;
- Savings from unspent amounts in the Contingency reserves; and
- Savings from unspent amounts in the management reserves (*i.e.*, appropriations established for revenue and economic uncertainties or to fund unanticipated items, including one-time projects, during the fiscal year).

The projected revenue under-realization to budget consists of a positive revenue variance in current property taxes, in other than current secured taxes, in revenue from use of money and property, in license permits and franchises, and in charges for current services and miscellaneous revenues combined, offset by a negative variance in all other sources of revenues (primarily in intergovernmental revenues and largely the result of expenditure savings in caseload driven programs).

Table 7 below sets forth the expenditures and revenues and other financing sources of the County's General Fund for Fiscal Year 2005-06 compared to Fiscal Year 2004-05. For Fiscal Year 2004-05, both the Adopted and final Adjusted Budgets are shown. For Fiscal Year 2005-06, the table sets forth the Adopted Budget, the Adjusted Budget as of March 31, 2006, the projected expenditures and revenues and other financing sources as reported in the Third Quarter Report, and the variance between the projected actual amounts and those contained in the 2005-06 Adjusted Budget. The table also sets forth the County's 2006-07 Adopted Budget (the "2006-07 Adopted Budget").

TABLE 7

COMPARISON OF GENERAL FUND ADOPTED AND ADJUSTED BUDGET FOR FISCAL YEAR 2004-05, ADOPTED AND ADJUSTED BUDGET AND PROJECTED RESULTS FOR FISCAL YEAR 2005-06 AND ADOPTED BUDGET FOR FISCAL YEAR 2006-07 (In Thousands)

	2004-05 Adopted Budget	2004-05 Adjusted Budget[1]	2005-06 Adopted Budget	2005-06 Adjusted Budget[2]	Projected Year End Results[3]	Variance From Adjusted Budget[4]	2006-07 Adopted Budget[5]
EXPENDITURES							
Public Safety	$ 944,105	$ 997,409	$ 972,205	$1,027,770	$ 990,158	$ 37,612	$ 1,053,618
Health and Human Services	1,432,507	1,460,726	1,481,763	1,522,843	1,407,122	115,721	1,581,047
Land Use and Environment	127,505	171,676	130,557	183,053	163,028	20,025	154,858
Community Services	37,624	77,757	43,124	85,902	78,127	7,775	48,964
Finance and General Government and Other	309,627	451,434	300,638	416,591	360,770	55,821	430,986
Contingency Reserve and Designations	18,200	15,600	15,600	15,600	0	15,600	20,000
Total Expenditures[6]	$2,869,568	$3,174,602	$2,943,886	$3,251,758	$2,999,204	$252,554	$3,289,473
REVENUES							
Current Property Taxes	$ 561,626	$ 359,553	$ 400,483	$ 400,483	$ 429,090	$ 28,607	$ 499,278
Taxes Other Than Current Property Taxes	56,150	258,223	272,987	277,187	348,613	71,426	357,482
Licenses, Permits and Franchises	31,876	31,876	32,081	32,081	32,115	34	34,361
Fines, Forfeitures and Penalties	44,186	53,789	52,236	55,343	52,670	(2,673)	49,942
Use of Money and Property	20,067	26,338	25,780	25,881	28,918	3,037	25,725
Aid from Other Government Agencies	1,238,443	1,358,903	1,285,348	1,364,472	1,253,597	(110,875)	1,662,838
Charges for Current Services	243,641	251,541	254,050	257,396	260,799	3,403	261,307
Miscellaneous Revenues and Other Financing Sources	540,384	573,872	560,735	589,023	588,920	(103)	290,082
Total Revenues[6]	$2,736,372	$2,914,095	$2,883,699	$3,001,866	$2,994,721	($ 7,146)	$3,181,014
Estimated Use of Unreserved and Designated Fund Balance	$ 3,986	$ 3,986	$ 3,690	$ 3,690	$ 3,690	$ 0	$ 2,614
Estimated Use of Unreserved and Undesignated Fund Balance	129,209	172,490	56,496	114,845	114,845	0	105,845
Estimated Use of Fund Balance Reserved for Encumbrances	0	84,031	0	131,356	131,356	0	0
Total Resources Utilized[6]	$2,869,568	$3,174,602	$2,943,886	$3,251,757	$3,244,612	($ 7,146)	$3,289,473
Net Savings from the 2005-06 Adjusted Budget	—	—	—	—	$ 245,408	$245,408	—

Source: County of San Diego Auditor and Controller

(1) This amount reflects expenditures and revenues included in the 2004-05 Adopted Budget, as amended and adjusted to include all budgeted appropriations and revenues as of June 30, 2005.

(2) This amount reflects expenditures and revenues included in the 2005-06 Adopted Budget, as amended and adjusted to include all budgeted appropriations and revenues as of March 31, 2006.

(3) These amounts reflect, as of March 31, 2006, projections of the expenditures and revenues of the County's General Fund for Fiscal Year 2005-06.

(4) These amounts reflect the difference between the budgeted expenditures, revenues and other financing sources of the County's General Fund in the 2005-06 Adjusted Budget as of March 31, 2006 and the projected expenditures, revenues and other financing sources of the County's General Fund for Fiscal Year 2005-06. Amounts without parentheses indicate a variance favorable to the County's General Fund. Amounts with parentheses indicate a variance unfavorable to the County's General Fund.

(5) This amount reflects expenditures and revenues included in the 2006-07 Adopted Budget.

(6) Total may not equal the sum of the line items due to rounding.

The unreserved and undesignated portion of the General Fund Balance as of June 30, 2005 was $264.2 million. See the table entitled "General Fund Balance Sheet" herein for a description of the fund balance of the General Fund for the Fiscal Years ending June 30, 2004 and June 30, 2005, respectively. Included in the 2005-06 Adopted Budget were appropriations based on the unreserved and undesignated portion of the General Fund Balance of approximately $56.5 million. Accordingly, the available unreserved and undesignated portion of the General Fund Balance was reduced to $207.7 million. The General Fund balance was used as the funding source for various one-time or project specific purposes in the 2005-06 Adopted Budget, including temporary staffing, the purchase of safety and other equipment including the rebudget of appropriations for a mugshot replacement system and the Jail Information Management System retrofit project, management reserves, offsets for the costs of processing building permits for victims of Firestorm 2003, the rebudget of Firestorm 2003 appropriations to rebuild parks and trails, the rebudget of appropriations for the Fire Safety and Fuels Reduction Program, a set aside for the multi-year cost of the enterprise-wide Documentum document management system, the required match for the multi-year stormwater grant, one-time technology projects, County Administration Center major maintenance projects, and awarding Community Projects grants.

Subsequently, the Board of Supervisors approved the appropriation of an additional $105.1 million in unreserved and undesignated General Fund Balance for various items including employee incentive compensation payments, information technology contract transition costs, increases to management reserves, a new web-based training tool, auditing software, major maintenance projects, and unanticipated election costs, split payroll costs, the Medical Examiner design completion, San Elijo Lagoon Nature Center expansion, Central Avenue drainage work, and for the Edgemoor Skilled Nursing Facility construction project. The Board of Supervisors also approved the designation of fund balance in three instances: $2.1 million for Environmental Health, $1.3 million for a prepaid lease purchase payment for the Housing Authority building, and $3.0 million for future capital projects related to the Sheriff's Department. It is also anticipated that the Board of Supervisors will approve the appropriation of $3.5 million for Land Use and Environmental Group fire services in June 2006 from the unreserved and undesignated General Fund Balance. The total of these actual or anticipated adjustments reduces the available unreserved and undesignated fund balance to $92.7 million. The use of fund balance is considered to be a one-time resource and the County adheres to its policy of not spending one-time resources on any on-going operational needs. As noted above, the County projects that the General Fund expenditures will be $252.5 million less than budgeted in the 2005-06 Adjusted Budget and General Fund revenues will be $7.1 million less than budgeted in the 2005-06 Adjusted Budget for a net savings of $245.4 million. This projected positive variance would be added to any remaining unreserved and undesignated General Fund Balance as of June 30, 2006. Therefore, the County projects that if there were to be no further uses of available unreserved and undesignated General Fund Balance and no changes in net projected variances for 2005-06, the unreserved and undesignated portion of the General Fund Balance as of June 30, 2006 would be approximately $338.1 million (representing the $92.7 million remaining available fund balance plus the $245.4 million General Fund projected net savings), which would result in an increase of approximately $73.9 million from the General Fund Balance as of June 30, 2005.

The County does not prepare any formal update of its General Fund Balance projections after the Third Quarter Report. The next formal update of the County's General Fund Balance will occur in connection with the audit of the general purpose financial statements of the County for Fiscal Year ended June 30, 2006, which is expected to be completed by January 2007.

Vehicle License Fee

The Vehicle License Fee ("VLF") is an annual fee collected by the State for any vehicle subject to registration in California. Prior to the State's Fiscal Year 2004-05 budget, revenue from or equal to the VLF was appropriated by the State to cities and counties for use in health, mental health and social services programs pursuant to certain State statutory mandates and as general purpose revenue.

Cities' and counties', including the County's, share of VLF general purpose revenues was eliminated by the State's Fiscal Year 2004-05 budget and replaced with money shifted from the Educational Revenue Augmentation Fund (the "ERAF"). The ERAF was a fund originally created by the State in Fiscal Year 1992-93 to deposit certain prescribed amounts of property tax to be shifted from local governmental agencies to local schools. Beginning in Fiscal Year 2004-05, the State directed that certain amounts be shifted (the "ERAF Shift") from the ERAF and deposited in the VLF Property Tax Compensation Fund (the "VLF Property Tax Compensation Fund"). In Fiscal Year 2004-05, the State established initial allocations from the VLF Property Tax Compensation Fund to cities and counties, including the County. The State has provided for an allocation from the VLF Property Tax Compensation Fund in Fiscal Year 2005-06 to be based on a formula that takes into account adjusted actual allocations for Fiscal Year 2004-05 and the increase in gross taxable assessed value of property within the County. The County has continued to receive VLF revenues from the State for health, mental health and social services programs. Based on information released by the State in October 2005, the County received a $17.7 million positive adjustment for Fiscal Year 2004-05 and the County's Fiscal Year 2005-06 property tax in lieu of vehicle license fee base was set at $247.3 million, resulting in VLF-related revenues to the County in excess of the budgeted amount by approximately $64 million in Fiscal Year 2005-06.

On March 17, 2005, the County sold, on a non-recourse basis, its rights to VLF receivables from the State relating to Fiscal Year 2003-04 and used the proceeds of such sale to pay for the design and installation of a replacement computer system to administer the County's property tax collection system and to reduce the UAAL (herein defined) associated with the County's pension program. See "– San Diego County Employees Retirement Association" below. The State made an early payment in full of the VLF receivables, which payment was applied to the defeasance of the VLF-related obligations, which produced unbudgeted interest income of approximately $2.6 million for the County.

County's 2006-07 Adopted Budget and the Operational Plan

The County annually prepares a two-year operational plan, the most recent of which was formally adopted by the County's Board on August 1, 2006 (the "Adopted Operational Plan"). Once adopted by the County's Board, the first year of the Operational Plan is the Adopted County Budget for the 2006-07 Fiscal Year (the "2006-07 Adopted Budget") and the second year represents a projection of the revenues and expenditures of the County for Fiscal Year 2007-08.

The County's Adopted Budget for the County General Fund for Fiscal Year 2006-07 is approximately $3.289 billion, with Total Appropriations of approximately $3.289 billion, Total Revenues of approximately $3.181 billion, and total estimated use of the Unreserved and Designated Fund Balance and the Unreserved and Undesignated Fund Balance of approximately $2.61 million and $105.8 million, respectively. See table entitled "COMPARISON OF GENERAL FUND ADOPTED AND ADJUSTED BUDGET FOR FISCAL YEAR 2004-05, ADOPTED AND ADJUSTED BUDGET AND PROJECTED RESULTS FOR FISCAL YEAR 2005-06 AND ADOPTED BUDGET FOR FISCAL YEAR 2006-07" herein for a summary of the County's 2006-07 Adopted Budget.

Summary of General Fund Financing Sources.

General Fund Financing Sources total approximately $3.289 billion for Fiscal Year 2006-07, a $345.6 million or 11.7% increase from the adopted General Fund budget for Fiscal Year 2005-06. The high growth rates in General Fund Financing Sources for Fiscal Year 2006-07 are primarily due to significant growth in general purpose revenues as well as growth in certain program revenues and use of fund balance. Overall, the previous three fiscal years saw growth rates of 4.4% or $116.6 million in Fiscal Year 2003-04, 3.0% or $84.5 million in Fiscal Year 2004-05, and 2.6% or $74.3 million in Fiscal Year 2005-06. General Fund Financing Sources can be categorized as one of three types: Program Revenues, General Purpose Revenues, or Fund Balance (including reserve/designation decreases).

Program Revenues. Program Revenues are budgeted at approximately $2.27 billion in Fiscal Year 2006-07. These revenues make up 69.1% of General Fund Financing Sources in Fiscal Year 2006-07, and are derived from State and federal subventions and grants, charges and fees earned from specific programs, Proposition 172 - Public Safety Sales Tax, State Realignment Funds, and Tobacco Settlement funds, among others. Program Revenues are dedicated to and can be used only for the specific programs with which they are associated, have increased by 5.2% over the Fiscal Year 2005-06 Adopted Budget. The average annual growth for the last three years was 3.0%. State, federal, and other intergovernmental funds of $1.66 billion in Fiscal Year 2006-07 comprise 73% of Program Revenues.

General Purpose Revenues. General Purpose Revenues, which are budgeted at approximately $906.3 million in Fiscal Year 2006-07, comprise approximately 27.6% of General Fund Financing Sources. The revenues come from property taxes, property tax in lieu of VLF, sales taxes (and property tax in lieu of sales tax), real property transfer tax, and miscellaneous other sources. They may be used for any purpose that is a legal expenditure of County funds. The Board, therefore, has the greatest flexibility in allocating these revenues.

The growth in these revenues is principally affected by the local and State economies. In recent years, San Diego's economy has outperformed both State and national growth. The growth in general purpose revenues has averaged 6.2% annually since Fiscal Year 2000-01, but for Fiscal Year 2006-07, an overall growth rate of 25.7% ($185.3 million) is estimated compared to the 2005-06 Adopted Budget. This increase is due in part to conservative revenue estimates for 2005-06 in both property taxes and property tax in lieu of vehicle license fees (see "Vehicle License Fee" above), as well as the restoration of $27.5 million in property taxes that the State required to be shifted to the Educational Revenue Augmentation Fund ("ERAF") in fiscal years 2004-05 and 2005-06, and continued strong growth in real estate values. This high rate of growth is not indicative of projected out-year revenue growth.

Use of Fund Balance. Use of Fund Balance, which totals approximately $108.5 million in Fiscal Year 2006-07, including reserve/designation decreases, represents 3.3% of General Fund Financing Sources in Fiscal Year 2006-07. This resource is used for one-time expenses, not for the support of ongoing operations. This compares with $60.2 million in uses of fund balance in the Fiscal Year 2005-06 Adopted Budget, which equaled 2.0% of total General Fund Financing Sources.

In the Adopted Operational Plan, a portion of the projected General Fund Balance used as the funding source for various one-time or project specific purposes such as park maintenance and development, management reserves, offsets for the costs of processing building permits for victims of the 2003 fires in the County, funding for the Fire Services Program, Emergency Operations Center upgrades, a set aside for the multi-year cost of the enterprise-wide document management system, the required match for the multi-year storm water grant, one-time technology projects, and awarding community projects grants.

Summary of Total Appropriations.

Appropriations total approximately $4.37 billion in the Adopted Operational Plan for Fiscal Year 2006-07. This is an increase of $188.0 million or 4.5% from the Fiscal Year 2005-06 Adopted Budget. Of the Total Appropriations of $4.37 billion, an amount equal to approximately $3.289 billion represents appropriations for the General Fund, which constitutes 75% of the Total Appropriations of the County.

In the Adopted Operational Plan appropriations are increasing in Public Safety, Land Use and Environment, Community Services, Finance & General Government, the Capital Program, and Finance-Other. Appropriations are decreasing in the Health and Human Services Agency. The Health and Human Services Agency, at $1.61 billion, continues to be the largest share of the budget, 37%, followed by the Public Safety Group at $1.3 billion or 30%.

Public Safety Group. A net increase of 8.36% or $100.6 million over the Fiscal Year 2005-06 Adopted Budget. The adopted budget provides resources to: increase jail capacity and the security of detentions operations; address an increase in operating costs, including energy costs, in detention and in court facilities; increase the ability to investigate and prosecute certain crimes such as gang activity and domestic violence; re-open a dorm at the Probation Department's Camp Barrett Facility to expand sentencing alternatives for youthful offenders; add public defenders to better respond to community needs; add medical examiner investigators to decrease response times; and provide an allowance for negotiated cost of living adjustments. Appropriations for Child Support Services are decreasing due to lower federal funding for the program.

Health and Human Services Agency. A net decrease of 11.4% or $207.4 million over the Fiscal Year 2005-06 Adopted Budget. The net decrease is primarily the result of an accounting change that eliminated the Realignment Special Revenue Fund and the dual fund (Special Revenue Fund and General Fund) treatment of these revenues. Increases reflect an allowance for negotiated increases in salaries and benefits; caseload increases and the rising cost of doing business within the In-Home Supportive Services program; increased funding for County medical services for hospital and clinic services; ongoing costs for Adult/Older Adult Mental Health Services, Children's Mental Health Services and the California Work Opportunities Information Network (CalWIN); and implementation of the Mental Health Services Act (Proposition 63).

Land Use and Environment Group. A net increase of 6.5% or $21.5 million from the Fiscal Year 2005-06 Adopted Budget. The increase is primarily due to the rebudgeting of a grant funded tree removal program; allowance for negotiated cost of living adjustments; the addition of staff years for laboratory support, testing, inspection, public health protection, parks and recreation programs, fire prevention, and code enforcement; and for increased workload related to Road Fund capital projects. Other increases include one-time funding for park paving projects and right-of-way acquisitions. These increases are offset by decreases due to the completion of Airport and Sanitation District capital projects and the completion of one-time projects in Parks and Recreation.

Community Services Group. A net increase of 7.9% or $18.8 million from the Fiscal Year 2005-06 Adopted Budget. The increase is due to an allowance for negotiated cost of living adjustments, funding for one-time projects including County real estate management and maintenance, increasing the efficiency of Library operations, and increased costs for utilities, fuel, parts and major maintenance projects.

Finance and General Government Group. A net increase of 5.0% or $14.5 million from the Fiscal Year 2005-06 Adopted Budget. The increase is due to an allowance for negotiated cost of living adjustments, enhanced internal auditing support, a one-time transition cost related to the selection of a

new information technology vendor for the County, major maintenance projects, increases in insurance costs and the implementation of new employee development programs.

Capital. A net increase of $95.4 million or 1,355.5% from Fiscal Year 2005-06. The net increase includes $80.0 million for a new Medical Examiner/County Veterinarian Facility, as well as increased ongoing funding for land acquisitions for the Multiple Species Conservation Program (MSCP) and one-time funds for development of sports fields and trails, park land acquisition and other park improvements including Americans with Disabilities Act upgrades.

Finance-Other. A net increase of $144.6 million or 48.1% from Fiscal Year 2005-06. This group of programs includes miscellaneous funds and programs that are predominantly Countywide in nature, have no staffing associated with them, or exist for proper budgetary accounting purposes. Included in this Group are such programs as the Contingency Reserve, the General Fund's Contribution to the Capital Outlay Fund and the Library Fund, lease-purchase payments on the County's certificates of participation issued by the San Diego County Capital Asset Leasing Corporation, the Employee Benefits Internal Service Fund (ISF), the Public Liability Internal Service Fund, the Pension Obligation Bond Fund, the Community Enhancement Program, and the Community Projects Program. The increase reflects the General Fund contribution for the capital projects noted above, raising the Contingency Reserve to $20.0 million from $15.6 million, higher anticipated costs in the public liability fund, and higher scheduled payments for pension obligation bonds. Scheduled lease purchase payments have decreased and there is a slight decrease in the Employee Benefits ISF for Workers' Compensation and Unemployment Insurance claims.

Impact of State's 2006-07 Budget Act on the County's 2006-07 Adopted Budget.

The 2006-07 Budget Act (the "2006-07 Budget Act") was passed by the State Legislature on June 27, 2006 and signed by the Governor on June 30, 2006. The 2006-07 Budget Act included the following items:

ERAF – The 2006-07 Budget Act is consistent with the two year budget agreement reached between the State and local governments with respect to the ERAF Shift. The two-year shift of $27.5 million of property taxes to the Educational Revenue Augmentation Fund (ERAF) to assist the State in meeting funding obligations to schools was completed in Fiscal Year 2005-06. See "County Financial Information – Vehicle License Fee" herein.

State Mandated Costs – The 2006-07 Budget Act includes $169.9 million for the first two years of a 15-year payment plan to reimburse counties for mandated costs for which funding was deferred in years prior to 2004-05. Separately, the County of San Diego had sought relief through the courts with respect to the State's non-payment of mandated costs and in March, 2006 received a judgment that established that the State owed $41.6 million to the County and that it was to be paid the amount owed plus interest over a 15-year period. The estimated annual payment is $3.0 million. In addition, as in Fiscal Year 2005-06, the State 2006-07 Budget Act includes funding to reimburse current mandated cost claims.

Transfer of Fees – The 2005-06 Budget Act required counties to transfer revenues from certain court imposed fees, fines, and forfeitures to the local trial court that would otherwise have gone to the counties, extending the transfers for Fiscal Years 2003-04 and 2004-05 for four more years. The County's share was $2.1 million for Fiscal Years 2003-04 and 2004-05 and $0.8 million in Fiscal Year 2005-06. For Fiscal Years 2006-07 and 2007-08, the County's share each year is expected to be $0.6 million and $0.4 million, respectively. One-time resources will be used to fund this requirement.

Property Tax Administration Grant – The 2006-07 Budget Act continues the suspension for a second year of the State Property Tax Administration Grant program that has assisted counties in maintaining timely property assessments. The County's revenue loss of $5.4 million was not anticipated in the Fiscal Year 2005-06 Adopted Operational Plan, and was offset mid-year by unanticipated additional General Purpose Revenues. For 2006-07, General Purpose Revenues continue to replace the loss of these grant funds.

Information Technology Outsourcing Program

The County outsourced its telecommunications and information technology services under a seven-year agreement, valued at approximately $644 million, in December 1999. The current contract with Computer Sciences Corporation and their partners, collectively referred to as the Pennant Alliance, will expire on December 12, 2006. The County awarded a contract to Northrop Grumman Information Technology ("NGIT"), effective January 24, 2006. NGIT is partnering with three other primary companies, Electronic Data Systems, Bearing Point and AT&T, to provide a full range of information technology services. The contract term is seven years, with a five year extension. The contract costs for Fiscal Year 2006-07 are included in the County's 2006-07 Adopted Budget.

Teeter Plan

In Fiscal Year 1993-94, the County adopted the alternative method of secured property tax apportionment available under Chapter 3, Part 8, Division 1, of the Revenue and Taxation Code of the State of California (also known as the "Teeter Plan"). This alternative method provides for funding each taxing entity included in the Teeter Plan with its total secured property taxes during the year the taxes are levied, including any amount uncollected at Fiscal Year end. Under this plan, the County assumes an obligation to advance funds to these entities to cover expected delinquencies. The County's general fund benefits from future collections of penalties and interest on delinquent taxes collected on behalf of participants in this alternative method of apportionment.

From June 1996 through June 2005, the County issued on an annual basis its Teeter Obligation Commercial Paper Notes ("Teeter Notes") to finance delinquent property tax receivables. The County did not issue Teeter Notes for June 15, 2006 delinquencies (the statutory payout date for participating entities). The County paid in full its outstanding Teeter Notes on June 20, 2006.

Pursuant to the Law, the County is required to establish a tax losses reserve fund to cover losses that may occur in the amount of tax liens as a result of special sales of tax-defaulted property (i.e., if the sale price of the property is less than the amount owed). The amount required to be on deposit in the tax losses reserve fund is, at the election of the County, one of the following amounts: (1) an amount not less than 1% of the total amount of taxes and assessments levied on the secured roll for a particular year for entities participating in the Teeter Plan, or (2) an amount not less than 25% of the total delinquent secured taxes and assessments calculated as of the end of the Fiscal Year for entities participating in the Teeter Plan. The County's tax losses reserve fund is fully funded, in accordance with the County's election to be governed by the second alternative, with a $10,281,000 balance for Fiscal Year 2005-06. Accordingly, any additional penalties and interest that otherwise would be credited to the tax losses reserve fund are credited to the County's General Fund.

Temporary Transfers

Section 6 of Article XVI of the California Constitution provides for temporary transfers of funds by the Treasurer-Tax Collector of the County to cover short-term operational deficits occurring as a result of imbalances between receipts and expenditures. The California Constitution prohibits Temporary

Transfers by participants of the Treasury Pool (herein defined) (including the County) prior to the first day of the Fiscal Year or after the last Monday of April of each Fiscal Year, and of amounts in excess of 85% of the school district taxes levied by a county under Section 21 of Article XIII of the California Constitution and of amounts apportioned to such school district under Section 6 Article IX of the California Constitution. Treasury Pool participants may utilize Temporary Transfers from time to time for various purposes. A Temporary Transfer must be repaid from the Treasury Pool participant's first revenues received thereafter before any other obligation and thus, in the case of the County, would have a priority over the County's general fund debt obligations. The only Temporary Transfer utilized by the County in the past ten years was in Fiscal Year 1996-97 in the amount of $25,000,000.

San Diego County Employees Retirement Association

The following information concerning the San Diego County Employees Retirement Association (the "Association") is excerpted from publicly available sources, which the County believes to be accurate. The Association is not obligated in any manner for payment of debt service on the Series 2006 Certificates, and the assets of the County's pension plan are not available for such payment.

General

The Association, which was established July 1, 1939 under provisions of the County Employees Retirement Law of 1937 (the "Retirement Law"), is a contributory defined benefit plan covering substantially all compensated employees of the County. Benefits under the County's pension plan are paid in finite amounts, derived from a formula based on age, service credit and levels of compensation, as calculated by the Association in accordance with applicable law and agreements. As of June 30, 2006, there were 17,451 active members, 12,049 retired members and beneficiaries and 4,687 deferred members. Deferred members are those members whose employment has terminated with a participating employer and who left their respective retirement contributions with the Association. The System operates on a fiscal year basis, with its year ending June 30.

The County is one of the employers that participates in the Association. In addition to the County, participating employers include the San Diego Superior Court (the "Courts"), the Local Agency Formation Commission, the San Dieguito River Valley Joint Powers Authority, and the San Diego County Office of Education. The County and these other participating employers are collectively referred to herein as the "Employers" and contributions to the Association made by such Employers are referred to herein as "Employer Contributions". The County is obligated to make 91.5% of the annual Employer Contributions to the Association and the other participating employers are obligated to make 8.5% of the annual Employer Contributions to the Association, based on the estimated relative percentage of payroll of the County and the other participating employers for Fiscal Year 2006-07.

There are numerous measures in the State Legislature proposing changes to or reform of pension plans. No prediction can be made as to whether any of these proposals will become effective or, if adopted and implemented, whether the impact upon local agencies, such as the County, would be adverse. In addition, in light of the significant current political interest to reform pension practices of the State and of local agencies, other proposals may be suggested which, if adopted, may be adverse to the County's financial condition.

General Funding Practices of the Association

Introduction. The Retirement Law requires the Association to commission an actuarial valuation and an experience study at least every three years. The Association's practice has been to conduct an actuarial valuation on an annual basis as of June 30 of each year, which is the end of the Association's

fiscal year. The valuation must be completed by an Enrolled Actuary, covering the mortality, service, and compensation experience of the members and beneficiaries, and must evaluate the valuation assets and actuarially determined liabilities of the Association. The Retirement Law requires the Retirement Board of the Association (the "Retirement Board") to recommend to the Board of Supervisors and the other Employers such changes in the rate of contribution by the Employers and members, and in the County's and the other Employers' appropriations as necessary. Once the Retirement Board recommends any such changes, the Retirement Law requires the Employers (including the County) to implement such changes. The most recent actuarial valuation is as of June 30, 2006. The Segal Company (the "Actuary") has been retained as the Association's actuary.

UAAL and its Calculation. Currently, the Association uses the "entry age normal cost method" to calculate the Employers' annual rates of contribution. The actuarially required contribution has two components, the "normal cost" and the amortized amount of the unfunded actuarial accrued liability ("UAAL"). Normal cost represents the portion of the actuarial present value of the benefits that the Employers and their respective employees will be expected to fund that are attributable to a current year's employment. The amortization of the UAAL represents the current year's portion of the unfunded accrued costs (*i.e.*, the UAAL) attributable to past years' employment. The UAAL may increase or decrease as a result of changes in actuarial assumptions, benefit improvements and other experience which differs from that anticipated by the actuarial assumptions. There is a lag between the point in time at which the actuary completes the actuarial valuation and the date that the contribution rates calculated in the valuation go into effect. This lag is typically 12 months. For example, the recommended contributions contained in the actuarial report as of June 30, 2006 would apply to contributions to be made by the County and the other Employers for the fiscal year beginning July 1, 2007.

The UAAL is an estimate based on a series of assumptions that operate on demographic data of the Association's membership. This process is necessary to determine, as of the date of the calculation, how sufficient the assets in the Association are to fund, as of the date of calculation, the accrued costs attributable to currently active, deferred vested members and retired members. The funding sufficiency is typically expressed as the ratio of the valuation assets to the actuarial accrued liabilities. If the actuarially calculated funding level of a plan is less than 100%, the plan has a UAAL. Examples of the actuarial assumptions that are used in this process are the assumed rate of earnings on the assets of the plan into the future, the assumed future pay increases for current employees, assumed rates of disability, the assumed retirement ages of active employees, the assumed marital status at retirement, and the post-employment life expectancies of retirees and beneficiaries.

When measuring assets for determining the UAAL, many pension plans, including the Association, "smooth" gains and losses to reduce volatility. If in any year the actual investment return on the Association's assets is lower or higher than the actuarial assumed rate of return (which is 8.25%, net of expenses), then the shortfall or excess is smoothed or spread over a five-year period. The impact of this will result in "smoothed" assets which are lower or higher than the market value of assets depending upon whether the remaining amount to be smoothed is either a net gain or a net loss. In the case of the Association, as a consequence of this smoothing practice, as of June 30, 2006, there were approximately $757.8 million of gains and approximately $35.0 million of losses yet to be smoothed in, leaving a total net unsmoothed gain of $722.8 million remaining to be spread over the five years ending June 30, 2011.

Further, various plans use differing amortization periods for paying off (or "amortizing") a UAAL. Some plans use different rolling periods and still others use "fixed" periods such as a 30-year fixed period, meaning that the actuarially required contribution in a particular year would be the unfunded actuarial accrued liability amortized over the remaining years in the fixed period. On June 17, 2004, the Retirement Board changed the Association's amortization period from a 15-year rolling amortization period to a 20-year fixed layered amortization period.

The 20-year fixed layered method of amortizing the UAAL amortizes each year's change in UAAL over a new 20 year period. Accordingly, the increase or decrease in UAAL from the current year's actuarial valuation began a new 20 year amortization schedule. The prior year increase or decrease in UAAL has 19 years remaining on its 20 year amortization schedule. The balance of the UAAL as of June 30, 2004 has 18 years remaining on its 20 year amortization schedule. As with other assumptions, the Retirement Board may change the amortization period from time to time, which would result in the Employer's contributions to the Association in a particular year being higher or lower.

Investors are cautioned that, in considering the amount of the UAAL as reported by the Association and the resulting amounts of required contributions by the County and the other Employers, this is "forward looking" information in that it reflects the judgment of the Retirement Board and the Association's actuary as to the amount of assets which the Association will be required to accumulate to fund future benefits over the lives of the currently active employees, vested terminated members and existing retired members. These judgments are based upon a variety of assumptions, one or more which may prove to be inaccurate or be changed in the future, and will change with the future experience of the Association.

Demographic Assumptions. The Retirement Board and the Association's actuary periodically review the various demographic assumptions that are employed in calculating the UAAL against actual experience at least every three years. The Association's actuary last conducted an experience study in 2004. Pursuant to the experience study, the Retirement Board elected in March 2004 to modify certain of the assumptions used to calculate the UAAL. The changed assumptions included the assumed future pay increases for current employees, the assumed rates of disability, the assumed retirement ages of active employees, the assumed marital status at retirement, and the post-employment life expectancies of retirees and beneficiaries. The changed assumptions were included in the actuarial valuation report as of the year ended June 30, 2003. The next experience study is expected to be available in early 2007. Any changed assumptions resulting from the experience study are expected to be included in the actuarial valuation report as of the year ended June 30, 2007.

Economic Assumptions. At the May 6, 2004 meeting of the Retirement Board, the Association's actuary recommended and the Retirement Board approved an asset smoothing methodology pursuant to which the expected investment return on the market value of assets (instead of the expected return on the valuation value of assets) will be compared to the actual investment return on the market value of assets, and the difference will be "smoothed" over a five-year period. This smoothing methodology became effective with return deviations beginning with the fiscal year ended June 30, 2005 and may accelerate the rate at which investment losses and gains are realized. For a discussion on actions of the Retirement Board with respect to the disposition of Excess Earnings (as defined herein), subsequent to consultation with the Actuary, see "County Financial Information – San Diego County Employees Retirement Association – Transfers of Investment Earnings by the Association" herein. For a discussion on recommended changes to the assumed investment return, rate of inflation, and individual salary increases currently under consideration by the Retirement Board, see "– Prospective Funding Status of the Association" herein.

On an annual basis, the Retirement Board receives the Actuary's recommendations on and considers the assumptions to be used by the Actuary to project the assets and liabilities of the pension fund, including the actuarial assumed rate of earnings. The County cannot predict at this time the further recommendations to be made by the Actuary, the Retirement Board's determinations with respect thereto and their potential effects on the Association's assets and liabilities.

Funding Status of the Association

Current Status. As of June 30, 2006, the date of the most recent actuarial valuation report, the valuation value of assets of the Association was approximately $6.263 billion, the actuarial accrued liability was approximately $7.495 billion and the funded ratio was approximately 83.6%. The actuarial value of assets may increase or decrease as a result of investment results of the Association increasing or decreasing below the actuarially assumed rate of 8.25% per annum as a consequence of increases or decreases in the securities market. No assurance can be given that the actuarial value of assets of the Association will not materially decrease.

As of June 30, 2006, the UAAL was approximately $1.232 billion. The Association's funded ratio and the UAAL as of June 30, 2006 reflect the contributions by the County of the proceeds of all POBs (herein defined), as well as the additional discretionary contribution of $24.9 million in Fiscal Year 2004-05 and $40.0 million in Fiscal Year 2005-06. In the valuation as of June 30, 2006, the combined contribution rate for the County for 2007-08 was calculated at 23.28%. The UAAL as of June 30, 2006 excludes a total net unsmoothed gain of $722.8 million as of June 30, 2006, which amount will be spread over the five years ending June 30, 2011. See "– UAAL and its Calculation" herein.

Historical Funding Status. Table 8 below sets forth for each of the ten years ended June 30, 2006 the amount of the total Employer Contributions made by the County and the other Employers, the UAAL as of the end of each such fiscal year and the funded ratio of the Association as of the end of each of such fiscal years. On March 17, 2005, the County transferred approximately $24.9 million to the Association from the proceeds of the County's VLF-related obligations, which amount was in addition to the County's actuarially determined contribution for Fiscal Year 2004-05. See "– Vehicle License Fee" herein. The County also made an additional discretionary contribution of $40.0 million in Fiscal Year 2005-06.

TABLE 8

HISTORICAL FUNDING STATUS
Fiscal Years Ended June 30, 1997 through 2006
(In Millions)

Fiscal Year	Employer Contribution[1]	Employer Offsets[1]	UAAL[2]	Funded Ratio[2]
1997	$ 23.3	$38.3	$ (200.2)	108.1%
1998	24.3	37.2	(157.0)	105.9
1999	0.0	36.4	(221.8)	107.4
2000	0.0	38.2	(319.8)	109.9
2001	2.0	39.1	(238.8)	106.8
2002	5.3	45.2	905.1[3]	82.5[3]
2003	12.2[4]	53.9	1,435.4[4]	75.5[4]
2004	195.0[3][4]	55.2	1,202.7[4]	81.1[4]
2005	260.0[5]	56.1	1,378.4	80.3
2006	243.7[7]	58.8	1,232.3[6]	83.6

Source: County of San Diego.

(1) These contribution amounts reflect the aggregate contribution amount of all Employers and not only that of the County. The County share of Employer Contributions and Employer Offsets are estimated to be 91.5% based on the estimated relative percentage of payroll of the County for Fiscal Years 2003-04 and 2004-05. See "County Financial Information – San Diego County Employees' Retirement Association – General" herein.

(2) In each year the amounts indicated under the columns Employer Contribution and the Employer Offsets were based on the valuations as reported in the actuarial valuation dated as of the end of the second preceding year ended June 30. Negative numbers represent an actuarially accrued surplus.

(3) The UAAL and Funded Ratio indicated for the fiscal year ending June 30, 2002 are those calculated in an October 2002 actuarial valuation. The October 2002 actuarial valuation report reflected the contribution by the County of $550 million of proceeds of the 2002 POBs to the Association on October 3, 2002. The use by the Retirement Board of the October 2002 actuarial valuation to establish the Employer required contributions had been subject to litigation; see "County Financial Information – San Diego County Employees' Retirement Association – Litigation Relating to the Association – 2003-04 Contribution Litigation" for a description of this litigation. If the Retirement Board had established the Employer required contribution based on the June 30, 2002 actuarial valuation report, then the Employer required contributions in the year ended June 30, 2004 would have been approximately $308 million, and the Employer Offsets with respect to the same year would have been the same as indicated above.

(4) These contributions do not include any of the amounts contributed by the County from the proceeds of the issuance of the POBs in the indicated Fiscal Years. However, such amounts are reflected in the UAAL and Funded Ratios of the Association as of the end of such Fiscal Years.

(5) Includes $235.1 million of required contributions plus an additional discretionary contribution of $24.9 million.

(6) Excludes a total net unsmoothed gain of $722.8 million as of June 30, 2006, which amount will be spread over the five years ending June 30, 2011. See "– UAAL and its Calculation" herein.

(7) Includes $203.7 million of required contributions plus an additional discretionary contribution of $40.0 million.

Impacts to UAAL. As shown in the foregoing table, from June 30, 2001 to June 30, 2003, the UAAL increased from ($238.8) million (an "overfunded" situation) to slightly above $1.435 billion, and the funded ratio as of the same dates declined from 106.8% to 75.5%. A number of events occurred during this period which adversely affected the UAAL and the funded ratio, including, but not limited to, (1) effective March 8, 2002, the Board of Supervisors increased retirement benefits for active employees which in turn increased actuarially determined liabilities, (2) effective March 8, 2002, the County and a number of other counties in California agreed to increase benefits, which in turn required transfers from valuation assets; (3) investment results of the Association were below the actuarially assumed rate of 8.25% per annum as a consequence of declines in the securities market; (4) the Association adjusted several demographic assumptions based on a regular experience study conducted by its actuary that evaluates the reasonableness of the Association's assumptions and implemented those in the actuarial valuation report as of June 30, 2003; (5) the Association ceased including amounts in the Undistributed Reserve (as defined herein) as valuation assets when calculating the Association's UAAL; and (6) deviations between actual experience and those assumptions used in calculating the UAAL. In October 2002, the County contributed $550 million from the proceeds of the 2002 POBs, thus refunding an equal amount of UAAL. In 2004, the County contributed an additional $450 million from the proceeds of the 2004 POBs (herein defined). See "Pension Obligation Bonds" herein. As of June 30, 2006, the UAAL was approximately $1.2 billion and the funded ratio was 83.6% due in part to the issuance of the 2004 POBs and investment returns that have exceeded the assumed rate of interest.

Employee Contributions Paid by the Employers. In addition to making annual contributions to the Association in accordance with the applicable actuarial valuation, the Employers also have agreed pursuant to the collective bargaining arrangements with their employee unions to pay a portion of the employees' required contribution to the Association (these payments by the Employers are referred to herein as the "Employer Offsets"), which, for non-safety employees of the Employers range from 3% to 9.5% of their salary, and for safety employees range from 2.75% to 16.42% of their salary. In most instances, the amount of Employer Offsets will be less than the total required employee annual contribution. Some of these collective bargaining agreements expire in 2007, but since 1982, the Employers' agreement to pay Employer Offsets has been a consistent feature of these collective bargaining arrangements. See "County Financial Information – San Diego County Employees Retirement Association – Historical Funding Status" herein for information regarding payments by the Employer of Employer Offsets for each of the ten years ending June 30, 2006.

Transfers of Investment Earnings by the Association

Introduction. Pursuant to statutory authority under the Retirement Law, the Retirement Board annually directs the crediting of the Association's investment earnings to reserves, some of which are part of valuation assets, and some of which are not. Valuation assets are those assets used in calculating the UAAL and the funded ratio. For the purpose of such crediting, the Retirement Board has defined investment earnings as current income (*i.e.,* the interest, dividends, and rents) plus net realized capital gains on the book value of the Association's valuation and non-valuation assets. All of the Association's investment earnings on the Association's assets are transferred to and kept in a reserve entitled the "Undistributed Excess Earnings Reserve," and from there such earnings are transferred in accordance with Retirement Board policy. The Undistributed Excess Earnings Reserve is currently not part of valuation assets and, except in certain limited circumstances described herein, amounts in the Undistributed Excess Earnings Reserve are not included as assets for purposes of calculating the Association's UAAL.

Pursuant to the statutory authority of the Retirement Law, the Retirement Board has adopted certain "Interest Crediting Goals" which direct that investments earnings be transferred from the Undistributed Excess Earnings Reserve to the following Association reserves, effectively, in the

following order. First, such earnings are credited to the Association's valuation assets up to an amount determined by the Retirement Board's policies, currently in an amount equal to 8.25% of the value of the Association's valuation assets as of the end of the prior fiscal year. Second, an amount of such earnings is transferred to a contingency reserve (the "Contingency Reserve") that is necessary to maintain the amount on deposit in the Contingency Reserve, which is not part of valuation assets, equal to one percent of the total valuation assets of the Association. The Association may transfer amounts from the Contingency Reserve to valuation assets when current investment earnings are insufficient to credit the valuation asset reserves with the 8.25% interest target. Earnings in excess of the amounts transferred to the Contingency Reserve are referred to herein as "Excess Earnings."

Although the Retirement Law permits the Association to use any Excess Earnings to pay certain supplemental benefits to retirees as well as crediting Excess Earnings to the Association's valuation assets, the Retirement Board on September 7, 2006 voted unanimously to allocate Excess Earnings to the Health Reserve (herein defined) and the STAR COLA reserve (herein defined) to maintain amounts in each reserve at levels at least equal to that necessary to cover the costs of the respective benefits for current eligible retirees for five years, as estimated by the Association's actuary, was $217.4 million as of June 30, 2006. The Retirement Board also voted unanimously to apply any remaining Excess Earnings to valuation assets to fund a portion of the pension benefits. The Health Reserve is a reserve from which the Association reimburses the Employers for amounts that the Employers contribute for the payment of post-retirement health care benefits, and the STAR COLA reserve is a reserve established for a supplemental targeted adjustment for a cost of living adjustment.

Allocation of Excess Earnings may impact the UAAL and thus the amount of Employer Contributions required to fund pension benefits in the future in part because both the Health Reserve and the STAR COLA reserve are outside of valuation assets and are not included as assets when calculating the Association's UAAL. When earnings are held outside of valuation assets, those amounts are not available to decrease an unfunded actuarial accrued liability because they are not available to pay benefits under the County's pension plan. For a discussion of the STAR COLA benefits paid by the Association and certain other related issues, see "County Financial Information – STAR COLA Benefits" herein. For a discussion of post-retirement health care benefits paid by the Association and certain other related issues, see "County Financial Information – Post-Retirement Health Care Benefits" herein.

On May 4, 2006, the Retirement Board approved a change to the methodology for calculating excess earnings of the retirement fund. Beginning with the measurement of earnings for Fiscal Year 2005-06, the Actuary will use the change in actuarial value to calculate excess earnings. Previously, the change in book value was used to measure excess earnings. No impact on the UAAL is anticipated as a result of the change in methodology.

Historical Transfers of Investment Earnings. Table 9 below sets forth the amount of the Association's investment earnings that the Retirement Board has transferred from the Undistributed Reserve into reserves that are separate from valuation assets during the ten fiscal years ending June 30, 2006:

TABLE 9

TRANSFERS OF INVESTMENT EARNINGS TO NON-VALUATION RESERVES
Fiscal Years Ended June 30, 1997 through 2006
(In Millions)

Fiscal Year	Post-Retirement Health Care[1]	STAR COLA[2]	Contingency Reserve[3]	Total
1997	$ 23.3	--	--	$ 6.5
1998	112.3	$50.5	--	162.8
1999	7.3	0.0	--	7.3
2000	32.0	9.8	--	41.8
2001	45.5	8.2	--	53.7
2002	117.0	24.2	$35.3	176.5
2003	0.0	0.0	0.0	0.0
2004	0.0	19.6	19.8	39.4
2005[4]	0.0	9.3	8.5	17.8
2006	31.4	10.0	9.7	51.1
Total	$376.20	$131.60	$73.3	$564.3

Source: The Association.

(1) Reflects amounts that the Association has transferred to the Health Reserve from Excess Earnings.

(2) Reflects amounts that the Association has transferred from Excess Earnings to a reserve established for the payment of STAR COLA. The Association began providing STAR COLA benefits in the year ended June 30, 1999, and transfers to the STAR COLA reserve began in the year ended June 30, 1998.

(3) Reflects amounts that the Association has transferred from the Association's investment earnings to the Contingency Reserve. The Contingency Reserve was created in the fiscal year ended June 30, 2002. Before the creation of the Contingency Reserve, the 1% contingency amounts required by the Retirement Law were maintained in the Undistributed Reserve and were not separated from valuation assets.

(4) The Retirement Board determined that no amounts would be transferred from Excess Earnings to the Health Reserve for the year ended June 30, 2005 based on a determination that the amounts on deposit in the Health Reserve at the time was sufficient to pay post retirement health care benefits for at least 5 years from the date of determination.

In certain of the years indicated in the foregoing table, the amounts credited to the STAR COLA reserve and the Health Reserve were actually transferred after the end of the fiscal year with retroactive effect. The Association does not track either the Employer or the departments or funds of any Employer from which retired personnel receiving STAR COLA or health benefits, when in active service, were paid.

Reserve Levels. As of June 30, 2006, there were no funds on deposit in the Undistributed Excess Earnings Reserve, approximately $73.3 million was on deposit in the Contingency Reserve, approximately $54.4 million was on deposit in the STAR COLA reserve (see "County Financial Information – STAR COLA Benefits" herein), and approximately $217.4 million was on deposit in the Health Reserve. For a discussion on actions of the Retirement Board with respect to the transfer of certain Excess Earnings to the Health Reserve and the STAR COLA reserve, see "County Financial

Information – San Diego County Employees Retirement Association – Transfers of Investment Earnings by the Association" herein. See also "County Financial Information – STAR COLA Benefits" and "County Financial Information – Post-Retirement Healthcare Benefits – Health Reserve" herein.

Prospective Funding Status of the Association

Table 10 below sets forth projections by the Association's actuary relating to future Employer Contribution amounts, Employer Offsets, UAAL, and funded ratio. The information contained in this table, and the related assumptions, are "forward-looking" in nature and are not to be construed as representations of fact or representations that in fact the various tabular information shown will be the correct amounts for the years indicated. Rather, these reflect good faith estimates by the Association's actuary and the Association, taking into account a variety of assumptions, a number of which are discussed herein. Accordingly, prospective investors are cautioned to review these estimates as general indications of orders of magnitude and not as precise amounts.

On June 1, 2006, the Association's Actuary presented to the Retirement Board for discussion purposes a report entitled "Review of Economic Actuarial Assumptions for the June 30, 2006 Actuarial Valuation," pursuant to which the Actuary recommended certain changes to the assumed rate of earnings, rate of inflation, and individual salary increases. The Actuary indicated in discussions with the County that its recommended changes could result in an estimated $200 million increase in the Association's UAAL and an approximate two percentage points increase in the Employer Contribution rate for Fiscal Year 2007-08, which is approximately $20 million higher than the projected Employer Contribution amount for Fiscal Year 2007-08 calculated using the actuarial assumptions currently in effect. Consistent with the Retirement Board's practice regarding discussion items, the Retirement Board took no immediate action on the Actuary's recommendations. Although, the Retirement Board unanimously approved a substantial portion of the Actuary's recommendations at its July 6, 2006 meeting, the Retirement Board did not adopt the Actuary's recommendation to reduce the assumed rate of earnings due in part to the higher-than-assumed historical rate of earnings experienced by the Association through June 2006. See "County Financial Information – San Diego County Employees Retirement Association – General Funding Practices of the Association – Investment Policy" for a discussion of the impact of the Associations investment strategies on its assumed rate of earnings. The County cannot predict whether the Association with change the assumed rate of interest or other assumptions in the future, or the effects of any such changes on the Association's assets and liabilities. The amounts shown in Tables 10, 11, and 12 below reflect the currently adopted assumptions, as noted in the footnotes to these tables.

TABLE 10

PROSPECTIVE FUNDING STATUS OF THE ASSOCIATION
Fiscal Years Ended June 30, 2007 through 2013
(In Millions)

Fiscal Year	Employer Contributions[(1)(3)(4)]	Employer Offsets[(2)(3)(4)]	UAAL[(1)(3)(4)]	Funded Ratio[(1)(4)]
2007	$241	$62	$915	88.6%
2008	238	65	567	93.4
2009	224	68	350	96.2
2010	207	71	220	97.8
2011	200	74	176	98.3
2012	200	77	148	98.7
2013	207	80	120	99.0

Source: The Segal Company.

(1) The following assumptions have been applied in preparing the foregoing estimates:

(a) The annual investment return on the market value of assets is 8.25% after June 30, 2006.
Under the Retirement Board's asset smoothing method, if actual return on market value of assets is above/below the expected return on market value of assets, the difference between the actual and the expected return will be recognized over a five-year period. There was a total of $722.8 million in unrecognized investment gain as of June 30, 2006.

(b) All of the actuarial assumptions used in developing the contribution rates in the June 30, 2006 valuation will be met in the future.

(c) In projecting the payroll, the Actuary assumed that the estimated Fiscal Year 2006-07 payroll of $979.4 million used in the June 30, 2006 actuarial valuation will increase by 4.25% per annum.

(d) The Retirement Board's current valuation methodologies, such as the 20-year fixed layered amortization period for the UAAL and the five-year smoothing asset valuation method (described in (a)), will remain unchanged.

(e) The Employee Offsets (*i.e.*, the County's pickup of member contributions) of about $59 million (reported by the Association for the 2005-06 Fiscal Year) will increase by the 3.75% inflation plus the 0.50% across-the-board salary increase assumptions used in the June 30, 2006 every year after June 30, 2006 to $62 million for Fiscal Year 2006-07. The Employee Offsets for Fiscal Year 2007-2008 and thereafter have been approximated by increasing the prior year's offsets by 4.25%. See "County Financial Information – San Diego County Employees Retirement Association – General" herein. This is a simplifying assumption as the actual Employee Offsets amount is governed by bargaining agreements with employee groups and actual membership demographics.

(f) No excess interest earnings will be credited to the non-valuation reserves. However, the Actuary assumes the Retirement Board will transfer earnings sufficient to maintain a 1% Contingency Reserve so that health benefits and STAR benefits can be paid by the Association.

(g) The above projections do not reflect the impact of any assumption changes that may be adopted by the Retirement Board after the June 30, 2006 valuation.

(2) Employer Offsets for each year will increase over the prior year by approximately 4.25%. Employer Offsets are governed by collective bargaining agreements with the Employers' employee groups and reflect in part actual membership demographics, since the actual amount of contributions depend upon length of service with the County.

(3) The County is obligated to make 91.5% of the annual Employer Contributions to the Association and the other participating employers are obligated to make 8.5% of the annual Employer Contributions to the Association, based on the estimated relative percentage of payroll of the County and the other participating employers for Fiscal Year 2006-07.

(4) In each year the Employer-Required Contribution and the Employer Offsets will be based on the UAAL as reported in the actuarial valuation dated as of the end of the second preceding year ended June 30. Indicated projected amounts under the columns entitled "UAAL" and "Funded Ratio" are as of June 30 of the years indicated.

The amounts shown in the foregoing table do not give effect to any transfers of Excess Earnings to non-valuation assets (such as to the Health Reserve or to the STAR COLA reserve); however, a transfer of earnings sufficient to maintain the amount on deposit in the Contingency Reserve equal to 1% of the market value of all of the Association's assets is reflected in the indicated amounts. Historically, the Association has transferred from Excess Earnings to the Health Reserve and the STAR COLA reserve, collectively, approximately $211.5 million for the five years ended June 30, 2006. See "County

Financial Information – San Diego County Employees Retirement Association – Transfers of Investment Earnings by the Association" for a description of how transfers from excess earnings remove assets from valuation assets which, over time, may increase the UAAL and the required contributions of the County and the other Employers. If such transfers occur in one or more of the years shown, which will most likely occur but the amounts to be transferred or when any transfers will in fact occur is not known, the effect of such transfers will be to increase Employer Contributions and UAAL.

Investment Policy.

General. The Retirement Law grants the Retirement Board exclusive control over the investment of the Association's assets. The Retirement Law provides general guidelines which generally require the Retirement Board to manage the investments for the purpose of providing benefits to members, minimizing Employer Contributions, and defraying the reasonable expenses of administering the Association. The Retirement Law further requires the Retirement Board to manage the Association's investments prudently and to diversify investments.

The Retirement Board has adopted an investment policy statement and related policies to ensure that the Association is managed prudently and in compliance with the Retirement Law. These policies set investment return and risk objectives and provide for extensive guidelines with respect to diversification of assets, securities, lending, commission recapture, value-added strategies, proxy voting, and corporate governance issues. The Association's assets are invested in diversified asset classes, including equity, fixed income and real estate assets. Table 11 below sets forth the Association's asset allocation policy (the "Asset Allocation Policy") as of September 30, 2006. The asset allocation policy is managed and monitored by the Association's staff with the assistance of external investment consultants. As of June 30, 2006 the total portfolio market value of the Association's assets was $7.281 billion. As of September 30, 2006 that total portfolio market value was $7.549 billion.

TABLE 11

San Diego County Employees Retirement Association
Asset Allocation Policy[1]

Investment Description	Allocation
Fixed Income	
Core U.S. Fixed Income	6.00%
High Yield	7.00
TIPS	4.00
Non-U.S. Fixed Income	8.00
Emerging Market Debt	6.00
Total:	31.00
Real Estate	10.00
Equity	
U.S. Equity	24.00[2]
Non-U.S. Equity	19.00
Emerging Markets Equity	6.00
Alternative Equity	5.00
Total:	54.00
Commodities	5.00
Total Assets	100.00
Expected Compound Annual Return	8.17[3]

Source: San Diego County Employees Retirement Association.

(1) The current Asset Allocation Policy was adopted on March 17, 2005 and continues to be in effect.

(2) As of September 30, 2006, this target portfolio allocation was split between small capitalization stocks which represented 4% of the target portfolio allocation directly held by the Association, and large capitalization stocks, which represented 20% of the target portfolio allocation held by the Association through its investments in derivative securities.

(3) Excludes adjustment to the expected rate of earnings as a result of the Alpha Engine strategy described below.

The assumed rate of return adopted by Retirement Board and applicable to the projection of the Association's assets and liabilities is .08% above the 8.17% expected compound annual passive return of the Association's Asset Allocation Policy as calculated by the Association's Investment Consultant. The Investment return assumption of 8.0% recommended by the Actuary is based on a number of assumptions, including the average assumed passive rate of earnings by asset class from a sample of investment consultants to several public pension funds including the Association's investment consultant and then applied to the Associations asset allocation policy portfolio. In 2005 and 2006, the Retirement Board elected to maintain the assumed rate of earnings at 8.25% for the up-coming fiscal year, a rate acceptable by the actuary, in part because the active management strategy of the Association, including the application of the Alpha Engine (herein defined) strategy, as described below, historically yielded rates of earnings higher than the rates recommended by the Actuary. See "– Historical Investment Return". The use of the Alpha Engine has also subjected the Association to certain greater investment risks. See "– Amaranth Investment Loss" below. The Association diversifies the risks associated with such investments by diversifying the number of fund managers used by the Association and the types of strategies employed by such managers.

Historical Investment Return. The historical annual net investment return on the market value of the Association's assets was 14.7% for the year ended June 30, 2006, 16.6% for the three years then ended, 9.5% for the five years then ended and 9.8% for the ten years then ended. This compares to the 8.25% actuarial assumed rate of return that the Association's actuary uses to calculate the normal

Employer and employee contribution rates and the UAAL on a year-to-year basis (which is done by projecting into the future a variety of estimates, including how much will be earned on the assets of the Association in future years). On July 6, 2006, the Retirement Board reaffirmed and approved the continued use of an assumption of an 8.25% return on plan assets of the Association for purposes of calculating normal Employer and employee annual contributions and UAAL in Fiscal Year 2007-08.

Amaranth Investment Loss. In September 2006 one of the Association's hedge fund investments, Amaranth Advisors LLC ("Amaranth"), reported a substantial loss. Amaranth informed the Association that the fund experienced a loss in the original value of the investment of approximately $82.2 million, resulting a net fund value of approximately $90 million. While the loss is expected to have a minimal impact on the Association's investment returns and retirement program, the Board of Retirement announced on October 19, 2006 that it is investigating potential legal action against Amaranth regarding this investment. Following the report of Amaranth's losses, Standard & Poor's issued a release stating that the loss would not affect the Association's "AA+" credit rating. The County does not expect the loss associated with its Amaranth investment and the resulting impact on the rate of earnings of the Association's assets to materially impact the County's future annual financial obligations with respect to its share of Employer Contributions.

Absolute Return Funds and Hedge Funds. The Association's diversified investment strategy includes the use of absolute return funds and hedge funds. As of September 30, 2006, the 24% target portfolio allocation for U.S. Equity was split between small and large capitalization stocks. Approximately 4% of the target portfolio allocation was for small capitalization stocks and 20% was allocated to large capitalization stocks. For the large capitalization stock allocation, the Association uses an internally managed strategy that uses swap contracts on the Standard & Poor's 500 index ("S&P 500 Index") to replicate the return generated by U.S. large capitalization stocks together with investments in absolute return funds and hedge funds that, in the aggregate, seeks to achieve returns higher than the S&P 500 Index. The absolute return fund and hedge fund investments strategy are referred to by the Association as the "Alpha Engine." There is no standard definition of what constitutes a hedge fund. Using nomenclature that is consistent with peer funds, the Association considers absolute return funds as managers that tend to exhibit low volatility with the aim of market neutrality. Also consistent with peer funds, the Association considers hedge funds as managers that tend to employ higher volatility strategies, have lock-up periods, and may or may not be registered with the Securities and Exchange Commission ("SEC") under the Securities Act of 1933, as amended (the "Securities Act"). Hedge funds not registered under the Securities Act typically issue their securities in "private offerings" and are not required to make periodic reports under the Securities and Exchange Act of 1934, as amended. As of September 30, 2006 there was approximately $1.4 billion net notional exposure, in the S&P 500 via futures and swap contracts with a number of counterparties. Currently, approximately $71.9 million, or 5% of the Alpha Engine, is held in cash for quarterly swap settlements. The market value of the eleven hedge and absolute return fund investments in the Alpha Engine was approximately $1.304.3 billion, or 17.3% of the total market value of the portfolio. The four hedge fund investments in the Alpha Engine were valued at approximately $484.1 million, or 6.4% of the total market value of the portfolio and the seven absolute return fund investments were valued at $820.1 million, or 10.9% of the total market value of the portfolio. The Association identifies five of the eleven funds in the Alpha Engine (four hedge funds and one absolute return fund), or $623.2 million, as higher volatility funds. The remaining six funds, or $681.1 million, are classified by the Association as lower volatility funds. At the aggregate level, volatility is diversified and controlled. The volatility of the Alpha Engine is maintained below 3%, which is consistent with other active S&P implementations. In addition, the Association identifies the four hedge fund investments as funds without full position transparency. The Retirement Board and Association's staff are taking several steps, including reviewing the use of hedge and absolute return funds, to ensure that the Association's portfolio continues to be managed prudently.

Pension Obligation Bonds

Introduction. The County has issued taxable pension obligation bonds ("POBs") and transferred the proceeds to the Association to reduce the UAAL. Under California law, the obligation to fund the UAAL by making actuarially required contributions is an obligation imposed by law. The effect of issuance of POBs is to refinance that obligation and convert it from an obligation to make actuarially required contributions to an obligation to make interest and principal payments on bonds which are sold to the public.

County Pension Obligation Bonds. In February 1994, the County issued $430,430,000 in principal amount of POBs (the "1994 POBs") and in October 2002 the County issued an additional $737,340,000 in principal amount of POBs (the "2002 POBs"), in part to refund a portion of the 1994 POBs. In June 2004, the County issued $454,112,915.70 in principal amount of POBs (the "2004 POBs"). The County has contributed to the Association an aggregate amount of $1,428,500,000 from the issuance of the 1994 POBs, the 2002 POBs and the 2004 POBs to reduce the UAAL. As of June 30, 2006, the County has POBs outstanding in the aggregate principal amount of $1.191 billion (which amount does not include the 1994 POBs subject to the escrow and pledge of funds described under the caption "County Financial Information – San Diego County Employees Retirement Association – Pension Obligation Bonds – Escrow and Pledge of Funds for 1994 POBs" herein). The County may, from time to time, finance all or a portion of the UAAL through the additional issuances of POBs.

Swaps. The County has entered into swap agreements in connection with the 2002 POBs with Citibank, N.A. New York ("Citibank") and Morgan Stanley Capital Services Inc. ("Morgan") (collectively, the "Swap Providers"). The County entered into interest rate swaps to attain a "synthetic" fixed interest rate on a portion of the underlying POBs, which provided for variable interest rates, at a cost expected by the County to be less than rates associated with fixed-rate obligations at the time the related POBs were issued. See Appendix B – "County of San Diego Audited Financial Statements for the Fiscal Year Ended June 30, 2005" Note 4(J) attached to the Official Statement. Except in the event of an early swap termination, the notional amounts set forth in the table below are amortized in accordance with the scheduled reductions for the related POBs.

Table 12 below sets forth information regarding the County's interest rate swaps with respect to a portion of its 2002 POBs as of the date hereof.

TABLE 12

INTEREST RATE SWAPS

Initial and Current Notional Amount Covered by Swaps	Effective Date	Fixed Rate Paid by County	Variable Rate Received by County	Current Ratings of Swap Providers	Termination Date
$263 million[1]	9/17/02	5.30%	4.98%[2]	Aaa/AA/AA+[1] [3]	2/15/31
$142 million[4]	9/17/02	5.30%	4.98%[2]	Aa3/A+/AA-[3] [4]	2/15/31

(1) The counterparty is Citibank, N.A.
(2) Variable rate received by the County is a variable rate based on the One-Month LIBOR, which as of October 11, 2006 was 5.32%. The actual rate received is the One-Month LIBOR average rate for the six months preceding the payment dates of February 15 and August 15 over the life of the swap. As of August 15, 2006, the average One-Month LIBOR rate for the preceding six months was 4.98%.
(3) Ratings of Moody's Investors Service, Standard & Poor's Ratings Service and Fitch Ratings, respectively.
(4) The counterparty is Morgan Stanley Capital Services Inc.

Scheduled payments made to the County by the Swap Providers are on a parity with the respective series of POBs to which they relate. The County's rights and obligations under the swaps do not alter the County's obligation to pay the principal of, premium, if any, and interest on the respective POBs. If a Swap Provider defaults on its payment obligations under its respective swap agreement, the swap may terminate and, depending on market conditions, a termination payment (which could be substantial) may be due from the County. The County would then potentially have to pay any prospective increases in the variable interest rates payable on that portion of its POBs related to the swap.

Escrow and Pledge of Funds for 1994 POBs. On September 27, 2004, the County deposited with BNY Western Trust Company approximately $63.5 million (the "Deposit"), which was invested in an Investment Agreement (the "Investment Agreement") entered into by the Trustee and an obligor. The obligations of the obligor under the Investment Agreement are guaranteed by American International Group, Inc. ("AIG"), which has been assigned long-term credit ratings from Moody's Investors Service and Standard & Poor's Ratings Services of "Aa2" and "AA," respectively. Under the Investment Agreement, the obligor made payments to the BNY Western Trust Company in July of each of 2005 and 2006, and will make such payments in July 2007, in amounts which will be sufficient to meet the County's remaining annual payment obligations to a counterparty under a Debt Service Forward Sale Agreement (the "Forward Agreement") currently in effect for the 1994 POBs until the final maturity of the 1994 POBs on August 15, 2007. In exchange for the County's annual payments, the Forward Agreement requires the counterparty thereto to deposit securities (which must be non-callable obligations issued or guaranteed by the United States of America or certain instrumentalities or agencies of the United States of America) into the Bond Fund relating to the 1994 POBs, the cash flows of which are sufficient to pay each scheduled payment of principal of and interest on the 1994 POBs during the applicable fiscal year. The 1994 POBs will remain outstanding until their regularly scheduled maturities. If the obligor under the Investment Agreement and AIG under its related guaranty, or the counterparty to the Forward Agreement defaults in its respective obligations for any reason, the County remains obligated to make any affected payment of principal of and interest on the 1994 POBs. The 1994 POBs will remain a liability of the County until they are no longer outstanding.

Pension Related Payments and Obligations

Payments. Table 13 below sets forth the historical and estimated Employer Contributions, Employer Offsets and POB debt service for Fiscal Years 2002 through 2015. The estimates contained in this table, and the related assumptions, are "forward-looking" in nature and are not to be construed as representations of fact or representations that in fact the various estimates shown will be the correct amounts for the years indicated. Rather, these reflect good faith estimates by the County taking into account a variety of assumptions, a number of which are discussed herein. Accordingly, prospective investors are cautioned to review these estimates as general indications of orders of magnitude and not as precise amounts.

TABLE 13

PENSION RELATED PAYMENTS
Fiscal Years Ended June 30, 2002 through 2015
(In Millions)

Fiscal Year	Employer Contributions[3]	Employer Offsets	County Pension Obligation Bonds Debt Service[4]	Total Pension Related Payments	Percent Change Year to Year
2002[1]	$ 5.3	$45.2	$53.8	$104.3	12.9%
2003[1]	12.2	53.9	60.8	126.9	21.6
2004[1]	195.0[5]	55.2	51.9	302.1[6]	138.1
2005[1]	260.0	56.1	56.3	372.4	23.3
2006[1]	243.7	58.8	63.6	366.1	0.0
2007[2][7]	241.0	62.0	70.4	373.4	0.0
2008[2][7]	238.0	65.0	70.0	373.0	0.0
2009[2][7]	224.0	68.0	85.5	377.5	0.0
2010[2][7]	207.0	71.0	86.9	364.9	0.0
2011[2][7]	200.0	74.0	88.2	362.2	0.0
2012[2][7]	200.0	77.0	89.5	366.5	0.0
2013[2][7]	207.0	80.0	90.9	377.9	0.0
2014[2][7]	215.0	83.0	92.4	390.4	0.0
2015[2][7]	224.0	87.0	94.0	405.0	0.0

Source: The Segal Company; County of San Diego.

(1) Actual.

(2) Estimated. The amounts indicated are subject to the same assumptions as set forth in footnotes (1) through (4) to the "Prospective Funding Status of the Association" table herein.

(3) Contribution amounts reflect the aggregate contribution amount of all Employers and not only that of the County. The County General Fund share of Employer Contributions and Employer Offsets are estimated to be 92% based on the estimated relative percentage of payroll of the County General Fund for Fiscal Years 2003-04 and 2004-05. See "County Financial Information – San Diego County Employees Retirement Association – General" herein.

(4) A portion of the 2002 POBs in the principal amount of $100,000,000 (the "Variable 2002 POBs") currently bears interest at a variable rate. In projecting debt service for fiscal years 2006 to 2015, the County has made the following assumptions with respect to the variable interest rate for the Variable 2002 POBs. $405,125,000 principal amount of the Variable 2002 POBs has been synthetically fixed pursuant to a swap agreement between the County and the Swap Providers, and the balance of the Variable 2002 POBs are not subject to such agreement. The County has assumed that those Variable 2002 POBs subject to the swap agreement will bear interest at 5.30% during the indicated fiscal years, and that Swap Providers will perform their obligations under the swap agreement in all material respects. For a description of the swap agreement with respect to the Variable 2002 POBs, see "County Financial Information – San Diego County Employees Retirement Association – Pension Obligation Bonds – Swaps" herein. The balance of the Variable 2002 POBs are assumed to bear interest at a variable rate of 6.18%, which consists of the historical average rate from March 2005 through March 2006 of 3.87%, plus an additional 2.00% contingency amount and an additional 0.31% to account for ongoing broker-dealer fees. The County converted the Variable 2004 POBs to a fixed rate of interest on August 15, 2006. On September 27, 2004, the County established an Escrow and Pledge Fund with respect to the 1994 POBs. See "County Financial Information – San Diego County Employees Retirement Association – Pension Obligation Bonds – Escrow and Pledge of Funds for 1994 POBs" herein. Accordingly, debt service with respect to the 1994 POBs for Fiscal Years ending after June 30, 2005 is not reflected in this table.

(5) See footnote (3) to the "Historical Funding Status" table herein.

(6) Increased total pension payments in 2004 are primarily a result of the implementation of enhanced benefit levels and investment results that were below the actuarially assumed rate of 8.25%. See "County Financial Information – San Diego County Employees Retirement Association – Funding Status of the Association – Impacts to UAAL" herein. Increased total pension payments in 2005 are primarily a result of changes in actuarial assumptions for the valuation as of June 30, 2003 based on an experience study and recognition of smoothed losses.

(7) Estimated; based on data, results and assumptions used in preparation the actuarial valuation as of June 30, 2006.

Obligations. Table 14 below sets forth the historical and estimated UAAL and expected outstanding principal amounts of POBs for the years indicated, assuming no additional POBs are issued and the outstanding POBs mature on their respective amortization schedules. The estimates contained in

this table, and the related assumptions, are "forward-looking" in nature and are not to be construed as representations of fact or representations that in fact the various estimates shown will be the correct amounts for the years indicated. Rather, these reflect good faith estimates by the County taking into account a variety of assumptions, a number of which are discussed herein. Accordingly, prospective investors are cautioned to review these estimates as general indications of orders of magnitude and not as precise amounts.

TABLE 14

COUNTY PENSION RELATED OBLIGATIONS
Fiscal Years Ended June 30, 2002 through 2013
(In Millions)

Fiscal Year	UAAL[5]	Outstanding Pension Obligation Bonds[1]	Total Outstanding Obligations
2002	905.1[2]	282.9	1,188.0
2003	1,435.4	980.8	2,416.2
2004	1,202.7	1,269.0	2,471.7
2005	1,378.0	1,193.6	2,571.6
2006	1,232.0	1,197.2[4]	2,429.2
2007	915.0[3]	1,191.3[4]	2,106.3
2008	567.0[3]	1,186.7[4]	1,753.7
2009	350.0[3]	1,165.9[4]	1,515.9
2010	220.0[3]	1,143.0[4]	1,363.0
2011	176.0[3]	1,117.7[4]	1,293.7
2012	148.0[3]	1,089.9[4]	1,237.9
2013	120.0[3]	1,073.9[4]	1,193.9

Source: The Segal Company; County of San Diego.

(1) On September 27, 2004, the County established an Escrow and Pledge Fund with respect to the 1994 POBs. See "County Financial Information – San Diego County Employees Retirement Association – Pension Obligation Bonds – Escrow and Pledge of Funds for 1994 POBs" herein. Accordingly, outstanding principal balances with respect to the 1994 POBs for Fiscal Years ending after June 30, 2004 are not reflected in this table.

(2) See footnote (3) to the "Historical Funding Status" table herein.

(3) Estimated; based on data, results and assumptions used in preparation of the actuarial valuation as of June 30, 2006.

(4) Includes a portion of the 2004 POBs issued as capital appreciation bonds (the "CABs"), for which interest accretes semiannually on February 15 and August 15, but is not payable until the final maturity of each respective capital appreciation bond. The initial total issuance amount of the CABs was $64,927,915.70, which will accrete to a total maturity value of $100,170,000 over the respective maturity dates commencing August 15, 2009 and ending August 15, 2015.

STAR COLA Benefits

STAR COLA Benefits. The STAR COLA benefits provide retirees with additional cost-of-living adjustments. The Retirement Board's STAR COLA policy preserves 80% of a retiree's purchasing power calculated against when that retiree retired. The Retirement Law does not require the Association to provide any STAR COLA payments. In addition, in the opinion of County Counsel, the County has not entered into any collective bargaining agreements or other arrangements that require the County or the Association to maintain STAR COLA benefits. Therefore, in the view of County Counsel, the Association's payments of STAR COLA benefits is an unvested benefit which can be cancelled at any time and for any reason by the Association.

STAR COLA Reserve; Historical Payments. Since it authorized the payment of STAR COLA benefits in 1998, the Retirement Board's historical practice has maintained an amount in the STAR COLA reserve that the Association's actuary estimates will be necessary to cover the costs of the STAR COLA benefits for current eligible retirees for five years. Each year, the Association's actuary prepares an estimate of the amounts necessary to be contributed to the STAR COLA reserve to meet this targeted level. For a discussion on actions of the Retirement Board with respect to the transfer of certain Excess Earnings to the Health Reserve and the STAR COLA reserve, see "County Financial Information – San Diego County Employees Retirement Association – Transfers of Investment Earnings by the Association" herein. As of June 30, 2006, approximately $54.4 million was on deposit in the STAR COLA reserve.

Table 15 below sets forth the amounts paid by the Association to retirees out of the STAR COLA reserve since 2000. The Association does not track either the Employer or the departments or funds of any Employer from which retired personnel receiving STAR COLA benefits, when in active service, were paid.

TABLE 15

PAYMENTS FROM STAR COLA RESERVE
Fiscal Years Ended June 30, 2000 through 2006

Fiscal Year Ending June 30	Payments from STAR COLA Reserve (in millions)
2000	$ 9.2
2001	8.2
2002	8.1
2003	7.2
2004	11.3
2005	11.0
2006	10.7

Post-Retirement Healthcare Benefits

General. The Association offers to its retirees a health benefit to offset or reimburse the cost of medical insurance premiums. A variety of health care and dental plans with varying providers and levels of premiums are sponsored by the Association. Once a retiree elects a particular health care or dental plan, the amount of the premium is deducted from the retiree's monthly retirement check. Alternatively, retirees may be reimbursed for health insurance premiums of non-Association sponsored plans. With respect to those retirees who have 10 or more years of service credit before retirement, the Association currently offers a monthly medical allowance that ranges from $200 to $400 depending on the years of service credit and Medicare eligibility. With respect to those retirees who are Medicare eligible, the maximum monthly medical allowance is reduced to $300, but the Association reimburses such retirees for their Medicare Part B premium, which for 2006 is $88.50.

Nature of the Post-Retirement Health Care Payments. The Retirement Law does not require the Association to provide any post-retirement health care payments. In addition, in the opinion of County Counsel, the County has not entered into any collective bargaining agreements or other arrangements that require the County or the Association to maintain post-retirement health care benefits (although some members of the Association have stated that the County did promise retirees such benefits, which the County disputes). Therefore, in the view of County Counsel, the Association's payment of post-retirement health care benefits is an unvested benefit which can be cancelled at any time and for any reason by the Association. Nonetheless, the Association has continuously provided post-retirement health care benefits for many years.

Accounting Considerations. Currently, governmental agencies that are on a pay-as-you-go basis, such as the County, are not required to accrue for post-employment healthcare benefits in the same manner as they accrue for pension benefits. In 2004, the Governmental Accounting Standards Board ("GASB") issued two statements that address other post-employment benefits ("OPEB"), which are defined to include post retirement health care benefits. GASB Statement No. 43, Financial Reporting for Post-employment Benefits Plans Other Than Pension Plans ("GASB 43"), establishes financial reporting standards for OPEB in a manner similar to those currently in effect for pension benefits. The provisions of GASB 43, which focuses on the entity that administers such benefits (currently the Association) and requires an actuarial valuation to determine the funded status of benefits accrued, must be implemented by the Association no later than the Fiscal Year ending June 30, 2007. The Association has taken steps to inform itself, its members, the County and the general public about funding healthcare and cost-of-living benefits. In connection therewith, the Association held three retiree healthcare workshops between December 2005 and March 2006. One of the workshops was led by the Actuary; another specifically focused on benefits that could be available through a voluntary employee benefits association and other trust options.

The Actuarial Valuation and Review of Postretirement Welfare Benefits as of June 30, 2005, dated November 18, 2005 (the "2005 Postretirement Benefits Valuation"), delivered to the Association with respect to its post-retirement healthcare benefits does not provide disclosure information that may be required under GASB 43. In particular, the appropriate interest rate for liabilities will need to be determined. It may be determined that the interest rate used to calculate GASB 43 liabilities is lower than the rate used in the 2005 Postretirement Benefits Valuation, in which case the actuarial accrued liabilities would be higher than reported.

The 2005 Postretirement Benefits Valuation indicated that the actuarial accrued liability for post retirement health care benefits, whether vested or not vested, was approximately $639.5 million, approximately 16.6% above the actuarial accrued liability of $548.4 million as of June 30, 2003, the date of the last actuarial valuation for post-retirement benefits. Approximately $217.4 million was on deposit in the Health Reserve as of June 30, 2006. See " – Health Reserve" herein.

GASB Statement No. 45, Accounting and Financial Reporting by Employers for Post-employment Benefits Other Than Pensions ("GASB 45"), establishes financial reporting standards designed to measure, recognize and disclose OPEB costs. GASB 45 requires substantially different financial accounting of OPEB, or any post-employment benefits that are provided separately from a pension plan, such as post-employment healthcare. For the County, the affected benefits include the post-employment health care benefits paid by the Association. GASB 45 seeks to associate the costs of the OPEB with the periods in which the employee services are rendered in exchange for the OPEB. Currently, however, OPEB is accounted for by the County on a pay-as-you-go basis, which does not require the accrual of costs associated with OPEB that are attributable to current and past fiscal years.

The core requirement of GASB 45 is that at least biennially an actuarial analysis must be prepared with respect to projected benefits ("Plan Liabilities"); against this would be measured the actuarially determined value of the related assets (the "Plan Assets"). To the extent that Plan Liabilities exceeded Plan Assets, then similar to the actuarial and accounting practices for pension plan liabilities, the difference would be amortized over a period which could be up to 30 years. The method of financial reporting for OPEB costs would be similar to financial reporting for pension plan normal costs and UAAL.

The requirements that GASB 45 imposes on the County only affect the County's financial statements and would not impose any requirements regarding the funding of any OPEB plans. The County is required to include the disclosure required by the Statement beginning with the fiscal year ending June 30, 2008. The UAAL of OPEB has not been determined, nor have actuarial contribution rates been established to fund the UAAL. The County's ability to fund OPEB on an accrual basis in the future is unknown, but the liability is expected to be substantial. At this time, the County does not intend to implement GASB 45 prior to the issuance of financing statements for the fiscal year ending June 30, 2008.

Source of Benefit Payment. The Retirement Law authorizes a mechanism for the payment of post-retirement health care benefit costs pursuant to which a portion of the Employers' contributions are applied to the payment of these post-retirement health care benefits and the amounts of those contributions are credited to the Employers as part of their current-year contributions. The Employers currently designate up to 25% of their respective normal cost and employer offset annual contributions to the payment of the monthly medical allowance and Medicare Part B premium reimbursement. Upon receiving the Employers' contributions, the Association transfers from the Health Reserve an amount equal to that contributed by the Employers to the Association's valuation assets as a credit for the Employers' current-year contributions.

Health Reserve. The Association has transferred varying annual amounts to the Health Reserve from Excess Earnings, as described above under "County Financial Information – San Diego County Employees Retirement Association – Transfers of Investment Earnings by the Association." For a discussion on actions of the Retirement Board with respect to the transfer of certain Excess Earnings to the Health Reserve and the STAR COLA reserve, see "County Financial Information – San Diego County Employees Retirement Association – Transfers of Investment Earnings by the Association" herein. As of June 30, 2006, approximately $217.4 million was on deposit in the Health Reserve.

Action by the County Board. On December 5, 2006, the County Board adopted a resolution that urges the Retirement Board to eliminate the subsidy that the Association contributes to the health insurance premiums of retired safety and non-safety members who are entitled to the highest vested retirement payments, commonly known as Tier A members. The Board action directs the Chief Financial Officer of the County to designate the County's contribution to the Association for retiree health care payments if (a) by June 30, 2007, the Association has adopted and continues to maintain a policy limiting health care allowance payments to certain members (Tier I and Tier II) only and (b) except as provided in (a) above, the Association continues the provision of its retiree health allowance program relating to qualifications for benefits and maximum payments at levels no greater than what is authorized as of December 5, 2006. If the Retirement Board does not accept the recommendations made by the County Board, the County would no longer contribute to retiree health benefits.

The County's preliminary estimates indicate that limiting these benefits only to Tier I and Tier II members would reduce the annual Employer Contributions from an estimated $60-70 million per year to approximately $20-30 million per year, thereby reducing the total estimated annual Employer

Contributions over 20 years from $1.8 billion to $637 million and reducing the County's actuarial accrued liability for retiree health benefits from approximately $640 million to approximately $290 million.

Payments. Table 16 below sets forth the amounts for each of the ten years ended June 30, 2006 that the Association has paid to its members from the Health Reserve:

TABLE 16

PAYMENTS FROM HEALTH RESERVE
Fiscal Years Ended June 30, 1997 through 2006

Fiscal Year	Payments from Health Reserve (in millions)
1997	$ 6.5
1998	6.6
1999	8.0
2000	9.0
2001	10.8
2002	14.3[1]
2003	20.0[1]
2004	26.4[1]
2005	32.6[1]
2006	32.9[1]

[1] A portion of the indicated amounts are allocated to the administrative expenses related to the provision of the post-retirement health care benefits.

According to cash flow projections conducted by the Actuary, reimbursements to Association members from the Health Reserve are projected to increase by almost 90% over the next 10 years, reaching approximately $61.5 million in 2015. The Association does not track either the Employer or the departments or funds of any Employer from which retired personnel receiving post-retirement health care benefits, when in active service, were paid.

Litigation Relating to the Association

Amortization Litigation. Three residents of the County, two of whom are retired members of the Association, brought an amended complaint against the County and the Association seeking, among other things, a judicial determination that the Retirement Law does not permit the negative amortization alleged included in the first three years of the Retirement Board's 20-year layered fixed amortization policy, monetary damages against the County, without borrowing, payable to the Association, for the amount of unfunded liability of the retirement system that existed on June 30, 1975, with interest, that was not "fully paid" as of June 30, 2005, an injunction prohibiting the Association from adopting any actuarial method or practice that includes negative amortization of the retirement system's unfunded liability, and a judicial determination that the Retirement Board violated Section 17(b) of Article XVI of the State Constitution by allegedly giving precedence to minimizing the County's annual Employer Contribution rather than assuring the sufficiency of the assets of the retirement system to deliver the retirement and other statutorily-authorized benefits that may be provided to the Association's members under the Retirement Law. The trial court sustained the Association's demurrer in connection with the initial complaint.

The amortization policy approved by the Retirement Board is within the 30 year amortization limit set forth under the Retirement Law. In addition, Section 17 of Article XVI of the State Constitution provides retirement boards with "sole and exclusive power to provide for actuarial service". The County has transferred to the Association over the last two Fiscal Years an aggregate $65 million above the County's annual required contribution that has offset any effect of negative amortization. See "County Financial Information – San Diego County Employees Retirement Association – General Funding Practices of the Association" herein.

The Superior Court dismissed the plaintiffs' complaint on September 15, 2006 "without prejudice," which permits the plaintiffs to file the same or a similar action at a later date. The County, however, has not been informed of any intent by the plaintiffs to refile the complaint.

Risk Management

The County is required to obtain and maintain public liability insurance and workers' compensation insurance under various types of its financing lease obligations. These financing leases generally require public liability insurance to be issued by a responsible carrier or be in the form of self-insurance or self-funding to cover claims for damages including death, personal injury, bodily injury, or property damage arising from operations involving the facilities covered by such leases, affording protection with a combined single limit loss of not less than $5,000,000 per occurrence with respect to bodily injury, death or property damage liability. In addition, these financing leases generally require the County to obtain and maintain workers' compensation insurance issued by a responsible carrier or in the form of self-insurance or self-funding to cover all persons employed by the County in connection with the facilities covered by such leases and to cover full liability for compensation under the act requiring workers' compensation. Any self-insurance or self-funding for these risks is subject to certain conditions, including, but not limited to, providing evidence of self-insurance and annual certification to the trustee with respect to such financing leases by an authorized representative of the County's risk management division or an independent insurance consultant of the sufficiency of coverage. Appropriation of such funds as may be necessary for self-funding, are made by the County.

The County operates a Risk Management Program, whereby it is self-insured for premises liability, medical malpractice, errors and omissions, false arrest, forgery, general liability and workers' compensation. The County purchases insurance for property damage, certain casualty claims, public officials bond, employee dishonesty, faithful performance, volunteers, airport comprehensive, and loss of money and securities based upon site locations. Settlements in the areas covered have not exceeded insurance coverage for each of the past three fiscal years. The County allocated the cost of providing claims service to all its operating funds as a "premium" charge expressed as a percentage of payroll. In accordance with Government Accounting Standards Board Statement 10, "Accounting and Financial Reporting for Risk Financing and Relating Insurance Items," the County established two Internal Service Funds, the Public Service Liability Fund and the Worker's Compensation Fund (collectively, the "ISF") to report all of its uninsured risk management activities. Risk management liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. Actuarial evaluations were obtained which determine estimates of known and projected public liability and workers compensation claim liabilities. At June 30, 2006, the amount of these liabilities, including an estimate for claims incurred but not reported and allocated and unallocated loss adjustment expenses was estimated at $122.3 million, including $31 million in public liability and $91.3 million in workers' compensation. As of June 30, 2006, the ISF had available cash in the approximate amount of $86.4 million. The estimate of claims liabilities were recorded in the ISF. In Fiscal Year 2005-06, the County deposited $2 million into the Worker's Compensation Fund and appropriated sufficient funds to pay anticipated claims. For Fiscal Year 2006-07, the County deposited $4.0 million into the Workers' Compensation Fund in addition to appropriating sufficient funds to pay anticipated claims. The County's 2006-07 Adopted Budget provides

for a deposit of $4.0 million into the Workers' Compensation Fund in addition to appropriating sufficient funds to pay anticipated claims.

Litigation

CMS Litigation. Section 17000 of the California Welfare & Institutions Code requires the County to provide relief and support to all incompetent, poor and indigent persons, and those incapacitated by age, disease, or accident, who are lawful residents in the County, if those person are not supported or relieved by some other means. The County satisfies its Section 17000 obligation to provide medical care through its County Medical Services (the "CMS") program. Persons who are eligible to receive medical care services under the CMS program are those who have net income below a certain level designated by the CMS program (the "Eligibility Level") and are not otherwise eligible for medical care services from the State or Federal Government. The County pays for medically necessary care received by individuals who are eligible and have qualified for the CMS program.

The County was sued by five individuals who were denied eligibility under the CMS program because their respective net incomes exceeded the Eligibility Level. Plaintiffs sought to invalidate the income eligibility requirements of the CMS program and to compel the County to implement new eligibility requirements. Class action status was requested by the plaintiffs and granted by the court. The class includes all individuals whose applications for CMS were denied on or after January 24, 2004 because their net income exceeded the Eligibility Level.

As a result of the litigation, the County Board of Supervisors, on December 6, 2005, adopted new income standards for determining eligibility for the CMS program. Pursuant to the court's order, the new standards are retroactive to January 24, 2004. On April 7, 2006, the court approved the new income eligibility standards adopted by the County and approved the County's plan of implementation for notifying class members who were denied eligibility on or after January 24, 2004, of the procedure for filing claims to obtain reimbursement of amounts paid for medical services. The plaintiffs have filed a timely appeal of the court's determination. The new standards became effective November 30, 2005, and will result in an increased number of applicants who will be eligible for benefits from the CMS program and an increase in the overall cost to the County in administering the CMS program. The County budgeted $66.3 million for the provision of these benefits (without regard to any new eligibility requirements) in the 2005-06 Adopted Budget and provided for $72.3 million for the provision of these benefits (accounting for new eligibility requirements) in the 2006-07 Adopted Budget. Additional costs incurred in Fiscal Year 2005-06 will be paid from existing appropriations.

The County currently expects the newly-implemented standards to result in an approximate $4 million a year increase in expenditures. However, the number of additional persons who may be eligible for benefits under the new standards will not be fully known until after the new standards have been fully implemented and in effect for at least one fiscal year, and the amount of increased expenditures may be affected by the further appeals described above. Because the CMS program is not fully funded on an on-going basis by the State or Federal Government, the County's general purpose revenues may be used to pay for any cost increases in providing these benefits. See "County Financial Information – County's 2006-07 Adopted Budget and the Operational Plan" for a description of the County's general purpose revenues.

Wrongful Conviction Litigation. Ken Marsh filed a claim against the County of San Diego seeking damages in excess of $50,000,000. He alleged that the County and some of its employees conspired with employees of Children's Hospital to wrongfully convict him of the murder of 2 ½ year old Phillip Buell. The claim was rejected and on August 9, 2005, Marsh filed a complaint for damages in the United States District Court, Southern District of California, Case No. 05cv1568 WQH(NLS). The trial

for this case is expected to commence in January 2008. In the County's opinion, to prevail in the civil action Marsh must prove that a County pathologist and deputy coroner lied about Phillip's cause of death in concert with physicians at Children's Hospital, and then committed perjury during the criminal trial to secure the conviction of Marsh. While the outcome of any litigation is uncertain, the County does not expect any facts will be uncovered during the civil case to establish liability and anticipates that the matter will be resolved favorably by the trial judge on motion. The County anticipates that any impact of this litigation will not adversely affect the ability of the County to pay its obligations as and when due.

Short-Term Borrowing

On July 3, 2006, the County issued its 2006-07 Tax and Revenue Anticipation Notes (the "2006 TRANs") on behalf of the County and certain school districts within the County in an aggregate principal amount of $273,490,000, of which $220,000,000 represent notes issued by the County. The 2006 TRANs mature on July 27, 2007. The 2006 TRANs were issued for the purpose of financing seasonal cash flow requirements for general fund expenditures.

During the 1990s, the County has utilized Temporary Transfers from time to time for various purposes, including the finance of County library programs and other County programs. Should the County find it necessary to use a Temporary Transfer, then such borrowing, pursuant to the California Constitution, must be repaid from the first County revenues received thereafter before any other obligation, including the Notes, is paid from such revenues.

General Obligation Debt, Pension Obligation Bonds, Lease Obligations and Long-Term Loans

The County has no outstanding general obligation bonds. As of June 30, 2006, the County has POBs outstanding in the aggregate principal amount of $1.191 billion (which amount does not include the 1994 POBs subject to the escrow and pledge of funds described under the caption "County Financial Information – San Diego County Employees Retirement Association – Pension Obligation Bonds – Escrow and Pledge of Funds for 1994 POBs" herein). Starting with the financing of the El Cajon Administrative Building in 1955, the County has made use of various lease arrangements with joint powers authorities, a nonprofit corporation, a redevelopment agency and private parties to finance capital project needs. Under these arrangements, the financing entity usually constructs or acquires capital assets with the proceeds of lease revenue bonds or certificates of participation and then leases the asset or assets to the County. The annual long-term lease payments and annual debt service payments on the POBs of the County aggregated to approximately $120.5 million for Fiscal Year 2005-06 and will aggregate to approximately $120.8 million for Fiscal Year 2006-07. As of June 30, 2006, there was approximately $1.58 billion aggregate principal amount of long-term general fund obligations outstanding. In addition, the County has approximately $1,048,981 of capital leases outstanding as of June 30, 2006. The debt service on all such capital leases was approximately $1,293,665 for Fiscal Year 2005-06 and will aggregate to approximately $713,675 for Fiscal Year 2006-07.

Table 17 below sets forth a summary of long-term bonded obligations payable from the General Fund:

TABLE 17

COUNTY OF SAN DIEGO
SUMMARY OF LONG-TERM BONDED OBLIGATIONS
PAYABLE FROM THE GENERAL FUND
As of June 30, 2006
(In Thousands)

	Interest Rates	Final Maturity Dates	Original Principal Amounts	Principal Amounts Outstanding
Certificates of Participation:				
San Diego County Capital Asset Leasing Corporation (SANCAL):				
1993 Master Refunding, issued May 1993	2.50-5.625%	2012	$ 203,400	$ 57,600
1997 Central Jail Refunding, issued July 1997	4.00-5.42	2025	80,675	65,415
1998 Downtown Courthouse Refunding, issued December 1998	4.00-4.94	2023	73,115	51,905
1999 East Mesa Refunding, issued September 1999	3.60-4.75	2009	15,010	6,780
2000 Information Technology, issued May 2000	4.50-5.125	2010	51,620	23,715
2002 Motorola, issued March 2002	2.00-5.00	2010	26,060	15,320
2005 Edgemoor & RCS Refunding, issued February 2005	3.00-5.00	2030	112,395	107,745
2005 North and East County Justice Facilities Refunding, issued September 2005	3.25-5.00	2020	28,210	28,210
Total SANCAL			$ 590,485	$ 356,690
San Diego Regional Building Authority (SDRBA):				
2001 MTS Tower Refunding, issued September 2001	2.15-5.25%	2019	$ 36,960	$ 30,845
Total SDRBA			$ 36,960	$ 30,845
Total Certificates of Participation			$ 627,445	$ 387,535
Third Party Financing Leases:				
Others, various beginning dates from March 1991 to present	4.24-8.00%	2006-08	$ 8,705	$ 1,048
Total Third Party Financing Leases			$ 8,705	$ 1,048
Taxable Pension Obligation Bonds:				
Taxable Pension Obligation Bonds, Series A, issued February 1994	6.38-6.60%	2008	$ 430,430	$ 39,830
Taxable Pension Obligation Bonds, issued September 2002				
Series A	3.88-4.95	2015	132,215	132,215
Series B1, B2, B3, B4	Variable Rate	2032	505,125	505,125
Series C (PINES)	6.13	2032	100,000	100,000
Taxable Pension Obligation Bonds, issued June 2004				
Series A	3.28-5.865	2022	241,360	241,360
Series B1, B2	Variable Rate	2024	147,825	147,825
Series C	4.66-5.76	2015	64,928	64,928
Total Taxable Pension Obligation Bonds			$1,621,883	$1,231,283
Unamortized Issuance Premium[3]			$ 8,033	$ 7,257
Unamortized Issuance Discount[3]			(25,588)	(22,602)
Unamortized Deferred Amount on Refunding[3]			(62,878)	(48,583)
Total General Fund Long Term Bonded Obligations			$2,177,600	$1,555,938

Source: The County.

SAN DIEGO COUNTY INVESTMENT POOL

General

Pursuant to a resolution adopted July 8, 1958, the Board of Supervisors delegated to the Treasurer the authority to invest and reinvest funds of the County. Applicable law limits this delegation of authority to a one-year period and must be renewed annually by action of the Board of Supervisors. In addition to funds of the County (and the various departments in the County, such as Public Works and Public Administration), funds of certain local agencies within the County, including school districts in the County, are required under state law to be deposited into County treasury ("Involuntary Depositors"). In addition, certain agencies, including community college districts, invest certain of their funds in the County treasury on a voluntary basis ("Voluntary Depositors" and together with the Involuntary Depositors, the "Depositors"). Deposits made by the County and the various local agencies are commingled in a pooled investment fund (the "Treasury Pool" or the "Pool"). No particular deposits are segregated for separate investment.

Under State law, Depositors in the Pool are permitted to withdraw funds which they have deposited on 30 days notice. The County does not expect that the Pool will encounter liquidity shortfalls based on its current portfolio and investment guidelines or realize any losses that may be required to be allocated among all Depositors in the Pool.

The County has established an Oversight Committee pursuant to State law. The Oversight Committee consists of members appointed from the County Treasurer-Tax Collector, the County Auditor and Controller, a representative appointed by the Board, the County superintendent of schools or his or her designee, a representative selected by a majority of the presiding officers of the governing bodies of the school districts and community college districts in the county, a representative selected by a majority of the presiding officers of the legislative bodies of the special districts in the county that are required or authorized to deposit funds in the County Treasury and up to five other members of the public. The Oversight Committee directs the preparation of an annual audit, which audit may include issues relating to the structure of the investment portfolio and its related risk, to determine the County Treasury's compliance with law.

The Treasury Pool's Portfolio

As of September 30, 2006, the securities in the Treasury Pool had a market value of $3,401,776,853 and a book value of $3,407,340,765, for a net unrealized loss of $5,563,913 of the book value of the Treasury Pool. As of September 30, 2006, the weighted average maturity of the Pool portfolio was approximately 240 days. As of September 30, 2006, 25.7% of the Pool was invested in securities with maturities ranging from 1-30 days, 11.5% of the Pool was invested in securities with maturities ranging from 31-90 days, 19.8% of the Pool was invested in securities with maturities ranging from 91-180 days, 23.3% of the Pool was invested in securities with maturities ranging from 181-365 days, 10.5% of the Pool was invested in securities with maturities ranging from 366 days to 2 years, and 9.4% of the Pool was invested in securities with maturities between 2 and 5 years.

The effective duration for the Treasury Pool was 0.555 years as of September 30, 2006. "Duration" is a measure of the price volatility of the portfolio and reflects an estimate of the projected increase or decrease in the value of the portfolio based upon a decrease or increase in interest rates. A duration of 0.555 means that for every one percent increase in interest rates the market value of the portfolio would decrease by 0.555%.

As of September 30, 2006, approximately 1.85% of the total funds in the Pool were deposited by Voluntary Depositors, such as cities and fire districts, 6.87% by community colleges, 40.86% by the County, and 50.42% by K-12 school districts.

Standard & Poor's, a Division of the McGraw-Hills Companies, Inc. maintains ratings on the Pool's ability to meet its financial commitments of "AAAf" (long-term) and "S1" (short-term volatility). The rating reflects only the view of the rating agency and any explanation of the significance of such rating may be obtained from such rating agency as follows: Standard & Poor's, 55 Water Street, New York, New York 10041.

Investments of the Treasury Pool

Authorized Investments.

Investments of the Pool are placed in those securities authorized by various sections of the California Government Code, which include obligations of the United States Treasury, Agencies of the United States Government, local and State bond issues, bankers acceptances, commercial paper of prime quality, certificates of deposit (both collateralized and negotiable), repurchase and reverse repurchase agreements, medium term corporate notes, shares of beneficial interest in diversified management companies (mutual funds), and asset backed (including mortgage related) and pass-through securities. Generally, investments in repurchase agreements cannot exceed a term of one year and the security underlying the agreement shall be valued at 102% or greater of the funds borrowed against the security and the value of the repurchase agreement shall be adjusted no less than quarterly. In addition, reverse repurchase agreement generally may not exceed 20% of the base value of the portfolio and the term of the agreement may not exceed 92 days. Securities lending transactions are considered reverse repurchase agreements for purposes of this limitation. Base Value is defined as the total cash balance excluding any amounts borrowed (*i.e.*, amounts obtained through selling securities by way of reverse repurchase agreements or other similar borrowing methods).

Legislation which would modify the currently authorized investments and place restrictions on the ability of municipalities to invest in various securities is considered from time to time by the California State Legislature. Therefore, there can be no assurances that the current investments in the Treasury Pool will not vary significantly from the investments described herein.

The Investment Policy.

The County's Investment Policy (the "Investment Policy") (which may be modified, amended, or otherwise changed at any time at the sole discretion of the Treasurer) currently states that the objectives of the Treasurer when investing, reinvesting, purchasing, acquiring, exchanging, selling and managing public funds are as follows: the primary objective is to safeguard the principal of the funds under the Treasurer's control, the secondary objective is to meet the liquidity needs of the Pool Participants, and the third objective is to achieve an investment return on the funds under the control of the Treasurer within the parameters of prudent risk management. The Investment Policy contains a goal that 50% of the Pool should be invested in securities maturing one year or less with the remainder spread over 1-5 years on the yield curve depending on opportunities in the marketplace. With respect to reverse repurchase agreements, the Investment Policy provides for a maximum maturity of 92 days (unless the reverse repurchase agreement includes a written guarantee of a minimum earning or spread for the entire period of such agreement) and a limitation on the total amount of reverse repurchase agreements to 20% of the total investments in the Pool. The Investment Policy states that the purpose of reverse repurchase agreements is to invest the proceeds form the agreement into permissible securities that have the highest short-term credit rating, to supplement the yield on securities owned by the Pool or to provide funds for

the immediate payment of an obligation, and that the maturity of the reverse repurchase agreement and the maturity of the security purchased be the same.

The Investment Policy also authorizes investments in covered call options or put options, which are options on the part of a third party to buy from the Pool a specified security within a finite time at a specified price. Under the Investment Policy, securities subject to covered calls are not to be used for reverse repurchase agreements, cash sufficient to pay for outstanding puts are to be invested in securities maturing on or before the expiration date of the option, the maximum maturity of a covered call option/put option is to be 90 days and not more than 10% of the total investments in the Pool could have options (in contrast to "derivatives") written against them at any one time.

Certain Information Relating to Pool

Table 18 below sets forth information with respect to the Pool as of the close of business September 30, 2006. As described above, a wide range of investments is authorized by state law. Therefore, there can be no assurances that the investments in the Pool will not vary significantly from the investments described herein. In addition, the value of the various investments in the Pool will fluctuate on a daily basis as a result of a multitude of factors, including generally prevailing interest rates and other economic conditions. Therefore, there can be no assurance that the values of the various investments in the Pool will not vary significantly from the values described herein. In addition, the values specified in the following tables were based upon estimates of market values provided to the County by a third party. Accordingly, there can be no assurance that if these securities had been sold on September 30, 2006, the Pool necessarily would have received the values specified. The County has no Pool investments in any corporation that has filed for bankruptcy.

TABLE 18

TREASURER-TAX COLLECTOR
SAN DIEGO COUNTY PORTFOLIO STATISTICS
(AS OF SEPTEMBER 30, 2006)

	Percent of Portfolio	Book Value	Market Price	Accrued Interest	Market Value	Unrealized Gain/(Loss)	Yield to Maturity
Federal Farm Credit Bank Notes	6.79%	$234,000,000	98.77%	$1,094,593	$231,121,856	($2,878,144)	2.47%
Federal Home Loan Bank Notes	11.81	403,017,671	99.53	4,168,383	401,731,876	(1,285,795)	3.97
Federal National Mortgage Association Notes	5.02	172,200,000	99.08	1,334,111	170,620,609	(1,579,391)	3.76
Federal Home Loan Mortgage Corporation Notes	15.28	520,740,625	99.69	6,157,062	519,651,590	(1,089,035)	4.68
Corporate Medium Term Notes	3.03	102,707,127	98.12	889,420	103,029,995	322,868	4.89
Asset Backed Notes	2.67	90,688,017	99.34	699,761	90,895,798	207,781	4.45
Money Market Funds	1.13	38,330,223	100.00	33,990	38,330,223	0	5.17
Repurchase Agreements	5.88	200,000,000	100.00	60,389	200,000,000	0	5.44
Negotiable Certificates of Deposit	24.23	823,822,372	100.13	10,479,940	824,413,827	591,455	5.43
Commercial Paper	24.11	820,143,730	99.44	0	820,290,079	146,349	5.39
Collateralized Certificates of Deposit	0.05	1,691,000	100.00	3,817	1,691,000	0	4.93
Totals for September 2006	100.00%	$3,407,340,765	99.59	$24,921,465	$3,401,776,853	($5,563,913)	4.80
Totals for August 2006	100.00%	$3,584,990,619	99.47	$21,422,428	$3,576,248,748	($8,741,871)	4.78%
Change From Prior Month		($ 177,649,854)	0.12%		($ 174,471,895)	$3,177,958	0.02%
Portfolio Effective Duration	0.555 years						

	Sept 2006 Return	Annualized	Fiscal Year to Date Return	Annualized	Calendar Year to Date Return	Annualized
Book Value	0.396%	4.818%	1.184%	4.695%	3.161%	4.226%
Market Value	0.534%	6.503%	1.713%	6.795%	4.238%	5.666%

CONSTITUTIONAL AND STATUTORY LIMITATIONS ON TAXES, REVENUES AND APPROPRIATIONS

Article XIII A

On June 6, 1978, California voters approved Proposition 13, adding Article XIII A to the California Constitution. Article XIII A, among other things, affects the valuation of real property for the purpose of taxation in that it defines the full cash property value to mean "the county assessor's valuation of real property as shown on the 1975-76 tax bill under 'full cash value,' or thereafter, the appraised value of real property newly constructed, or when a change in ownership has occurred after the 1975 assessment." The full cash value may be adjusted annually to reflect inflation at a rate not to exceed 2% per year, or a reduction in the consumer price index or comparable local data at a rate not to exceed 2% per year, or reduced in the event of declining property value caused by damage, destruction or other factors including a general economic downturn. The amendment further limits the amount of any ad valorem tax on real property to 1% of the full cash value except that additional taxes may be levied to pay debt service on indebtedness approved by the voters prior to July 1, 1978, and bonded indebtedness for the acquisition or improvement of real property approved on or after July 1, 1978 by two-thirds of the votes cast by the voters voting on the proposition.

Legislation enacted by the California Legislature to implement Article XIII A provides that all taxable property is shown at full assessed value as described above. In conformity with this procedure, all taxable property value included in this Official Statement (except as noted) is shown at 100% of assessed value and all general tax rates reflect the $1 per $100 of taxable value. Tax rates for voter approved bonded indebtedness are also applied to 100% of assessed value.

Future assessed valuation growth allowed under Article XIII A (new construction, change of ownership, 2% annual value growth) will be allocated on the basis of "situs" among the jurisdictions that serve the tax rate area within which the growth occurs. Local agencies and school districts will share the growth of "base" revenue from the tax rate area. Each year's growth allocation becomes part of each agency's allocation the following year. The County is unable to predict the nature or magnitude of future revenue sources which may be provided by the State to replace lost property tax revenues. Article XIII A effectively prohibits the levying of any other ad valorem property tax above the 1% limit except for taxes to support indebtedness approved by the voters as described above.

Article XIII B

On November 6, 1979, California voters approved Proposition 4, which added Article XIII B to the California Constitution. In May 1990, the voters through their approval of Proposition 111 amended Article XIII B. Article XIII B of the California Constitution limits the annual appropriations of the State and any city, county, school district, authority or other political subdivision of the State to the level of appropriations for the prior fiscal year, as adjusted annually for changes in the cost of living, population and services rendered by the governmental entity. The "base year" for establishing such appropriation limit is the 1978-79 fiscal year. Increases in appropriations by a governmental entity are also permitted (i) if financial responsibility for providing services is transferred to a governmental entity, or (ii) for emergencies so long as the appropriations limits for the three years following the emergency are reduced to prevent any aggregate increase above the Constitutional limit. Decreases are required where responsibility for providing services is transferred from the government entity.

Appropriations subject to Article XIII B include generally any authorization to expend during the fiscal year the proceeds of taxes levied by the State or other entity of local government, exclusive of certain State subventions, refunds of taxes, benefit payments from retirement, unemployment insurance

and disability insurance funds. Appropriations subject to limitation pursuant to Article XIII B do not include debt service on indebtedness existing or legally authorized as of January 1, 1979, on bonded indebtedness thereafter approved according to law by a vote of the electors of the issuing entity voting in an election for such purpose, appropriations required to comply with mandates of courts or the Federal government, appropriations for qualified outlay projects, and appropriations by the State of revenues derived from any increase in gasoline taxes and motor vehicle weight fees above January 1, 1990 levels. "Proceeds of taxes" include, but are not limited to, all tax revenues and the proceeds to any entity of government from (i) regulatory licenses, user charges, and user fees to the extent such proceeds exceed the cost of providing the service or regulation, (ii) the investment of tax revenues and (iii) certain State subventions received by local governments. Article XIII B includes a requirement that if an entity's revenues in any year exceed the amount permitted to be spent, the excess would have to be returned by revising tax rates or fee schedules over the subsequent two fiscal years.

As amended in May 1990, the appropriations limit for the County in each year is based on the limit for the prior year, adjusted annually for changes in the costs of living and changes in population, and adjusted, where applicable, for transfer of financial responsibility of providing services to or from another unit of government. The change in the cost of living is, at the County's option, either (i) the percentage change in California per capita personal income, or (ii) the percentage change in the local assessment roll for the jurisdiction due to the addition of nonresidential new construction. The measurement of change in population is a blended average of statewide overall population growth, and change in attendance at local school and community college ("K-14") districts.

As amended by Proposition 111, the appropriations limit is tested over consecutive two-year periods. Any excess of the aggregate "proceeds of taxes" received by the County over such two-year period above the combined appropriations limits for those two years is to be returned to taxpayers by reductions in tax rates or fee schedules over the subsequent two years.

Article XIII B permits any government entity to change the appropriations limit by vote of the electorate in conformity with statutory and Constitutional voting requirements, but any such voter-approved change can only be effective for a maximum of four years.

The Board adopted the annual appropriation limit for the Fiscal Year 2006-07 of approximately $3.4 billion. The limitation applies only to proceeds of taxes and therefore does not apply to service fees and charges, investment earnings on non-proceeds of taxes, fines, and revenue from the sale of property and taxes received from the State and federal governments that are tied to special programs. Based on the 2006-07 Adopted Budget, the funds subject to limitation total approximately $1.0 billion (total General Operating Budget minus non-proceeds of taxes and debt service) and are approximately $2.4 billion below the Article XIII B limit

Proposition 46

On June 3, 1986, California voters approved Proposition 46, which added an additional exemption to the 1% tax limitation imposed by Article XIII A. Under this amendment to Article XIII A, local governments and school districts may increase the property tax rate above 1% for the period necessary to retire new general obligation bonds, if two-thirds of those voting in a local election approve the issuance of such bonds and the money raised through the sale of the bonds is used exclusively to purchase or improve real property.

Proposition 62

Proposition 62 was adopted by the voters at the November 4, 1986, general election which (a) requires that any new or higher taxes for general governmental purposes imposed by local governmental entities such as the County be approved by a two-thirds vote of the governmental entity's legislative body and by a majority vote of the voters of the governmental entity voting in an election on the tax, (b) requires that any special tax (defined as taxes levied for other than general governmental purposes) imposed by a local government entity be approved by a two-thirds vote of the voters of the governmental entity voting in an election on the tax, (c) restricts the use of revenues from a special tax to the purposes or for the service for which the special tax was imposed, (d) prohibits the imposition of ad valorem taxes on real property by local governmental entities except as permitted by Article XIII A of the California Constitution, (e) prohibits the imposition of transaction taxes and sales taxes on the sale of real property by local governmental entities, and (f) requires that any tax imposed by a local governmental entity on or after August 1, 1985, be ratified by a majority vote of the voters voting in an election on the tax within two years of the adoption of the initiative or be terminated by November 15, 1988.

On September 28, 1995, the California Supreme Court, in the case of *Santa Clara County Local Transportation Authority v. Guardino*, upheld the constitutionality of Proposition 62. In this case, the court held that a county-wide sales tax of one-half of one percent was a special tax that, under Section 53722 of the Government Code, required a two-thirds voter approval. Because the tax received an affirmative vote of only 54.1%, this special tax was found to be invalid.

Following the California Supreme Court's decision upholding Proposition 62, several actions were filed challenging taxes imposed by public agencies since the adoption of Proposition 62. On June 4, 2001, the California Supreme Court released its decision in one of these cases, *Howard Jarvis Taxpayers Association v. City of La Habra, et al.* ("La Habra"). In this case, the court held that public agency's continued imposition and collection of a tax is an ongoing violation, upon which the statute of limitations period begins anew with each collection. The court also held that, unless another statute or constitutional rule provided differently, the statute of limitations for challenges to taxes subject to Proposition 62 is three years. Accordingly, a challenge to a tax subject to Proposition 62 may only be made for those taxes received within three years of the date the action is brought. The portion of the County's taxes subject to Proposition 62, including the County's transient occupancy tax, is in compliance with Proposition 62 requirements.

Proposition 218

On November 5, 1996, the voters of the State approved Proposition 218, a constitutional initiative, entitled the "Right to Vote on Taxes Act" ("Proposition 218"). Proposition 218 added Articles XIII C and XIII D to the California Constitution and contained a number of interrelated provisions affecting the ability of local governments, including the County, to levy and collect both existing and future taxes, assessments, fees and charges. The County is unable to predict whether and to what extent Proposition 218 may be held to be constitutional or how its terms will be interpreted and applied by the courts. Proposition 218 could substantially restrict the County's ability to raise future revenues and could subject certain existing sources of revenue to reduction or repeal, and increase the County's costs to hold elections, calculate fees and assessments, notify the public and defend its fees and assessments in court. However, the County does not presently believe that the potential financial impact on the County as a result of the provisions of Proposition 218 will adversely affect the County's ability to pay its debt obligations and perform its other obligations payable from the General Fund as and when due.

Article XIII C requires that all new local taxes be submitted to the electorate before they become effective. Taxes for general governmental purposes of the County require a majority vote and taxes for

specific purposes, even if deposited in the County's General Fund, require a two-thirds vote. Further, any general purpose tax that the County imposed, extended or increased without voter approval after December 31, 1994 may continue to be imposed only if approved by a majority vote in an election held within two years of November 5, 1996. The County has not enacted, imposed, extended or increased any tax without voter approval since January 1, 1995. These voter approval requirements of Proposition 218 reduce the flexibility of the County to raise revenues through General Fund taxes, and no assurance can be given that the County will be able to impose, extend or increase such taxes in the future to meet increased expenditure requirements.

Article XIII C also expressly extends to voters the power to reduce or repeal local taxes, assessments, fees and charges through the initiative process, regardless of the date such taxes, assessments, fees or charges were imposed. This extension of the initiative power is not limited by the terms of Proposition 218 to fees imposed after November 6, 1996 and absent other legal authority could result in retroactive reduction in any existing taxes, assessments or fees and charges.

SB 919 provides that the initiative powers extended to voters under Article XIII C likely excludes actions construed as impairment of contracts under the contract clause of the United States Constitution. SB 919 provides that the initiative power provided for in Proposition 218 "shall not be construed to mean that any owner or beneficial owner of a municipal security, purchased before or after November 6, 1998, assumes the risk of, or in any way consents to, any action by initiative measure that constitutes an impairment of contractual rights" protected by the United States Constitution. However, no assurance can be given that the voters of the County will not, in the future, approve an initiative which reduces or repeals local taxes, assessments, fees or charges that currently are deposited into the County's General Fund. Further, "fees" and "charges" are not defined in Article XIII C or SB 919, and it is unclear whether these terms are intended to have the same meanings for purposes of Article XIII C as they do in Article XIII D. Accordingly, the scope of the initiative power under Article XIII C could include all sources of General Fund moneys not received from or imposed by the federal or State government or derived from investment income.

The initiative power granted under Article XIII C of Proposition 218, by its terms, applies to all local taxes, assessments, fees and charges. The County is unable to predict whether the courts will ultimately interpret the initiative provision to be limited to property related local taxes, assessments, fees and charges. No assurance can be given that the voters of the County will not, in the future, approve an initiative which reduces or repeals local taxes, assessments, fees or charges which are deposited into the County's General Fund. The County believes that in the event that the initiative power was exercised so that all local taxes, assessments, fees and charges which may be subject to the provisions of Proposition 218 are reduced or substantially reduced, the financial condition of the County, including its General Fund, would be materially adversely affected. As a result, there can be no assurances that the County would be able to pay the Series 2006 Certificates as and when due or any of its other obligations payable from the General Fund.

Article XIII D of Proposition 218 adds several new requirements to make it more difficult for local agencies to levy and maintain "assessments" for municipal services and programs. "Assessment" is defined in Proposition 218 and SB 919 as any levy or charge upon real property for a special benefit conferred upon the real property. This includes maintenance assessments imposed in County service areas and in special districts. In most instances, in the event that the County is unable to collect assessment revenues relating to specific programs as a consequence of Proposition 218, the County will curtail such services rather than use amounts in the General Fund to finance such programs. Accordingly, the County anticipates that any impact Proposition 218 may have on existing or future taxes, fees, and assessments will not adversely affect the ability of the County to pay the Series 2006 Certificates as and

when due. However, no assurance can be given that the County may or will be able to reduce or eliminate such services in the event the assessments that presently finance them are reduced or repealed.

Article XIII D also adds several provisions, including notice requirements and restrictions on use, affecting "fees" and "charges" which are defined as "any levy other than an ad valorem tax, a special tax, or an assessment, imposed by a local government upon a parcel or upon a person as an incident of property ownership, including a user fee or charge for a property related service." The annual amount of revenues that are received by the County and deposited into its General Fund which may be considered to be property related fees and charges under Article XIII D of Proposition 218 is not substantial. Accordingly, presently the County does not anticipate that any impact Proposition 218 may have on future fees and charges will not adversely affect the ability of the County to pay the principal and interest on the Series 2006 Certificates as and when due. However, no assurance can be given that the County may or will be able to reduce or eliminate such services in the event the fees and charges that presently finance them are reduced or repealed.

The County has a clean water enterprise fund which is self-supporting from fees and charges that may ultimately be determined to be property related for purposes of Article XIII D of Proposition 218. Further, the fees and charges of the County's enterprise funds, including those which are not property related for purposes of Article XIII D of Proposition 218, may be determined to be fees and charges subject to the initiative power as provided in Article XIII C of Proposition 218, as described above. In the event that fees and charges cannot be appropriately increased or are reduced pursuant to the exercise of the initiative power, the County may have to choose whether to reduce or eliminate the service financed by such fees or charges or finance such service from its General Fund. Further, no assurance can be given that the County may or will be able to reduce or eliminate such services in the event the fees and charges that presently finance them are reduced or repealed.

Additional implementing legislation respecting Proposition 218 may be introduced in the State legislature from time to time that would supplement and add provisions to California statutory law. No assurance may be given as to the terms of such legislation or its potential impact on the County.

Proposition 1A

Proposition 1A (SCA 4) ("Proposition 1A"), proposed by the Legislature in connection with the 2004-05 Budget Act and approved by the voters in November 2004, provides that the State may not reduce any local sales tax rate, limit existing local government authority to levy a sales tax rate or change the allocation of local sales tax revenues, subject to certain exceptions. Proposition 1A generally prohibits the State from shifting to schools or community colleges any share of property tax revenues allocated to local governments for any fiscal year, as set forth under the laws in effect as of November 3, 2004. Any change in the allocation of property tax revenues among local governments within a county must be approved by two-thirds of both houses of the Legislature. Proposition 1A provides, however, that beginning in fiscal year 2008-09, the State may shift to schools and community colleges up to 8% of local government property tax revenues, which amount must be repaid, with interest, within three years, if the Governor proclaims that the shift is needed due to a severe state financial hardship, the shift is approved by two-thirds of both houses and certain other conditions are met. The State may also approve voluntary exchanges of local sales tax and property tax revenues among local governments within a county. Proposition 1A also provides that if the State reduces the VLF rate currently in effect, 0.65 percent of vehicle value, the State must provide local governments with equal replacement revenues. Further, Proposition 1A requires the State, beginning July 1, 2005, to suspend State mandates affecting cities, counties and special districts, excepting mandates relating to employee rights, schools or community colleges, in any year that the State does not fully reimburse local governments for their costs to comply with such mandates.

Future Initiatives

Article XIII A, Article XIII B, Article XIII C, Article XIII D and Propositions 62 and 1A were each adopted as measures that qualified for the ballot pursuant to the State's initiative process. From time to time, other initiative measures could be adopted, further affecting revenues of the County or the County's ability to expend revenues. The nature and impact of these measures cannot be predicted by the County.

STATE OF CALIFORNIA BUDGET INFORMATION

The following information concerning the State's budgets has been obtained from publicly available information which the County believes to be reliable; however, the County takes no responsibility as to the accuracy or completeness thereof and has not independently verified such information. Information about the State Budget is regularly available at various State-maintained websites. Text of the budget may be found at the Department of Finance website, www.dof ca.gov, under the heading "California Budget." An impartial analysis of the budget is posted by the Office of the Legislative Analyst at www.lao.ca.gov. In addition, various State official statements, many of which contain a summary of the current and past State budgets, may be found at the website of the State Treasurer, www.treasurer.ca.gov. The information referred to is prepared by the respective State agency maintaining each website and not by the County or the Underwriters, and the County and the Underwriters take no responsibility for the continued accuracy of the internet addresses or for the accuracy or timeliness of information posted there, and such information is not incorporated herein by these references.

State Budget for Fiscal Year 2004-05

On July 31, 2004, Governor Schwarzenegger signed the 2004-05 Budget Act (the "2004-05 Budget Act") into law. The 2004-05 Budget Act assumed the State General Fund revenues would increase from $76.6 billion in Fiscal Year 2003-04 to $77.3 billion in Fiscal Year 2004-05. The State General Fund expenditures were expected to increase from $77.6 billion in Fiscal Year 2003-04 to $78.8 billion in Fiscal Year 2004-05. The 2004-05 Budget Act projected a year-end reserve of $678 million as of June 30, 2005. Approximately $268 million of the reserve was designated for Proposition 98 and the remaining $410 million was designated for non-Proposition 98 purposes.

Certain of the features of 2004-05 Budget Act affecting local governments included the following:

1. The Vehicle License Fee ("VLF") rate was lowered from 2.0 percent to 0.65 percent and the VLF backfill was eliminated. The State would provide increased property tax revenues to compensate for the reduction in revenues local governments previously received from VLF.

2. A diversion of $1.3 billion from local governments in Fiscal Years 2004-05 and 2005-06, including $350 million from counties, $350 million from cities, $350 million from special districts and $250 from redevelopment agencies. Each county's reduction reflected its proportionate share of statewide county VLF revenues, property taxes and sales taxes.

3. The 2004-05 Budget Act proposed a constitutional amendment to protect certain local government revenues ("Proposition 1A"), which was approved by the voters in November 2004. For a discussion of Proposition 1A, see "Constitutional and Statutory Limitations on Taxes, Revenues and Appropriations – Proposition 1A" herein.

State Budget for Fiscal Year 2005-06

The 2005-06 Budget Act authorized $113 billion in spending, of which $90 billion was from the General Fund and $23 billion was from special funds, and reflected an improving State fiscal outlook resulting from better-than-expected growth in General Fund revenues.

Fiscal Year 2004-05 began with a prior-year balance of $7.3 billion, which amount included approximately $4 billion in amnesty-related payments. General Fund Revenues, including transfers, were estimated to total $79.9 billion in Fiscal Year 2004-05 and $84.5 billion in Fiscal Year 2005-06, which amounts assumed the approximately $1 billion reduction in tax collections for each of Fiscal Year 2004-05 and Fiscal Year 2005-06. The 2005-06 Budget Act includes $525 million in one-time revenues from the refinancing of a previous tobacco-settlement backed bond, a $428 million loan to fund a settlement relating to flood-related damage that occurred in 1986 and the retention of $380 million in transportation-related sales tax proceeds in the General Fund. The 2005-06 Budget Act also included approximately $6 billion in savings and related budget solutions, about one-half of which related to holding 2004-05 Proposition 98 funding at the level set forth in the 2004-05 Budget Act and $450 million of which related to reductions in social services programs.

The 2005-06 Budget Act included projected expenditures of approximately $81.7 billion in Fiscal Year 2004-05 and approximately $90 billion in Fiscal Year 2005-06. The increase in projected expenditures partly reflected (1) the Proposition 42 transfers, which were deferred in Fiscal Year 2004-05 but fully funded in Fiscal Year 2005-06, (2) the prepayment of the $1.2 billion local government loan in Fiscal Year 2005-06 and (3) increases in both kindergarten through twelfth grade and higher education. The excess of expenditures over revenues in both Fiscal Year 2004-05 and 2005-06 was expected to decrease the General Fund reserve to approximately $1.3 billion by the end of Fiscal Year 2005-06.

According to the Legislative Analyst, the savings included in the 2005-06 Budget Act would address part of the State's ongoing structural budget shortfalls, but the legally-required expenditures would exceed projected revenues by approximately $6.9 billion in Fiscal Year 2006-07, including an $880 million transfer to the Budget Stabilization Account required by Proposition 58. Absent corrective actions, the remaining year-end shortfall projected for Fiscal Year 2006-07 would be approximately $4.8 billion, which amount assumed the availability of the $1.3 billion reserve projected for the end of Fiscal Year 2005-06.

State Budget for Fiscal Year 2006-07

The 2006-07 Budget Act (the "2006-07 Budget Act") was passed by the State Legislature on June 27, 2006 and signed by the Governor on June 30, 2006. The 2006-07 Budget Act authorized $127.9 billion in spending, of which $101.3 billion was from the General Fund and $26.6 billion was from special funds, and reflected an improving State fiscal outlook resulting from continued stronger-than-expected growth in General Fund revenues.

Fiscal Year 2005-06 began with a prior-year balance of $9.5 billion, which amount included past budgetary borrowing. General Fund revenues, including transfers, were estimated to total $92.7 billion in Fiscal Year 2005-06 and $94.4 billion in Fiscal Year 2006-07. The 2006-07 Budget Act included projected expenditures of approximately $92.7 billion in Fiscal Year 2005-06 and approximately $101.3 billion in Fiscal Year 2006-07. The approximately $6.9 billion excess of expenditures over revenues in both Fiscal Year 2006-07 is expected to decrease the General Fund reserve to approximately $2.1 billion by the end of Fiscal year 2006-07. The projected General Fund reserve amount does not yet include the fiscal impacts of future collective bargaining contracts approved by the State Legislature.

Based on the Legislative Analyst's current projections of revenues and expenditures, presuming a continuation of the policies set forth under the 2006-07 Budget Act, the State could continue to face operating shortfalls in the range of $4.5 billion to $5 billion in each of Fiscal Years 2007-08 and 2008-09. The carryover reserve from Fiscal Year 2006-07 would be available to offset a portion of the projected shortfall in Fiscal Year 2007-08.

Future State Budgets

No prediction can be made by the County as to whether the State will continue to encounter budgetary problems in this or in any future Fiscal Years, and if it were to do so, it is not clear what measures would be taken by the State to balance its budget, as required by law. In addition, the County cannot predict the final outcome of future State budget negotiations, the impact that such budgets will have on its finances and operations or what actions will be taken in the future by the State Legislature and Governor to deal with changing State revenues and expenditures. Current and future State budgets will be affected by national and State economic conditions and other factors, including the current economic downturn, over which the County has no control.

ECONOMIC AND DEMOGRAPHIC INFORMATION

General

The County is the southernmost major metropolitan area in the State of California. The County covers 4,255 square miles, extending 70 miles along the Pacific Coast from the Mexican border to Orange County, and inland 75 miles to Imperial County. Riverside and Orange counties form the northern boundary. The County is approximately the size of the State of Connecticut.

Topography of the County varies from broad coastal plains and fertile inland valleys to mountain ranges in the east which rise to an elevation of 6,500 feet. Eastern slopes of these mountains form the rim of the Anza-Borrego Desert and the Imperial Valley. The Cleveland National Forest occupies much of the interior portion of the County. The climate is equable in the coastal and valley regions where most of the population and resources are located. The average annual rainfall in the coastal areas is approximately 10 inches.

The County possesses a diverse economic base consisting of a significant manufacturing presence in the fields of electronics and shipbuilding, a large tourist industry attracted by the favorable climate of the region, and a considerable defense-related presence.

In April 2004, PETCO Park opened in the City of San Diego, providing a 42,000 fixed seat baseball stadium for the San Diego Padres. PETCO Park is located in a 26-block neighborhood that contains existing and proposed hotels, office space, retail and housing units within walking distance from the San Diego Convention Center and the Gaslamp Quarter. The baseball stadium is also within walking distance of a Trolley station and nearby parking facilities.

In September 2001, the expansion of the San Diego Convention Center was completed, doubling the size of the existing facility to 2.6 million total gross square feet. The Convention Center generated approximately $1.2 billion in Fiscal Year 2004 in total economic impact (direct and indirect spending).

The County is also growing as a major center for culture and education. Over 30 recognized art organizations, including the San Diego Opera, the Old Globe Theatre productions, the La Jolla Chamber Orchestra, as well as museums and art galleries, are located in the County. Higher education is provided through five two-year colleges and six four-year colleges and universities.

In addition to the City of San Diego, other principal cities in the County include Carlsbad, Chula Vista, Oceanside, El Cajon, Escondido, La Mesa and National City. Most County residents live within 20 miles of the coast. Farther inland are agricultural areas, principally planted in avocados and tomatoes, while the easternmost portion of the County has a dry, desert-like topography.

The County is the delivery system for federal, state and local programs. The County provides a wide range of services to its residents including: (1) regional services such as courts, probation, medical examiner, jails, elections and public health; (2) health, welfare and human services such as mental health, senior citizen and child welfare services; (3) basic local services such as planning, parks, libraries and Sheriff's patrol to the unincorporated area, and law enforcement and libraries by contract to incorporated cities; and (4) infrastructure such as roads, waste disposal and flood control to the unincorporated area of the County.

County Government

The County was incorporated on February 18, 1850, and functions under a charter adopted in 1933, as subsequently amended from time to time. The County is governed by a five-member Board of Supervisors elected to four-year terms in district nonpartisan elections. The Board of Supervisors appoints the Chief Administrative Officer and the County Counsel. The Chief Administrative Officer appoints the Chief Financial Officer and the Auditor and Controller. Elected officials include Assessor/Recorder/County Clerk, District Attorney, Sheriff and Treasurer-Tax Collector.

Population

There are 18 incorporated cities in the County, and several unincorporated communities. For many years the population of the County has grown at a greater rate than that of the State and the nation. As of January 2006, the County population was estimated to be approximately 3,066,820, the third largest County by population in California. The 2006 population increased approximately 0.92% from the County population as of January 2005.

Table 19 below sets forth the population in the County, the State and the United States for the years 1997 to 2006.

TABLE 19

POPULATION ESTIMATES[1]
(In Thousands)

Year	San Diego County	Percent Change	State of California	Percent Change	United States[2]	Percent Change
1997	2,653	1.23%	32,207	1.16%	267,784	0.92%
1998	2,703	1.88	32,657	1.40	270,248	0.90
1999	2,751	1.78	33,140	1.48	272,691	0.90
2000	2,813	2.25	33,873	2.22	282,192	3.48
2001	2,863	1.77	34,441	1.91	285,102	1.03
2002	2,920	1.99	35,088	1.87	287,941	0.99
2003	2,971	1.74	35,691	1.71	290,789	1.04
2004	3,013	1.41	36,271	1.62	293,657	0.99
2005	3,039	0.86	36,728	1.26	296,410	0.94
2006	3,067	0.92	37,172	1.21	N/A[3]	N/A[3]

Sources: State of California Department of Finance; U.S. Bureau of the Census
(1) As of January 1 of the year shown, except as noted.
(2) As of July 1 of the year shown.
(3) Information not available.

Employment

The County's total labor force, consisting of the number of persons who work or are available for work, averaged approximately 1,505,200. The number of employed workers in the labor force averaged approximately 1,440,500. Table 20 below sets forth information regarding the size of the civilian labor force, employment and unemployment rates for the County, the State and the United States for the years 2001 through 2005.

TABLE 20

CIVILIAN LABOR FORCE, EMPLOYMENT AND UNEMPLOYMENT
ANNUAL AVERAGES 2001-2005
By Place of Residence
(In Thousands)

	2001	2002	2003	2004	2005
County of San Diego[1]					
Labor Force	1,409.2	1,448.5	1,468.0	1,489.2	1,505.2
Employment	1,350.3	1,374.0	1,391.6	1,418.5	1,440.5
Unemployment Rate	4.2%	5.1%	5.2%	4.7%	4.3%
State of California[1]					
Labor Force	17,152.1	17,330.7	17,403.9	17,499.6	17,695.6
Employment	16,220.0	16,168.2	16,212.6	16,407.9	16,746.9
Unemployment Rate	5.4%	6.7%	6.8%	6.2%	5.4%
United States[2]					
Labor Force	143,734.0	144,863.0	146,510.0[3]	147,401.0[3]	149,320.0[3]
Employment	136,933.0	136,485.0	137,736[3]	139,252.0[3]	141,730.0[3]
Unemployment Rate	4.7%	5.8%	6.0%[3]	5.5%[3]	5.1%[3]

Sources: County and State Data - California Employment Development Department; National Data – U.S. Department of Labor, Bureau of Labor Statistics.

(1) Data reflects March 2005 benchmark and Census 2000 population controls.

(2) As of October, 2006; data is subject to change due to changes in population controls.

(3) Data are not strictly comparable with data for prior years because of the revisions in the population controls used in the household survey.

Table 21 below sets forth the annual average employment within the County by employment sector, other than farm industries, for 2001 through 2005. The service sector constitutes the largest non-farm employment sector in the County, representing approximately 51% of all non-farm employment.

TABLE 21

SAN DIEGO COUNTY
NON-AGRICULTURAL LABOR FORCE AND INDUSTRY EMPLOYMENT
ANNUAL AVERAGES[1]
2001-2005
(In Thousands)

Employment Sector	2001	2002	2003	2004	2005
Natural Resources and Mining	0.3	0.3	0.3	0.4	0.4
Construction	75.1	76.4	80.2	87.7	91.4
Manufacturing	119.0	112.3	105.3	104.3	104.2
Trade, Transportation and Utilities	209.0	208.6	209.7	215.3	219.1
Information	38.8	37.7	36.9	36.6	37.3
Financial Activities	72.0	75.0	79.9	81.9	83.2
Professional and Business Services	198.2	201.7	201.2	204.5	209.8
Educational and Health Services	116.0	119.7	121.8	121.7	122.8
Leisure and Hospitality	131.4	133.8	140.7	145.7	150.2
Other Services	44.9	45.6	46.8	47.9	48.7
Government	213.8	219.7	217.3	214.3	214.8
Total	1,218.5	1,230.8	1,240.1	1,260.3	1,281.9

Source: California Employment Development Department.
(1) Total may not equal the sum of the line items due to rounding.

Regional Economy

In recent years the County has enjoyed economic stability, out-pacing the State economy despite a general recession in the State. Much of this strength was evidenced by and due to outstanding employment gains, population growth, personal income increases, and high levels of commercial and industrial development.

The Gross Regional Product ("GRP") for 2004 is estimated to be $141.7 billion. This is an increase from the County's estimated GRP of $133.5 billion in 2003. The County's GRP is forecasted to rise to $151.1 billion and $161.1 billion in 2005 and 2006, respectively. The GRP is an estimate of the value for all goods and services produced in the region.

Table 22 below sets forth the County's GRP from 1999 through 2008.

TABLE 22

COUNTY OF SAN DIEGO
GROSS REGIONAL PRODUCT
1999-2008

Year	Gross Regional Product (In Billions)[1]	Annual Percent Change Current Dollars San Diego	Annual Percent Change Real Change* San Diego
1999	$ 99.7	10.2%	9.4%
2000	108.0	8.4	7.0
2001	111.2	2.9	1.4
2002	117.6	5.7	4.0
2003	123.9	5.4	3.4
2004	134.1	8.2	5.7
2005	143.7	7.1	4.7
2006[2]	152.0	5.8	3.6
2007[3]	160.8	5.8	3.4
2008[3]	171.2	6.5	4.6

Sources: Bureau of Economic Analysis, U.S. Department of Commerce (the "BEA"); Economic Research Bureau, San Diego Regional Chamber of Commerce.

* Adjusted by GDP/GSP Implicit Price Deflator.

(1) Based upon County and State statistics from the BEA, which statistics remain subject to revision.

(2) Estimate.

(3) Forecast.

Economic activity and population growth in the local economy are closely related. Helping to sustain the County's economy is the performance of three basic industries of the region, which consist of manufacturing, the military, and tourism. The U.S. Department of Defense contributes about $10 billion annually to the local economy, through wages paid to the uniformed military and civilian personnel, and for equipment and services purchased from local businesses. San Diego's military presence is anticipated to remain relatively stable and may even increase due to the consolidation of military operations and facilities from elsewhere in California, the West, and throughout the United States. The Department of Defense closed and vacated the Naval Training Center in 1997. However, three procurement agencies have recently relocated to San Diego, including the Naval Space and Warfare Systems Command, the Naval Aviation Engineering Servicing Unit, which hires private contractors to service jets, and the Naval Aviation Technical Service Facility, which stores approximately 10 million jet blueprints.

Building Activity

Building permit valuation for both residential and non-residential construction in the County in 2005 decreased over 2004 levels by approximately 4%. Measures limiting new housing remain in effect in areas throughout the County, resulting in a 8% decrease in residential valuations. Non-residential valuations increased 7%.

Table 23 below sets forth the annual total building permit valuation and the annual unit total of new residential permits from 2001 through 2005:

TABLE 23

COUNTY OF SAN DIEGO
BUILDING PERMIT ACTIVITY
2001-2005
(In Thousands)

	2001	2002	2003	2004	2005
Valuation:					
Residential	$3,167,920	$3,475,108	$3,683,807	$3,875,359	$3,562,702
Non-Residential	1,193,866	1,168,866	1,169,397	1,288,130	1,381,794
Total	$4,361,786	$4,643,974	$4,853,204	$5,163,489	$4,944,496
New Housing Units:					
Single Family	9,312	9,749	9,455	9,555	7,904
Multiple Family	6,326	5,989	8,859	7,751	7,354
Total	15,638	15,738	18,314	17,306	15,258

Source: Construction Industry Research Board.

Commercial Activity

Table 24 below sets forth information regarding taxable sales in the County for the years 2001-2004.

TABLE 24

COUNTY OF SAN DIEGO
TAXABLE SALES
2001-2004
(In Thousands)

Type of Business	2001	2002	2003	2004
Apparel Stores	$ 1,274,552	$ 1,374,858	$ 1,466,233	$ 1,644,428
General Merchandise	4,445,352	4,557,457	4,832,2826	5,204,962
Specialty Stores	3,718,292	3,803,803	4,144,293	4,541,225
Food Stores	1,595,933	1,650,104	1,685,203	1,736,610
Home Furnishings/Appliances	1,314,860	1,353,158	1,458,403	1,549,482
Eating and Drinking Establishments	3,366,463	3,505,859	3,757,136	4,047,726
Building Materials	2,343,008	2,510,931	2,757,706	3,341,105
Automotive	7,426,582	7,862,366	8,563,690	9,318,277
All Other Retail Stores	778,296	803,063	855,601	961,645
Business and Personal Services	1,957,109	1,977,606	2,040,077	2,146,781
All Other Outlets	9,478,886	9,196,342	9,303,350	9,978,097
TOTAL ALL OUTLETS	$37,699,333	$38,595,547	$40,863,978	$44,470,338

Source: California State Board of Equalization, Taxable Sales in California.

Personal Income

Table 25 below sets forth the total effective buying income and the median household effective buying income for the County, the State, and the United States between 2001 and 2005.

TABLE 25

PERSONAL INCOME
2001 through 2005

Year and Area	Total Effective Buying Income (In Thousands)	Median Household Effective Buying Income
2001		
San Diego County	54,337,662	44,292
California	652,190,282	44,464
United States	5,230,824,904	39,129
2002		
San Diego County	55,210,119	44,146
California	650,521,407	43,532
United States	5,303,481,498	38,365
2003		
San Diego County	54,831,958	42,315
California	647,879,427	42,484
United States	5,340,682,818	38,035
2004		
San Diego County	57,680,880	43,346
California	674,721,020	42,924
United States	5,466,880,008	38,201
2005		
San Diego County	60,578,879	44,506
California	705,108,410	43,915
United States	5,692,909,567	39,324

Source: Sales and Marketing Management – Survey of Buying Power.

Transportation

Surface, sea and air transportation facilities serve County residents and businesses. Interstate 5 parallels the coast from Mexico to the Los Angeles area and points north. Interstate 15 runs inland, leading to Riverside-San Bernardino, Las Vegas, and Salt Lake City. Interstate 8 runs eastward through the southern United States.

San Diego's International Airport (Lindbergh Field) is located approximately three miles northwest of the downtown area and sits on 614 acres. The facilities are owned and maintained by the San Diego County Regional Airport Authority and are leased to commercial airlines and other tenants.

The airport is California's third most active commercial airport, served by 18 passenger carries and six cargo carriers. In addition to San Diego International Airport there are two naval air stations and seven general aviation airports located in the County.

Public transit in the metropolitan area is provided by the Metropolitan Transit Development Board. The San Diego Trolley, developed by the Metropolitan Transit Development Board beginning in 1979, has been expanded. A total of 17.6 miles were added to the original 108 miles; construction was completed in 1990.

San Diego is the terminus of the Santa Fe Railway's main line from Los Angeles. Amtrak passenger service is available at San Diego, with stops at Solana Beach and Oceanside in the North County.

San Diego's harbor is one of the world's largest natural harbors. The Port of San Diego is administered by the San Diego Unified Port District, which includes the cities of San Diego, National City, Chula Vista, Imperial Beach, and Coronado.

Visitor and Convention Activity

An excellent climate, proximity to Mexico, extensive maritime facilities, and such attractions as the San Diego Zoo and Wild Animal Park, Sea World, Cabrillo National Monument, and Palomar Observatory allow San Diego to attract a high level of visitor and convention business each year. Contributing to the growth of visitor business has been the development of the 4,600-acre Mission Bay Park at San Diego and the construction of meeting and convention facilities at the San Diego Community Concourse.

San Diego's visitor industry is a major sector of the region's economy. Visitor revenues in San Diego County reached approximately $5.8 billion in 2005, according to an estimate by the San Diego Convention and Visitors Bureau, an increase of approximately $300 million from the prior year. The County hosted 54 conventions and trade shows in 2005, attended by approximately 470,950 delegates, who spent approximately $462,117,578.

Education

Forty-two independent school districts provide educational programs for the elementary and secondary public school children in the County. Each school system is governed by a locally elected board of education and administered by a superintendent or other chief administrative officer appointed by the board. In the County there are three types of school districts: elementary, union high and unified. Elementary districts educate elementary students, union high districts educate for the most part secondary students, and unified districts educate both elementary and secondary students. There are currently 12 unified, 24 elementary and 6 union high school districts in the County.

Community colleges in California are locally operated and administered two-year institutions of higher education. They offer Associates in Arts and Associates in Science degrees and have extensive vocational curricula. There are five community college districts in the County with students at eleven campuses and numerous adult and community centers.

Among the institutions of higher education offering bachelors and graduate programs in metropolitan San Diego are San Diego State University, the University of California, San Diego, National University, the University of San Diego, Point Loma College, California State University - San Marcos, Alliance International University and the University of Phoenix.

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APPENDIX B

COUNTY OF SAN DIEGO AUDITED FINANCIAL STATEMENTS FOR THE FISCAL YEAR ENDED JUNE 30, 2005

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MACIAS GINI & COMPANY LLP

515 S. Figueroa Street, Ste. 325
Los Angeles, California 90071

213.612.0200 PHONE
213.286.6426 FAX

INDEPENDENT AUDITOR'S REPORT

Board of Supervisors
County of San Diego, California

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the County of San Diego, California (County), as of and for the year ended June 30, 2005, which collectively comprise the County's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the County's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the First 5 Commission of San Diego (Commission), the discretely presented component unit, and the San Diego County Employees Retirement Association (SDCERA), which represents 63%, 65%, and 6% of the assets, net assets/fund balances and revenues, respectively, of the aggregate remaining fund information as of and for the year ended June 30, 2005. Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinion, insofar as it relates to the amounts included for the Commission and SDCERA, is based on the reports of the other auditors.

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. The financial statements of SDCERA were not audited in accordance with *Government Auditing Standards*. 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the County's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the reports of other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the County as of June 30, 2005, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note V. of the basic financial statements, effective July 1, 2004, the County adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 40 – *Deposit and Investment Risk Disclosures – an amendment of GASB Statement No. 3*.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 19, 2005 on our consideration of the County's internal control over financial reporting and on 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 reporting 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.

The management's discussion and analysis, budgetary comparison information, and schedule of funding progress on pages 23 through 39, 112 through 114, and 116, respectively, are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We and the other auditors have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we and the other auditors did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the County's basic financial statements. The introductory section, combining and individual nonmajor fund financial statements and schedules, and statistical tables are presented for purposes of additional analysis and are not a required part of the basic financial statements. The combining and individual nonmajor fund financial statements and schedules 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 introductory section and statistical tables have not been subjected to the auditing procedures applied by us and the other auditors in the audit of the basic financial statements and, accordingly, we express no opinion on them.

Macias, Gini & Company LLP

Certified Public Accountants

Los Angeles, California
December 19, 2005

Management's Discussion and Analysis

Don Steuer
Chief Financial Officer

Tracy M. Sandoval
Auditor and Controller

This section of the County of San Diego's (County) Comprehensive Annual Financial Report provides a narrative overview and analysis of the basic financial activities of the County as of and for the year ended June 30, 2005. The intent of the information presented here, in conjunction with the Letter of Transmittal is to provide the reader with a clearer picture of the County's overall financial status. Unless otherwise indicated, all amounts in this section are expressed in thousands of dollars.

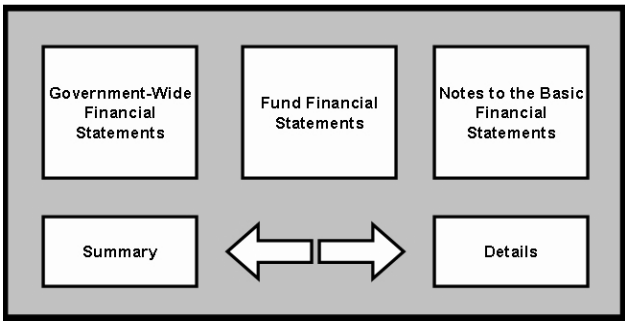
Financial Highlights

- The assets of the County exceeded liabilities at the close of the fiscal year 2004-2005 by $2.18 billion (net assets). Of this amount, $224 million is restricted for specific purposes (restricted net assets), and $2.43 billion is invested in capital assets, net of related debt. The remaining portion of the net assets represents a deficit balance in unrestricted net assets of $465 million.
- Total net assets increased by $201 million. For governmental activities, revenues exceeded expenses by $198 million. For business type activities, revenues exceeded expenses by $3 million.
- General revenues for governmental activities were $970 million. Of this amount, property taxes and property taxes in lieu of vehicle license fees accounted for $646 million or 67 percent; other taxes, interest and other general revenues accounted for $324 million or 33 percent.
- Program revenues for governmental activities were $2.2 billion. Of this amount, $1.8 billion or 81 percent was attributable to operating grants and contributions while charges for services accounted for $414 million or 19 percent.
- The total expenses for governmental activities were $2.99 billion. Public assistance accounted for $973 million or 33 percent of this amount, while public protection accounted for $960 million or 32 percent. Additionally, health and sanitation accounted for $546 million or 18 percent.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the County's basic financial statements. The County's basic financial statements comprise three components: 1) *Government-wide* financial statements 2) *Fund* financial statements, and 3) *Notes* to the basic financial statements. Required Supplementary Information is included in addition to the basic financial statements.

The illustration below depicts the required components of the basic financial statements.



Government-wide Financial Statements are designed to provide readers with a broad overview of County finances, in a manner similar to a private-sector business.

The *statement of net assets* presents information on all County assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the County is improving or deteriorating.

The *statement of activities* presents information showing how the County's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenue and expenses are reported in this statement for some items that will result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave).

Both of the aforementioned government-wide financial statements distinguish functions of the County that are principally supported by taxes and intergovernmental revenues (governmental activities) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (business-type activities). The governmental activities of the County include general government, public protection, public ways and facilities, public assistance, health and sanitation, recreational and cultural, and education. The business-type activities of the County include airport operations, wastewater management and sanitation districts.

Fund Financial Statements are groupings of related accounts that are used to maintain control over resources that have been segregated for specific activities or objectives. The County, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the County can be divided into three categories: governmental funds, proprietary funds and fiduciary funds.

Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental funds financial statements focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating a county's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental funds balance sheet and the governmental funds statement of revenues, expenditures and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

The County maintains twenty-eight individual governmental funds. Information is presented separately in the governmental funds balance sheet and in the governmental funds statement of revenues, expenditures and changes in fund balances for the General Fund and the Tobacco Securitization Special Revenue Fund, both of which are considered to be major funds. Data from the other twenty-six governmental funds are combined into a single, aggregated presentation. Individual fund data for each of these nonmajor governmental funds is provided in the Combining Financial Statements and Supplementary Information section in this report.

Proprietary funds are generally used to account for services for which the County charges customers - either outside customers, or internal departments of the County. Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail. The County maintains the following types of proprietary funds:

Enterprise funds are used to report the same functions presented as business-type activities in the government-wide financial statements. The County uses enterprise funds to account for sanitation services, wastewater management and airport operations. These nonmajor enterprise funds are combined and aggregated. Individual fund data for each nonmajor enterprise fund is provided in the Combining Financial Statements and Supplementary Information section in this report.

Internal service funds are an accounting device used to accumulate and allocate costs internally among the County's various functions. Internal service funds are used to account for the financing of public works and communications equipment; the financing of materials and supplies (purchasing); for start up services for new and existing county service districts; for the County's uninsured risk management activities; the financing of fleet services; for facilities management activities; for the financing of information technology services; and for the financing of clothing and personal sundry items for persons institutionalized at various County facilities. Additionally, mail services are included within the facilities function, and printing and record storage services are included in the purchasing function. Because all of these services predominantly benefit governmental rather than business-type functions, they have been included within governmental activities in the government-wide financial statements.

The County's *eight internal service funds* are combined into a single, aggregated presentation in the proprietary funds financial statements. Individual fund data for the internal service funds is provided in the form of combining statements in the Combining Financial Statements/Schedules and Supplementary Information section in this report.

Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of these funds are not available to support the County's own programs. The accounting used for fiduciary funds is much like that used for proprietary funds.

Notes to the Basic Financial Statements provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements.

Required Supplementary Information is presented concerning the County's General Fund budgetary schedule, and San Diego County Employees Retirement Association (SDCERA) pension schedules. The County adopts an annual appropriated budget for its General Fund. A budgetary comparison schedule has been provided for the General Fund to demonstrate compliance with this budget. In addition, a budgetary comparison schedule has been provided for the Tobacco Securitization Special Revenue Fund for it was determined to be a major governmental fund. The SDCERA pension schedules have been provided to present SDCERA's progress in funding its obligation to provide pension benefits to County employees.

Combining Financial Statements/Schedules and Supplementary Information section of this report presents combining and individual fund statements and schedules referred to earlier that provide information for nonmajor governmental funds, enterprise funds and internal service funds and are presented immediately following the Required Supplementary Information section of this report.

Government-wide Financial Analysis

Net Assets
June 30, 2005 (In Thousands)

	Primary Government					
	Governmental Activities		Business-Type Activities		Total	
	2005	2004	2005	2004	2005	2004
ASSETS						
Current and other assets	$ 2,456,419	1,678,164	79,091	81,031	2,535,510	1,759,195
Capital assets	2,674,393	2,680,570	87,581	81,938	2,761,974	2,762,508
Total assets	5,130,812	4,358,734	166,672	162,969	5,297,484	4,521,703
LIABILITIES						
Long-term liabilities	2,335,192	2,301,177	3,250	3,538	2,338,442	2,304,715
Other liabilities	771,977	231,636	2,696	1,588	774,673	233,224
Total liabilities	3,107,169	2,532,813	5,946	5,126	3,113,115	2,537,939
NET ASSETS						
Invested in capital assets, net of related debt	2,341,126	2,324,806	84,416	78,485	2,425,542	2,403,291
Restricted	223,565	169,983			223,565	169,983
Unrestricted	(541,048)	(668,868)	76,310	79,358	(464,738)	(589,510)
Total net assets	$ 2,023,643	1,825,921	160,726	157,843	2,184,369	1,983,764

Analysis of Net Assets

Net assets may serve over time as a useful indicator of a government's financial position. In the case of the County, assets exceeded liabilities by $2.18 billion at the close of fiscal year 2004-2005. The County also had positive balances in two of its categories of net assets, (Invested in capital assets net of related debt and Restricted net assets). Unrestricted net assets had a deficit balance of $465 million.

The largest portion of the County's net assets (111 percent) reflects its investment of $2.43 billion in capital assets (e.g. land, infrastructure, buildings, and equipment); less any related outstanding debt used to acquire those assets. The County uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending.

Although the County's investment in capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be liquidated for these liabilities.

An additional portion of the County's net assets, $224 million (10 percent), represents resources that are subject to external restrictions on how they may be used. External restrictions include those imposed by grantors, contributors, laws/regulations of other governments, or restrictions imposed by law through constitutional provisions or legislation.

The remaining portion of the County's net assets represents a deficit unrestricted net assets balance of $465 million (an increase of $125 million). This increase was in large part due to increased Property taxes collected in lieu of vehicle license fee(VLF) revenue ($204 million), decrease in the State allocation of sales tax and VLF ($121 million) and an increase in other taxes ($44 million). A more detailed discussion of these revenue sources can be found below in the Analysis of Changes in Net Assets Revenues section.

Changes in Net Assets
For the Year Ended June 30, 2005 (In Thousands)

	Governmental Activities		Business-type Activities		Total	
	2005	2004	2005	2004	2005	2004
Revenues:						
Program revenues						
Charges for services	$ 414,384	351,928	30,651	27,404	445,035	379,332
Operating grants and contributions	1,769,805	1,747,368	3,700	4,671	1,773,505	1,752,039
Capital grants and contributions	32,303	67,357	1,036	1,539	33,339	68,896
General revenues						
Property taxes	441,716	412,587			441,716	412,587
Property taxes in lieu of vehicle license fees	203,788				203,788	
Other taxes	96,927	52,489			96,927	52,489
State allocation of sales tax and vehicle license fees	106,548	227,688			106,548	227,688
Interest	38,066	21,992	1,730	417	39,796	22,409
Other	83,079	92,138	287	24	83,366	92,162
Total revenues	3,186,616	2,973,547	37,404	34,055	3,224,020	3,007,602
Expenses:						
Governmental Activities						
General government	232,826	286,997			232,826	286,997
Public protection	960,227	1,124,382			960,227	1,124,382
Public ways and facilities	122,797	164,551			122,797	164,551
Health and sanitation	545,805	592,426			545,805	592,426
Public assistance	972,592	1,017,705			972,592	1,017,705
Education	27,394	31,722			27,394	31,722
Recreation and cultural	21,405	26,774			21,405	26,774
Interest expense	106,612	91,897			106,612	91,897
Business-type Activities						
Airport			8,117	7,373	8,117	7,373
Wastewater Management			5,076	4,005	5,076	4,005
Sanitation Districts			20,564	15,828	20,564	15,828
Total expenses	2,989,658	3,336,454	33,757	27,206	3,023,415	3,363,660
Excess (deficiency) before transfers	196,958	(362,907)	3,647	6,849	200,605	(356,058)
Transfers	764	673	(764)	(673)		
Increase (decrease) in net assets	197,722	(362,234)	2,883	6,176	200,605	(356,058)
Net assets at beginning of year	1,825,921	2,188,155	157,843	151,667	1,983,764	2,339,822
Net assets at end of year	$ 2,023,643	1,825,921	160,726	157,843	2,184,369	1,983,764

Analysis of Changes in Net Assets

The County's net assets increased by $201 million during the fiscal year 2004-2005. (Certain fiscal year 2003 - 2004 balances were reclassified to conform with the current year presentation.)

Governmental activities:

Governmental activities increased the County's net assets by $197.7 million for the year ended June 30, 2005, accounting for 99% of the total increase in net assets. Governmental activities operating revenues exceeded operating expenses by $196.9 million. Transfers provided a total increase in net assets of $.8 million.

Revenues:

Total revenues for governmental activities were $3.19 billion, an increase of 7 percent or $213 million from the previous year. Total program revenues increased $50 million, due in part to increases in realignment revenues which fund health, mental health and social services programs.

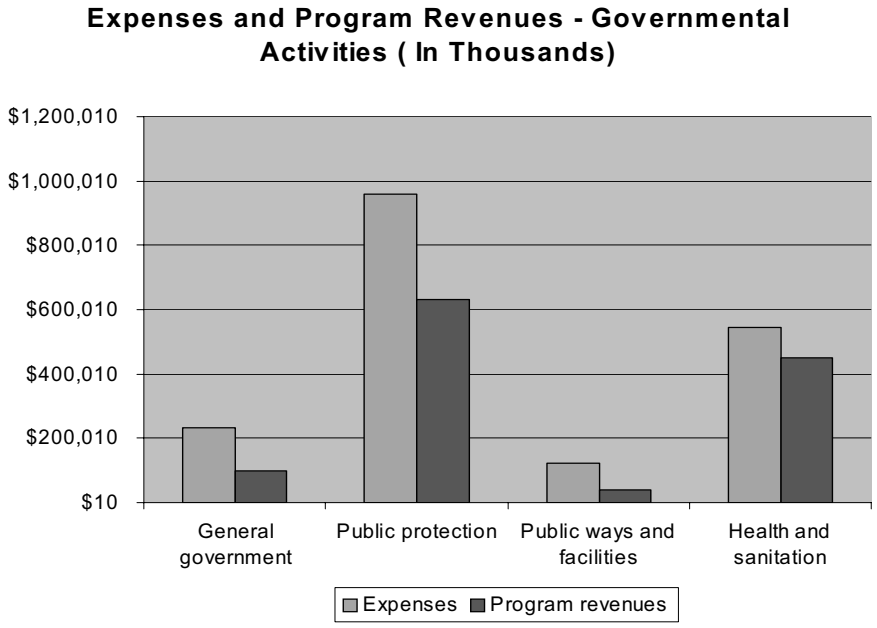
The $163 million increase in general revenues is primarily due to the following:

$29 million of the increase was due to property taxes, which increased 7% over the previous year. The increase was due to significant growth in assessed property values as real estate activity remained strong.

$204 million of the increase is due to property taxes in lieu of vehicle license fee(VLF) revenue. Beginning in Fiscal Year 2004-2005, the County's share of general purpose VLF was eliminated and replaced with property tax revenue previously distributed in the County for education funding via the Educational Revenue Augmentation Fund(ERAF). The ERAF fund was established by state law in Fiscal Year 1992-93 to capture prescribed amounts of property tax to be shifted from local governmental agencies to local schools. The swap of property tax for VLF general purpose revenues resulted from the State's Fiscal Year 2004-05 budget actions and the signing of SB1099. The mechanism used to shift property tax revenues from ERAF to cities and counties was the establishment of a new VLF Property Tax Compensation Fund which holds initial allocations of property tax before distributions to cities and counties in January and May of the fiscal year. The County's share of this "swapped" revenue was $204 million.

$121 million represents a decrease in the State allocation of sales tax and VLF. Decreases in VLF are a result of the "swap" explained above while decreased sales taxes were caused by the State's exchange of sales tax revenue for property tax revenue. Effective July 1, 2004, provisions of AB7X1, one of the 2003-04 State budget bills referred to as the "triple flip" took effect. It redirected one-quarter cent of sales tax to the State to repay up to $15 billion in bonds authorized by Proposition 57 (March 2004) to help the State finance its past debt. In turn, the State replaced the County's loss of sales tax revenue with a like amount of property tax revenue.

Interest earnings increased $16 million or 73%, as the annual pool investment earnings rate increased to 2.24% from the prior year of 1.59%.



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Expenses:

Total expenses for governmental activities were $2.99 billion, a decrease of 10% or $347 million from the prior year. Public assistance is the largest function in expense (33 percent), followed by public protection (32 percent) and health and sanitation (18 percent).

The total decrease in program expenses is attributed generally to the following:

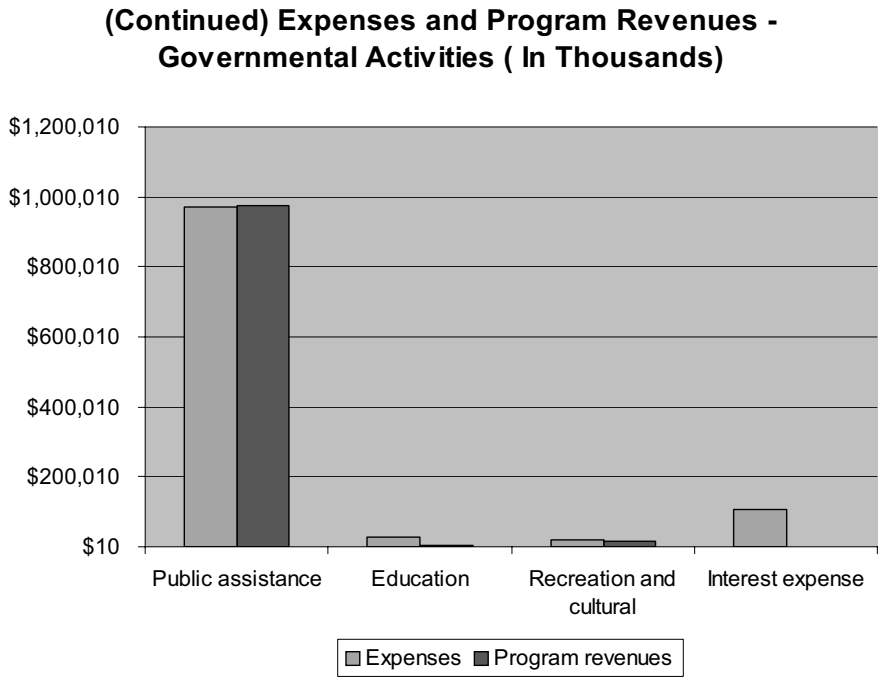
$450 million represented savings as a result of the prior year's contributions paid to SDCERA to reduce the County's unfunded accrued actuarial liability (UAAL). This was offset by Board action to pay down $25 million of the UAAL in the current fiscal year, for a net overall decrease in this category of expense of $425 million. The reduced expense was applicable across all functions.

Offsetting the above decrease are the following increases in expenses:

$30 million is attributable to increases in salaries and benefit costs, an increase of 2.4% over the previous year. As a service delivery entity, the County's major cost component is salaries and benefits, amounting to approximately 43% of the total County expenditures. The County's overall strategy whereby some positions are deleted, some are frozen and others are temporarily funded has minimized the impact of negotiated salary increases and increased benefit costs.

$15 million is attributable to increased interest expense on borrowings to meet cash flow needs of operations.

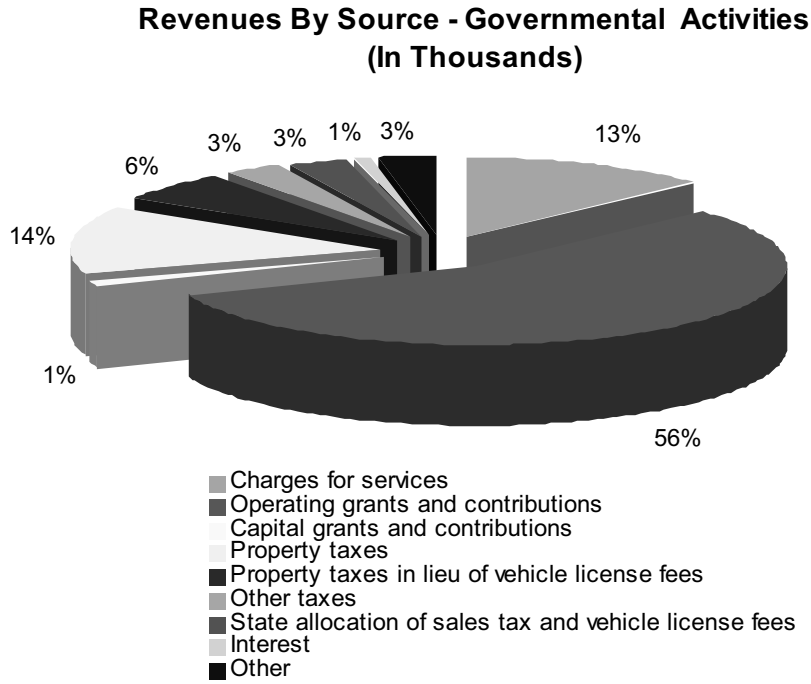
$3 million represents basic increases in the costs of services and supplies across all functions.



Revenues By Sources:

The County's governmental activities rely on several sources of revenue to finance ongoing operations. As shown, for governmental activities overall, without regard to program, operating grants and contributions are the largest single source of funds (56 percent). Operating grants and contributions are monies received from parties outside the County and are generally restricted to one or more specific programs. Examples of operating grants and contributions include State and Federal revenue for public assistance programs and for health and sanitation programs. General revenues such as property taxes and property taxes in lieu of vehicle license fees are not shown by program, but are effectively used to support program activities County-wide. Combined, these revenues account for 20% of governmental activities.

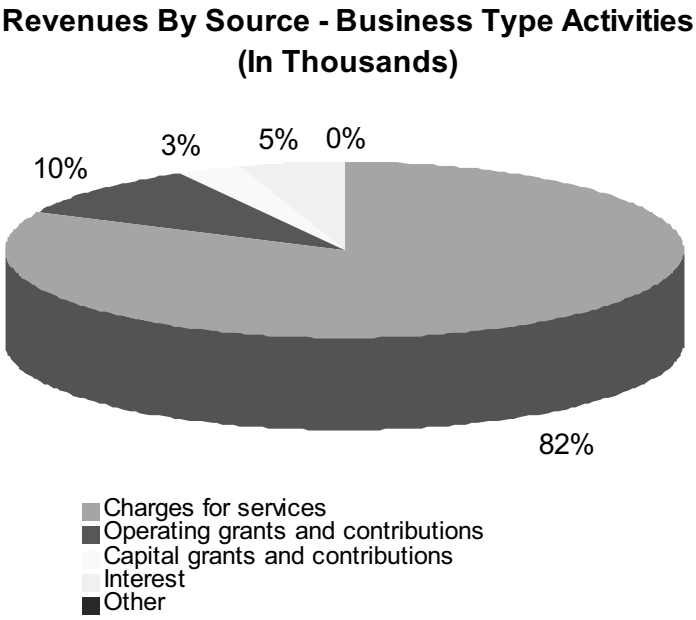
At the end of fiscal year 2004-2005, total revenues for the governmental activities were $3.19 billion, while total expenses for governmental activities were $2.99 billion.



Other factors concerning the finances of the County's major governmental funds are discussed in the Governmental Funds section of the "Financial Analysis of the County's Funds."

Business-type Activities:

The net assets of business-type activities increased by $2.9 million or 1.8%, indicating that these activities generated revenues sufficient to cover the costs of operations. Revenues increased 9% to $37.4 million due to an increase in charges for services and expenses of 20% to $33.7 million, primarily due to increased costs of sewage processing and costs of repairs and maintenance.



Financial Analysis of the County Funds

The County uses fund accounting to demonstrate and ensure compliance with finance-related legal requirements.

Governmental Funds:

The focus of the County's governmental funds is to provide information on near-term inflows, outflows, and balances of resources that are available for spending. Such information is useful in assessing the County's financing requirements. In particular, unreserved fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year. Types of Major Governmental Funds reported by the County include the General Fund and the Tobacco Securitization Special Revenue Fund. Nonmajor Governmental Funds include Special Revenue Funds, Debt Service Funds, and Capital Project Funds.

As of the end of fiscal year 2004-2005, the County's governmental funds reported combined ending fund balances of $1.52 billion, an increase of $224 million in comparison with the prior year fund balance. Of the total June 30, 2005 amount, $942 million constitutes unreserved fund balance, which is available for spending at the County's discretion. The remainder of fund balance is reserved to indicate that it is not available for new spending because it has already been committed, (1) to liquidate existing contracts and purchase orders ($177 million), (2) for landfill closure costs ($26 million), (3) to pay debt service ($148 million), and (4) for a variety of other purposes ($225 million).

Revenues for governmental functions overall totaled $3.12 billion representing a 6 percent increase. Expenditures for governmental functions, totaled $3.0 billion, a 13 percent decrease from the fiscal year ended June 30, 2004.

General Fund:

The General Fund is the chief operating fund of the County. At the end of fiscal year 2004-2005, the unreserved fund balance of the General Fund was $376 million, while total fund balance was $667 million, an increase of $116 million from fiscal year 2003-2004. This was primarily attributed to increases in property tax revenues of $215 million, federal aid of $31 million and charges for current services of $8 million offset by a decrease in State aid of $138 million. As a measure of the General Fund's liquidity, it may be useful to compare both unreserved fund balance and total fund balance to total fund expenditures. Unreserved fund balance represents 15 percent of total General Fund expenditures of $2.5 billion, while total fund balance represents 26 percent of that same amount.

Tobacco Securitization Special Revenue Fund:

This Special Revenue Fund is used to account for the $411 million (net of closing costs and reserve requirements) the County received from the Tobacco Asset Securitization Corporation related to the sale of 25 years of tobacco settlement revenue in fiscal year 2001-2002. The County will continue to invest these funds in investment products to maximize the sustained long-term use of these dollars. At the end of fiscal year 2004-2005, fund balance was $332 million, a decrease of $14 million from fiscal year 2003-2004. This represents the net of transfers out of the fund of $23 million to support health related program expenditures and interest earnings of $9 million.

Other Governmental Funds:

Other Governmental funds consist of twenty-six nonmajor funds, which include Special Revenue Funds, Debt Service Funds, and Capital Project Funds. Individual fund data for each of these nonmajor governmental funds is provided in the Combining Financial Statements and Supplementary Information Section of this report. As of the end of fiscal year 2004-2005, the Fund Balance of the Other Governmental Funds totaled $518 million, an increase of $122 million over the prior year. The change is primarily due to the following: an increase in the fund balance of the SANCAL Capital Projects Fund of $63 million due to proceeds from a bond issuance; an increase of $52 million in the fund balance of the Pension Obligation Bonds Fund due to transfers in of $106 million and principal and interest payments of $16 million and $41 million, respectively; an increase of $16 million in the fund balance of the Edgemoor Development Fund due to proceeds from the sale of capital assets.

Proprietary Funds:

The County's proprietary funds provide the same type of information found in the government-wide financial statements, but in more detail. The nonmajor Enterprise Funds and the Internal Service Funds are combined into single, aggregated presentations in the proprietary fund financial statements with the individual fund data provided in combining statements, which can be found in the Combining Financial Statements/Schedules and Supplemental Information section of this report. Due to the quantitative nature of the Sanitation Districts, the County has elected not to report them as a major fund beginning fiscal year 2004-05.

As of the end of fiscal year 2004-2005, the Net Assets of the Enterprise Funds totaled $160 million, an increase of $3 million over the prior year, primarily due to an increase in the net assets of the Airport Fund as a result of an increase in charges for services of $2 million and a decrease in non-operating expenses of $1.7 million.

Net Assets of the Internal Service Funds totaled $103 million, a decrease of $10 million from the prior year. The net change in the Internal Service Funds is primarily due to a decrease of $6 million in the Risk Financing Fund due to an excess of claims ($43 million) over revenue ($37 million); a decrease in the Facilities Management Fund of $3 million due to increase utilities ($2 million) and repairs and

maintenance costs ($1 million); and a decrease of $1 million in the Fleet Services Fund due to increased fuel expense.

Fiduciary Funds:

The County maintains fiduciary funds for the assets of the Pension Trust Fund, the Investment Trust Fund, and the Agency Funds.

Pension Trust Fund:

This fund is under the control of the Board of Retirement. The fund accumulates employer and employee contributions and earnings from the fund's investments. Disbursements are made from the fund for retirement, disability and death benefits and refunds. This fund includes all assets of the retirement system. As of the end of fiscal year 2004-2005, the net assets of the Pension Trust Fund totaled $6.4 billion, an increase of $850 million over the prior year. The change is primarily due to the following: (a) County and member contributions of $356 million, (b) appreciation in the fair value of pension trust investments and investment income of $795 million; less (c) member benefits paid and pension costs of $302 million.

Investment Trust Fund:

This fund was established to account for the external portion of the County Treasurer's investment pool. This fund consists of school districts, special districts, and funds held for other governments. The Investment Trust Fund's net assets totaled $2.6 billion, an increase in net assets of $164 million, primarily resulting from undistributed school bond proceeds, undistributed property tax collections and prepaid unsecured taxes.

Agency Funds:

The Agency Funds maintain assets held in an agent capacity for other governments, organizations and individuals. These assets do not support the County's programs or services. Any portion of the Agency Funds' assets held at fiscal year end for other County funds, are reported in those funds rather than in the Agency Funds.

General Fund Budgetary Highlights

The County's final budget differs from the original budget in that it contains supplemental appropriations approved during the fiscal year for various programs and projects, as well as transfers of appropriations, budget corrections, re-budgets, and account reclassifications. At June 30, 2005, the variances between the original and final budgets for the excess of revenues over expenditures, $49.5 million, and for other financing sources, $35.5 million, resulted in a total change of $85 million in budgeted fund balance between the original and final budgets.

Increased appropriations caused significant variances between the original and the final budgets as follows:

- $33.2 million for the Integrated Property Tax System funded from securitizing the repayment of the Vehicle License Fee Gap loan.
- $25 million to reduce the unfunded actuarial accrued liability to SDCERA also funded from securitizing the repayment of the Vehicle License Fee Gap loan.
- $7.5 million increase based on increased State revenues. The Governor's Proposed Budget cut funding in the Probation Department Temporary Assistance for Needy Families (TANF). The shortfall would have resulted in the closure of a juvenile camp and ranch treatment beds and other reductions in juvenile and adult probation services, therefore, General Purpose Revenues replaced the TANF funding for these programs in the County's Adopted Operational Plan. In the final State budget, however, State General Revenues were allocated to continue State categorical funding for these programs. This allowed the County to reallocate the General Purpose

Revenues to fund a variety of one-time and on-going services including capital projects, major maintenance and increased costs in the Defense Attorney/Contract Administration department.

- $7.4 million for salaries and benefits for incentives earned through the County's Fiscal Year 2003-2004 Quality First program, funded by fund balance.
- $16.2 million net change in appropriated management reserves for future one-time projects.
- $8.4 million for costs associated with closing the San Marcos landfill, funded from the Environmental Trust Fund ($3 million), Land Acquisition-Divestiture Holding Fund ($4 million) and the Solid Waste Landfill Closure Reserve ($1.4 million), bringing the total project cost to $23.2 million.
- $7.7 million to fund unbudgeted expenditures related to revenue sharing requirements of the Memorandum of Understanding with the State Courts and for payments for undesignated fees pursuant to Assembly Bill 1759 based on traffic court fines, fees and forfeitures ($6.5 million) and fund balance ($1.2 million).
- $8.8 million to fund increased costs in the In-Home Supportive Services Program in Aging and Independence Services based on increased funding from the State Department of Social Services.
- $60.5 million reduction in appropriations for carryover adjustments for year-end encumbrances.

Actual revenues fell short of the final budgeted amounts by $80 million, while expenditures fell short of the budgeted amount by $275.7 million. The combination of revenue and expenditure shortfalls resulted in a net favorable operating variance of $195.7 million. Other financing sources and uses of funds resulted in a favorable variance from budget of $50.9 million and there was no variance in the increase to the reserve for inventories of materials and supplies. These combined variances result in a variance in the net change in fund balance of $246.6 million. Some highlights of the actual results compared to budgeted results are:

Property Tax in Lieu of Vehicle License Fee (VLF): In Fiscal Year 2004-05, the State established initial allocations from the VLF Property Tax Compensation Fund to cities and counties. This replaced the previous distribution of vehicle license fees to local governments. The County budgeted $196.9 million for this revenue source and received $204 million, resulting in a favorable variance of $7.1 million. In addition, during Fiscal Year 2005-06 the County will be receiving a $17.7 million positive true-up adjustment for Fiscal Year 2004-05. (For further VLF discussion see the section below entitled "Economic Factors and Next Year's Budget and Rates.)

Salaries and Benefits: In the continuing environment of uncertainty over State and Federal funding, many County functions have deferred hiring staff for ongoing programs in anticipation of future budget constraints. The total favorable variance in this category is $36.3 million across all functions.

Health and Human Services Agency: Funded by a combination of State, Federal, and County revenues, most Agency programs are carried out in the functional areas of health and sanitation and public assistance, with favorable expenditure variances of $31.8 million and $75.9 million respectively. The expenditure variances result from demand for services being less than the budgeted level. These lowered expenditures are offset by corresponding reductions in Federal and State revenue.

Strong real estate markets: The real estate markets in San Diego County have been robust for several years due to low interest rates and high demand for residential and commercial real estate. This segment of the economy contributed to a positive variance of $24.6 million in property taxes.

Delayed expenditures: Many County projects such as maintenance and information technology take place over more than one fiscal year; however, at inception they are budgeted at full expected cost, resulting in favorable expenditure variances that are re-budgeted into the new fiscal year. For example, $17.0 million has been re-budgeted in the Department of Public Works for the Hazardous Fuels Reduction Program and $2.4 million has been re-budgeted in the Department of Parks and Recreation for parks repair and other fire-related projects. In public protection, $5.0 million in unexpended appropriations for the Regional Communications System, the Jail Information Management System, the North County Regional Gang Task Force, the Cal-ID mugshot replacement system and U.S. Department of Justice Grants involving DNA analysis were re-budgeted the next fiscal year. Additionally, $1.3 million was re-budgeted in the Multi-Species Conservation and Watershed programs and another $.5 million was re-budgeted for document management technology costs.

Reserves: The County annually appropriates management and contingency reserves based on both ongoing general purpose revenues and prior years' fund balance for a variety of one-time capital and operating expenditures as well as potential emergencies. Unexpended reserves resulted in a positive variance of $43.5 million. In addition, in FY 2004-05, the County set aside $17.4 million for economic uncertainty with the intent that it not be spent unless unusual needs arose; of that amount, $14.8 million was unexpended at year end.

Capital Assets and Debt Administration

Capital Assets

At June 30, 2005, the County's capital assets for both the governmental and business-type activities was $2.76 billion net of accumulated depreciation. Investment in capital assets includes land, construction in progress, structures and improvements, equipment, and infrastructure (including roads, bridges, flood channels, and traffic signals). The significant capital asset activity in fiscal year 2004-2005 was as follows:

Governmental Activities:

- $23 million towards the construction and improvement of County maintained roads, bridges, and other road related infrastructure. An additional $23 million was donated by developers.
- $8.21 million towards the construction of the Edgemoor Skilled Nursing Facility in Santee. Total project costs are estimated at $83.79 million.
- $4.37 million towards the construction of the North County Animal Shelter. Total project costs are estimated at $6.69 million.
- $3.09 million for the acquisition of real property in the Otay River Valley area for open space habitat restoration and passive recreation.
- $2.34 million towards the construction of the Bonita Library. Total project costs are estimated at $4.49 million.
- $1.53 million towards the construction of a control panel system at the Vista Detention Facility. Total project costs are estimated at $2.65 million. ·
- $1.34 million towards the construction of a nursery at Polinsky Children's Center. Total project costs are estimated at $2.42 million.
- $1.25 million towards the construction of the East Mesa Juvenile Detention Facility. Total project costs are estimated at $52.95 million.
- $12.96 million towards the construction of numerous other capital outlay projects.

During fiscal year 2004-2005, capital assets valued at $18.81 million, representing the four transit centers, was removed from inventory as a result of the divestiture of the County Transit System to the Metropolitan Transit Development Board.

Business-Type Activities:

- $2.21 million towards the replacement of the Galloway Pump Station Force Main in Alpine Sanitation District. Total project costs are estimated at $4.28 million.
- $1.88 million towards runway rehabilitation at Gillespie Field Airport in El Cajon. Total project costs are estimated at $4.97 million.
- $1.01 million was donated by developers for sewer lines in the East Otay Mesa area.

For government-wide financial statement presentation, governmental fund depreciable capital assets were depreciated from the acquisition date to the end of the current fiscal year. Governmental fund financial statements record capital asset purchases as expenditures.

More detailed capital assets information, including depreciation as of June 30, 2005, can be found in Note IV-D of the notes to the basic financial statements.

Capital Commitments

As of June 30, 2005, capital commitments included the following:

- $72 million for the Integrated Voting System, Integrated Property Tax System, RCS Equipment, SMART system, Revenue Plus Collection System, Medics Health Information System, and the Automated Records Management and Field Reporting Software Installation.
- $80 million for the construction of the Edgemoor Skilled Nursing Facility, the Air Pollution Control Facility in Scripps Ranch, Valley Center Road, Spring Valley Gym/Teen Center, Mission Road, and Forester Creek Drainage system.
- $4.4 million for the Jamacha Boulevard Sewer and the Gillespie Field Runway.

More detailed capital commitments information, including depreciation as of June 30, 2005, can be found in Note IV-D.2 of the notes to the basic financial statements.

Long-Term Obligations

At June 30, 2005, the County had outstanding governmental activity long-term obligations of $2.3 billion. Of this amount, $393 million pertains to outstanding certificates of participation, $35 million pertains to capital leases, and $1.9 billion pertains to other long-term obligations that include $1.25 billion of taxable pension obligation bonds, $430 million of San Diego County Tobacco Asset Securitization Corporation Bonds, $104 million for claims and judgments, $48 million for landfill closure and postclosure costs, $77 million for compensated absences, $7.3 million for other loans, $4 million for the 1995 Redevelopment Agency revenue bonds.

Long-term obligations for business-type activities totaled $3.2 million and consisted of $2.9 million for capital loans and $324 thousand for compensated absences.

During fiscal year 2004-2005, the County's total principal amount of bonds and notes payable for governmental activities increased by $24 million, before giving affect to the unamortized issuance premiums, discounts and unamortized deferred amount on refunding. The increase is due primarily to the County of San Diego's issuance of $112 million in certificates of participation for the Edgemoor/Regional Communication System refunding. Offsets were $60 million in principal debt service payments and $30 million reduction of principal due to the refunding of the 1996 Regional Communication System. The long-term obligations for the business-type activities decreased by $93 thousand due to a debt service payments on capital loans.

More detailed long-term obligation activity, including interest rates and maturity dates, can be found in Note IV-I through IV-I-6 of the notes to the basic financial statements.

The County's credit ratings on its bonded program are as follows:

Credit Ratings	Moody's	Standard & Poor's	Fitch Ratings
Certificates of Participation	A1	AA-	AA-
Pension Obligation Bonds:			
1994 Series A	Aa3	AA-	Not Rated
2002 Series A, B & C	Aa3	AA-	AA-
2004 Series A, B & C	Aa3	AA-	AA-

In addition, the County has an Issuer Credit Rating of Aa2 from Moody's and AA from Standard & Poor's. These ratings reflect the County's favorable general credit characteristics, which include a strong local economy, a sound financial position and a moderate debt profile. There were no changes in the credit ratings from the previous year.

Economic Factors and Next Year's Budget and Rates

The budget for FY 2005-06 resources to support County services contains an increase of $98.7 million, 2.4% over FY 2004-2005.

The San Diego economy continues to show positive growth (i.e., gross regional product at 4.9% for 2002, 4.5% for 2003, 4.4% for 2004, and forecasted at 4.5% for 2005).

The 2005-06 Budget Act is consistent with the two-year budget agreement reached between the State and local governments in July 2004 and the passage of Proposition 1A on the November 2004 ballot with respect to general purpose revenues. For the second year in a row the County will transfer $27.5 million of its property taxes to the Educational Revenue Augmentation Fund (ERAF) to assist the State to meet its funding obligations to local schools. This revenue loss was anticipated and factored into the County's 2005-06 Adopted Budget.

Since 1995-96 the State Property Tax Administration Grant program has assisted counties maintain timely property assessments. The 2005-06 Budget Act suspends for two years the entire $60 million that has historically been budgeted for the program. For the County, the revenue loss is $5.4 million and was not anticipated in the County's 2005-06 Adopted Budget. The County will be reviewing its options including identifying where costs can be reduced and whether any other funding source is available to cover all or a portion of this revenue loss.

Salaries and benefits are increasing by a net $63.8 million or 4.5%. This reflects negotiated increases in base pay and health insurance along with required payments to the retirement fund offset by the reduction of 65 staff years.

The County's *general purpose revenues* continue to perform well. Specifically:

- The largest source of general purpose revenues is property taxes ($400.5 million), representing 55% of the total. The demand for housing, boosted by low interest rates, has remained strong as attested to by significant increases in property values. For the last five years, local secured growth has been high (8.2% average annual growth excluding the State's 2004-05 property tax shift to schools) due to the County's strong overall economy and healthy real estate market. At present, real estate activity is still strong due to stable, historically low mortgage rates, the limited supply of housing for sale, and the area's population growth. As noted above, per the two-year agreement with the State, the County will relinquish $27.5 million in property tax revenues to ERAF. Current secured property tax revenues budgeted in the Fiscal Year 2005-06 Adopted Budget were based on the assumption that assessed value growth through June 30, 2005 would be 10%. Actual assessed value growth exceeded

13%, which is projected to raise current secured property tax revenue collections by $12.9 million.

- *Property Taxes in Lieu of Vehicle License Fees (VLF)* comprises 27.8% (an estimated $200.5 million) of General Purpose Revenues in Fiscal Year 2005-06. This revenue source replaces the previous distribution of vehicle license fees to local governments. In Fiscal Year 2004-05, the State established initial allocations from the VLF Property Tax Compensation Fund to cities and counties. The allocations for Fiscal Year 2005-06 are to be calculated based on a formula that takes into account adjusted actual allocations for Fiscal Year 2004-05 and growth in gross taxable assessed value in each county. Information on the adjusted actuals was released on October 14, 2005 and the County will be receiving a $17.7 million true-up adjustment for Fiscal Year 2004-05. In addition, the published assessed value growth factor for 2005-06 is 13.3% which establishes the County's 2005-06 property tax in lieu of vehicle license fee base at $247.3 million.

At June 30, 2005, *unreserved General Fund balance* was $376 million. Of this amount, the County appropriated to the General Fund $56.5 million of unreserved, undesignated fund balance and $3.7 million in reserved fund balance for Fiscal Year 2005-2006 expenditures of one-time items. The County's *Adopted Operational Plan* for Fiscal Years 2005-2006 (the Adopted Budget) and for Fiscal Year 2006-2007 (for planning purposes) and the County's *Capital Program* can be found on the internet at http://www.sdcounty.ca.gov/auditor/budinfo.html

Requests for Information

This financial report is designed to provide our citizens, taxpayers, customers, and investors and creditors with a general overview of the County's finances and to demonstrate the County's *accountability* for the money it receives. If you have questions about this report or need additional financial information, please contact the Auditor and Controller's Office, County of San Diego, located at 1600 Pacific Highway, San Diego, California 92101.

Basic Financial Statements

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

STATEMENT OF NET ASSETS
June 30, 2005
(In Thousands)

	Primary Government			Component Unit
	Governmental Activities	Business-type Activities	Total	First 5 Commission Fund
ASSETS				
Current assets:				
Equity in pooled cash and investments	$ 925,568	68,937	994,505	172,983
Cash with fiscal agent	118,139		118,139	
Collections in transit	6,716	9	6,725	
Imprest cash	313	2	315	
Investments	69,894		69,894	
Receivables, net	366,567	880	367,447	8,774
Taxes receivable, net	105,784		105,784	
Internal balances	(9,263)	9,263		
Inventory of materials and supplies	11,170		11,170	
Deposits with others	2,370		2,370	
Deferred charges	2,552		2,552	
Prepaid items	1,009		1,009	2
Restricted assets:				
Cash with fiscal agent	97,877		97,877	
Investments	395,773		395,773	
Total current assets	2,094,469	79,091	2,173,560	181,759
Noncurrent assets:				
Restricted assets:				
Investments	335,905		335,905	
Deferred charges	26,045		26,045	
Capital assets:				
Land and construction in progress	407,581	27,489	435,070	
Other capital assets, net of depreciation	2,266,812	60,092	2,326,904	
Total noncurrent assets	3,036,343	87,581	3,123,924	
Total assets	5,130,812	166,672	5,297,484	181,759
LIABILITIES				
Current liabilities:				
Accounts payable	142,965	2,161	145,126	5,813
Accrued payroll	60,374	271	60,645	
Amount due for tax and revenue anticipation notes	369,280		369,280	
Accrued interest	28,743		28,743	
Amount due for commercial paper notes	74,990		74,990	
Unearned revenue	95,625	264	95,889	
Current portion of long-term obligations	117,125	213	117,338	
Total current liabilities	889,102	2,909	892,011	5,813
Noncurrent liabilities:				
Noncurrent portion of long-term obligations	2,218,067	3,037	2,221,104	
Total noncurrent liabilities	2,218,067	3,037	2,221,104	
Total liabilities	3,107,169	5,946	3,113,115	5,813
NET ASSETS				
Invested in capital assets, net of related debt	2,341,126	84,416	2,425,542	
Restricted for:				
Capital projects	20,949		20,949	
Debt service	128,046		128,046	
Inactive landfill maintenance	25,720		25,720	
Other purposes	48,850		48,850	175,946
Unrestricted	(541,048)	76,310	(464,738)	
Total net assets	$ 2,023,643	160,726	2,184,369	175,946

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

STATEMENT OF ACTIVITIES
For the Year Ended June 30, 2005
(In Thousands)

		Program Revenues			Net (Expenses) Revenue and Changes in Net Assets			
					Primary Government			Component Unit
	Expenses	Charges for Services	Operating Grants and Contri-butions	Capital Grants and Contri-butions	Governmental Activities	Business-type Activities	Total	First 5 Commission Fund
Functions/Programs:								
Governmental Activities								
General government	$ 232,826	84,769	14,812	453	(132,792)		(132,792)	
Public protection	960,227	229,150	403,613		(327,464)		(327,464)	
Public ways and facilities	122,797	13,874	3,645	23,236	(82,042)		(82,042)	
Health and sanitation	545,805	75,034	376,623	8	(94,140)		(94,140)	
Public assistance	972,592	3,296	969,887		591		591	
Education	27,394	1,359	993	558	(24,484)		(24,484)	
Recreation and cultural	21,405	6,902	232	8,048	(6,223)		(6,223)	
Interest expense	106,612				(106,612)		(106,612)	
Total governmental activities	2,989,658	414,384	1,769,805	32,303	(773,166)		(773,166)	
Business-type Activities								
Airport	8,117	8,345	3,653			3,881	3,881	
Wastewater Management	5,076	5,357	21			302	302	
Sanitation Districts	20,564	16,949	26	1,036		(2,553)	(2,553)	
Total business-type activities	33,757	30,651	3,700	1,036		1,630	1,630	
Total primary government	3,023,415	445,035	1,773,505	33,339	(773,166)	1,630	(771,536)	
Component Unit								
First 5 Commission	40,137		42,652					2,515
Total component unit	$ 40,137		42,652					2,515

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

STATEMENT OF ACTIVITIES
For the Year Ended June 30, 2005
(In Thousands)

	Net (Expenses) Revenue and Changes in Net Assets			
	Primary Government			Component Unit
	Governmental Activities	Business-type Activities	Total	First 5 Commission Fund
Revenues:				
General revenues:				
Taxes:				
Property taxes	$ 441,716		441,716	
Other taxes	96,927		96,927	
Property taxes in lieu of vehicle license fees	203,788		203,788	
Unrestricted contributions from State				
State allocation of sales tax	106,548		106,548	
Total general tax revenues	848,979		848,979	
Interest	38,066	1,730	39,796	2,576
Other	83,079	287	83,366	
Total general revenues	970,124	2,017	972,141	2,576
Transfers	764	(764)		
Total general revenues and transfers	970,888	1,253	972,141	2,576
Change in net assets	197,722	2,883	200,605	5,091
Net assets at beginning of year (Component Unit restated)	1,825,921	157,843	1,983,764	170,855
Net assets at end of year	$ 2,023,643	160,726	2,184,369	175,946

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

BALANCE SHEET
GOVERNMENTAL FUNDS
June 30, 2005
(In Thousands)

	General Fund	Tobacco Securitization Special Revenue Fund	Other Governmental Funds	Total Governmental Funds
ASSETS				
Equity in pooled cash and investments	$ 496,759	9,878	255,658	762,295
Cash with fiscal agent	43,902		74,237	118,139
Collections in transit	5,362		351	5,713
Imprest cash	298		13	311
Investments	2		69,892	69,894
Receivables, net	224,527	1,229	135,767	361,523
Taxes receivable, net	105,009		775	105,784
Due from other funds	172,209		7,491	179,700
Advances to other funds	928		102	1,030
Inventory of materials and supplies	8,795		1,777	10,572
Deposits with others			2,370	2,370
Prepaid items	5		1,004	1,009
Restricted assets:				
Cash with fiscal agent		3	97,874	97,877
Investments	360,000	323,928	47,750	731,678
Total assets	1,417,796	335,038	695,061	2,447,895
LIABILITIES AND FUND BALANCES				
Liabilities:				
Accounts payable	101,766		25,158	126,924
Accrued payroll	55,366		3,443	58,809
Amount due for tax and revenue anticipation notes	369,280			369,280
Due to other funds	21,342	2,779	119,614	143,735
Advances from other funds			10,699	10,699
Deferred credits and other liabilities	44,624		5,254	49,878
Amount due for commercial paper notes	74,990			74,990
Unearned revenue	82,970		12,655	95,625
Total liabilities	750,338	2,779	176,823	929,940
Fund balances:				
Reserved Fund Balance				
Reserved for encumbrances	131,356		46,003	177,359
Reserved for notes receivable and advances	7,295		35,875	43,170
Reserved for deposits with others			58	58
Reserved for inactive landfill maintenance	16,170		9,550	25,720
Reserved for inventory of materials and supplies	8,795		1,777	10,572
Reserved for debt service			147,996	147,996
Reserved for other purposes	128,216		43,057	171,273
Unreserved:				
Designated for subsequent years' expenditures	111,448			111,448
Undesignated	264,178	332,259		596,437
Unreserved, reported in nonmajor:				
Special Revenue Funds				
Designated for landfill postclosure and inactive landfill maintenance			66,902	66,902
Undesignated			82,631	82,631
Capital Projects Funds				
Undesignated			84,389	84,389
Total fund balances	667,458	332,259	518,238	1,517,955
Total liabilities and fund balances	$ 1,417,796	335,038	695,061	2,447,895

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

RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET TO THE GOVERNMENT-WIDE STATEMENT OF NET ASSETS June 30, 2005 (In Thousands)	
Total fund balances-governmental funds	$ 1,517,955
Costs of issuances are reported as expenditures in governmental funds and thus have the effect of reducing fund balance because current financial resources have been used. In the government-wide statements however, bond issuance costs are reported as a deferred charge and amortized over the life of the bond issue.	28,597
When capital assets (land, buildings, equipment, infrastructure) that are to be used in governmental activities are purchased or constructed, the costs of those assets are reported as expenditures in governmental funds. However, the statement of net assets includes those capital assets among the assets of the County as a whole.	2,578,776
Interest on long-term debt is not accrued in governmental funds, but rather is recognized as an expenditure when due.	(28,743)
Because the focus of governmental funds is on short-term financing, some assets will not be available to pay for current-period expenditures. Those assets (for example, receivables) are offset by deferred revenues in the governmental funds and thus are not included in fund balance.	49,878
Long-term liabilities applicable to the County's governmental activities are not due and payable in the current period and accordingly are not reported as fund liabilities. All liabilities, current and long-term, are recorded in the statement of net assets.	(2,225,724)
Internal service funds are used by management to charge the costs of certain activities, such as insurance and telecommunications, to individual funds. The assets and liabilities of the internal service funds are included in governmental activities in the statement of net assets.	102,904
Net assets of governmental activities	$ 2,023,643

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

STATEMENT OF REVENUES, EXPENDITURES,
AND CHANGES IN FUND BALANCES-GOVERNMENTAL FUNDS
For the Year Ended June 30, 2005
(In Thousands)

	General Fund	Tobacco Securitization Special Revenue Fund	Other Governmental Funds	Total Governmental Funds
Revenues:				
Taxes	$ 671,850		45,324	717,174
Licenses, permits and franchise fees	32,015		10,939	42,954
Fines, forfeitures and penalties	51,000		4,538	55,538
Revenue from use of money and property	29,308	8,810	12,693	50,811
Aid from other governmental agencies:				
State	511,830		568,833	1,080,663
Federal	620,477		109,248	729,725
Other	60,415		13,857	74,272
Charges for current services	254,585		32,046	286,631
Other revenue	38,057		46,353	84,410
Total revenues	2,269,537	8,810	843,831	3,122,178
Expenditures:				
Current:				
General	204,566		6,955	211,521
Public protection	928,375		10,695	939,070
Public ways and facilities	4,348		80,212	84,560
Health and sanitation	499,471		42,450	541,921
Public assistance	858,487		111,721	970,208
Education	597		26,522	27,119
Recreation and cultural	18,300		1,314	19,614
Capital outlay	17,928		36,229	54,157
Debt service:				
Principal			60,849	60,849
Interest and other fiscal charges	12,310		82,246	94,556
Bond issuance costs			1,915	1,915
Total expenditures	2,544,382		461,108	3,005,490
Excess (deficiency) of revenues over (under) expenditures	(274,845)	8,810	382,723	116,688
Other financing sources (uses):				
Sale of capital assets			18,400	18,400
Issuance of bonds and loans				
Face value of bonds issued			83,510	83,510
Face value of loans issued			160	160
Bond premiums			5,960	5,960
Refunding bonds issued			28,885	28,885
Payment to refunded bond escrow agent			(31,633)	(31,633)
Transfers in	568,677		250,813	819,490
Transfers out	(179,228)	(23,278)	(617,121)	(819,627)
Total other financing sources (uses)	389,449	(23,278)	(261,026)	105,145
Net change in fund balances	114,604	(14,468)	121,697	221,833
Fund balances at beginning of year	551,000	346,727	396,436	1,294,163
Increase in:				
Reserve for inventory of materials and supplies	1,854		105	1,959
Fund balances at end of year	$ 667,458	332,259	518,238	1,517,955

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

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES For the Year Ended June 30, 2005 (In Thousands)	
Net change in fund balances-total governmental funds	$ 221,833
Governmental funds accrue property tax revenue, which is deemed collectible within sixty days. However, in the statement of activities the total amount estimated to ultimately be collected is accrued.	25,257
Adjustment for reserve for inventory of materials and supplies.	1,959
Long-term receivables are not available as current resources, and therefore are not reported as revenue in the governmental funds.	(4,274)
The proceeds from the sale of capital assets are reported as other financing sources in the governmental funds.	(18,400)
The book value of the sale of such assets is removed from the capital assets account in the statement of net assets and offset against the sales proceeds resulting in a "loss on sale of capital assets" recorded as an expense in the statement of activities. Governmental funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over the estimated useful lives and reported as depreciation expense. This is the amount by which asset acquisition and donations exceeded depreciation in the current period.	15,178
Internal service funds are used by management to charge the costs of certain activities, such as insurance and telecommunications, to individual funds. The adjustments for internal service funds "close" those funds by charging additional amounts to participating governmental activities to completely cover the internal service fund's costs for the year.	(9,357)
Repayment of bond principal and other long term obligations are reported as expenditures in governmental funds and thus has the effect of reducing fund balance because current financial resources have been used. For the County as a whole however, the principal and other payments for liabilities reduce the liabilities in the statement of net assets and do not result in an expense in the statement of activities. The County's long term obligations include bonds, loans and notes payable, capital leases, accumulated unpaid employee leave balances, arbitrage rebate, and closure and postclosure costs for the San Marcos landfill. The County's long term debt was reduced by these payments, principal payments to bondholders, and the adjustment to the San Marcos landfill closure and postclosure liability.	96,168
Bond issuance costs are expended in the governmental funds when paid, and are capitalized and amortized in the statement of activities. This is the amount by which current year amortization expense exceeded bond issuance costs.	(194)
Interest expense in the statement of activities differs from the amount reported in governmental funds because additional interest was calculated for bonds and notes payable and amortization of capitalized bond premiums, discounts and deferred amount of refunded debt that are expended in the governmental funds in the year paid.	(17,893)
Bond proceeds are reported as financing sources in governmental funds and thus contribute to the change in fund balance. In the government-wide statements however, issuing debt increases long-term liabilities in the statement of net assets and does not effect the statement of activities.	(112,555)
Change in net assets of governmental activities	$ 197,722

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

STATEMENT OF NET ASSETS
PROPRIETARY FUNDS
June 30, 2005
(In thousands)

	Business-Type Activities Enterprise Funds	Governmental Activities - Internal Service Funds
ASSETS		
Current assets:		
Equity in pooled cash and investments	$ 68,937	163,273
Collections in transit	9	1,003
Imprest cash	2	2
Receivables, net	880	5,044
Due from other funds	936	16,315
Advances to other funds	9,312	596
Inventory of materials and supplies		598
Total current assets	80,076	186,831
Noncurrent assets:		
Capital assets:		
Land	10,677	
Construction and contracts in progress	16,812	
Buildings and equipment	43,938	149,528
Infrastructure	64,921	
Accumulated depreciation	(48,767)	(53,911)
Total noncurrent assets	87,581	95,617
Total assets	167,657	282,448
LIABILITIES		
Current liabilities:		
Accounts payable	2,161	16,041
Accrued payroll	271	1,565
Due to other funds	1,247	51,969
Advances from other funds	239	
Unearned revenue	264	
Bonds, loans and notes payable	181	176
Compensated absences	32	224
Claims and judgments		43,251
Total current liabilities	4,395	113,226
Noncurrent liabilities:		
Bonds, loans and notes payable	2,745	3,483
Compensated absences	292	2,016
Claims and judgments		60,318
Total noncurrent liabilities	3,037	65,817
Total liabilities	7,432	179,043
NET ASSETS		
Invested in capital assets, net of related debt	84,416	95,606
Unrestricted net assets	75,809	7,799
Total net assets	$ 160,225	103,405
Adjustment to reflect the consolidation of internal service fund activities related to enterprise funds.	501	
Net assets of business-type activities	$ 160,726	

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

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
PROPRIETARY FUNDS
For the Year Ended June 30, 2005
(In Thousands)

	Business-Type Activities Enterprise Funds	Governmental Activities - Internal Service Funds
OPERATING REVENUES		
Charges for services	$ 30,948	255,435
Miscellaneous	22	1,017
Total operating revenues	30,970	256,452
OPERATING EXPENSES		
Salaries	5,746	29,587
Repairs and maintenance	5,405	24,532
Equipment rental	538	1,227
Sewage processing	13,617	
Contracted services	2,992	117,293
Depreciation	2,269	10,316
Utilities	142	22,237
Cost of material		4,272
Claims and judgments		42,968
Fuel		7,441
Other operating expenses	2,362	7,629
Total operating expenses	33,071	267,502
Operating (loss)	(2,101)	(11,050)
NONOPERATING REVENUES (EXPENSES)		
Interest and dividends	1,729	726
Grants	3,668	243
Interest expense	(184)	(125)
Loss on disposal of capital assets		(590)
Other nonoperating revenues		55
Other nonoperating expenses	(1)	(17)
Total nonoperating revenues (expenses)	5,212	292
Income (loss) before contributions and transfers	3,111	(10,758)
Capital contributions	1,036	
Transfers in		4,448
Transfers out	(764)	(3,547)
Change in net assets	3,383	(9,857)
Net assets at beginning of year		113,262
Net assets at end of year	$	103,405
Adjustment to reflect the consolidation of internal service fund activities related to enterprise funds.	(500)	
Change in net assets of business-type activities	$ 2,883	

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

STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
For the Year Ended June 30, 2005
(In Thousands)

	Business-Type Activities Enterprise Funds	Governmental Activities - Internal Service Funds
Cash flows from operating activities:		
Cash received from customers	$ 32,100	117,660
Cash received from other funds	459	139,847
Cash payments to suppliers	(19,646)	(200,687)
Cash payments to employees	(5,766)	(29,500)
Cash payments to other funds	(7,775)	(23,503)
Net cash provided (used) by operating activities	(628)	3,817
Cash flows from non-capital financing activities:		
Operating grants	3,666	243
Transfers from other funds		4,448
Transfers to other funds	(764)	(3,547)
Advances from other funds	(20)	161
Advances to other funds	235	
Net cash provided by non-capital financing activities	3,117	885
Cash flows from capital and related financing activities:		
Capital grants revenue	1,035	
Acquisition of capital assets	(6,197)	(7,529)
Proceeds from sale of assets		1,065
Retirement of capital leases, bonds and loans	(368)	(159)
Bond sale proceeds and loans received	100	1,785
Interest paid on long-term debt	(184)	(139)
Net cash used for capital and related financing activities	(5,614)	(4,977)
Cash flows from investing activities:		
Interest	1,535	615
Net increase (decrease) in cash and cash equivalents	(1,590)	760
Cash and cash equivalents at beginning of year	70,538	163,518
Cash and cash equivalents at end of year	68,948	164,278
Reconciliation of operating loss:		
Operating loss	(2,101)	(11,050)
Adjustments to reconcile:		
Increase (decrease) in compensated absences	(20)	87
Increase (decrease) in accrued payroll	1	41
Increase (decrease) in due to other funds	(1,747)	(1,747)
Increase (decrease) in accounts payable	(617)	(2,426)
Increase (decrease) in claims and judgments		7,259
Increase (decrease) in deferred credits and other liabilities	(15)	(43)
Decrease (increase) in accounts and notes receivable	696	(1,853)
Decrease (increase) in due from other funds	906	2,969
Decrease (increase) in Inventory of materials and supplies		264
Depreciation	2,269	10,316
Net cash provided (used) by operating activities	(628)	3,817
Non-cash investing and capital financing activities:		
Accrued interest	200	220
Adjustment to capital leases		11
Capital acquisitions included in accounts payable	1,715	956
Total non-cash investing and capital financing activities	1,915	1,187

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

STATEMENT OF FIDUCIARY NET ASSETS
FIDUCIARY FUNDS
June 30, 2005
(In Thousands)

	Pension Trust Fund	Investment Trust Fund	Agency Funds
ASSETS			
Equity in pooled cash and investments	$ 418	2,557,644	405,835
Cash with fiscal agent	175,335		11,409
Collections in transit		216	9,860
Imprest cash		31	4
Investments:			
Domestic equity securities	882,662		
Cash, cash equivalents, and securities domestic equity swaps and futures	1,368,556		
International equity securities	1,489,825		
Securities lending collateral	503,102		
United States government obligations	628,206		
Domestic corporate bonds	557,566		
International bonds	794,671		
Cash and securities for overlay futures	58,557		
Alternative equity and real estate	548,694		
Receivables:			
Accounts receivable		23,390	29,039
Trade receivable	47,146		
Interest receivable	23,509		
Due from other governments	8,738		
Capital assets, net	2,894		
Total assets	7,089,879	2,581,281	456,147
LIABILITIES			
Accounts payable	228,303	9,709	45,678
Due to other governments			410,469
Obligations under securities lending	503,102		
Total liabilities	731,405	9,709	456,147
NET ASSETS			
Held in trust for pension benefits and other purposes	$ 6,358,474	2,571,572	

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

STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS
FIDUCIARY FUNDS
For the Year Ended June 30, 2005
(In Thousands)

	Pension Trust Fund	Investment Trust Fund
ADDITIONS		
Contributions:		
Employer	$ 316,075	
Plan members	40,766	
Contributions on pooled investments		15,396,428
Total contributions	356,841	15,396,428
Investment earnings:		
Net increase (decrease) in fair value of investments	658,060	(16,996)
Interest income	99,175	53,333
Securities lending income	11,196	
Other income	84,675	
Total investment earnings	853,106	36,337
Expenses deducted from investment earnings:		
Investment expenses	(48,451)	
Securities lending expenses	(9,896)	
Total additions	1,151,600	15,432,765
DEDUCTIONS		
Benefits	292,089	
Refunds of contributions	2,185	
Administrative expenses	7,491	
Distribution from pooled investments		15,268,436
Total deductions	301,765	15,268,436
Changes in net assets	849,835	164,329
Net assets at beginning of year	5,508,639	2,407,243
Net assets at end of year	$ 6,358,474	2,571,572

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

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I. Summary of Significant Accounting Policies

A. The Reporting Entity

The County of San Diego (the "County"), is a political subdivision of the State of California (the "State") charged with general governmental powers and governed by an elected five-member Board of Supervisors (the "Board"). The County provides a full range of general government services including police protection, detention and correction, public assistance, health and sanitation, recreation, library, flood control, public ways and facilities, inactive waste management, airport management and general financial and administrative support.

As required by generally accepted accounting principles in the United States of America (GAAP), these financial statements present the County (the primary government) and its component units, entities for which the County is considered to be financially accountable. The component units discussed below are included in the County's reporting entity because of the significance of their operational or financial relationships with the County. Management applied the criteria of Governmental Accounting Standards Board (GASB) Statement No. 14, "The Financial Reporting Entity," and Statement No. 39, "Determining Whether Certain Organizations are Component Units - an amendment of GASB Statement No. 14," to determine whether the following component units should be reported as blended or discretely presented component units. Blended component units, although legally separate entities are, in substance, part of the County's operations. Data from these component units are combined with the data from the primary government. The discretely presented component unit is reported in a separate column in the government-wide financial statements to emphasize that it is legally separate from the County.

1. Blended Component Units

Blended component units governed by the Board of Supervisors include the County of San Diego In-Home Support Services Public Authority (IHHS), the San Diego County Housing Authority, the San Diego County Redevelopment Agency, as well as various service areas and districts which provide specific services County-wide or to distinct geographic areas within the County. While each of these component units is legally separate from the County, the County is financially accountable for these entities. Financial accountability is demonstrated by the County Board of Supervisors acting as the governing board for each of these component units. Descriptions of these component units are as follows:

County of San Diego In-Home Supportive Services Public Authority (IHSS) - This authority was established to serve as the employer of record for the IHSS program which provides in-home assistance to low-income aged, blind, and disabled individuals enabling them to remain safely in their own homes and avoid institutionalization. The IHSS program is a state-mandated. This fund is included as a *special revenue fund*.

San Diego County Housing Authority - This authority accounts for revenues and expenditures related to providing decent housing in a suitable environment for individuals who cannot afford standard private housing. Contracts with the U.S. Department of Housing and Urban Development provide the major funding sources. This fund is included as a *special revenue fund*.

San Diego County Redevelopment Agency - This agency was established to provide a method of eliminating slums and blighted areas, improving housing, expanding employment

opportunities, and providing an environment for the social, economic and psychological growth, and well-being of all citizens of the County. This agency is included in the *debt service and capital projects funds*.

Air Pollution Control District - This district was established to provide for control of air pollution from motor vehicles and other sources in order to attain health-based air quality standards. Revenue sources include license and permit fees, fines, state and federal funds, charges to property owners and vehicle registration fees. This fund is included as a *special revenue fund*.

County Service Districts - These special districts were established to provide authorized services such as road, park, lighting maintenance, fire protection or ambulance service to specific areas in the county. They are financed by ad valorem property taxes in the area benefited or by special assessments levied on specific properties. These funds are included as *special revenue funds*.

Flood Control District - This district was established to account for revenues and expenditures related to providing flood control in the County. It is financed primarily by ad valorem property taxes and federal grants. This fund is included as a *special revenue fund*.

Lighting Maintenance District - This district was established to provide street and road lighting services to specified areas of the County. Revenue sources include ad valorem taxes, benefit fees, state funding and charges to property owners. This fund is included as a *special revenue fund*.

Sanitation Districts - These districts are used to account for the activities of all individual sanitation districts governed by the County Board of Supervisors. They are included as *enterprise funds*.

Blended component units governed by Boards other than the Board of Supervisors include the San Diego County Capital Asset Leasing Corporation, the San Diego County Tobacco Asset Securitization Corporation, the Tobacco Securitization Joint Powers Authority of Southern California and the San Diego County Employee Retirement Association (SDCERA). Because of their relationship with the County and the nature of their operations, the first three of these component units are, in substance, part of the County's operations and, accordingly, the activities of these component units are combined (blended) with the activities of the County for purposes of reporting in the accompanying basic financial statements. The basis for blending these component units is that the governing bodies are substantially the same as the County Board of Supervisors. Although SDCERA is legally separate from the County, it is reported as if it were part of the primary government because it benefits the County almost exclusively by providing services to the County's employees.

Descriptions of these component units are as follows:

San Diego County Capital Asset Leasing Corporation (SANCAL) - This corporation was established to finance the acquisition of County buildings and equipment. It is a nonprofit corporation governed by a five-member Board of Directors, which is appointed by the County Board of Supervisors. This corporation is included in the *special revenue, debt service* and *capital projects funds*.

The San Diego County Tobacco Asset Securitization Corporation (Corporation) - This is a separate legal nonprofit public benefit corporation created under the California Nonprofit Public Benefit Corporation Law. It was established to purchase tobacco settlement payments allocated to the County from the State of California, pursuant to the Master Settlement Agreement concluded on November 23, 1998 between the major tobacco companies and 46 states (including California), the District of Columbia and four U.S. Territories. The Corporation is governed by the Board of Directors consisting of three members, two of which are employees of the County of

San Diego and one independent director who is not an employee of the County. This fund is included as a *special revenue fund*.

The Tobacco Securitization Joint Powers Authority of Southern California (TSJPA) - This is a separate legal public entity created by a Joint Exercise of Powers Agreement by and between the County of San Diego and the County of Sacramento pursuant to the Government Code of the State of California. The authority's purpose is to finance a loan via the sale of bonds to the San Diego County Tobacco Asset Securitization Corporation which in turn uses the loan proceeds to purchase the County's future tobacco settlement revenues under the Purchase and Sale Agreement. The Authority is administered by the Board of Directors consisting of three members, two members who are appointed by the County of San Diego Board of Supervisors and the third member is appointed by the Sacramento County Board of Supervisors. This fund is included as a *special revenue fund*.

The San Diego County Employee Retirement Association - SDCERA is a multiple-employer public retirement system organized under the 1937 Retirement Act and provides retirement, disability and death benefits for plan members and beneficiaries. The County is the major participant and contributes 93.4 percent of total employer contributions. SDCERA is governed by a nine-member board which includes the County Treasurer-Tax Collector, four members appointed by the Board of Supervisors and four members elected by the SDCERA membership. The activity of SDCERA is reported within the *pension trust fund* and included in the *fiduciary funds*.

2. Discretely Presented Component Unit

The following component unit is discretely presented because its Board is not substantively the same as the County's Board and it does not provide services entirely or almost entirely to the County.

First 5 Commission of San Diego (Commission) - The Commission was established by the County as a separate legal entity to administer the County's share of tobacco taxes levied by the State pursuant to Proposition 10. Its purpose is to develop, adopt, promote and implement early childhood development programs in the County. The Commission is a separate legal entity, and the County appoints a voting majority of the Commission's board. The County is able to impose its will on the Commission, due to its ability to change the appointees. The two boards (County and Commission) are not substantively the same and the Commission does not provide services entirely or almost entirely to the County, but to the citizens instead.

3. Additional Detailed Financial Information and/ or Financial Reports

Additional detailed information and/or separately issued financial reports of the County's component units may be obtained from the County Auditor and Controller's Office located at 1600 Pacific Highway, Room 166, San Diego, California 92101. Also, complete financial statements for SDCERA may be obtained from the San Diego County Employees Retirement Association, 401 West A Street, San Diego, California 92101.

B. Government-Wide and Fund Financial Statements

1. Government-Wide Financial Statements

The government-wide financial statements consist of the statement of net assets and the statement of activities and report information on all of the nonfiduciary activities of the primary government and its component units. As a general rule, the effect of interfund activity has been eliminated from the government-wide financial statements. All internal balances in the statement of net assets have been eliminated, with the exception of those

representing balances between the governmental activities and the business-type activities, which are presented as internal balances and eliminated in the total government column. The statement of activities presents function revenue and expenses of governmental activities and business-type activities. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. In the statement of activities, internal service funds' revenue and expenses related to interfund services have been eliminated. Revenue and expenses related to services provided to external customers have not been eliminated and are presented within governmental activities.

The government-wide financial statements distinguish functions of the County that are principally supported by taxes and intergovernmental revenues (governmental activities) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (business-type activities). The governmental activities of the County include general government and support services, public protection, public ways and facilities, public assistance, health and sanitation, recreational and cultural, and education activities. The business type activities of the County include sanitation, wastewater and airport.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenues include (1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and (2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenues.

2. Fund Financial Statements

Separate fund financial statements are provided for governmental funds, proprietary funds and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds and major individual enterprise funds are reported as separate columns in the fund financial statements. The focus of governmental and proprietary fund financial statements is on major funds. The financial information of each major fund is shown in a separate column in the fund financial statements, with the data for all nonmajor governmental funds aggregated into one single column on the Governmental Funds Balance Sheet, and with data for all nonmajor enterprise funds aggregated into one single column on the Statement of Net Assets Proprietary Funds.

The County reports the following major governmental funds:

The *General Fund* is the County's primary operating fund. It accounts for all financial resources of the County except those required to be accounted for in another fund. Revenues are primarily derived from taxes; licenses, permits and franchises; fines, forfeitures and penalties; use of money and property; intergovernmental revenues; charges for services; and other revenues. Expenditures are expended for functions of general government, public protection, public ways and facilities, health and sanitation, public assistance, education, and recreational and cultural. They also include capital outlay, and debt service.

The *Tobacco Securitization Special Revenue Fund* accounts for tobacco settlement payments allocated to the County from the State of California, pursuant to the Master Settlement

Agreement concluded on November 23, 1998 between the major tobacco companies and 46 states (including California), the District of Columbia and four U.S. Territories.

The County reports the following additional funds and fund types:

Enterprise Funds account for airport, sanitation district and wastewater management activities, including operations and maintenance, sewage collection and treatment services.

Internal Service Funds account for the financing of public works and communications equipment; the financing of materials and supplies (purchasing); for start up services for new and existing county service districts; for the County's uninsured risk management activities; the financing of fleet services; for facilities management activities; for the financing of information technology services; and for the financing of clothing and personal sundry items for persons institutionalized at various county facilities. Additionally, mail services are included within the facilities function, and printing and record storage services are included in the purchasing function. The goods or services provided by one County department to other County departments are on a cost reimbursement basis.

The following *fiduciary funds* account for resources that are held by the County as a trustee or agent for outside parties and cannot be used to support the County's programs.

The *Pension Trust Fund* accounts for the activities of SDCERA. This fund is under the control of the Board of Retirement and is governed by the rules and regulations of the 1937 Retirement Act. The fund accumulates employer and employee contributions and earnings from the fund's investments. Disbursements are made from the fund for retirements, disability and death benefits and refunds and administrative costs. This fund includes all assets of the retirement system.

The *Investment Trust Fund* accounts for the external portion of the County Treasurer's investment pool. This fund consists of school districts, special districts and funds held for other governments.

Agency Funds are custodial in nature and do not involve measurement of results of operations and account for assets held by the County as an agent for various local governments, organizations and individuals. Included are funds for child support payments; payroll taxes; public administrator and public guardian accounts; and apportioned taxes for other local governments.

C. Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The government-wide, proprietary, pension and investment trust fund financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Agency Funds are reported using the accrual basis of accounting.

Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Nonexchange transactions, in which the County gives (or receives) value without directly receiving (or giving) equal value in exchange, include property taxes and sales taxes, grants, entitlements, and donations. On the accrual basis, revenue from property taxes is recognized in the fiscal year for which the taxes are levied. Revenue from sales taxes is recognized when the underlying transactions take place. Revenue from grants, entitlements and donations is recognized in the fiscal year in which all eligible requirements have been satisfied.

Governmental Funds are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Under this method, revenues are recognized when measurable and available. Sales taxes, interest, state and federal grants, and charges

for services are accrued when their receipt occurs within 180 days following the end of the fiscal year. Property taxes are accrued if they are collectible within 60 days after the end of the accounting period. Expenditures are generally recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences, claims, and judgments, are recorded only when payment is due. General capital assets acquisitions and general principal payments are reported as expenditures in governmental funds. Proceeds of general long-term debt and capital leases are reported as other financing sources.

Proprietary Funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the County's enterprise funds and internal service funds are charges to customers for services. Operating expenses for enterprise funds and internal service funds include the cost of services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

For *business-type activities*, the County has elected to apply all applicable Governmental Accounting Standards Board (GASB) pronouncements as well as any applicable pronouncements of the Financial Accounting Standards Board (FASB), the Accounting Principles Board, or any Accounting Research Bulletins issued on or before November 30, 1989 unless those pronouncements conflict with or contradict GASB pronouncements. The County has elected to not apply the FASB standards issued subsequent to November 30, 1989. The GASB periodically updates its codification of the existing Governmental Accounting and Financial Reporting Standards, which, along with subsequent GASB pronouncements (Statements and Interpretations), constitutes GAAP for governmental users.

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

Fiduciary Funds include all *Trust and Agency Funds*, which account for assets held by the County as a trustee or as an agent for individuals or other government units.

D. Assets, Liabilities, and Net assets or Fund Balance

1. Deposits and Investments

The County follows the practice of pooling cash and investments of all funds with the County Treasurer-Tax Collector's *Investment Pool (Pool)*, except for certain restricted funds which are generally held by outside custodians and classified as "cash with fiscal agent" or investments on the accompanying financial statements. The individual funds' portions of the Pool's fair value are presented as "equity in pooled cash and investments." For purposes of reporting cash flows, equity in pooled cash and investments, (which includes cash in banks and investments with original maturities of 90 days or less), collections in transit and imprest cash are considered cash equivalents. Pooled cash and investment carrying amounts are similar to demand deposits i.e. funds may be deposited and withdrawn any time without prior notice or penalty. Earnings on pooled funds are apportioned and paid or credited to the funds quarterly based on the average daily balance of each participating fund. A separately issued comprehensive annual financial report of the San Diego County Investment Pool can be accessed at http://www.sdtreastax.com/mcf_afreports.html.

The *Pool's* investments are reported at fair value at June 30, 2005 based on market prices. Securities that are traded on a national or international exchange are valued at the last reported sales price at current exchange rates.

The County Employees Retirement Law of 1937 (Law) grants exclusive control to the Board of Retirement over the investment of SDCERA's investment portfolio. The Law allows for the Board to invest, or delegate the authority to invest, the investment portfolio through the purchase, holding, or sale of any form or type of investment, financial instrument or financial transaction when prudent in the informed opinion of the Board.

The *Pension Trust Fund's* cash and short-term investments consist of cash and securities with fiscal agents and deposits held in a pooled account with the County of San Diego. All participants in the pool proportionately share earnings and losses. Short-term investments consist of cash held in money market accounts and securities readily convertible to cash. Cash equivalents and securities for swaps and futures consist of money market securities and collective short-term investments with original maturities of three months or less.

Investments are reported at fair value at June 30, 2005 in the Pension Trust Fund based upon closing sale prices reported on recognized securities exchanges on the last business day of the period. For listed securities having no sales reported and for unlisted securities, fair value is based upon last reported bid prices. All purchases and sales of investments are accounted for on a trade-date basis, and dividends declared but not received are accrued on the ex-dividend date. Realized and unrealized gains or losses of securities are determined on the basis of average cost. Real estate investments are reported at estimated fair value, which has been determined by appraisals performed by independent real estate advisors approximately every three years.

2. Receivables and Payables

Activity between funds that are representative of lending and borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds." Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as "internal balances."

All property taxes and accounts receivable are shown net of an allowance for uncollectibles. Property taxes are levied on July 1 each fiscal year on taxable real and personal property, which is situated in the County as of the preceding January 1 lien date. However, upon a change in ownership of property or completion of new construction, State law requires an accelerated recognition and taxation of changes in real property assessed valuation. For assessment and collection purposes, property is classified either as "secured" or "unsecured" and is listed accordingly on separate parts of the assessment roll. The "secured roll" is that part of the assessment roll containing locally assessed and State assessed property secured by a lien, which is sufficient, in the opinion of the assessor, to secure payment of the taxes. Other property is assessed on the "unsecured roll."

Property taxes on the secured roll are payable in two installments, due November 1 and February 1. If unpaid, such taxes become delinquent after 5:00 p.m. on December 10 and April 10, respectively, and a ten percent penalty attaches. Property on the secured roll with unpaid delinquent taxes is declared tax-defaulted after 5:00 p.m. on June 30th. Such property may thereafter be redeemed by payment of the delinquent taxes, the ten percent delinquency penalty, a ten dollar cost,

a fifteen dollar per parcel redemption fee (from which the State receives five dollars), and a redemption penalty of one and one-half percent per month starting July 1 and continuing until the end of redemption collectively, the "Redemption Amount". If taxes remain unpaid after five years on the default roll, the property becomes subject to tax sale by the County Treasurer-Tax Collector.

Property taxes on the unsecured roll are due as of the January 1 lien date and become delinquent, if unpaid, on August 31. A ten percent penalty attaches to delinquent taxes on property on the unsecured roll and an additional penalty of one and one-half percent per month begins to accrue on November 1.

As established by the *Teeter Plan*, the Auditor and Controller allocates to the County and other agencies 100% of the secured property taxes billed but not yet collected by the County; in return, as the delinquent property taxes and associated penalties and interest are collected, the County retains such amounts in a separate fund. To the extent that fund's tax loss reserves are higher than required, transfers may be made to benefit the County's General Fund. The tax loss reserve requirement for fiscal year 2004-2005 was $7.5 million. The fund balance of the tax loss reserve fund as of June 30, 2005 was $8.2 million, which is included in the General Fund for reporting purposes.

3. County Leased Property

The County leases real property to the private sector and other governmental agencies. In the government-wide and proprietary funds financial statements, non-cancelable and cancelable leases are reported in the applicable governmental activities or proprietary funds statement of net assets.

4. Inventories and Prepaid Items

Inventories, which consist of expendable supplies, are stated at average cost. They are accounted for as expenditures at the time of purchase and reported in the balance sheet of the General Fund and the Other Governmental Funds as an asset with an offsetting reserve. Proprietary fund types are carried at average cost and are expended when consumed. Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both the government-wide and fund financial statements. The inventories and prepaid items recorded in the governmental funds do not reflect current appropriable resources and thus, an equivalent portion of fund balance is reserved.

5. Deferred Charges

Bond issuance costs are deferred and amortized over the life of the bonds using the straight-line method. In the government-wide financial statements, deferred charges are reported as assets in the governmental activities.

6. Restricted Cash and Investments

Debt covenants require resources to be set aside to repay principal and interest thereon for tax and revenue anticipation notes, pension obligation bonds and SANCAL certificates of participation as restricted assets. Additionally, Tobacco Securitization Special Revenue Fund resources have been restricted and set aside to fund new and existing programs.

7. Capital Assets

Capital assets are defined as assets of a long-term character that are intended to be held or used in operations, such as land, buildings and improvements, equipment, and infrastructure. Infrastructure assets include roads, bridges, flood channels, street lights, signals, and sewers.

Capital assets are recorded at *historical cost* if purchase or constructed. Donated capital assets are recorded at *estimated fair market value* at the date of donation. Capital assets with an original unit cost equal to or greater

than the County's *capitalization threshold* shown in **Table 1** below are reported in the applicable *governmental* or *business-type activities* columns in the government-wide financial statements.

Table 1 (Note I - D-7)

Structures and improvements	$	50
Infrastructure (permanent road divisions, county service areas, sanitation and special districts)	$	25
Infrastructure (all others)	$	50
Equipment	$	5

Depreciation is charged over the capital assets' estimated useful lives using the *straight-line method* for proprietary and governmental fund types. Governmental fund type depreciation is only shown in the statement of activities. Proprietary fund type depreciation is shown both in the fund statements and the statement of activities. The estimated useful lives are shown in **Table 2** below:

Table 2 (Note I - D -7)

Structures and improvements	50 years
Infrastructure	10-50 years
Equipment	5-20 years

8. Deferred and Unearned Revenue

Under both the accrual and modified accrual basis of accounting revenue may be recognized only when earned. Therefore, the government-wide statement of net assets as well as governmental and enterprise funds defer revenue recognition in connection with resources that have been received as of year-end, but not yet earned. In the government-wide statement of net assets deferred revenue represents unearned revenue. Assets recognized in connection with a transaction before the earnings process is complete are offset by a corresponding liability for both deferred and unearned revenue. Under the modified accrual basis it is not enough that revenue has been earned if it is to be recognized in the current period. Revenue must also be susceptible to accrual (i.e. measurable and available to finance expenditures of the current period). Governmental funds report deferred revenues in connection with receivables for revenues not considered available to liquidate liabilities of the current period.

9. Lease Obligations

The County leases various assets under both *operating* and *capital* lease agreements. In the government-wide and proprietary funds financial statements, capital lease and operating lease obligations are reported as liabilities in the applicable governmental activities or proprietary funds statement of net assets.

10. Long-term Obligations

In the government-wide financial statements, and proprietary fund types in the fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund type statement of net assets. Bond premiums and discounts, as well as issuance costs discussed above, are *deferred* and *amortized* over the life of the bonds using the *straight-line method*. Bonds payable are reported net of the applicable bond premium, discount, or deferred amount on refunding. In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

11. Employee Compensated Absences

The County's policy is to permit employees to accumulate *earned* but *unused* vacation, compensatory time, holiday and sick pay benefits. All vacation pay and a certain portion of compensatory and sick pay for specified employee classes is accrued when incurred in the government-wide and proprietary funds financial statements. In the governmental funds, only those amounts that are due and payable at year-end are accrued. Except for specified employee classes, there is no liability for *unpaid accumulated* sick leave since the County does not pay any amounts when employees separate from service with the County. However, employees eligible for retirement benefits that meet minimum balance requirements may apply unused sick leave toward determining their length of service for purposes of determining their retirement benefits.

Amounts recorded as accumulated leave benefits include an amount representing salary-related payments such as the employer's share of Social Security and Medicare taxes associated with payments made for such compensated absences. Accumulated leave benefits including vacation, sick leave, and compensatory time worked in the amount of approximately $76.7 million for the governmental activities as of June 30, 2005, is recorded in the statement of net assets. These amounts would not be expected to be liquidated from expendable available financial resources but would be expected to be liquidated in future years as employees elect to use these benefits as prescribed by Civil Service rules and regulations.

12. Fund Balance

In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

13. Net Assets Invested in Capital Assets, Net of Related Debt

This amount is derived by subtracting the outstanding debts incurred by the County to buy or construct capital assets shown in the statement of net assets. Capital assets cannot readily be sold and converted to cash.

14. Restricted Net Assets

Restricted net assets arise when restrictions on the use of net assets are externally imposed by a creditor, (such as through debt covenants), grantors, contributors, or laws or regulations of other governments; or imposed by law through constitutional provisions or enabling legislation.

15. Unrestricted Net Assets

These assets are resources of the County that can be used for any purpose, though they may not necessarily be liquid. In addition, assets in a restricted fund that exceed the amounts required to be restricted by external parties or enabling legislation are reported as unrestricted net assets.

16. Indirect Costs

Expenditures and expenses for functional activities include County indirect costs that are allocated to benefiting departments under the County's Fiscal Year 2004-2005 *Countywide Cost Allocation Plan* which was prepared in accordance with the Federal Office of Management and Budget Circular A-87.

17. Use of Estimates

The preparation of the basic financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the basic financial statements and

accompanying notes. Actual results could differ from those estimates. Where significant estimates have been made in preparing these financial statements, they are described in the applicable footnotes.

II.Reconciliation of Government-Wide and Fund Financial Statements

A. Funds Balance Sheets/Statement of Net Assets

Explanations of certain differences between the governmental funds balance sheet and the government-wide statement of net assets are detailed in **Table 3** below:

Total fund balance of the County governmental funds, $1,517,955, differs from net assets of governmental activities, $2,023,643 reported in the statement of net assets. The difference primarily results from the *long-term economic resources measurement focus* and the accrual basis of accounting in the statement of net assets versus the *current financial resources measurement focus* and modified accrual basis of accounting in the governmental fund balance sheets.

Table 3 (Note II-A)
Balance Sheet/Statement of Net Assets- Reconciliation
PRIMARY GOVERNMENT

	Total Governmental Funds	Long-term Assets and Liabilities (1)	Internal Service Funds (2)	Reclassi-fications and Eliminations (3)	Statement of Net Assets Totals
ASSETS					
Cash and cash equivalents	$ 768,319		164,278		932,597
Cash with fiscal agent	216,016				216,016
Investments	801,572				801,572
Taxes receivables, net	105,784				105,784
Internal balances				(9,263)	(9,263)
Accounts and notes receivables, net	361,523		5,044		366,567
Due from other funds	179,700		16,315	(196,015)	
Advances to other funds	1,030		596	(1,626)	
Inventory of materials and supplies	10,572		598		11,170
Deferred charges and other assets	3,379	28,597			31,976
Capital assets		2,578,776	95,617		2,674,393
Total assets	2,447,895	2,607,373	282,448	(206,904)	5,130,812
LIABILITIES					
Accounts payable	126,924		16,041		142,965
Accrued payroll	58,809		1,565		60,374
Amount due for tax and revenue anticipation notes	369,280				369,280
Accrued interest		28,743			28,743
Due to other funds	143,735		52,470	(196,205)	
Advances from other funds	10,699			(10,699)	
Deferred credits and other liabilities	124,868	(49,878)			74,990
Unearned revenue	95,625				95,625
Long-term liabilities		2,225,724	109,468		2,335,192
Total liabilities	929,940	2,204,589	179,544	(206,904)	3,107,169
FUND BALANCE/NET ASSETS					
Total fund balances/net assets	1,517,955	402,784	102,904		2,023,643
Total liabilities and fund net assets	$ 2,447,895	2,607,373	282,448	(206,904)	5,130,812

(1) Costs of issuances are reported as expenditures in governmental funds and thus have the effect of reducing fund balance because current financial resources have been used. In the government-wide statements however, bond issuance costs are reported as a deferred charge and amortized over the life of the bond issue.

Net cost of issuance	$	28,597
Total deferred charges and other assets	$	28,597

When capital assets (land, buildings, equipment, and infrastructure) that are to be used in governmental activities are purchased or constructed, the costs of those assets are reported as expenditures in governmental funds. However, the statement of net assets includes those capital assets among the assets of the County as a whole.

Cost of capital assets	$	3,611,933
Accumulated depreciation		(1,033,157)
Net capital assets	$	2,578,776

Interest on long-term debt is not accrued in governmental funds, but rather is recognized as an expenditure when due.

Total accrued interest	$	(28,743)

Because the focus of governmental funds is on short-term financing, some assets will not be available to pay for current-period expenditures. Those assets (for example, receivables) are offset by deferred revenues in the governmental funds and thus are not included in fund balance.

Adjustment of deferred revenue	$	49,878
Total deferred credits and other liabilities	$	49,878

Long-term liabilities applicable to the County's governmental activities are not due and payable in the current period and accordingly are not reported as fund liabilities; including bond premiums, discounts, and the cost of refunded debt that are recognized as revenue (premiums) and expenditures in governmental funds in the year of sale. However, all liabilities, current and long-term, are reported in the statement of net assets. Bond premiums, discounts and deferred costs on refunded debt are recorded as additions (premiums) and reductions of a liability respectively and amortized over the life of the corresponding bonds. Balances at June 30, 2005 were:

Bonds, notes and loans payable	$	(2,083,916)
Unamortized issuance Premium		(6,031)
Unamortized issuance Discount		9,054
Unamortized deferred amount on refunding		12,103
Capital leases		(34,614)
Compensated absences		(74,429)
Landfill closure and postclosure - San Marcos Landfill		(47,891)
Total long-term liabilities	$	(2,225,724)

(2) Internal service funds are used by management to charge the costs of certain activities, such as insurance and telecommunications, to individual funds. The assets and liabilities of the internal service funds are included in governmental activities in the statement of net assets.

Costs	$	102,904

(3) The government-wide financial statements are designed to minimize the duplicative effects of transactions between funds for internal activities. Therefore, due to/from and advances to/from balances have been eliminated on the government-wide financial statements. The net amount due between governmental and business-type activities after eliminations, are reported as internal balances in the government-wide statement of net assets. Due to/from and advances to/from transactions between governmental funds and fiduciary funds are reclassified as receivables and payables in the government-wide statement of net assets.

B. Funds Statement of Revenues, Expenditures, and Changes in Fund Balances/Statement of Activities

The net change in fund balances for governmental funds $221,833 differs from the change in net assets for governmental activities $197,722 reported in the statement of activities. The differences arise primarily from the long-term economic resources measurement focus and the accrual basis of accounting in the statement of activities versus the current financial resources measurement focus and modified accrual basis of accounting in the governmental funds. The effect of the differences is illustrated in **Table 4** below.

Table 4 (Note II-B)
Statement of Revenues, Expenditures, and Changes in Fund Balances/Statement of Activities-Reconciliation
PRIMARY GOVERNMENT

	Total Governmental Funds	Long-term Revenues/ Expenses (4)	Capital Related Items (5)	Internal Service Funds (6)	Long-term Debt Transactions (7)	Statement of Activities Totals
Revenues:						
Taxes	$ 717,174	25,257				742,431
Licenses, permits and franchise fees	42,954					42,954
Fines, forfeitures and penalties	55,538					55,538
Revenue from use of money and property	50,811			726		51,537
Aid from other governmental agencies:						
State	1,080,663					1,080,663
Federal	729,725					729,725
Other	74,272					74,272
Charges for current services	286,631			19,493		306,124
Other revenue	84,410	(4,274)	23,236			103,372
Total revenues	3,122,178	20,983	23,236	20,219		3,186,616
Expenditures:						
Current:						
General	211,521	(1,855)	3,756	21,312	(1,908)	232,826
Public protection	939,070	(16)	15,469	5,373	331	960,227
Public ways and facilities	84,560	(67)	37,974	330		122,797
Health and sanitation	541,921	(26)	2,643	1,267		545,805
Public assistance	970,208		693	1,691		972,592
Education	27,119	5	78	192		27,394
Recreation and cultural	19,614		1,602	189		21,405
Capital outlay	54,157		(54,157)			
Debt service:						
Principal	60,849				(60,849)	
Interest and other fiscal charges	94,556			123	11,933	106,612
Bond issuance costs	1,915				(1,915)	
Total expenditures	$ 3,005,490	(1,959)	8,058	30,477	(52,408)	2,989,658

Table 4 (Note II-B)(Continued)

Statement of Revenues, Expenditures, and Changes in Fund Balances/Statement of Activities-Reconciliation

PRIMARY GOVERNMENT

	Total Governmental Funds	Long-term Revenues/ Expenses (4)	Capital Related Items (5)	Internal Service Funds (6)	Long-term Debt Transactions (7)	Statement of Activities Totals
Other financing sources (uses):						
Sale of capital assets	$ 18,400		(18,400)			
Issuance of bonds and loans						
Face value of bonds issued	83,510				(83,510)	
Face value of loans issued	160				(160)	
Bond premiums	5,960				(5,960)	
Refunding bonds issued	28,885				(28,885)	
Payment to refunded bond escrow agent	(31,633)				31,633	
Transfers (net)	(137)			901		764
Total other financing sources (uses)	105,145		(18,400)	901	(86,882)	764
Net change for the year	$ 221,833	22,942	(3,222)	(9,357)	(34,474)	197,722

Explanations of certain differences between the governmental funds statement of revenues, expenditures, and changes in fund balances and the government-wide statement of activities are detailed below.

(4) Governmental funds accrue property tax revenue, which is deemed collectible within sixty days. However, in the statement of activities the total amount estimated to ultimately be collected is accrued.

Property taxes	$	25,257

Adjustment for reserve for inventory of materials and supplies.

Adjustment	$	1,959

Long-term receivables are not available as current resources, and therefore are not reported as revenue in the governmental funds.

Adjustment of deferred revenue	$	(4,274)

(5) The proceeds from the sale of capital assets are reported as other financing sources in the governmental funds.

Proceeds from sale of capital assets	$	(18,400)

The book value of the sale of capital assets is removed from the capital assets account in the statement of net assets and offset against the sales proceeds resulting in a "loss on sale of capital assets" recorded as an expense in the statement of activities. Governmental funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over the estimated useful lives and reported as depreciation expense. This is the amount by which asset acquisition and donations exceeded depreciation in the current period.

Loss on disposal of assets	$	(1,100)
Capital outlay		77,182
Depreciation expense		(84,140)
Subtotal		(8,058)
Donated infrastructure - roads		23,236
Difference	$	15,178

(6) Internal service funds are used by management to charge the costs of certain activities, such as insurance and telecommunications, to individual funds. The adjustments for internal service funds "close" those funds by charging additional amounts to

participating governmental activities to completely cover the internal service fund's costs for the year.

Adjustments	$	(9,357)

(7) Repayment of bond principal as well as refunding of bonds which are considered a repayment of principal and other costs of refunding, and other long-term obligations are reported as expenditures in governmental funds and thus has the effect of reducing fund balance because current financial resources have been used. For the County as a whole however, the principal and other payments for liabilities reduce the liabilities in the statement of net assets and do not result in an expense in the statement of activities. The County's long-term obligations include bonds, loans and notes payable, capital leases, accumulated unpaid employee leave balances, arbitrage rebate, and closure and postclosure costs for the San Marcos landfill. The County's long-term debt was reduced by these payments, principal payments to bondholders, and the adjustment to the San Marcos Landfill closure and postclosure liability.

Other miscellaneous debt reductions-general function	$	4,017
Other miscellaneous debt reductions - public protection function		650
Change in accounting estimate for closure and postclosure costs public Protection function - San Marcos Landfill		(981)
Principal payments made		60,849
Payment to refunded bond escrow agent - SANCAL		31,633
Total repayment of long-term obligations	$	96,168

Bond issuance costs are expensed in governmental funds when paid, and are capitalized and amortized over the life of the corresponding bonds for purposes of the statement of activities.

Bond issuance costs	$	1,915
Amortization of bond issuance costs - general function		(2,109)
Difference	$	(194)

Interest expense in the statement of activities differs from the amount reported in governmental funds because additional interest was calculated for bonds and notes payable and amortization of capitalized bond premiums, discounts and deferred amount of refunded debt that are expended in the governmental funds in the year paid.

Accrued interest	$	(7,814)
Premium		(5,960)
Amortization of bond premium		484
Amortization of bond discounts		(511)
Amortization of deferred amount on refunding		(4,092)
Total reduction in interest	$	(17,893)

Bond proceeds are reported as financing sources in governmental funds and thus contribute to the change in fund balance. In the government-wide statements however, issuing debt increases long-term liabilities in the statement of net assets and does not affect the statement of activities. Bond proceeds were received from:

Proceeds of refunding bonds	$	(28,885)
Face Value of bonds issued		(83,510)
Face Value of loans issued		(160)
Total long-term debt proceeds	$	(112,555)

III. Stewardship, Compliance and Accountability

A. Fund Deficits

The following funds in **Table 5** below have an accumulated deficit at June 30, 2005. The deficit within the Redevelopment Agency Capital Projects fund is due to the construction of various capital projects including streets, utilities, sidewalks, traffic signals and other improvements. This deficit will be reduced in future years upon the receipt of the incremental tax revenues. The deficit in the Risk Financing Internal Service fund resulted from accrual of known and projected Workers' Compensation claim liabilities based on actuarial studies. The deficit has increased from the previous fiscal year due to mandated indemnity benefits and a trend of rising medical costs. The County intends to reduce the deficit by focusing resources on injury prevention and safety training programs, and by increasing charges to County departments to provide sufficient cash flow to the Risk Financing fund. The deficit within the Facilities Management Internal Service fund is due to the use of loan proceeds for expenses incurred for maintenance cost for energy conservation equipment. This deficit will be reduced as fees are collected in future years.

Table 5 (Note III-A)

Fund Deficits - Various Funds		
Capital Projects Fund:		
San Diego County Redevelopment Agency (SDCRA)	$	4,964
Internal Service Funds:		
Risk Financing	$	23,079
Facilities Management	$	4,561

IV. Detailed Notes on all Funds

A. Deposits and Investments

1. San Diego County Investment Pool

The *San Diego County Investment Pool (the pool)* is a local government investment pool with approximately $4.1 billion in assets as of June 30, 2005, (consisting of the primary government, pension trust and other fiduciary funds and the First 5 Commission Component Unit). It is headed by the Treasurer-Tax Collector, an elective office that is responsible for tax collection, banking, investment, disbursement and accountability of public funds. The San Diego County Investment Pool is managed by the County Treasurer's Office on behalf of the Pool participants, which include the County, local school districts, local community colleges and other districts and agencies. The local school districts are required by State statutes to deposit their funds with the County of San Diego. "*Mandatory*" participants in the Pool comprise the majority of the Pool's assets, approximately *98%*. All participants comply with the same requirements per the Pool Investment Policy.

The San Diego County Investment Pool operates unde the prudent person standard. Specifically, California Government Code Sections 27000.1-27000.5, 27130-27137, and 53600-53686, authorize the Treasurer to invest funds in permissable types of investment or financial instruments. These include government obligation securities, commercial paper, medium-term notes, asset-backed securities, negotiable certificates of deposit, repurchase and reverse repurchase agreements, money market mutual funds, and collateralized certificates of deposit. The Pool's *investment objectives* are to safeguard principal, meet the liquidity needs of the participants, and achieve an investment return on the funds within the parameters of prudent risk managment.

Pursuant to Sections 27130-27137 of the California Government Code, the Board of Supervisors has established the Treasurer's Oversight Committee (TOC) that monitors and reviews the Pool's investment policy. The TOC consists of members appointed from the districts or offices that they represent, and up to five members of the public, having expertise in, or an academic background in public finance. This Committee requires a financial audit to be conducted annually on a fiscal year basis, which includes limited tests of compliance with laws and regulations. The San Diego County Investment Pool is not registered with the Securities and Exchange Commission (SEC) as an investment company. The Pool does not have any legally binding guarantees of share values.

Each fund type's portion of the pool is displayed on the balance sheet as "Equity in pooled cash and investments." Interest earned on the pooled deposits is accrued in a pooled interest apportionment agency fund and is allocated based on the average daily cash balances of the participating funds. All participating funds share *earnings* and *losses proportionately*. State law permits interest income related to certain funds to be considered as income of the General Fund of the County. Such interest has been recorded as revenue in the General Fund.

2. Investments Outside of the Pool

a. Cash and Investments with Fiscal Agents

Cash with Fiscal Agents totaled $402.8 million on deposit with trustees for the General Fund, Tobacco Securitization Joint Special Revenue Fund, Air Pollution Special Revenue Fund, SANCAL Special Revenue Fund, Housing Authority Special Revenue Fund, Pension Obligation Bond Debt Service Fund, SANCAL Debt Service Fund, Redevelopment Agency Debt Service Fund, SANCAL Capital Projects Fund, and Other Agency Funds.

Investments with Fiscal Agents totaled approximately $801.6 million with Trustees. These amounts are accounted for in the General Fund, Tobacco Securitization Special Revenue Fund, Inactive Wastesites Fund, Pension Obligation Bonds Debt Service Fund and SANCAL Debt Service Fund.

b. Pension Trust Fund

SDCERA had *investments* of approximately $6.8 billion as of June 30, 2005. Investments are reported at fair value upon closing sale prices reported on recognized securities exchanges on the last business day of the period. For listed securities having no sales reported or for unlisted securities, fair value is based upon last reported bid prices. All purchases and sales of investments are accounted for on a trade-date basis, and dividends declared but not received are accrued on the ex-dividend date. Realized and unrealized gains or losses of securities are determined on the basis of average costs. Real estate investments consist of real estate equities primarily in office, industrial, retail and residential properties with 98% in the United States and 2% International.

In addition to the above, SDCERA utilizes derivative financial instruments, such as equity swap agreements and stock and bond futures contracts that allow SDCERA to build portfolios with performance characteristics very similar to benchmarks and to manage allocation of risk. As of June 30, 2005 SDCERA had two types of derivative financial instruments; equity swaps and financial futures.

Equity swaps allow SDCERA to exchange a money market return for the rights to the return on a specific index of equity securities. As of June 30, 2005 SDCERA entered into S&P 500 Swap contracts with a notional value of $1.185 billion and a fair value of $1.173 billion. Futures represent commitments to purchase or sell securities at a future date and at a specified price. Future contracts are traded on organized exchanges (exchange traded) thereby minimizing credit risk. The net change in the futures contracts value is settled daily in cash with the exchanges. As shown in **Table 6** below, as of June 30, 2005 SDCERA had the following futures balances:

Table 6 (Note IV-A-2-b)

Notional Amount		Long/(Short)
International Equity	$	253,720
Domestic Equity		(169,527)
International Fixed Income		36,550
Domestic Fixed Income		249,907
Commodities		225,000
Total	$	532,650

These financial instruments are intended to be equivalent to the asset they are designed to emulate. SDCERA's use of swaps and futures is structured such that market exposure is fundamentally equivalent to the direct cash investments. SDCERA will only execute a swap agreement with counterparties rated A or higher. The use of swap agreements exposes SDCERA to the risk of dealing with financial counterparties and their ability to meet the terms of the contracts. However, all swaps are fully collateralized by cash at least equal to the notional value of the most recent cash reset. Allowing insufficient collateral is strictly prohibited as a trading strategy by SDCERA's investment policies.

3. Deposits

(For Notes IV-A-3., Deposits through IV-A-11., Securities Lending Transactions, please refer to **Tables 7 through 18** on **pages 81** through **86)**.

County Investment Pool - At year-end the carrying amount of the County's demand deposits was $48.698 million. Of this balance $494 thousand was covered by federal deposit insurance and $48.204 million was considered a collateralized custodial credit risk.

Cash and Investments with Fiscal Agents - At year-end the carrying amount of the County's demand deposits was $227.425 million. Of this balance $1.666 million was covered by federal deposit insurance; $61.991 million was collateralized with securities held by the

pledging agent but not in the County's name and the remaining $163.768 million was uncollateralized.

SDCERA Investment Portfolio - At year-end the carrying amount of SDCERA's demand deposits was $175.335 million. A deposits and investments reconciliation as reported in the basic financial statements is summarized on **Table 7** on page **81.**

4. Investments

As of June 30, 2005, investments in *the County Pool,* with *Fiscal Agents* and in the *Pension Trust Fund, (SDCERA) are shown on* **Tables 8 through 10** on **pages 82** and **83.**

5. Deposit and Investment Risk

In accordance with GASB Statement 40, Deposit and Investment Risk Disclosures, investment risk disclosure is required for; interest rate risk, credit risk (including custodial credit risk and concentrations of credit risk) and foreign currency risk.

As of June 30, 2005, the Pool had the following investments and maturities shown on **Table 8** on **page 82.**

6. Interest Rate Risk

County's Investment Pool - The Pool does not have a general policy to manage interest rate risk, however it is banned from purchasing Inverse Floaters, Range Notes, Interest only strips derived from a pool of mortgages, and any security that could result in zero interest accrual. It is limited on maturity levels, which in turn, allows the Pool to manage its exposure to fair value losses arising from increased rates.

Investments with Fiscal Agents - No general policies have been established to manage interest rate risk, however, moneys held by trustees on behalf of the County may generally only be invested in permitted investments specified in trustee or indenture agreements. As of June 30, 2005, the following investments and maturities with fiscal agents were as shown on **Table 11 on page 83.**

SDCERA Investment Portfolio - SDCERA does not have a general policy to manage interest rate risk, but requires investment managers to diversify by issue, maturity, sector, coupon and geography. As of June 30, 2005, SDCERA had the following investments and maturities as shown on **Table 12** on **page 83.**

7. Credit Risk

County's Investment Pool - As of June 30, 2005, the Investment Pool's Security Ratings are shown on **Table 8** on **page 82.**

Investments with Fiscal Agents - No general policies have been established for credit risk, however, moneys held by trustees on behalf of the County may generally only be invested in permitted investments specified in trustee or indenture agreements. The security ratings for these investments are shown on **Table 13** on **page 84.**

SDCERA Investment Portfolio - SDCERA's Investment guidelines address fixed income quality requirements by investment category. The minimum investment grade held in domestic fixed income portfolios shall be no lower than "BBB" (as rated by Moody, Standard & Poor's, or Fitch's equivalent). Domestic high yield fixed income portfolios must have a weighted average quality of B/B+ or higher (Moody or Standard & Poor's equivalent). Not rated issues must be evaluated by the manager and determined that if rated they would not lower the weighted average below B/B+. SDCERA has no policy for Global and Emerging Market Fixed Income.

Tables 14 and 15 on **pages 84 and 85** illustrate SDCERA's Fixed Income securities ratings as of June 30, 2005, shown as a percentage of the total portfolio.

Domestic Fixed Income Portfolio

SDCERA's Domestic Fixed Income portfolio of government securities, collateralized mortgage obligations, corporate bonds, private placements, and other bonds include $456.296 million or 99.5% that are rated BBB or higher and $2.283 million or 0.5% currently rated BB.

Global Fixed Income Portfolio

SDCERA's Global Fixed Income portfolio includes corporate bonds and sovereign debt. The weighted average rating for Global Fixed Income portfolio was AA/AAA, excluding $652 thousand or 0.1% of unrated securities.

High Yield Fixed Income Portfolio

The weighted average quality of the High Yield Fixed Income Portfolio as of June 30, 2005 was B/BB, excluding $40.107 million or 10.3% of unrated securities in the portfolio.

Emerging Market Debt

SDCERA's Emerging Market Debt portfolio invests in sovereign debt of emerging countries. As of June 30, 2005, the weighted average rating for Emerging Market Debt portfolio was rated BB, excluding $74 million or 23.3% of unrated securities in the portfolio.

8. Concentration of Credit Risk

County's Investment Pool - The Pool Investment Policy limits the amount of exposure to any one single issuer. The Investment Policy is limited to 5% per issuer and cannot exceed this limit. An exclusion to this limit is dependent upon the weighted average days to maturity for commercial paper. If the weighted average days is 5 days or less the issuer limit can increase to 10% of total portfolio. The County of San Diego adheres to both State law and the County's Investment Policy for limits on investments.

Cash and Investments with Fiscal Agents - No general policies have been established to limit the amount of exposure to any one single issuer, however, moneys held by trustees on behalf of the County may generally only be invested in permitted investments specified in trustee or indenture agreements.

SDCERA Investment Portfolio - Fixed income managers are expected to adhere to the following guidelines as a means of limiting credit risk. Domestic Fixed Income managers are limited within their portfolios to no more than 5% exposure in any single security, with the exception of United States Treasury and government agencies. High Yield and International Fixed Income managers limit is 10% exposure in any single security, with the exception of United States Treasury and government agencies. As of June 30, 2005, SDCERA has no single issuer that exceeds 5% of total fixed income investments.

9. Custodial Credit Risk

County's Investment Pool - The County of San Diego does not invest in Category 3 type investments. The Investment policy does not permit investments in uninsured and unregistered securities not held by the County. However, the Policy does permit for securities lending transactions. The portfolio has not been exposed to these types of investments during the fiscal year.

Cash and Investments with Fiscal Agents - There are no general policies addressing custodial credit risk, however, moneys held by trustees on behalf of the County may generally only be invested in permitted investments specified in trustee or indenture agreements.

SDCERA Investment Portfolio - SDCERA does not have a general policy addressing custodial credit risk, but it is the practice of the Fund that all investments are insured, registered, or held by the plan or its agent in the Plan's name. Deposits are to be insured, registered or collateralized with securities held at fiscal agents in the Plan's name. SDCERA also retains investment managers that specialize in the use of a particular asset class. Investment managers are subject to the guidelines and

controls established in the SDCERA Investment Policy and contracts executed with the Board. SDCERA utilizes a third party as custodian over the plan assets.

In March 2005 the Board of Retirement completed a comprehensive asset/liability study that resulted in a new asset allocation strategy. This strategy specified an asset allocation target of 24% Domestic Equity, 25% International Equity, 31% Fixed Income, 10% Real Estate, 5% Commodities and 5% Alternative Equity.

10. Foreign Currency Risk

County's Investment Pool - There are no general policies addressing foreign currency based securities, however the County does not invest in foreign currency based securities.

Cash and Investments with Fiscal Agents - There are no general policies addressing foreign currency based securities, however, moneys held by trustees on behalf of the County may generally only be invested in permitted investments specified in trustee or indenture agreements.

SDCERA Investment Portfolio - SDCERA's investment policy allows international managers to enter into foreign exchange contracts provided that the contracts have a maturity of one year or less and are limited to hedging currency exposure existing in the portfolio. SDCERA's exposure to foreign currency risk derives from its positions in foreign currency denominated international equity and fixed income investments.

SDCERA's net exposure to foreign currency risk is shown on **Table 16** on **page 85**.

11. Securities Lending Transactions

County's Investment Pool - Although the Pool's Policy permits securities lending transactions, the portfolio has not been exposed to these types of investments during the fiscal year.

Cash and Investments with Fiscal Agents - There are no general policies addressing securities lending transactions, however, moneys held by trustees on behalf of the County may generally only be invested in permitted investments specified in trustee or indenture agreements.

SDCERA Investment Portfolio - SDCERA lends U.S. government obligations, domestic and international bonds, and equities to various brokers with a simultaneous agreement to return collateral for the same securities plus a fee in the future. The securities lending agent manages the securities lending program and receives securities and cash as collateral. Collateral cash is pledged at 102% and 105% of the fair value of domestic securities and non-domestic securities lent, respectively. There are no restrictions on the amount of securities that can be lent at one time. The term to maturity of the loaned securities is generally not matched with the term to maturity of the investment of the cash collateral.

SDCERA's securities lending transactions as of June 30, 2005, are summarized on **Table 17** on **page 86.** The Fund lent $612.033 million in securities and received collateral of $123.832 million and $503.190 million in securities and cash, respectively from borrowers.

SDCERA receives a premium on all securities it holds as collateral. As of June 30, 2005, the cash collateral that was received from the borrowers was then invested in the investment types as shown on **Table 18** on **page 86.**

SDCERA's investment guidelines require that certificates of deposit, commercial paper, notes, bonds, and other debt obligations that are maturing within one year shall be no lower than A-I as rated by Standard & Poor's, or P-I by Moody's. Obligations may have fixed, floating, or variable rate interest payment provisions. Obligations maturing beyond one year shall be rated at least A/A2 (as rated by Standard & Poor's or Moody's equivalent). As of June 30, 2005, all of SDCERA's securities lending investment's maturing in less than one year

were rated A-1/P-1 for US corporate and certificate of deposit floating rate, and AAA/Aaa for asset backed securities and bank notes as rated by Standard & Poor's and Moody's. For obligations maturing beyond one year, eleven percent of the investment in asset backed securities was rated AAA/Aaa by Standard & Poor's and Moody's. The remaining 89 percent of US corporate floating rate, bank notes, and certificates of deposit floating rate were rated AA/Aa3.

SDCERA does not have the ability to pledge or sell collateral securities without a borrower default. At the end of the fiscal year, SDCERA has no credit risk exposure to borrowers because the amounts the system owes them exceed the amounts they owe the system. As with other extensions of credit, SDCERA may bear the risk of delay in recovery or of rights in the collateral should the borrower of the securities fail financially. In addition, the Bank of New York indemnifies SDCERA against all borrower default.

Table 7 (Note IV-A-3)

Deposits and Investments Reconciliation

	Primary Government	Fiduciary Funds	Sub-Total	Component Unit	Total
Equity in pooled cash and investments	$ 994,505	2,963,897	3,958,402	172,983	4,131,385
Cash with fiscal agent	118,139	186,744	304,883		304,883
Restricted cash with fiscal agent	97,877		97,877		97,877
Collections in transit	6,725	10,076	16,801		16,801
Imprest cash	315	35	350		350
Investments	69,894	6,831,839	6,901,733		6,901,733
Restricted investments	731,678		731,678		731,678
Total	2,019,133	9,992,591	12,011,724	172,983	12,184,707
Less:					
Cash with fiscal agent					(304,883)
Restricted cash with fiscal agent					(97,877)
Collections in transit					(16,801)
Imprest cash					(350)
Deposits					(48,698)
Total investments	$				11,716,098
Investments in County Pool	$		4,082,687		
Deposits			48,698		
Equity in pooled cash and investments	$		4,131,385		
Investments in County Pool	$		4,082,687		
Investments with Fiscal Agent			801,572		
Investments in SDCERA			6,831,839		
Total Investment	$		11,716,098		

Table 8 (Note IV-A-4)

Investments - County Pool

Investment Type	Moody's Rating	S&P Rating	Rate Range%	Maturity Date Range	Par value	Amortized Cost	Fair Value	Yield To Maturity	Weighted Average Maturity	Percent of Total
U.S. Government Agencies:										
Federal Home Mortgage Corporation	Aaa	AAA	2.25 - 4.00	06/06 - 08/07	$ 100,000	100,000	98,646	2.89%	541	2%
Federal Home Loan Bank	Aaa	AAA	1.8 - 4.15	10/05 - 07/07	721,295	720,305	711,538	2.73%	412	17%
Federal National Mortgage Association	Aaa	AAA	2.00 - 4.00	12/05 - 09/07	500,691	500,604	494,429	2.55%	439	12%
Federal Farm Credit Bank	Aaa	AAA	1.85 - 3.50	10/05 - 05/08	496,040	495,719	488,681	2.41%	414	12%
U.S Treasury Notes	Aaa	AAA	1.50	3/06	100,000	99,588	98,555	2.06%	274	2%
Short Term Notes:										
Commercial Paper	P-1	A-1+	2.67 - 3.40	7/05 - 10/05	1,138,714	1,135,359	1,135,940	3.14%	34	28%
Medium - Term Notes	Aa2	AA+	2.00 - 5.35	12/05 - 11/06	293,987	296,807	294,883	2.92%	298	7%
Repurchase Agreements	P-1	A-1	3.51	07/05	50,000	50,000	50,000	3.51%	1	1%
Negotiable Certificates of Deposit	Aaa	AAA	2.15 - 3.75	07/05 - 04/06	625,000	624,937	623,287	2.80%	146	17%
Open - End Institutional Money Market Funds	Aaa	AAA	2.97 - 3.00	07/05	27,600	27,600	27,600	2.99%	1	1%
Asset-Backed Notes	Aaa	AAA	2.50 - 2.55	04/06 - 01/07	60,000	59,699	59,128	2.90%	449	1%
Total Investments					$ 4,113,327	4,110,618	4,082,687	2.81%	259	100%

Table 9 (Note IV-A-4)

Investments - With Fiscal Agents

Investment Type	Moody's Rating	S&P Rating	Maturity Under 1 Month	Maturity 1 to 6 months	Maturity 6 to 12 Months	Maturity Greater than 12 Months	Market Value	Coupon Rate	Maturity Date
Tax and Revenue Anticipation Notes-Investment Agreement	Unrated	Unrated	$ 360,000				360,000	NA	7/22/2005
Fixed Income Tax Exempt Bonds	Various	Various		25,557		298,371	323,928	1.79%-5.625%	11/15/2006-02/01/2042
Commercial Paper	P-1	A-1	44,995				44,995	NA	7/7/2005
Federal Farm Credit Bank Notes	NA	AAA	24,897				24,897	NA	10/28/2005
AIG Investment Agreement	Unrated	Unrated		39,277			39,277	NA	7/3/2007
Bayerische Investment Agreements	Unrated	Unrated			8,473		8,473	NA	4/26/2006
Common Stock	Aa2	AA-				2	2	NA	NA
Total Investments			$ 429,892	64,834	8,473	298,373	801,572		

Table 10 (Note IV-A-4)

Investments - Pension Trust Fund (SDCERA)	Fair Value
Domestic equity securities	$ 882,662
Cash, cash equivalents, and securities domestic equity swaps and futures	1,368,556
International equity securities	1,489,825
Securities lending collateral	503,102
United States government obligations	628,206
Domestic corporate bonds	557,566
International bonds	794,671
Cash and securities for overlay futures	58,557
Alternative equity and real estate	548,694
Total investments	$ 6,831,839

Table 11 (Note IV-A-6)

Investments and Maturities - With Fiscal Agents					
Investment Type	Market Value	Maturity Under 1 month	Maturity 1 to 6 Months	Maturity 6 to 12 Months	Maturity Greater than 12 Months
Tax and Revenue Anticipation Notes- Investment Agreement	$ 360,000	360,000			
Fixed Income Tax Exempt Bonds	323,928		25,557		298,371
Commercial Paper	44,995	44,995			
Federal Farm Credit Bank Notes	24,897	24,897			
AIG Investment Agreement	39,277		39,277		
Bayerische Investment Agreements	8,473			8,473	
Common Stock	2				2
Total Investments	$ 801,572	429,892	64,834	8,473	298,373

Table 12 (Note IV-A-6)

Investments and Maturities - SDCERA Investment Portfolio					
Investment Type	Fair Value	Maturity Less than 1 year	Maturity 1 to 5 years	Maturity 6 to 10 years	Maturity More than 10 years
Asset and mortgage backed securities	$ 169,055	4,182	6,005	2,065	156,803
Collateralized mortgage obligations	99,016		525		98,491
Convertible Bonds	191,442	7,133	101,021	5,530	77,758
Corporate bonds	281,555	9,300	89,217	126,633	56,405
Emerging market debt securities	317,911	1,975	33,993	39,256	242,687
International bonds	2,189			2,189	
International Governments	491,457	12,510	240,857	138,470	99,620
Managed Futures *	53,994	NA	NA	NA	NA
Municipals	7,922		219	3,533	4,170
Private placements	43,927		2,303	33,561	8,063
Treasury inflation protected securities	210,304		42,761	98,217	69,326
US Treasuries	111,671	28,438	33,496	21,753	27,984
Total Investments	$ 1,980,443	63,538	550,397	471,207	841,307

* Investment maturities for Managed Futures are not available and are therefore not included in the subtotals by maturity.

Table 13 (Note IV-A-7)

Securities Ratings - Investments With Fiscal Agents

Fixed Income Tax Exempt Bonds:	S&P Rating	Market Value	Percent of Total
ALASKA ST HSG FIN CORP	AAA/A-1+	$ 18,596	6%
ATLANTA GA ARPT PASSENGER FAC	AAA	15,225	5%
BARTON CNTY GA DEV AUTH POLLU	A	10,000	3%
BAY AREA TOLL AUTH CA TOLL BRG	AAA	9,975	3%
CALIFORNIA ST DEPT WTR RES PWR	AAA	5,628	2%
CALIFORNIA ST DEPT WTR RES PWR	AAA	1,124	0%
CALIFORNIA STATEWIDE CMNTYS	AAA	25,464	8%
CALIFORNIA STATEWIDE CMNTYS	A+/A-1	6,396	2%
CALIFORNIA STATEWIDE CMNTYS	A+/A-1	4,950	2%
DELAWARE VALLEY PA REGL FIN	AAA	10,000	3%
GRAND TRAVERSE CNTY MI HOSP	NR	19,700	6%
INDIANA HLTH FAC HOSP REV	AAA	8,500	3%
JEA FL ELEC SYS REV	AAA	15,000	5%
JEFFERSON CNTY AL SWR REV	AAA	20,000	6%
MEDFORD OR HOSP FACS AUTH REV	AAA	20,000	6%
METROPOLITAN TRANSN AUTH NY	AAA	20,000	6%
NEW YORK N Y	AAA	11,320	3%
PUTNAM CNTY GA DEV AUTH POLLUT	A/A-1	19,025	6%
SEATTLE WA NUM LT + PWR REV	AA+/A-1+	16,900	5%
SOUTH CAROLINA ST	AA+	9,849	3%
UNIVERSITY AL UNIV REVS	AAA	7,650	2%
WAKE CNTY NC INDL FACS + PLLTN	AAA	5,000	2%
WAKE CNTY NC INDL FACS + PLLTN	AAA	10,000	3%
WAKE CNTY NC INDL FACS + PLLTN	AAA	12,000	4%
WAYNE CNTY ARPT AUTH REV	AAA	16,000	5%
DAPHNE AL SPL CARE FACS	AAA	5,626	1%
Total		$ 323,928	100%

Table 14 (Note IV-A-7)

Fixed Income Securities Ratings - SDCERA Investment Portfolio

Credit Risk	Domestic Fixed Income	Global Fixed Income	High Yield Fixed Income	Emerging Market Debt Fixed Income	Total
AAA	$ 29,329	448,692	1,669		479,690
AA	222	28,944	1,691		30,857
A	304	70,323	11,679	7,248	89,554
BBB	2,997	77,920	34,731	87,076	202,724
BB	2,283	11,657	92,538	24,797	131,275
B		67	159,207	120,170	279,444
CCC			42,947	4,610	47,557
CC			3,184		3,184
D			2,984		2,984
NR		652	40,107	74,010	114,769
Govt	423,445	174,960			598,405
Total	$ 458,580	813,215	390,737	317,911	1,980,443

Table 15 (Note IV-A-7)

Fixed Income Securities Ratings (Percent of Portfolio)	SDCERA Investment Portfolio			
Credit Risk	Domestic Fixed Income	Global Fixed Income	High Yield Fixed Income	Emerging Market Debt Fixed Income
AAA	6.4%	55.2%	0.4%	0.0%
AA	0.1%	3.6%	0.4%	0.0%
A	0.1%	8.6%	3.0%	2.3%
BBB	0.6%	9.6%	8.9%	27.4%
BB	0.5%	1.4%	23.7%	7.8%
B	0.0%	0.0%	40.7%	37.8%
CCC	0.0%	0.0%	11.0%	1.4%
CC	0.0%	0.0%	0.8%	0.0%
D	0.0%	0.0%	0.8%	0.0%
NR	0.0%	0.1%	10.3%	23.3%
Govt	92.3%	21.5%	0.0%	0.0%
	100%	100%	100%	100%

Table 16 (Note IV-A-10)

Foreign Currency Exposure - SDCERA Investment Portfolio	
Currency	Fair Value
JAPANESE YEN	$ 410,945
EURO CURRENCY	249,013
BRITISH PND STERLING	218,812
AUSTRALIAN DOLLAR	195,174
SOUTH KOREAN WON	112,655
SWISS FRANC	110,169
SINGAPORE DOLLAR	67,378
MEXICAN NUEVO PESO	56,228
HONG KONG DOLLAR	53,570
SOUTH AFRICAN RAND	47,802
SWEDISH KRONA	41,642
BRAZILIAN REAL	34,878
TAIWAN DOLLAR	31,161
THAI BAHT	21,718
INDIAN RUPEE	21,648
INDONESIAN RUPIAH	17,724
MALAYSIAN RINGGIT	14,567
TURKISH LIRA	14,444
EGYPTIAN POUND	12,741
NORWEGIAN KRONE	11,468
RUSSIAN NEW RUBLE	8,983
CHILEAN PESO	8,905
NEW ZEALAND DOLLAR	8,188
DANISH KRONE	8,082
HUNGARIAN FORINT	8,044
RENMINBI YUAN	7,986
POLISH ZLOTY	5,386
CANADIAN DOLLAR	(41,928)
Other (Less than $2 million holdings)	9,292
Total	$ 1,766,675

Table 17 (Note IV-A-11)

Securities Lending Transactions - SDCERA Investment Portfolio			
Investment Type	Fair Value	Maturity Less than 1 year	Maturity 1 to 5 years
U.S. Corporate Floating Rate	$ 194,015	25,014	169,001
Asset Back Securities	52,918	8,506	44,412
Bank Notes	108,536	8,502	100,034
Certificates of Deposit Floating Rate	85,985	9,996	75,989
Repurchase Agreements	61,722	61,722	
Other (cash)	114	114	
Total	$ 503,291	113,854	389,437

Table 18 (Note IV-A-11)

Securities Lent - SDCERA Investment Portfolio			
Investment Type	SDCERA Securities Lent	Securities Received Value	Cash Received Value
Lent for cash collateral:			
U.S. government and agency securities	$ 123,384		124,251
International governments securities	21,980		22,989
Domestic corporate fixed income securities	125,762		128,479
Domestic equities	178,859		184,285
International equities	41,314		43,187
Lent for securities collateral:			
Domestic Equity	2,808	2,905	
Domestic Government Securities	104,150	106,186	
International equities	6,311	6,874	
International governments securities	7,465	7,866	
Total	$ 612,033	123,832	503,190

B. Receivables

Receivable balances not expected to be collected within the next fiscal year are as follows:

1. Community Development Block Grant - $14.176 million, Home Investment Partnership Program - $13.294 million, Mobile Home Opportunity Assistance Program - $5.178 million and various REHAB programs - $7.406 million. These are included in the General and Housing Special Revenue Funds and represent loans for the provision low-income housing development activities under these programs.

2. Metropolitan Transit Development Board (MTDB) - General Fund. The County leases the Metropolitan Transit System (MTS) Towers building from the San Diego Regional Building Authority. The County subleases a 27.61% share of the building to the Metropolitan Transit Development Board (MTDB). At June 30, 2005 the MTDB receivable balance was $12.684 million. Of this amount, $11.838 million will not be received in the next fiscal year.

3. Sale and Use of Surplus Land - Road Fund, Airport Enterprise Fund $842 thousand.

Table 19 below presents receivables at June 30, 2005 for the County's individual major funds, nonmajor internal service, governmental and business type activities' funds and the discrete component unit including the applicable allowances for uncollectible accounts.

Table 19 (Note IV-B)

Primary Government and Discretely Presented Component Unit Receivables	Accounts	Interest	Due From Other Gov't Agencies	Notes	Loans	Other	Total Receiv-ables	Allowance For Doubtful Accounts	Receivables Net
Governmental activities:									
General Fund	$ 1,033	4,819	197,314		19,052	13,008	235,226	(10,699)	224,527
Tobacco Securitization Special Revenue Fund	1,187	42					1,229		1,229
Other governmental funds	7,451	1,979	91,061	1,590	33,686		135,767		135,767
Internal service funds	257	219	4,568				5,044		5,044
Total governmental activities	9,928	7,059	292,943	1,590	52,738	13,008	377,266	(10,699)	366,567
Business-type activities:									
Enterprise Funds	253	464	163				880		880
Total business-type activities	253	464	163				880		880
Component Unit:									
First 5 Commission		544	8,230				8,774		8,774
Total component unit	$	544	8,230				8,774		8,774

C. County Property on Lease to Others

The County has *noncancelable* operating leases for certain properties which are not material to the County's governmental operations, except for the aforementioned sublease of a share of the Metropolitan Transit System (MTS) Towers. In this regard, the share of the County's property under this lease is an estimated $12.74 million in land and structures and improvements with accumulated depreciation of $4.3 million at June 30, 2005.

Additionally, the Airport Enterprise Fund derives a substantial portion of its revenues from noncancelable operating leases with air carriers and concessionaires. The Airport Enterprise Fund's property under operating leases includes an estimated $2.4 million in land at June 30, 2005,

Lease revenues for both non-cancelable and cancelable leases for the year ended June 30, 2005 were approximately $22.81 million.

Future minimum *revenue* to be received under these noncancelable operating leases as of June 30, 2005 are noted below in **Table 20**. (One lease extends through 2091 for a two acre parcel leased to a non-profit public benefit corporation.)

Table 20 (Note IV-C)

Lease Revenue County Property Leased To Others Fiscal Year	Minimum Lease Revenue
2006	$ 12,252
2007	11,608
2008	11,070
2009	10,818
2010	10,363
2011-2091	161,764
Total	$ 217,875

D. Capital Assets

1. Primary Government

Capital asset activity for the year ended June 30, 2005 was as follows:

Governmental Activities:

On **Table 21** below, building and infrastructure projects are recorded as construction in progress until completion. Intangible projects such as software acquisition and implementation are recorded as contracts in progress until implementation is completed.

Table 21 (Note IV-D)

Capital Assets Governmental Activities	Beginning Balance at July 1, 2004	Increases	Decreases	Ending Balance at June 30, 2005
Capital assets, not being depreciated:				
Land	$ 262,110	5,323	(473)	266,960
Construction in progress	175,086	30,330	(64,795)	140,621
Total capital assets, not being depreciated	437,196	35,653	(65,268)	407,581
Capital assets, being depreciated:				
Buildings and improvements	969,977	17,751	(25,098)	962,630
Equipment	167,976	74,590	(11,117)	231,449
Road network	2,074,421	45,427		2,119,848
Bridge network	39,193	760		39,953
Total capital assets, being depreciated	3,251,567	138,528	(36,215)	3,353,880
Less accumulated depreciation for:				
Buildings and improvements	(280,611)	(18,625)	6,286	(292,950)
Equipment	(88,800)	(15,882)	9,295	(95,387)
Road network	(627,137)	(59,202)		(686,339)
Bridge network	(11,645)	(747)		(12,392)
Total accumulated depreciation	(1,008,193)	(94,456)	15,581	(1,087,068)
Total capital assets, being depreciated, net	2,243,374	44,072	(20,634)	2,266,812
Governmental activities capital assets, net	$ 2,680,570	79,725	(85,902)	2,674,393

Depreciation expense was charged to functions of the primary government as shown in **Table 22** below:

Table 22 (Note IV-D)

Depreciation Expense - Governmental Activities	
General Government	$ 3,708
Public Protection	15,269
Public Ways and Facilities	60,212
Health and Sanitation	2,609
Public Assistance	684
Education	77
Recreational and Cultural	1,581
Internal Service Funds	10,316
Total Depreciation Expense - Governmental Activities	$ 94,456

Business Type Activities:

On **Table 23** below, building and infrastructure projects are recorded as construction in progress until completion.

Table 23 (Note IV-D)

Capital Assets - Business Type Activities	Beginning Balance at July 1, 2004	Increases	Decreases	Ending Balance at June30, 2005
Capital assets, not being depreciated:				
Land	$ 10,677			10,677
Construction in progress	15,516	4,480	(3,184)	16,812
Total capital assets, not being depreciated	26,193	4,480	(3,184)	27,489
Capital assets, being depreciated:				
Buildings and improvements	37,291	5,441		42,732
Equipment	1,214		(8)	1,206
Infrastructure		139		139
Sewer network	63,746	1,036		64,782
Total capital assets, being depreciated	102,251	6,616	(8)	108,859
Less accumulated depreciation for:				
Buildings and improvements	(19,627)	(907)		(20,534)
Equipment	(848)	(55)	8	(895)
Sewer network	(26,031)	(1,307)		(27,338)
Total accumulated depreciation	(46,506)	(2,269)	8	(48,767)
Total capital assets, being depreciated, net	55,745	4,347		60,092
Enterprise fund capital assets, net	$ 81,938	8,827	(3,184)	87,581

Depreciation expense was charged to *business type activities* as shown on **Table 24** below:

Table 24 (Note IV-D)

Depreciation Expense - Business Type Activities	
Airport	$ 911
Wastewater	23
Sanitation	1,335
Total Depreciation Expense	$ 2,269

2. Capital Commitments

At June 30, 2005, major contracts entered into for software development, construction in progress, buildings, equipment and infrastructure were as follow, listed by fund within *governmental and business-type activities* are shown below in **Table 25**:

Table 25 (Note IV-D)

Capital Commitments	Project Title	Remaining Commitments
Governmental Activities:		
General Fund	Registrar of Voters-Integrated Voting System and Optional Items	$ 29,779
	Integrated Property Tax System (PTS)	31,287
	Revenue Plus Collection System	1,379
	Automated Records MGMT & Field Reporting Cots Software Installation	1,705
	Regional Communications System Motorola Services and Equipment	3,739
	Service MGMT Access and Resource System (Smart)	2,416
	Creative Socio-Medics Corpublic Health Information System Acquisition	1,743
	Sub Total	72,048
Other Governmental Funds	Construction of Forester Creek Drainage	3,000
	Construction of Mission Road	3,008
	Construction of Valley Center Road South, Phase I	2,800
	Spring Valley Gym and Teen Center	1,744
	Construction of Edgemoor Skill Nursing Facility	61,891
	Construction of APCD Bldg in Scripps Ranch	7,508
	Sub Total	79,951
Business-type Activities:		
Enterprise Funds	Jamacha Blvd Sewer	2,000
	Construction of Gillespie Field Runway	2,424
	Sub Total	4,424
	Total	$ 156,423

E. Payables

The County's payables at June 30, 2005 are shown on **Table 26** for the General Fund, nonmajor internal service funds, governmental funds, business type activities' funds and the discrete component unit:

Table 26 (Note IV-E)

Payables	Vendors	Due to Other Gov't Agencies	Other	Total Payables
Governmental Activities:				
General Fund	$ 46,862	48,431	6,473	101,766
Other governmental funds	15,917	9,166	75	25,158
Internal service funds	15,797	244		16,041
Total governmental activities	78,576	57,841	6,548	142,965
Business-type activities:				
Enterprise Funds	2,122	39		2,161
Total business-type activities	2,122	39		2,161
Component Unit:				
First 5 Commission	5,813			5,813
Total component unit	$ 5,813			5,813

F. Interfund Transactions

The composition of interfund balances as of June 30, 2005, is as follows:

1. Due To/Due From Other Funds

Due to/due from other funds shown in **Table 27** below arise due to the exchange of goods or services between funds that were pending the transfer of cash as of June 30, 2005. These due to/from other funds have been eliminated in the government-wide financial statements, except for "internal balances" that are reflected between the governmental and business-type statements as of June 30, 2005.

Table 27 (Note IV-F-1)

Due To/From Other Funds

Receivable Fund	Payable Fund	Amount
General Fund	Tobacco Securitization Special Revenue Fund	$ 2,779
	Nonmajor Governmental Funds	117,745
	Nonmajor Enterprise Funds	75
	Internal Service Funds	51,610
Total General Fund		172,209
Nonmajor Governmental Funds	General Fund	6,496
	Nonmajor Governmental Funds	745
	Nonmajor Enterprise Funds	171
	Internal Service Funds	79
Total Nonmajor Governmental Funds		7,491
Nonmajor Enterprise Funds	General Fund	28
	Nonmajor Governmental Funds	1
	Nonmajor Enterprise Funds	906
	Internal Service Funds	1
Total Nonmajor Enterprise Funds		936
Internal Service Funds	General Fund	14,818
	Nonmajor Governmental Funds	1,123
	Nonmajor Enterprise Funds	95
	Internal Service Funds	279
Total Internal Service Funds		16,315
Total		$ 196,951

2. Advances

Advances to/from at June 30, 2005 are noted on **Table 28** below. The purpose of these advances was primarily for the establishment of loans that are not due within one year. These loans are for the planning, undertaking, construction or operation of redevelopment projects within the County. These advances to/from other funds have been eliminated in the government-wide financial statements, except for "internal balances" that are reflected between the governmental and business-type statements as of June 30, 2005.

Table 28 (Note IV-F-2)

Advances

Funds	Advances To Other Funds	Advances From Other Funds
General Fund	$ 928	
Nonmajor Governmental Funds	102	10,699
Nonmajor Enterprise Funds	9,312	239
Internal Service Funds	596	
Total	$ 10,938	10,938

3. Prior-Year Advance

Prior to the issuance of Revenue Bonds in 1995 by the San Diego County Redevelopment Agency, the County Airport Enterprise Fund funded the initial expenditures of the Agency's two airport projects. The Redevelopment Agency is required to reimburse the Airport Enterprise Fund, which spent approximately $9.6 million on the projects consisting of $3.7 million for initial expenditures and $5.9 million for 2001. The Agency pays interest on advances, but is not responsible for payment until funds are available for this purpose. As of June 30, 2005, interest of approximately $4.3 million has accrued on these advances; however such amounts have not been recorded because the ultimate collection has not been determined.

4. Transfers In/Transfers Out

The purposes of these transfers were primarily for reimbursement of project costs, lease payments, initiation fees and replacement costs. Transfers in/transfers out at June 30, 2005 were as follows on **Table 29** below:

Table 29 (Note IV-F-4)

Transfers In/Transfers Out		
From	To	Amount
General Fund	Nonmajor Governmental Funds	$ 175,599
	Internal Service Funds	3,629
Total General Fund		179,228
Tobacco Securitization Special Revenue Fund	General Fund	23,278
Nonmajor Governmental Funds	General Fund	544,668
	Nonmajor Governmental Funds	71,963
	Internal Service Funds	490
Total Nonmajor Governmental Funds		617,121
Nonmajor Enterprise Funds	Nonmajor Governmental Funds	588
	Internal Service Funds	176
Total Nonmajor Enterprise Funds		764
Internal Service Funds	General Fund	731
	Nonmajor Governmental Funds	2,663
	Internal Service Funds	153
Total Internal Service Funds		3,547
Total		$ 823,938

G. Short-Term Obligations

The County's short-term borrowing program consists of its annual Tax and Revenue Anticipation Notes (Notes), which fund the County's annual operating cash flow needs, and the issuance of Teeter Commercial Paper, which fund payments to public agencies their full share of property taxes levied. The County bears the risk of loss on delinquent property taxes that go unpaid; however, it also benefits from the penalties associated with these delinquent property taxes when they are paid.

On July 1, 2004, the County of San Diego issued $360 million of Notes with an interest and principal maturity date of July 25, 2005. The Notes carry an interest rate of 3.25% and a yield of 1.59%. The amount outstanding at June 30, 2005 is $369.28 million, including accrued interest payable of $9.28 million.

In 1995 the County of San Diego Board of Supervisors approved the Master Teeter Resolution providing the terms and conditions of its teeter plan obligations. Pursuant to this resolution, the County is able to issue additional Series B Teeter Commercial Paper each fiscal year. On May 17, 2005, the Board of Supervisors adopted a resolution for the issuance of additional Series B borrowings to finance the uncollected property taxes and assessments attributable to the fiscal year ended June 30, 2005. The Teeter commercial paper shall mature not more than 270 days after date of issuance and is not subject to redemption prior to maturity. The payment of principal and interest on each series is supported by an irrevocable direct pay letter of credit that will expire on December 31, 2015.

Short-term obligation activity (**Table 30** below) for the year ended June 30, 2005 was as follow

Table 30 (Note IV-G)

Short-Term Obligations	Beginning Balance at July 1, 2004	Issued	Redeemed	Ending Balance at June 30, 2005
Tax and Revenue Anticipation Notes	$	369,280		369,280
Teeter B-1 Tax - Exempt Principal	49,100	46,000	32,110	62,990
Teeter B-2 Taxable Principal	12,001	12,000	12,001	12,000
Total Teeter	$ 61,101	427,280	44,111	444,270

H. Lease Obligations

1. Lease Commitments- Real Property

The County has commitments under long-term property operating lease agreements for facilities used for operations through fiscal year 2012 (**Table 31** below). These leases do not meet the criteria for capitalization under FASB Statement 13. The County is the lessee under the terms of several non-cancelable operating leases for real property used to house certain County facilities. Total rental expense for all real property operating leases, including short-term cancelable leases for the year ended June 30, 2005, was approximately $26 million.

The combined rental cost for which the County is obligated under these leases is as follows:

Table 31 (Note IV-H-1)

Lease Commitments - Real Property	
Fiscal Year	Minimum Lease Payments
2006	$ 7,645
2007	7,172
2008	3,666
2009	3,094
2010	2,499
2011-2012	3,311
Total	$ 27,387

2. Lease Commitments- Personal Property

The County has also entered into long-term operating leases for personal property, a large portion of which represents data processing and duplicating equipment. Many of these leases are subject to annual adjustment based upon negotiations. Management expects that in the normal course of business, leases that expire will be renewed or replaced by other leases. Total rental expense for these operating leases for the year ended June 30, 2005, was $7.7million.

3. Capital Leases

a. Minimum Lease Payments

Certain buildings and equipment are being leased under capital leases as defined in FASB Statement 13. The present value of the minimum lease obligation has been capitalized in the statement of net assets and is reflected as a liability in that statement. The County assumes responsibility for all maintenance, repair, and structural modifications under the terms of the lease agreements. Future minimum lease payments (**Table 32** below)under capital leases at June 30, 2005 were as follows:

Table 32 (Note IV-H-3-a)

Capital Leases-Future Minimum Lease Payments	
Fiscal Year	Amount
2006	$ 4,359
2007	3,785
2008	3,454
2009	3,068
2010	3,053
2011-2015	13,535
2016-2020	15,290
2021-2023	3,057
Total minimum lease payments	49,601
Less: amount representing interest	(14,976)
Net lease payments	$ 34,625

b. Book Value

The book value of capital lease property (**Table 33**) at June 30, 2005 consisted of the following:

Table 33 (Note IV-H-3-b)

Capital Leases - Book Value

Capital Lease Property	Original Cost	Accumulated Depreciation	Net Book Value June 30, 2005
Land	$ 2,221		2,221
Buildings and Improvements	52,314	16,195	36,119
Total	$ 54,535	16,195	38,340

I. General Long-Term Obligations

Outstanding general long-term obligations at June 30, 2005 consist of certificates of participation, capital lease obligations, third party financing leases, and other long-term obligations. All obligations listed, carry a fixed interest rate with the exception of $505.125 million of the 2002 taxable pension obligation bonds and $147.8 million of the 2004 taxable pension obligation bonds which are variable rate and are subject to market fluctuations. The range listed in **Table 34** below represents the range of interest rates on the serial, term bonds or in the case of third party financing leases; it is the range of rates for the various leases. The variable interest rate used for the 2002 taxable pension obligation bonds Series B1 and for the 2004 taxable pension obligation bonds Series B1 - B2 is 3.34%, which represents the one-month London Interbank Offered Rate (LIBOR) at June 30, 2005. The variable rate used for the 2002 taxable pension obligation bonds Series B2 - B4 is 3.153%, which represents the average auction rate bond coupon for June 2005. The maximum interest rate on these bonds shall not exceed 17% per annum.

1. Outstanding long-term obligations

Outstanding long-term obligations at June 30, 2005 were as follows:

Governmental Activities:

The certificates of participation (COPs) of the SANCAL, a non-profit corporation, are secured by annual base rental lease payments payable primarily by the County General Fund for use of the facilities constructed or equipment purchased from the proceeds. There are also encumbrances on the facilities constructed or purchased with the proceeds of the SANCAL. The capital leases between the County and SANCAL have been eliminated for financial reporting purposes and the related assets and long-term obligation (e.g. certificates of participation of SANCAL) are reported as San Diego County's assets and debt, respectively.

Also, the County, in compliance with the Tax Reform Act of 1986 and subsequent U.S. Treasury Regulations, has performed arbitrage rebate calculations to determine probable amounts due to the Federal government. At June 30, 2005, the probable arbitrage rebate is zero.

Long-term obligations (**Table 34**) for *governmental activiteies* at June 30, 2005 were as follows:

Table 34 (Note IV-I-1)

Long-Term Obligations - Governmental Activities	Interest Rate	Final Maturity Date	Original Amount	Amount Outstanding
San Diego County Capital Asset Leasing Corporation (SANCAL):				
1993 Master Refunding issued May, 1993	2.50 - 5.625%	2012	$ 203,400	72,545
1996 North & East County Courthouse issued December, 1996	4.00 - 6.00%	2019	37,690	30,595
1997 Central Jail Refunding issued July, 1997	4.00 - 5.42%	2025	80,675	67,635
1998 Downtown Courthouse Refunding issued January, 1999	4.00 - 4.94%	2023	73,115	54,875
1999 East Mesa Refunding issued September, 1999	3.60 - 4.75%	2009	15,010	8,295
2000 Information Technology issued May, 2000	4.50 - 5.125%	2010	51,620	28,970
2002 Motorola issued March 2002	2.00 - 5.00%	2011	26,060	18,085
2005 Edgemoor & RCS Refunding issued February, 2005	3.00 - 5.00%	2030	112,395	112,395
Total certificates of participation			599,965	393,395
Capitalized Leases:				
San Diego Regional Building Authority				
Lease beginning September 2001	2.15 - 5.25%	2019	36,960	32,380
Third party financing leases with various beginning dates from August, 1997 to the present	4.24 - 8.00%	2007-2008	8,705	2,245
Total capitalized leases			45,665	34,625
Other long-term obligations:				
Capital loans:				
1997 United States Department of Agriculture	1.00%	2028	4,486	3,351
2002-2004 California Bank & Trust	7.75 - 8.75%	2007-2009	663	317
2003-2004 California Energy Commission	3.95 - 4%	2014-2015	3,648	3,648
Total Capital Loans			8,797	7,316
Taxable Pension Obligation Bonds:				
1994 Series A	4.7 - 6.6%	2007	430,430	60,790
2002 Series A, B & C	3.88 - 6.125%	2032	737,340	737,340
2004 Series A, B & C	3.28 - 5.86%	2024	454,113	454,113
Total Taxable Pension Obligation Bonds			1,621,883	1,252,243
1995 Redevelopment Agency Revenue Bonds	4.75 - 6.75%	2020	5,100	4,260
2001 San Diego County Tobacco Asset Securitization Corporation	4.00 - 6.00%	2043	466,840	430,350
Unamortized issuance premium			6,725	6,031
Unamortized issuance discount			(11,244)	(9,054)
Unamortized deferred amount on refunding			(23,231)	(12,103)
Compensated absences				76,669
Claims and judgments				103,569
Landfill closure and postclosure				47,891
Total other long-term obligations			2,074,870	1,907,172
Total governmental activities			$ 2,720,500	2,335,192

Business-Type Activities:

Long-term obligations (**Table 35**) for business-type activities at June 30, 2005 were as follows:

Table 35 (Note IV-I-1)

Long-Term Obligations - Business-Type Activities	Interest Rate	Final Maturity Date	Original Amount	Amount Outstanding
Enterprise funds				
Capital loans:				
Department of Transportation				
Beginning March 2001	5.63%	2019	$ 3,584	2,832
US Department of Agriculture				
Beginning December 2003	4.63%	2040	100	94
Compensated absences				324
Total business-type activities			$ 3,684	3,250

2. Debt Service Requirements to Maturity

Governmental Activities:

The following (**Table 36**) is a schedule of debt service requirements to maturity for *governmental activities'* long-term bond and note obligations outstanding at June 30, 2005. (The above table does not reflect the County's exposure to the interest rate swap on the 2002 Taxable Pension Obligation Bonds. See Interest Rate Swap disclosure below for further information.)

Table 36 (Note IV-I-2)

Governmental Activities - Debt Service Requirements To Maturity			
Fiscal year Ending June 30	Principal	Interest	Total
2006	$ 59,342	100,892	160,234
2007	72,543	89,134	161,677
2008	59,654	85,821	145,475
2009	57,926	83,085	141,011
2010	58,492	83,166	141,658
2011-2015	244,716	396,629	641,345
2016-2020	319,344	327,191	646,535
2021-2025	460,473	230,100	690,573
2026-2030	278,232	160,239	438,471
2031-2035	227,415	97,220	324,635
2036-2040	101,505	60,642	162,147
2041-2043	147,922	21,461	169,383
Subtotal	2,087,564	1,735,580	3,823,144
Add:			
Unamortized issuance premium	6,031		
Less:			
Unamortized issuance discount	(9,054)		
Unamortized deferred amount on refunding	(12,103)		
Total	$ 2,072,438		

Business-Type Activities:

Debt service requirements to maturity for *business-type activities'* capital loans obligations outstanding at June 30, 2005 (**Table 37**) were the following:.

Table 37 (Note IV-I-2)

Business-Type Activities -

Debt Service Requirements to Maturity

Fiscal Year Ending June 30	Principal	Interest	Total
2006	$ 181	163	344
2007	193	153	346
2008	206	142	348
2009	218	131	349
2010	231	119	350
2011-2015	1,342	385	1,727
2016-2020	487	53	540
2021-2025	13	14	27
2026-2030	17	11	28
2031-2035	21	7	28
2036-2040	17	2	19
Total	$ 2,926	1,180	4,106

3. Special Assessment Debt

In July of 1991, the County issued $28.804 million of bonds to finance the acquisition and construction of various public improvements required for the development of land located in north San Diego County west of Interstate 15 and the community of Rancho Bernardo. In July of 1997 the bonds were refunded. The County Treasurer-Tax Collector acts as an agent for property owners and bondholders in collecting and forwarding special assessment monies. The County is not obligated to pay for any special assessment bonds. Special assessment debt is solely the obligation of various separate governmental agencies. The amount of the 4-S Ranch special assessment debt outstanding for which the County is a fiduciary is $16.9 million at June 30, 2005.

4. Prior Year Defeasance of Long-Term Debt

In prior years, the County defeased certain certificates of participation (COPs) and taxable pension obligation bonds by placing the proceeds of the original issue plus additional County contributions in an irrevocable trust to provide for all future debt service payments on the old obligations. Accordingly, the trust account assets and the liability for the defeased obligations are not included in the County's financial statements. At June 30, 2005, $86.4 million of bonds and COPs were legally defeased and remain outstanding.

5. Advance Refunding of Long-Term Debt Including New Long-Term Debt

In February 2005, the San Diego County Capital Asset Leasing Corporation issued $112.395 million of fixed rate serial Certificates of Participation titled, 2005 Edgemoor Project and 1996 Regional Communications System Refunding (the "Certificates)." These certificates have maturity dates beginning in February 2006 with a final maturity of February 2030. Each maturity date carries a different fixed interest rate beginning in February 2006 at a fixed rate of 3 percent with fixed rates ranging to 5 percent. The face value of the new certificates attributed to refunding debt is $28.885 million.

These certificates were issued with a premium of $5.960 million. The $118.355 million in proceeds of the Certificates along with approximately $5.36 million of funds held by the 1996 Regional Communication System trustee were distributed as follows: 1) approximately $77.486 million will be used to finance the construction of a skilled nursing facility to replace the existing County of San Diego skilled nursing facility located in the City of Santee; 2) approximately $31.633 million was transferred to the refunded bond escrow agent to advance refund the entire $29.51 million outstanding 1996 Regional Communications System Financing Certificates of Participation; 3) to fund a Reserve Fund in the amount of approximately $3.181 million; 4) to fund capitalized interest in the amount of approximately $9.5 million to fund a portion of the Certificates through July 1, 2007; and, 5) and to pay for certain costs of issuance of $1.915 million incurred in connection with the

Series 2005 Certificates. The $31.633 million was used to purchase Treasuries and have been placed in an irrevocable trust with an escrow agent to provide for all future remaining debt service payments on the 1996 Regional Communications System Financing. As a result, the 1996 COPs are considered to be defeased and the liability for those bonds has been removed from the Government-wide Statement of Net Assets Governmental Activities Current and Non-Current. The advance refunding will result in reducing the County's debt service payments by $2.4 million over the next 14 years to obtain an economic gain (difference between the present values of the debt service payments on the refunded debt and refunding debt) of $1.2 million.

6. Changes in Long-Term Obligations

Long-term obligation activity (Governmental Activities) for the year ended June 30, 2005 was as follows in **Table 38** below:

Table 38 (Note IV-I-6)

Long-Term Obligations - Governmental Activities

	Beginning Balance at July 1, 2004	Additions		Reductions	Ending Balance at June 30, 2005	Amounts Due within One Year
Bonds and notes payable:						
Certificates of participation	$ 344,365	112,395		(63,365)	393,395	35,710
Redevelopment Agency	4,400			(140)	4,260	150
San Diego County Tobacco Securitization Corporation	440,305			(9,955)	430,350	2,015
Taxable pension obligation bonds	1,268,878			(16,635)	1,252,243	20,960
Capital and retrofit loans	5,750	1,945	*	(379)	7,316	428
Total Bonds and notes payable, before issuance discount and premiums and deferred amount on refunding	2,063,698	114,340		(90,474)	2,087,564	59,263
Unamortized issuance premium, discount and deferred amount on refunding:						
Unamortized issuance premium	555	5,960		(484)	6,031	1,052
Unamortized issuance discount	(9,565)			511	(9,054)	666
Unamortized deferred amount on refunding	(14,072)	(2,123)		4,092	(12,103)	(4,895)
Total bonds and notes payable	2,040,616	118,177		(86,355)	2,072,438	56,086
Other liabilities:						
Capitalized leases	37,346	11	*	(2,732)	34,625	2,732
Arbitrage rebate	979	17		(996)		
Claims and judgments	97,789	48,748		(42,968)	103,569	43,251
Compensated absences	77,537	58,036		(58,904)	76,669	7,666
Landfill closure and postclosure	46,910	2,550		(1,569)	47,891	7,390
Total other liabilities	260,561	109,362		(107,169)	262,754	61,039
Total governmental activities	$ 2,301,177	227,539		(193,524)	2,335,192	117,125

* This includes loan additions recorded in Internal Service Funds.

The following funds presented in **Table 39** below have typically been used to liquidate other long-term liabilities in prior years:

Table 39 (Note IV-I-6)

Liquidated Liabilities	
Liability	Fund(s) Used to Liquidate in Prior Years
Arbitrage Rebate	Debt Service Fund- SANCAL
Claims and Judgments	Internal Service Fund - Risk Financing
Compensated Absences	General Fund; Special Revenue Funds - County Library, Road,Cable TV and Air Pollution; Internal Service Funds - Facilities Management, Fleet Services and Purchasing
Landfill Closure and Postclosure	General Fund and Inactive Wastesites Fund

Long-term obligation activity (Business Activities) for the year ended June 30, 2005 was as follows in **Table 40** below:

Table 40 (Note IV-I-6)

Long-Term Obligations - Business-Type Activities	Beginning Balance at July 1, 2004	Additions	Reductions	Ending Balance at June 30, 2005	Amounts Due within One Year
Enterprise Funds					
Capital loans	$ 2,998	100	(172)	2,926	181
Compensated absences	345	258	(279)	324	32
Total business-type activities	$ 3,343	358	(451)	3,250	213

J. Interest Rate Swap

To manage interest rate risk and lower the County's borrowing cost in its 2002 Taxable Pension Obligation Bonds, the County entered into an interest rate swap on September 17, 2002 with two counterparties. The swap converts the variable interest rates on several subseries of the 2002 Taxable Pension Obligation Bonds to a single long-term fixed rate that was lower than the "natural" fixed rate available at the time of the swap. The interest rate swap with Citibank N.A. (Citibank) and Morgan Stanley Capital Services (Morgan Stanley), (together the "counterparties") is governed by the International Swaps and Derivatives Association, Inc. Master Agreement (the Agreement) and a Confirmation. In fiscal year 2002-2003, the County issued $737.340 million of Pension Obligation Bonds of which $505.125 million of the Series B Bonds are Auction Rate Securities. Within the Series B Auction Rate Securities there are the following subseries: $100 million of Series B-1, $135.025 million of Series B-2, $135.05 million Series of B-3 and $135.05 million of Series B-4 bonds. The County swapped Series B-2, B-3 and B-4 totaling $405.125 million of the Auction Rate Securities for a contractually agreed fixed interest rate of 5.30%. Of the $405.125 million our exposure with Citibank is $263.325 million and our exposure with Morgan Stanley is $141.8 million notional.

Further details concerning this interest rate swap are the discussed below:

1. Terms

County payments are due to bondholders semi-annually on August 15 and February 15, beginning February 15, 2003. The effective date of the swap was September 17, 2002 and the initial six-month calculation period began February 15, 2003. The Agreement and the Confirmation terminate on February 15, 2031 and the series B-2, B-3 and B-4 bonds mature on August 15, 2030. The County did not receive any upfront payments but pursuant to the terms of the Agreement, each August 15 and February 15 the County will receive an amount from each of the counterparties based on the

notional amount of principal outstanding for the past six months at an interest rate of one month London Interbank Offered Rate (LIBOR) and each February 15 the County will pay the counterparties the scheduled 5.30% of the notional amount outstanding. The February 15 payment due from the counterparties will be netted against the 5.30% County payment. The notional amount of the swap will begin to decline in fiscal year 2016-2017 in direct proportion to the repayment of the bonds.

The obligations of the County to make payments to the counterparties under this Agreement constitute general obligations of the County, payable from taxes, income, revenue cash receipts and other moneys of the County legally available therefore in the General Fund. The payments due to the counterparties and the obligations of the County under this Agreement do not constitute any kind of indebtedness of the County as defined under and/or proscribed by any constitution, charter, law, rule, regulation, government code, constituent or governing instrument, resolution, guideline, ordinance, order, writ, judgment decree, or ruling.

As of June 30, 2005, the swap created a synthetic fixed rate for the bonds as noted in **Table 41** below:

Table 41 (Note IV-J-1)

Interest Rate Swap - Synthetic Fixed Rate	Terms	Rates
Fixed Rate to Counterparty	Fixed	5.30%
Variable Rate from Counterparty	1 month LIBOR	(3.340)%
Net Interest Rate Swap Payments		1.960%
Average Auction Rate Bond Coupon Payments		3.153%
Synthetic Interest Rate on Bonds		5.113%

2. Fair Value

As of June 30, 2005 the swaps had a mark to market fair value of $(39.3) million. The mid-market or indicative unwind valuation was derived from a proprietary model using the zero coupon method. This model takes into consideration estimates about relevant present and future market consideration as well as the size and liquidity of the position and any related actual or potential hedging transaction.

The primary risks associated with this transaction are: Credit Risk, Termination Risk, and Basis Risk.

3. Credit Risk

As of June 30, 2005 the County was not exposed to credit risk because the swap had a negative mark to market fair value of $39.3 million. However, should interest rates change and the fair value of the swap becomes positive the County would be exposed to credit risk in the amount of the swap's fair value. Citibank is rated Aa1/AA/AA+ by Moody's, Standard & Poors and Fitch, respectively and Morgan Stanley is rated Aa3/A+/AA- by Moody's, Standard & Poor's and Fitch, respectively. Pursuant to the Agreement if the rating issued by Standard & Poors or Moody's of the senior unsecured debt obligations of the counterparties is suspended or withdrawn or falls below "A-" in the case of Standard & Poors or below "A3" in the case of Moody's, collateral is to be delivered to a third party.

4. Termination Risk

The Agreement includes standard termination events such as failure to pay, bankruptcy and early termination. For this transaction, the swap and bond maturities match and carries an Interest Rate Swap Insurance Policy by MBIA Insurance Corporation (MBIA). If the Agreement is terminated for any of the conditions in the agreement, and at the time of the termination the swap has a negative fair value, the County would be liable to the counterparties for a payment equal to the swap's fair value. The swap can be terminated by the County for market value at any time. As of June 30, 2005 the fair value of the swap is a

$(39.3) million. Value is predominantly tied to changes in the market for the fixed swap rate for the remaining swap term.

5. Basis Risk

The County's exposure to basis risk arises when the one-month LIBOR rate index received from the counterparties may be less than the applicable auction rate that is being paid to the bondholders, that is the cash flow being received by the counterparty is not equal to the cash flow being paid to the variable rate bondholder. By using one month LIBOR, the County's objective is to mitigate the effect of the differential between the swap index and the bondholder variable rate. For fiscal year 2004-2005, the differential was $(68) thousand.

6. Swap Payments and Associated Debt

As of June 30, 2005, debt service requirements of the variable-rate debt and net swap payments, *assuming current interest rates remain the same*, for their term are presented in **Table 42**. As rates vary, variable rate bond interest payments and net swap payments will vary.

Table 42 (Note IV-J-5)

Swap Payments Associated with Debt

Fiscal Year Ending June 30	Principal	Interest (3.153%)	Interest Rates Swaps,Net (1.96%)	Total
2006		12,774	7,940	20,714
2007		12,774	7,940	20,714
2008		12,774	7,940	20,714
2009		12,774	7,940	20,714
2010		12,774	7,940	20,714
2011-2015		63,870	39,700	103,570
2016-2020	$ 79,625	59,021	36,688	175,334
2021-2025	128,100	41,671	25,904	195,675
2026-2030	169,500	18,359	11,412	199,271
2031-2033	27,900	440	273	28,613
Total	$ 405,125	247,231	153,677	806,033

K. Landfill Site Closure and Postclosure Care Costs

State laws and regulations require the placement of final covers on all landfill sites that stopped accepting solid waste after October 9, 1991 and the performance of certain maintenance and monitoring functions at these sites for a minimum of 30 years after closure. Closure and postclosure care costs are paid near or after the date a landfill stops accepting waste. The San Marcos Landfill is the sole waste disposal site owned by the County that is subject to these regulations. It was operational and accepted solid waste from 1979 until March 11, 1997. The formal closure of this landfill is expected to span from July 2004 through February 2006. Once closure is complete, post closure maintenance will begin.

The County is required by GASB Statement No. 18, "Accounting for Municipal Solid Waste Landfill Closure and Postclosure Care Costs", to report the projected closure and postclosure care costs as of each balance sheet date. The projected landfill closure and postclosure care liability at June 30, 2005 for the San Marcos Landfill was $47.891 million. This estimated amount is based on what it would cost to perform all closure and postclosure care in calendar year 2005 dollars and is subject to change as a result of such factors including but not limited to: inflation; deflation; advancements in technology; and amendments to laws and regulations.

In addition to the above, state regulations require that landfill closure and postclosure maintenance costs be fully funded at the time of closure, unless a landfill owner/operator can demonstrate financial responsibility towards these activities by using other approved financial assurance alternatives. A pledge of revenue is one of various alternatives allowed to fund estimated postclosure costs. Under this alternative, the Board of Supervisors, on February 3, 1998, approved Minute Order No. 5 "Postclosure Maintenance Funding for the San

Marcos Landfill", wherein the County entered into a pledge of revenue agreement with the California Integrated Waste Management Board (CIWMB). Pursuant to Resolution No. 98-24, adopted under Minute Order No. 5, the Board exacted that the amount of pledged revenue shall be equal to $790 thousand per year for the 30 year period of postclosure maintenance commencing upon completion of the final closure of the San Marcos Landfill. The pledged amount is a promise of existing funds rather than future revenues and may increase or decrease to match any adjustment to identified cost estimates that are mutually agreed to by the County and the CIWMB.

As of June 30, 2005, $25.72 million of the Net Assets of the Government-Wide Statement of Net Assets has been restricted for closure costs of the San Marcos Landfill.

Regulations governing solid waste management are promulgated by government agencies on the federal and state levels. These regulations address the design, construction, operation, maintenance, closure and postclosure maintenance of various types of facilities; acceptable and prohibited waste types; and inspection, permitting, environmental monitoring and solid waste recycling requirements. Regulations at both the state and federal levels could impose retroactive liability, particularly with respect to cleanup activities relating to any landfill site ever operated by the County, whether or not owned by the County. Thus, the County has potential liability with respect to every landfill ever owned, operated, contracted to be operated, or into which the County disposed waste. Compliance with these regulations may be costly, and, as more stringent standards are developed to protect the environment, these costs could increase.

L. Fund Balances Reserved For Other Purposes

At June 30, 2005, the fund balances reserved for other purposes (**Table 43**) were as follows:

Table 43 (Note IV-L)

Fund Balances Reserved For Other Purposes		
General Fund		
General Government	$	70,259
Public Protection		31,880
Health and Sanitation		19,415
Public Assistance		4,491
Education		1,138
Recreational and Cultural		1,033
Total General Fund	$	128,216
Special Revenue Funds		
Road-Future Road Improvements	$	22,862
Lighting Maintenance		16
County Library		86
County Service Districts-Advances		1,365
Flood Control-Future Drainage Improvements		17,220
Housing Authority-Escrow payment		25
Tobacco Securitization		231
Total Special Revenue Funds	$	41,805
Capital Projects Funds		
Edgemoor capital projects	$	250
Redevelopment Agency-Advances		1,002
Total Capital Projects	$	1,252

V. Other Information

A. Risk Management

The County operates a Risk Management Program, whereby it 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, public officials bond, employee dishonesty, faithful performance, volunteers, airport comprehensive, and loss of money and securities based upon site locations. Settlements in the areas covered have not exceeded insurance coverage for each of the past three fiscal years. The County's Internal Service Fund (ISF) is used to report all of its uninsured risk management activities. Risk management liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. Actuarial evaluations were obtained which determine estimates of known and projected public liability and workers compensation claim liabilities. At June 30, 2005, the amount of these liabilities, including an estimate for claims incurred but not reported and allocated and unallocated loss adjustment expenses was estimated at $103.6 million, including $17.5 million in public liability and $86.1 million in workers' compensation. The County began allocating the cost of providing claims service to all its operating funds as a "premium" charge expressed as a percentage of payroll beginning fiscal year 1996-1997. Changes in the balances of claim liabilities for fiscal year 2003-2004 and 2004-2005 are shown in **Table 44** below:

Table 44 (Note V-A)

Risk Management - Changes in Claim Liabilities

Fiscal Year	Beginning Balance at June 30	Current- Year Claims and Changes in Estimates	Claim Payments	Ending Balance at June 30
2003-2004	$ 100,588	29,096	(31,895)	97,789
2004-2005	97,789	42,968	(37,188)	103,569

B. Subsequent Events

1. Tax and Revenue Anticipation Notes

In July 2005, the County issued tax and revenue anticipation notes (TRANS) totaling $250 million due July 14, 2006 at a coupon rate of 4.00% and net interest cost of 2.58%. Proceeds from the notes will be used to meet fiscal year 2005-2006 cash flow requirements. Fiscal year 2005-2006 unrestricted revenues collateralize the notes.

2. San Diego County Capital Asset Leasing Corporation

In August 2005, the San Diego County Capital Asset Leasing Corporation (SANCAL) issued $28.21 million of fixed rate serial Certificates of Participation titled, "North and East County Justice Facility Refunding (the "Certificates")." These certificates have maturity dates beginning in November 2006 with a final maturity of November 2019. Each maturity date carries a different fixed interest rate beginning in November 2006 at a fixed rate of 3.25 percent with fixed rates ranging to 5 percent. These certificates were issued with a premium of $1.3 million. The proceeds were applied to 1) advance refund all of the outstanding certificates of participation for the 1996 North County Regional Center Expansion and East County Courthouse Detention Facility Conversion, 2) fund a reserve fund; and, 3) pay certain costs of issuance incurred in connection with the refunding.

C. Contingencies

1. Litigation

In addition to the accrued liability for litigation and workers compensation claims described in Note V-A, the County has a potential liability of $34.9 million that could result if unfavorable final decisions were rendered in numerous lawsuits to which the County is a named defendant. Appropriations are budgeted annually for those portions of obligations coming due that fiscal year. Estimates of potential liabilities described above include estimates of claims incurred but not reported at June 30, 2005.

2. Unrecorded Leave Benefits

County employees have unrecorded accumulated benefits of approximately $129.5 million in sick leave and compensatory time. These benefits are not payable to employees upon termination and are normally liquidated in future years as employees elect to use their benefits as prescribed by Civil Service rules and regulations. Accumulated vacation, sick leave, and compensatory time-off for which employees are eligible for payment upon separation have been recorded as current or long-term liabilities in the appropriate proprietary funds and the statement of net assets.

3. Federal and State Programs

Amounts received or receivable from grant agencies are subject to audit and adjustment by grantor agencies, principally the federal government. Any disallowed claims, including amounts already collected, may constitute a liability of the applicable funds. The amount, if any, of expenditures that may be disallowed by the grantor cannot be determined at this time, although the County expects such amounts, if any, to be immaterial.

D. Jointly Governed Organizations

The County Board of Supervisors jointly governs the Service Authority for Freeway Emergencies (S.A.F.E.). San Diego S.A.F.E. is governed by a seven-member board, whose members are appointed by the County Board of Supervisors and the eighteen cities within the county. The purpose of the authority is to provide for freeway emergency call boxes on major freeways within the County. Funding for the authority is provided by a $1dollar yearly fee on vehicle registrations in San Diego County, which are collected by the State and deposited into the County Treasury. The County provides minimal administrative staff support for the S.A.F.E. authority.

The County Board of Supervisors and the San Diego City Council jointly govern the San Diego Workforce Partnership (Partnership). The Partnership's Board of Directors consists of two members of the County Board of Supervisors, two members from the San Diego City Council and one member of a charitable organization. The purpose of the Partnership is to provide employment training to area residents. Funding for such training is provided by State and Federal grants.

The County also jointly governs the San Dieguito River Valley Authority, the Serra Cooperative Library System, Southern California Regional Training and Development Center, and the Van Horn Regional Treatment Facility. The governing boards of these entities consist of representatives from the County and/or other regional governments and other counties. The County does not appoint a voting majority to the above boards. Services provided by these entities include park land acquisition, coordination of library services, regional governmental training, and treatment of emotionally disturbed youth.

E. Joint Venture

The County is a participant with eighteen incorporated cities in a joint venture to operate an emergency services organization for the purpose of providing regional planning and mutual assistance in the event of an emergency or disaster in the region including accidents involving hazardous waste. The organization is governed by the Unified Disaster Council composed of one voting member from each represented jurisdiction. A contractual agreement requires that the cities provide one-half of the total required funding each year. The County, by agreement, also provides one-half of the required yearly funding. Any participant may terminate participation in the agreement by giving 120 days notice prior to the beginning of the next fiscal year. Total participant contributions for fiscal year 2004-2005 were $1.3 million. The organization had a cumulative surplus of $32 thousand at June 30, 2005. Separate financial statements for the joint venture may be obtained from the office of the Auditor and Controller.

F. San Diego County Employees Retirement System

1. Plan Description

The SDCERA administers a cost-sharing, multi-employer defined benefit plan, with County members representing 93.4% of covered employees, which provides retirement, disability, and death benefits for plan members and beneficiaries pursuant to the County Retirement Law of 1937, as enacted and amended by the State legislature. The plan is integrated with the Federal Social Security System. Cost-of-living adjustments are provided to members and beneficiaries at the discretion of the SDCERA Board of Retirement. SDCERA issues a publicly available financial report that includes financial statements and required supplementary information for the pension plan. The financial report may be obtained by writing to the San Diego County Employees Retirement Association, 401 West A Street, Suite 1300, San Diego, California 92101 or by calling (619) 515-0130.

2. Basis of Accounting, Estimates and Fair Value of Investments

a. Measurement Focus and Basis of Accounting

SDCERA's operations are accounted for on an economic resources measurement focus and the accrual basis of accounting. Employer and member contributions are recognized when due pursuant to formal commitments, as well as statutory or contractual requirements. Investment income is recognized as revenue when earned. Retirement benefits and refunds are recognized when due and payable in accordance with the terms of the Plan. Other expenses are recognized when the corresponding liabilities are incurred. The net appreciation/(depreciation) in fair value of investments held by SDCERA is recorded as an increase/(decrease) to investment income based on the valuation of investments.

b. Estimates

A number of estimates and assumptions have been made relating to the reporting of assets and liabilities, the disclosure of reserves and designation of plan assets to prepare these financial statements in conformity with accounting principles generally accepted in the United States of America. Actual results could differ from those estimates.

c. Fair Value of Investments

Please refer to details contained in Note IV. A. 2. b. (IV Detailed Notes on all Funds; A. Deposits and Investments; 2. Investments Outside the Pool; b. Pension Trust Fund.)

3. Funding Policy

State statutes require member contributions to be actuarially determined to provide a specific statutory level of benefit. Member contribution

rates, as a percentage of salary, vary according to age at entry, benefit tier level, and certain negotiated contracts which provide for the County to pay a portion of the employees' contribution. Member contribution rates (weighted average), in effect at June 30, 2005, expressed as a percentage of salary are 8.92%-9.49% for general members and 11.31% for safety members. The County is also required by State statutes to contribute at an actuarially determined rate, expressed as a percentage of annual covered payroll. The fiscal year 2004-2005 rates, expressed as a percentage of covered payroll, are 25.59% for general members and 34.99% for safety members. Additionally, in accordance with various agreements with employee bargaining units, the County has contributed $20.3 million on behalf of employees.

In March 2002, the County implemented a new enhanced retirement package. In October 2002, the County issued taxable Pension Obligation Bonds to fund a portion of its statutory obligations arising from enhanced benefits. In June 2004, the County issued Pension Obligation Bonds and transferred $450 million of the issuance to the retirement fund. The retirement plan's funding status (the ratio of system assets to system liabilities) was 80.3% at June 30, 2005.

4. Annual Pension Cost

For the fiscal year ended June 30, 2005, the County's annual pension cost was $264.8 million. The County's actual contribution during the fiscal year ended June 30, 2005 totaled $264.8 million, resulting in a net pension obligation of zero as of June 30, 2005, compared to zero at the end of the prior year. Additionally, in Fiscal Year 2004-05, the County contributed $24.866 million to SDCERA to pay down the Unfunded Actuarial Accrued Liability, increase the funded ratio and reduce the County's future contributions. The required contribution rates, as adopted by the SDCERA Board, were determined as part of the June 30, 2003 interim actuarial valuation based on entry-age actuarial cost method. The actuarial assumptions included (a) an 8.25% investment rate-of-return, (b) projected salary increases of 5.0% per year, and (c) cost-of-living increases for retirees of 3%.

5. Three-Year Trend Information

The following trend information concerning annual pension costs and the percentage of annual pension costs contributed for the last three fiscal years is included in **Table 45** below:

Table 45 (Note V-F-5)

Three-Year Trend Information

Fiscal Year Ended June 30	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
2003	$ 6,538	100.00%	$ 0
2004	194,580	100.00%	0
2005	264,816	100.00%	0

6. Retiree Health Benefits

Retiree health benefits may be available to eligible retirees to the extent that the Board of Retirement annually approves the payment of such benefits. SDCERA recognizes the cost of providing those benefits by expending annual insurance premiums, which approximated $32.6 million for fiscal year 2004-2005.

The Board of Supervisors and the Board of Retirement adopted a funding mechanism under Section 401(h) of the Internal Revenue Code, which calls for a portion of the County's contributions to be deposited to a separate health benefits 401(h) account each year. Any investment income earned on the account balance increases the balance and any losses reduce it.

The reserve for health benefits, established by the SDCERA Board of Directors, designates funds that may be used for future payments under the retiree health benefits program and related administrative expenses. The reserve for health benefits was approximately $193.8 million at June 30, 2005, a $36.7 million decrease from the previous fiscal year.

G. Restatement of Beginning Net Assets Balance

1. First 5 Commission

The beginning net asset balance of the First 5 Commission was restated as shown in **Table 46** below in the amount of $1.333 million resulting from 1.) An adjustment of prior year mark to market unrealized loss of $1.281 million and 2.) Unrecognized compensated absences of $52 thousand in the prior year.

Table 46 (Note V-G)

Restatement		
Net Asset balance as of June 30, 2004	$	169,522
Adjustment for restatement		1,333
Net Asset balance, restated June 30, 2004	$	170,855

H. Commitments

1. Third Party Debt

The tax code allows for certain types of nongovernmental borrowers to take advantage of tax-exempt financing through a governmental agency. The County of San Diego as a governmental agency, has issued tax-exempt debt on behalf of qualified borrowers. The County of San Diego is not responsible for the repayment of the debt. Accordingly, no liability for these bonds has been recorded in the statement of net assets.

a. Mortgage Revenue Bonds

Mortgage Revenue Bonds are issued to provide construction and permanent financing to developers of multi-family residential rental projects located in the County to be partially occupied by persons of low or moderate income. Between 1995 and 2002, the County issued $14 million of Mortgage Revenue Bonds of which $12.2 million were still outstanding as of June 30, 2005.

b. Certificates of Participation

The County has implemented a conduit program whereby the County is the issuer of tax-exempt bonds and loans, where the proceeds are provided to a qualifying for profit or nonprofit organization. The County has no obligation to pay for the bonds and loans. The original amounts of Certificates of Participation issued as well as the amounts outstanding per issue at June 30, 2005 are as follows in **Table 47**:

Table 47 (Note V-H-5)

Certificates of Participation - Conduit Program			
	Date Issued	Original Amount Issued	Amount Outstanding at June 30, 2005
Sharp Hospital	April 1998	$ 112,020	101,575
San Diego Natural History Museum	December 1998	15,000	13,800
Burnham Institute	September 1999	51,500	42,500
San Diego Museum of Art (principal due at maturity)	March 2000	6,000	6,000
Salk Institute	April 2000	15,000	14,305
University of San Diego	May 2001	36,870	34,500
San Diego-Imperial Counties Developmental Services	September 2002	10,750	10,250
Chabad Jewish Academy (principal due at maturity)	January 2003	11,700	11,410
San Diego Jewish Academy (principal due at maturity)	December 2003	13,325	13,325
Bishop School	June 2004	25,000	25,000
Museum of Contemporary Art	December 2004	13,000	13,000
Total		$ 310,165	285,665

c. Reassessment District Improvement Bonds

Reassessment District Improvement Bonds were issued to provide refunding an earlier issuance of improvement bonds for the 4-S Ranch assessment district. The District originally issued $28.8 million of Improvement Bonds in July 1991 to finance the acquisition of certain infrastructure improvements specially benefiting properties within an assessment district. In July 1997, the District issued $21.8 million of

Reassessment Bonds to refund the original issuance, of which $16.9 million were still outstanding as of June 30, 2005.

2. Deposits for Other Agencies

The Treasurer is a named paying agent for various bonds issued by other agencies, e.g., school districts, pursuant to the bond covenants. The proceeds from these issues are deposited in the County pool or as specified in the bond resolution. The amounts deposited belong to the specific agency which issued the bonds and are not assets of the County. The County has no liability with respect to these issues, the repayment of these bonds are from ad valorem taxes levied on the properties in the school district.

I. New Governmental Accounting Standards

1. Implemented

In March 2003, GASB issued Statement No. 40, *Deposit and Investment Risk Disclosures - an amendment of GASB Statement No. 3.* This statement addresses common deposit and investment risks related to credit risk, concentration of credit risk, interest rate risk, and foreign currency risk. As an element of interest rate risk, this statement requires certain disclosures of investments that have fair values that are highly sensitive to changes in interest rates. Deposit and investment policies related to the risk identified in this statement also should be disclosed. In Fiscal Year 2004-2005, the County implemented these new reporting requirements.

2. Under Analysis

The County is currently analyzing its accounting practices to determine the potential impact on the financial statements for the following GASB Statements:

In November 2003, GASB issued Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries.* This statement establishes accounting and financial reporting standards for impairment of capital assets. A capital asset is considered impaired when its service utility has declined significantly and unexpectedly. This statement also clarifies and establishes accounting requirements for insurance recoveries. This statement is effective for the County's fiscal year ending June 30, 2006.

In April 2004, GASB issued Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans.* This statement establishes uniform financial reporting standards for other postemployment benefits (OPEB) plans. The approach followed in this statement generally is consistent with the approach adopted for defined benefit pension plans with modifications to reflect differences between pension plans and OPEB plans. The statement applies for OPEB trust funds included in the financial reports of plan sponsors or employers, as well as for the stand-alone financial reports of OPEB plans or the public employee retirement systems, or other third parties, that administer them. This statement also provides requirements for reporting of OPEB funds by administrators of multiple-employer OPEB plans, when the fund used to accumulate assets and pay benefits or premiums when due is not a trust fund. This statement is effective for the County's fiscal year ending June 30, 2007.

In May 2004, GASB issued Statement No. 44, *Economic Condition Reporting: The Statistical Section-an amendment of NCGA Statement 1.* This statement amends the portions of NCGA Statement 1, *Governmental Accounting and Financial Reporting Principles* that guide the preparation of the statistical section. The statistical section presents detailed information, typically in ten-year trends, that assists users in utilizing the basic financial statements, notes to basic financial statements, and required supplementary information to assess the economic condition of a government. This statement adds new information that financial statement users have identified as important

and eliminates certain previous requirements. This statement is effective for the County's fiscal year ending June 30, 2006.

In June 2004, GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, which addresses how state and local governments should account for and report their costs and obligations related to postemployment healthcare and other nonpension benefits. Collectively, these benefits are commonly referred to as other postemployment benefits, or OPEB. The statement generally requires that employers account for and report the annual cost of OPEB and the outstanding obligations and commitments related to OPEB in essentially the same manner as they currently do for pensions. Annual OPEB cost for most employers will be based on actuarially determined amounts that, if paid on an ongoing basis, generally would provide sufficient resources to pay benefits as they come due. This statement's provisions may be applied prospectively and do not require governments to fund their OPEB plans. An employer may establish its OPEB liability at zero as of the beginning of the initial year of implementation; however, the unfunded actuarial liability is required to be amortized over future periods. This statement also establishes disclosure requirements for information about the plans in which an employer participates, the funding policy followed, the actuarial valuation process and assumptions, and, for certain employers, the extent to which the plan has been funded over time. This statement is effective for the County's fiscal year ending June 30, 2008.

In December 2004, GASB issued Statement No. 46, *Net Assets Restricted by Enabling Legislation - an amendment of GASB Statement No. 34*. This Statement requires that limitations on the use of net assets imposed by enabling legislation be reported as restricted net assets. A legally enforceable enabling legislation restriction is one that a party external to the County - such as citizens, public interest groups, or the judiciary - can compel a government to honor. This Statement is effective for the County's fiscal year ending June 30, 2006.

In June 2005, GASB issued Statement 47, *Accounting for Termination Benefits*. This Statement establishes accounting standards for termination benefits. This Statement requires employers to disclose a description of the termination benefit arrangement, the cost of the termination benefits (required in the period in which the employer becomes obligated if that information is not otherwise identifiable from information displayed on the face of the financial statements), and significant methods and assumptions used to determine termination benefit liabilities. The requirements of this Statement are effective in two parts. For termination benefits other than those provided through an existing defined OPEB plan, this Statement is effective for the County's fiscal year ending June 30, 2006. For termination benefits provided through an existing defined benefit OPEB plan, the provisions of this Statement should be implemented simultaneously with the requirements of Statement 45, and are therefore effective for the County's fiscal year ended June 30, 2008.

Required Supplementary Information

SCHEDULE OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE-BUDGET AND ACTUAL
General Fund
For the Year Ended June 30, 2005
(In Thousands)

	Budgeted Amounts		
	Original Budget	Final Budget	Actual
Revenues:			
Taxes	$ 617,776	617,776	671,850
Licenses, permits and franchise fees	31,876	31,876	32,015
Fines, forfeitures and penalties	68,608	70,699	51,000
Revenue from use of money and property	20,256	26,528	29,308
Aid from other governmental agencies:			
State	679,480	711,555	511,769
Federal	525,730	526,124	620,477
Other	64,491	72,710	60,415
Charges for current services	244,438	252,339	254,585
Other revenue	42,618	39,915	38,057
Total revenues	2,295,273	2,349,522	2,269,476
Expenditures:			
Current:			
General:			
Board of supervisors district #1	983	1,180	973
Board of supervisors district #2	1,010	1,139	966
Board of supervisors district #3	971	1,102	1,027
Board of supervisors district #4	986	1,151	920
Board of supervisors district #5	1,071	1,404	1,035
Board of supervisors general office	935	935	808
Clerk of the board of supervisors - legislative and administrative	2,423	2,501	1,955
Chief Administrative office - legislative and administrative	4,037	4,068	3,778
Community services	5,596	8,738	2,166
Public safety - legislative and administrative	6,732	16,870	8,987
Land use and environment - legislative and administrative	5,630	4,899	2,697
Financing and general government - Legislative and administrative	17,870	21,346	16,091
Auditor and controller	25,778	27,260	24,636
Countywide general expense	20,455	43,052	27,627
Assessor/recorder/county clerk - finance	31,821	31,834	29,148
Treasurer/tax collector	15,559	14,306	13,625
County counsel	18,278	18,431	17,919
Civil service commission	397	495	457
Human resources - personnel	15,369	14,291	12,993
Registrar of voters	9,483	12,350	12,220
Clerk of the board of supervisors - property management	3,065	2,990	2,827
CAC major maintenance	1,122	904	904
Contributions to capital outlay	4,826	6,989	3,117
Community enhancement	3,013	3,007	3,007
Community projects	11,513	5,207	5,207
Human resources - other general government	3,597	3,497	3,370
County technology office	6,908	6,658	6,120
Contingency reserve	15,600	15,600	
Total general	235,028	272,204	204,580
Public protection:			
Grand jury	509	507	468
Defense attorney/contract administration	8,098	11,022	10,026
Contributions for trial courts	68,266	76,083	75,674
District attorney-judicial	102,562	103,501	99,770
Public defender	42,887	43,615	42,230
Alternate public defender	12,975	13,216	11,915
Judicial - other budgetary entity	22,458	23,353	
Citizens law enforcement review board	513	525	442
Sheriff - police protection	261,147	273,456	263,189
Probation - police protection		2,399	2,399
Sheriff - detention and correction	23	14	1
Probation - detention and correction	98,351	96,350	92,357

See notes to required supplementary information

SCHEDULE OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE-BUDGET AND ACTUAL
General Fund
For the Year Ended June 30, 2005
(In Thousands)

(Continued)	Budgeted Amounts Original Budget	Final Budget	Actual
Public works, flood control, soil and water, general	1,965	945	945
Agriculture weights and measures	11,924	13,148	12,295
Land use and environment - other protection	1,071	652	558
LAFCO administration	226	226	226
Office of emergency services	17,891	21,797	5,852
Assessor/recorder/county clerk - other protection	13,290	15,331	15,331
Health and human services agency - other protection	3,035	3,034	2,961
Medical examiner	6,486	6,491	6,277
Department of animal services	10,622	10,699	10,494
Planning and land use	41,586	33,515	25,129
Public works, general - other protection	23,125	4,391	4,391
Child support	53,851	53,850	51,047
Sheriff - adult detention	173,538	168,439	163,410
Probation - adult detention	593	814	814
Probation - juvenile detention	31,508	30,551	30,160
Total public protection	1,008,500	1,007,924	928,361
Public ways and facilities:			
Public works, general - public ways	5,800	4,348	4,348
Total public ways and facilities	5,800	4,348	4,348
Health and sanitation:			
Health and human services agency - mental health	181,112	180,301	166,949
Environmental health	30,120	31,090	27,679
Health and human services agency - health	119,712	120,191	107,530
Public works, general - sanitation	4,417	13,633	13,374
Health and human services agency - medical care	132,187	130,004	126,732
Health and human services agency - California children services	15,368	15,370	14,515
Health and human services agency - health administration	47,897	47,376	42,692
Total health and sanitation	530,813	537,965	499,471
Public assistance:			
Health and human services agency - social administration	670,292	663,632	607,457
Probation - care of court wards	11,493	10,055	7,522
Health and human services agency - other assistance	192,784	200,740	198,919
Housing Authority	11,554	11,441	9,029
Health and human services agency - aid programs	53,496	53,496	35,560
Total public assistance	939,619	939,364	858,487
Education:			
Farm and home advisor	989	1,086	597
Total education	989	1,086	597
Recreation and cultural:			
Parks and recreation	25,203	22,758	18,300
Total recreational and cultural	25,203	22,758	18,300
Capital outlay	62,345	21,087	17,928
Debt service:			
Interest and other fiscal charges	7,085	13,353	12,310
Total expenditures	2,815,382	2,820,089	2,544,382
Excess of revenues over (under) expenditures	(520,109)	(470,567)	(274,906)
Other financing sources (uses):			
Long-term debt proceeds	25	25	
Transfers in	511,493	521,330	568,677
Transfers out	(208,474)	(182,848)	(179,228)
Total other financing sources (uses)	303,044	338,507	389,449
Net change in fund balance	(217,065)	(132,060)	114,543
Fund balances at beginning of year	217,065	551,000	551,000
Increase (decrease) in:			
Reserve for inventory of materials and supplies		1,854	1,854
Fund balances at end of year	$	420,794	667,397

See notes to required supplementary information

SCHEDULE OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE-BUDGET AND ACTUAL
Tobacco Securization Special Revenue Fund
For the Year Ended June 30, 2005
(In Thousands)

(Continued)	Budgeted Amounts Original Budget	Final Budget	Actual
Revenues:			
Revenue from use of money and property	$		8,810
Total revenues			8,810
Expenditures:			
Current:			
General:			
Tobacco Settlement	3,634	3,205	
Total general	3,634	3,205	
Total expenditures	3,634	3,205	
Excess of revenues over (under) expenditures	(3,634)	(3,205)	8,810
Other financing sources (uses):			
Transfers out	(23,666)	(24,095)	(23,278)
Total other financing sources (uses)	(23,666)	(24,095)	(23,278)
Net change in fund balance	(27,300)	(27,300)	(14,468)
Fund balances at beginning of year	27,300	346,727	346,727
Fund balances at end of year	$	319,427	332,259

See notes to required supplementary information

Budgetary Information

General Budget Policies

An operating budget is adopted each fiscal year by the Board of Supervisors for the governmental funds. The annual resolution adopts the budget at the object level of expenditures within departments. Annual budgets are not required to be adopted for: the Tobacco Securitization Joint Special Revenue Fund; SANCAL, a non-profit corporation, and the Debt Service and Capital Projects Funds (other governmental funds). Certain annual appropriations are budgeted on a project or program basis. If such projects or programs are not completed at the end of the fiscal year, unexpended appropriations, including encumbered funds, are carried forward to the following year with the approval of the Board of Supervisors.

Appropriations may also be adjusted during the year with the approval of the Board of Supervisors. Additionally, the Chief Financial Officer is authorized to approve certain transfers and revisions of appropriations within a department. Such adjustments are reflected in the final budgetary data. Accordingly, the legal level of budgetary control by the Board of Supervisors is the department level.

The reduction in appropriations during the year ended June 30, 2005, amounted to $20.919 million in the General Fund.

The Schedule of Revenues, Expenditures, And Changes In Fund Balance - Budget and Actual for the General Fund and the Tobacco Securitization Special Revenue Fund presented as Required Supplementary Information were prepared using the Generally Accepted Accounting Principles (GAAP) basis.

The Original Budget column consists of the Fiscal Year 2004-05 adopted budget plus the budget carried forward from Fiscal Year 2003-04. As such, the County has included encumbrances that are subject to automatic re-appropriation as part of the original budget. Also, the original budget is adjusted to reflect reserves, transfers, allocations, and supplemental appropriations that occur prior to the start of the fiscal year. The County adopts its budget subsequent to the start of the each new fiscal year (August 17, 2004). Therefore, under the circumstances, the complete budget that is adopted by the County Board of Supervisors constitutes the adopted budget, plus the approved carry forward for purposes of budgetary comparison presentation.

The Final Budget column consists of the Original Budget column plus amended budget changes occurring during FiscalYear 2004-05 plus technical amendments that occur after the close of the fiscal year less the amount of budget carried forward to Fiscal Year 2005-06.

The Actual column represents the actual amounts of revenue and expenditures reported on a GAAP basis which is the same basis that is used to present the aforementioned Original and Final Budget.

Schedule of Funding Progress

San Diego County Employees Retirement Association

Schedule of Funding Progress (In millions) (Unaudited)

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
6/30/2003	$ 4,417.7	$ 5,853.1	$ 1,435.4	75.5%	$ 906.1	158.4 %
6/30/2004	5,166.8	6,369.5	1,202.7	81.1	917.1	131.1
6/30/2005	5,612.3	6,990.7	1,378.4	80.3	921.8	149.5

APPENDIX C

SUMMARY OF PRINCIPAL LEGAL DOCUMENTS

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APPENDIX C

SUMMARY OF PRINCIPAL LEGAL DOCUMENTS

The Series 2005 Certificates represent proportionate, undivided interests in the right to receive Base Rental Payments under the Project Sublease and the Refunding Sublease. The Project Sublease has been amended by the First Amendment to Project Sublease, which among other matters increases the base rental payment under the Project Sublease in an amount sufficient to pay the principal and interest components of the Series 2006 Certificates. Base Rental Payments under the Trust Agreement include base rental payments under the Project Sublease and the Refunding Sublease, and Base Rental Payments are available to pay interest and principal with respect to the Series 2005 Certificates and the Series 2006 Certificates, ratably without preference or priority of any kind. Accordingly, what follows include references to and summaries of the Refunding Lease, the Refunding Sublease, the Refunding Property and related terms.

The following summary discussion of selected provisions of the Project Lease, the Project Sublease, the Refunding Lease, the Refunding Sublease, the Assignment Agreement and the Trust Agreement are made subject to all of the provisions of such documents. This summary discussion does not purport to be a complete statement of said provisions and prospective purchasers of the Certificates are referred to the complete texts of said documents, copies of which are available upon request sent to the Trustee.

Definitions

"Additional Certificates" means the certificates of participation authorized by a Supplemental Trust Agreement that are executed and delivered by the Trustee under and pursuant to the Trust Agreement.

"Additional Rental" means the additional rental payments payable by the County under and pursuant to (a) the Project Sublease and (b) the Refunding Sublease. Unless the context otherwise requires, as used under the caption "Project Sublease," the term "Additional Rental" shall mean only the Additional Rental that is payable under the Project Sublease and shall not include any Additional Rental payable under the Refunding Sublease. Unless the context otherwise requires, as used under the caption "Refunding Sublease," the term "Additional Rental" shall mean only the Additional Rental that is payable under the Refunding Sublease and shall not include any Additional Rental payable under the Project Sublease.

"Administrative Expense Fund" means the fund by that name established in accordance with the Trust Agreement.

"Annual Debt Service" means, for each Lease Year, an amount equal to the sum of all Base Rental Payments due in such Lease Year.

"Assignment Agreement" means that certain Assignment Agreement, dated as of February 1, 2005, by and between the Corporation and the Trustee, as it may from time to time be amended.

"Auditor and Controller" means the person holding the office of Auditor and Controller of the County, including any Acting or Interim Auditor and Controller.

"Authorized Denominations" means $5,000 or any integral multiple thereof.

"Average Annual Debt Service" means an amount equal to the average of the Annual Debt Service for all Lease Years, including the Lease Year in which the calculation is made.

"Base Rental Payment Fund" means the fund by that name established in accordance with the Trust Agreement.

"Base Rental Payments" means the aggregate base rental payments with interest components and principal components payable by the County under and pursuant to (a) the Project Sublease in the amounts and at the times set forth therein and (b) the Refunding Sublease in the amounts and at the times set forth therein. Unless the context otherwise requires, as used under the caption "Project Sublease," the term "Base Rental Payments" shall mean only those Base Rental Payments that are payable under the Project Sublease and shall not include any Base Rental Payments payable under the Refunding Sublease. Unless the context otherwise requires, as used under the caption "Refunding Sublease," the term "Base Rental Payments" shall mean only those Base Rental Payments that are payable under the Refunding Sublease and shall not include any Base Rental Payments payable under the Project Sublease.

"Beneficial Owner" shall have the meaning set forth in the Continuing Disclosure Agreement.

"Business Day" means a day other than (i) Saturday or Sunday or (ii) a day on which banking institutions in Los Angeles, California, New York, New York, or the city or cities in which the principal corporate trust office of the Trustee are closed or (iii) a day on which the New York Stock Exchange is closed. If the date for making any payment or the last date for performance of any act or the exercising of any right, as provided in the Trust Agreement, shall not be a Business Day, such payment may be made or act performed or right exercised on the next succeeding Business Day, with the same force and effect as if done on the nominal date provided in the Trust Agreement, and, unless otherwise specifically provided in the Trust Agreement, no interest shall accrue for the period from and after such nominal date.

"Capitalized Interest Account" means the account by that name established pursuant to the Trust Agreement.

"Certificate of Completion" means a Certificate of the County filed with the Trustee, stating that construction of the Project has been substantially completed and that all Construction Costs have been paid or provided for.

"Certificate of the Corporation" means an instrument in writing signed by the Chair or the Treasurer of the Corporation. If and to the extent required by the provisions of the Trust Agreement, each Certificate of the Corporation shall include the statements provided for in the Trust Agreement.

"Certificate of the County" means an instrument in writing signed by the Chief Financial Officer. If and to the extent required by the provisions of the Trust Agreement, each Certificate of the County shall include the statements provided for in the Trust Agreement.

"Certificate Reserve Fund" means the fund by that name established in accordance with the Trust Agreement.

"Certificate Reserve Fund Requirement" means, as of any date of calculation, the lesser of (i) the Maximum Annual Debt Service, (ii) 10% of the proceeds of the Certificates and any Additional Certificates, in accordance with the Tax Certificate to be made by the County under the Subleases until the final maturity of the Outstanding Certificates, or (iii) 125% of Average Annual Debt Service.

"Certificates" means, as appropriate to the context, the Series 2005 Certificates, the Series 2006 Certificates and/or any series of Additional Certificates.

"Chief Financial Officer" means the person holding the office of Chief Financial Officer of the County, including any Acting or Interim Chief Financial Officer.

"Code" means the Internal Revenue Code of 1986, as amended.

"Construction Costs" means all costs of constructing the Project, including, but not limited to:

(1) all costs which the Corporation or the County shall be required to pay to a manufacturer, vendor or contractor or any other person under the terms of any contract or contracts for the construction, installation or improvement of the Project;

(2) obligations of the Corporation, the County or others incurred for labor and materials (including obligations payable to the Corporation, the County or others for actual out-of-pocket expenses of the Corporation, the County or others) in connection with the construction, installation or improvements of the Project, including reimbursement to the Corporation, the County or others for all advances and payments made in connection with the Project prior to or after delivery of the Certificates.

(3) the costs of performance or other bonds and any and all types of insurance that may be necessary or appropriate to have in effect during the course of construction, installation or improvement of the Project;

(4) all costs of engineering and architectural services, including the actual out-of-pocket costs of the Corporation or the County for test borings, surveys, estimates, plans and specifications and preliminary investigations therefor, development fees and sales commissions, and for supervising construction, installation and improvement, as well as for the performance of all other duties required by or consequent to the proper construction, installation or improvement of the Project; and

(5) any sums required to reimburse the Corporation or the County for advances made by the Corporation or the County for any of the above items or for any other costs incurred and for work done by the Corporation or the County which are properly chargeable to the construction, installation or improvement of the Project.

"Construction Fund" means the fund by that name established pursuant to the Trust Agreement.

"Continuing Disclosure Agreement" means collectively, the Continuing Disclosure Agreement executed by the County at the time of execution and delivery of the Certificates, together with any Continuing Disclosure Agreement executed by the County at the time of execution and delivery of any series of Additional Certificates, as originally executed and as each such Continuing Disclosure Agreement may from time to time be amended in accordance with the provisions thereof.

"Corporation" means the San Diego County Capital Asset Leasing Corporation, a nonprofit public benefit corporation duly organized and existing under and by virtue of the laws of the State of California.

"Cost of Issuance Fund" means the fund by that name established in accordance with the Trust Agreement.

"Costs of Issuance" means all the costs of executing and delivering the Certificates, including, but not limited to, all printing and document preparation expenses in connection with the Trust Agreement, the Leases, the Subleases, the Assignment Agreement, the Certificates and the preliminary official statement and final official statement pertaining to the Certificates; rating agency fees; financial advisor fees; title insurance fees; CUSIP Service Bureau charges; market study fees; legal fees and expenses of counsel with respect to the lease of the Property and the refunding of the Prior Obligations; any computer and other expenses incurred in connection with the Certificates; the fees and expenses of the Trustee, the Prior Trustee, including fees and expenses of their respective counsel; and other fees and expenses incurred in connection with the execution of the Certificates or the implementation of the refunding of the Prior Obligations, to the extent such fees and expenses are approved by the County.

"County" means the County of San Diego, a political subdivision duly organized and existing under the Constitution and laws of the State of California.

"Defeasance Securities" means any of the following:

(1) Cash (insured at all times by the Federal Deposit Insurance Corporation),

(2) Obligations of, or obligations guaranteed as to principal and interest by, the U.S. or any agency or instrumentality thereof, when such obligations are backed by the full faith and credit of the U.S. including:

- U.S. treasury obligations;
- All direct or fully guaranteed obligations
- Farmers Home Administration
- General Services Administration
- Guaranteed Title XI financing
- Government National Mortgage Association (GNMA); and
- State and Local Government Series

"DTC" means The Depository Trust Company, New York, New York, a limited-purpose trust company organized under the laws of the State of New York, and its successors as securities depository for the Certificates including any such successor appointed pursuant to the Trust Agreement.

"Earnings Fund" means the fund by that name established in accordance with the Trust Agreement.

"Event of Default" means (1) with respect to any Event of Default under the Trust Agreement, any occurrence or event specified in and defined by the provisions of the Trust Agreement under the caption "Trust Agreement—Default and Limitations of Liability—Events of Default" below, (2) with respect to any Event of Default under the Project Sublease, any occurrence or event specified in and defined by the provisions of the Project Sublease under the caption "Project Sublease—Default" below, and (3) with respect to any Event of Default under the Refunding Sublease, any occurrence or event specified in and defined by the provisions of the Refunding Sublease under the caption "Refunding Sublease—Default" below.

"Expiry Date" means, with respect to the Project Sublease, February 1, 2030, and, with respect to the Refunding Sublease, February 1, 2019.

"Financial Guaranty Insurance Policy" means the financial guaranty insurance policy issued by the Insurer insuring the payment when due of the principal and interest with respect to the Certificates as provided therein.

"Financial Newspaper" means The Wall Street Journal or The Bond Buyer or, if neither such newspaper is being regularly published, any other newspaper or journal publishing financial news and selected by the County that is printed in the English language, is customarily published on each Business Day and is circulated in Los Angeles, California and New York, New York.

"**First Amendment to Project Sublease**" means that certain First Amendment to Project Sublease, dated as of December 1, 2006, with respect to the Project Property, by and between the County, as sublessee, and the Corporation, as sublessor.

"**First Supplemental Trust Agreement**" means the First Supplemental Trust Agreement among the Trustee, the County and the Corporation, dated as of December 1, 2006.

"Fitch" means Fitch IBCA, Inc., or any successor credit rating agency selected by the County.

"Hazardous Substances" means any substances, pollutants, wastes and contaminants now or hereafter included in such (or similar term) term under any federal state or local statute, ordinance, code or regulation now existing or hereafter enacted or amended.

"Insurance Proceeds and Condemnation Awards Fund" means the fund by that name established in accordance with the Trust Agreement.

"Insurer" means Ambac Assurance Corporation, a Wisconsin domiciled stock insurance company.

"Interest Fund" means the fund by that name established in accordance with the Trust Agreement.

"Interest Payment Date" means August 1, 2005 and each February 1, and August 1, thereafter.

"Interest Period" means each period from and including one Interest Payment Date to but excluding the next following Interest Payment Date.

"Lease Year" means the period from each February 1 to and including the following January 31 during the term of the Trust Agreement, the Project Sublease and the Refunding Sublease.

"Leases" means, collectively, the Project Lease and the Refunding Lease.

"Mandatory Sinking Account Payment" means the principal amount of any Certificates or Additional Certificates required to be paid on each Mandatory Sinking Account Payment Date pursuant to the terms of this Agreement or any Supplemental Trust Agreement.

"Mandatory Sinking Account Payment Date," if applicable, means February 1 of each year set forth in the Trust Agreement and in any Supplemental Trust Agreement.

"Maximum Annual Debt Service" means an amount equal to the largest Annual Debt Service for all future Lease Years beginning in the Lease Year in which the calculation is made.

"Moody's" means Moody's Investors Service, Inc., or any successor credit rating agency selected by the County.

"**Opinion of Counsel**" means a written opinion of counsel of recognized national standing in the field of law relating to municipal bonds, appointed and paid by the County.

"**Outstanding**" when used as of any particular time with reference to Certificates and Additional Certificates, means all Certificates and Additional Certificates, including, but not limited to, the Certificates as described in the Trust Agreement, except:

(1) Certificates and Additional Certificates previously canceled by the Trustee or delivered to the Trustee for cancellation;

(2) Certificates and Additional Certificates which pursuant to the Trust Agreement are not deemed outstanding;

(3) Certificates and Additional Certificates paid or deemed to have been paid within the meaning of the Trust Agreement; and

(4) Certificates and Additional Certificates in lieu of or in substitution for which other Certificates or Additional Certificates shall have been executed and delivered by the Trustee pursuant to the Trust Agreement.

"**Owner**" means any person who shall be the registered owner of any Outstanding Certificate or Additional Certificate as indicated in the registration books of the Trustee.

"Permitted Encumbrances" means, with respect to the Project Sublease or the Refunding Sublease, as applicable, as of any particular time: (i) liens for general *ad valorem* taxes and assessments, if any, not then delinquent, or which the County may, pursuant to the Project Sublease or the Refunding Sublease, as applicable, permit to remain unpaid; (ii) the Assignment Agreement, as it may be amended from time to time; (iii) the Project Sublease or the Refunding Sublease, as applicable, as they may be amended from time to time; (iv) the Project Lease or the Refunding Lease, as applicable, as they may be amended from time to time; (v) any right or claim of any mechanic, laborer, materialman, supplier or vendor not filed or perfected in the manner prescribed by law; (vi) easements, rights of way, mineral rights, drilling rights and other rights, reservations, covenants, conditions or restrictions, all of a non-monetary nature, which exist of record as of the date of initial delivery of the Certificates; and (vii) easements, rights of way, mineral rights, drilling rights and other rights, reservations, covenants, conditions or restrictions, all of a non-monetary nature, established following the date of recordation of the Project Sublease and to which the Corporation and the County consent in writing.

"**Permitted Investments**" means any of the following to the extent then permitted by applicable laws and any investment policies of the County:

(1) Defeasance Securities;

(2) Obligations of any of the following federal agencies which obligations represent the full faith and credit of the United States of America, including:

—Export-Import Bank;

—Rural Economic Community Development Administration;

—U.S. Maritime Administration;

—Small Business Administration;

—U.S. Department of Housing & Urban Development (PHAs);

—Federal Housing Administration; and

—Federal Financing Bank.

(2) Direct obligations of any of the following federal agencies which obligations are not fully guaranteed by the full faith and credit of the United States of America:

—Senior debt obligations issued by the Federal National Mortgage Association (FNMA) or Federal Home Loan Mortgage Corporation (FHLMC);

—Obligations of the Resolution Funding Corporation (REFCORP);

—Senior debt obligations of the Federal Home Loan Bank System; and

—Senior debt obligations of other Government Sponsored Agencies approved by the Insurer.

(4) U.S. dollar denominated deposit accounts, federal funds and bankers' acceptances with domestic commercial banks which have a rating on their short term certificates of deposit on the date of purchase of "P-1" by Moody's and "A-1" or "A-1+" by S&P and maturing not more than 360 calendar days after the date of purchase. (Ratings on holding companies are not considered as the rating of the bank).

(5) Commercial paper which is rated at the time of purchase in the single highest classification, "P-1" by Moody's and "A-1+" by S&P and which matures not more than 270 calendar days after the date of purchase.

(6) Investments in a money market fund rated "AAAm" or "AAAm-G" or better by S&P.

(7) Pre-refunded Municipal Obligations defined as follows: any bonds or other obligations of any state of the United States of America or of any agency, instrumentality or local governmental unit of any such state which are not callable at the option of the obligor prior to maturity or as to which irrevocable instructions have been given by the obligor to call on the date specified in the notice; and

(A) which are rated, based on an irrevocable escrow account or fund (the "escrow"), in the highest rating category of Moody's or S&P or any successors thereto; or

(B) (i) which are fully secured as to principal and interest and redemption premium, if any, by an escrow consisting only of cash or obligations described in clause (2) of the definition of "Defeasance Securities" contained in the Trust Agreement, which escrow may be applied only to the payment of such principal of and interest and redemption premium, if any, on such bonds or other obligations on the maturity date or dates thereof or the specified redemption date or dates pursuant to such irrevocable instructions, as appropriate, and (ii) which escrow is sufficient, as verified by a nationally recognized independent certified public accountant, to pay principal of and interest and redemption

premium, if any, on the bonds or other obligations described in this paragraph on the maturity date or dates specified in the irrevocable instructions referred to above, as appropriate;

(7) Municipal Obligations rated "Aaa/AAA" or general obligations of States with a rating of "A2/A" or higher by both Moody's and S&P.

(8) Investment Agreements approved in writing by the Insurer (supported by appropriate opinions of counsel); and

(9) Other forms of investments (including repurchase agreements) approved in writing by the Insurer.

Any references to long-term rating categories in this definition of "Permitted Investments" shall not take into account any plus or minus sign or numerical modifiers.

"**Prepayment Fund**" means the fund by that name established in accordance with the Trust Agreement.

"**Prior Escrow Agent**" means U.S. Bank National Association, acting as the Prior Trustee under the Prior Trust Agreement.

"**Prior Escrow Agreement**" means that certain Escrow Agreement dated as of February 1, 2005, by and between the County and the Prior Trustee as Escrow Agent providing for the defeasance and redemption of the Prior Obligations.

"Prior Obligations" means the County of San Diego Certificates of Participation (1996 Regional Communications System Financing), executed and delivered on May 31, 1996 in the principal amount of $52,230,000 pursuant to the Prior Trust Agreement, and secured by rental payments made by the County pursuant to that certain Lease Agreement, dated as of May 1, 1996.

"**Prior Trust Agreement**" means that Trust Agreement, dated as of May 1, 1996, between the Corporation and the Prior Trustee, pursuant to which the Prior Obligations were executed and delivered.

"**Prior Trustee**" means U.S. Bank National Association, as successor trustee under the Prior Trust Agreement.

"**Principal Corporate Trust Office**" means the corporate trust office of the Trustee at the address set forth in the Trust Agreement, except for purposes of payment, registration, transfer, exchange and surrender of Certificates, means the corporate trust office of the Trustee in Los Angeles, California, or such other office specified by the Trustee.

"**Principal Fund**" means the fund by that name established in accordance with the Trust Agreement.

"**Principal Payment**" means the principal amount of Certificates required to be paid on each Principal Payment Date.

"**Principal Payment Date**" means February 1 of each year, commencing February 1, 2006.

"**Project Lease**" means that certain Project Lease, dated as of February 1, 2005, with respect to the Project Property, by and between the County, as lessor, and the Corporation, as lessee, as originally executed and as it may be amended from time to time.

"**Project Property**" means the real property and all the improvements thereon or to be located thereon described in the Project Sublease (as the same may be changed from time to time by Removal or Substitution, as defined in the Project Sublease).

"**Project Sublease**" means that certain Project Sublease, dated as of February 1, 2005, with respect to the Project Property, by and between the County, as sublessee, and the Corporation, as sublessor, as amended by the First Amendment to Project Sublease and as it may be amended from time to time.

"**Property**" means, collectively, (a) Project Property and (b) the Refunding Property.

"**Purchasers**" means Banc of America Securities LLC and Lehman Brothers Inc., as underwriters and purchasers of the Certificates pursuant to the Series 2006 Certificates Purchase Contract.

"**Rebate Requirement**" means the Rebate Requirement as defined in the Tax Certificate.

"**Record Date**" means the close of business on the 15th day of the month preceding any Interest Payment Date, whether or not such day is a Business Day.

"**Refunding Lease**" means that certain Refunding Lease, dated as of February 1, 2005, with respect to the Refunding Property, by and between the County, as lessor, and the Corporation, as lessee, as originally executed and as it may be amended from time to time.

"**Refunding Property**" means the real property and all the improvements thereon or to be located thereon described in the Refunding Sublease (as the same may be changed from time to time by Removal or Substitution, as defined in the Refunding Sublease).

"**Refunding Sublease**" means that certain Refunding Sublease, dated as of February 1, 2005, with respect to the Refunding Property, by and between the County, as sublessee, and the Corporation, as sublessor, as originally executed and as it may be amended from time to time.

"Removal" means, with respect to the Project Sublease or the Refunding Sublease, the release of all or a portion of the Project Property or the Refunding Property, as applicable, from the leasehold of the Project Sublease or the Refunding Sublease, as applicable, and of the Project Lease or the Refunding Lease as provided in Project Sublease or the Refunding Sublease, as applicable.

"**Rental Payments**" means, collectively, the Base Rental Payments and the Additional Rental.

"**Representation Letter**" means the Letter of Representations from the County and the Trustee to DTC, or any successor securities depository for the Certificates, in which the County and the Trustee make certain representations with respect to the Certificates, the payment with respect thereto and delivery of notices with respect thereto.

"**Reserve Fund Credit Facility**" shall mean a letter of credit, line of credit, surety bond, insurance policy or similar facility deposited in the Certificate Reserve Fund in lieu of or in partial substitution for cash or securities on deposit therein.

"Series 2005 Certificates" means the County of San Diego Certificates of Participation (2005 Edgemoor Project and 1996 Regional Communications System Refunding) executed and delivered by the Trustee pursuant to the Trust Agreement.

"Series 2006 Certificates" means the County of San Diego Certificates of Participation (2006 Edgemoor Completion Project) executed and delivered by the Trustee pursuant to the Trust Agreement.

"Series 2006 Certificates Purchase Contract" means that certain Purchase Contract, dated _____, 2006, by and between the Purchasers and the County relating to the Series 2006 Certificates.

"**S&P**" means Standard & Poor's Ratings Services, or any successor credit rating agency selected by the County.

"**Subleases**" means, collectively, the Project Sublease and the Refunding Sublease.

"Substitution" means, with respect to the Project Sublease or the Refunding Sublease, as applicable, the release of all or a portion of the Project Property or the Refunding Property, as applicable, from the leasehold of the Project Sublease or the Refunding Sublease, as applicable, and of the Project Lease or the Refunding Lease, as applicable, and the lease of substituted real property and improvements thereunder as provided in the Project Sublease or the Refunding Sublease, as applicable.

"**Supplemental Trust Agreement**" means an agreement amending or supplementing the terms of the Trust Agreement entered into pursuant to the terms thereof.

"Surety Bond" means the surety bond issued by the Insurer guaranteeing certain payments into the Base Rental Payment Fund with respect to the Certificates as provided therein and subject to the limitations set forth therein.

"**Surplus Subaccount**" means the account by that name established in accordance with the Trust Agreement.

"**Tax Certificate**" means, collectively, the Tax Certificate executed by the County at the time of execution and delivery of the Certificates, together with any Tax Certificate executed by the County at the time of execution and delivery of any series of Additional Certificates, in each case, relating to the requirements of Section 148 of the Code, as originally executed and as each such Tax Certificate may from time to time be amended in accordance with the provisions thereof.

"**Term Certificates**" means any Certificates or Additional Certificates which are subject to prepayment prior to their stated maturity dates from Mandatory Sinking Account Payments.

"**Trust Agreement**" means the Trust Agreement by and among the Trustee, the County and the Corporation, dated as of February 1, 2005, as originally executed, as amended by the First Supplemental Trust Agreement, and as it may from time to time be amended or supplemented in accordance with the Trust Agreement.

"**Trustee**" means Zions First National Bank, a national banking association duly organized and existing under and by virtue of the laws of the United States of America and having a principal corporate trust office located at Los Angeles, California, or any other bank or trust company which may at any time be substituted in its place as provided in the Trust Agreement.

"**Written Request of the County**" means an instrument in writing signed by the Chief Financial Officer, County Treasurer-Tax Collector, the Capital Finance Manager or other officers who are specifically authorized by resolution of Board of Supervisors of the County to sign or execute such a document on its behalf, as reflected in a Certificate of the County to such effect delivered to the Trustee.

PROJECT SUBLEASE

The Project Property

Lease of the Project Property. The Corporation leases to the County, and the County rents and hires from the Corporation, the Project Property on the conditions and terms set forth in the Project Sublease. The County agrees and covenants that during the term of the Project Sublease, except as provided in the Project Sublease, it will use the Project Property for public purposes so as to afford the public the benefits contemplated by the Project Sublease and so as to permit the Corporation to carry out its agreements and covenants contained in the Project Sublease and in the Trust Agreement, and the County further agrees and covenants that during the term of the Project Sublease that it will not abandon or vacate the Project Property.

Quiet Enjoyment. The parties to the Project Sublease mutually covenant that the County, so long as it observes and performs the agreements, conditions, covenants and terms required to be observed or performed by it contained in the Project Sublease and is not in default under the Project Sublease, shall at all times during the term of the Project Sublease peaceably and quietly have, hold and enjoy the Project Property without suit, trouble or hindrance from the Corporation.

Right of Entry and Inspection. The Corporation shall have the right to enter the Project Property and inspect the Project Property during reasonable business hours (and in emergencies at all times) for any purpose connected with the Corporation's rights or obligations under the Project Sublease and for all other lawful purposes.

Prohibition Against Encumbrance or Sale. The County and the Corporation will not create or suffer to be created any mortgage, pledge, lien, charge or encumbrance upon the Project Property, except Permitted Encumbrances, and except incident to the execution and delivery of Additional Certificates as contemplated by the Project Sublease. The County and the Corporation will not sell or otherwise dispose of the Project Property or any property essential to the proper operation of the Project Property, except as otherwise provided in the Project Sublease. Notwithstanding anything to the contrary contained in the Project Sublease, with the consent of the Insurer, which will not be unreasonably withheld, the County may assign, transfer or sublease any and all of the Project Property or its other rights under the Project Sublease, provided that (a) the rights of any assignee, transferee or sublessee shall be subordinate to all rights of the Corporation under the Project Sublease, (b) no such assignment, transfer or sublease shall relieve the County of any of its obligations under the Project Sublease, (c) the assignment, transfer or sublease shall not result in a breach of any covenant of the County contained in the Project Sublease, (d) any such assignment, transfer or sublease shall by its terms expressly provide that the fair rental value of the Project Property for all purposes shall be first allocated to the Project Sublease, as the same may be amended from time to time before or after any such assignment, transfer or sublease and (e) no such assignment, transfer or sublease shall confer upon the parties thereto any remedy which allows reentry upon the Project Property unless concurrently with granting such remedy the same shall be also granted under the Project Sublease by an amendment to the Project Sublease which shall in all instances be prior to and superior to any such assignment, transfer or sublease.

Liens. In the event the County shall at any time during the term of the Project Sublease cause any improvements to the Project Property to be constructed or materials to be supplied in or upon or attached

to the Project Property, the County shall pay or cause to be paid when due all sums of money that may become due or purporting to be due for any labor, services, materials, supplies or equipment furnished or alleged to have been furnished to or for the County in, upon, about or relating to the Project Property and shall keep the Project Property free of any and all liens against the Project Property or the Corporation's interest therein. In the event any such lien attaches to or is filed against the Project Property or the Corporation's interest therein, and the enforcement thereof is not stayed or if so stayed such stay thereafter expires, the County shall cause each such lien to be fully discharged and released at the time the performance of any obligation secured by any such lien matures or becomes due. If any such lien shall be reduced to final judgment and such judgment or any process as may be issued for the enforcement thereof is not promptly stayed, or if so stayed and such stay thereafter expires, the County shall forthwith pay and discharge or cause to be paid and discharged such judgment. The County shall, to the maximum extent permitted by law, indemnify and hold the Corporation and its assignee and its directors, officers and employees harmless from, and defend each of them against, any claim, demand, loss, damage, liability or expense (including attorneys' fees) as a result of any such lien or claim of lien against the Project Property or the Corporation's interest therein.

Substitution or Removal of Project Property.

(a) The County may amend the Project Sublease and the Project Lease to substitute other real property and/or improvements (the "Substituted Property") for existing Project Property and/or to remove real property (including undivided interests therein) and/or improvements from the definition of Project Property, with the consent of the Insurer, which shall not be unreasonably withheld, and upon compliance with all of the conditions set forth in subsection (b) below. After a Substitution or Removal, the part of the Project Property for which the Substitution or Removal has been effected shall be released from the leasehold under the Project Sublease and the Project Lease.

(b) No Substitution or Removal shall take place under the Project Sublease until the County delivers to the Corporation and the Trustee the following:

(1) A Certificate of the County containing a description of all or part of the Project Property to be released and, in the event of a Substitution, a description of the Substituted Property to be substituted in its place;

(2) A Certificate of the County (A) stating that the annual fair rental value of the Project Property after a Substitution or Removal, in each year during the remaining term of the Project Sublease, is at least equal to the maximum annual Base Rental Payments payable under the Project Sublease attributable to the Project Property prior to said Substitution or Removal, as determined by the County on the basis of an appraisal of the Project Property after said Substitution or Removal conducted by a member of the Appraisal Institute of America (MAI) designated by the County; (B) demonstrating that the useful life of the Project Property after Substitution or Removal equals or exceeds the remaining term of the Project Sublease; and (C) stating that the Project Property after a Substitution or Removal is as essential to the operations of the County as was the Project Property immediately prior to such Substitution or Removal;

(3) An Opinion of Counsel to the effect that the amendments to the Project Sublease and to the Project Lease contemplating Substitution or Removal have been duly authorized, executed and delivered and constitute the valid and binding obligations of the County and the Corporation enforceable in accordance with their terms;

(4) (A) In the event of a Substitution, a policy of title insurance in an amount equal to the principal portion of the then-remaining Base Rental Payments payable under the Project

Sublease multiplied by a fraction, the numerator of which is that portion of the principal portion of the then-remaining Base Rental Payments payable under the Project Sublease attributable to the Substituted Property and the denominator of which is the principal portion of the then-remaining Base Rental Payments payable under the Project Sublease, insuring the County's leasehold interest in the Substituted Property (except any portion thereof which is not real property) subject only to Permitted Encumbrances, together with an endorsement thereto making said policy payable to the Trustee for the benefit of the Owners of the Certificates and any Additional Certificates, and (B) in the event of a partial Removal, evidence that the title insurance in effect immediately prior thereto is not affected;

(5) In the event of a Substitution, an opinion of the County Counsel of the County to the effect that the exceptions, if any, contained in the title insurance policy referred to in (4) above do not interfere with the beneficial use and occupancy of the Substituted Property described in such policy by the County for the purposes of leasing or using the Substituted Property;

(6) An Opinion of Counsel that the Substitution or Removal does not cause the interest with respect to the Certificates and any Additional Certificates to be includable in gross income of the Owners thereof for federal income tax purposes;

(7) Evidence that the County has complied with the covenants contained in the Project Sublease relating to insurance requirements with respect to the Substituted Property; and

(8) Evidence that the Substitution or Removal, in and of itself, has not or will not cause a downgrade or withdrawal of the then existing credit ratings on the Certificates and any Additional Certificates.

Term of the Project Sublease

Commencement of the Project Sublease. The effective date of the Project Sublease is February 2, 2005, and the term of the Project Sublease shall end on the Expiry Date, unless such term is extended or sooner terminated as provided in the Project Sublease. If on the Expiry Date, the rental payable under the Project Sublease shall not be fully paid and all Certificates and Additional Certificates shall not be fully paid and retired, or if the rental payable under the Project Sublease shall have been abated at any time and for any reason, then the term of the Project Sublease shall be extended until ten days after the rental payable under the Project Sublease shall be fully paid and all Certificates and Additional Certificates shall be fully paid, except that the term of the Project Sublease shall in no event be extended beyond February 1, 2035. If prior to the Expiry Date, the rental payable under the Project Sublease shall be fully paid and all Certificates and Additional Certificates shall have been fully paid, or deemed fully paid, in accordance with the Trust Agreement, the term of the Project Sublease shall end ten days thereafter or ten days after written notice by the County to the Corporation to the effect that the rental payable under the Project Sublease shall be fully paid and all Certificates and Additional Certificates have been fully paid, whichever is earlier, and the Project Sublease shall thereupon terminate.

Use of Proceeds; Tax Covenants

Use of Proceeds. The parties to the Project Sublease agree that the proceeds of the Certificates will be used to refund and defease the Prior Obligations, to pay Construction Costs with respect to the Project and to pay the costs of executing and delivering the Certificates and incidental and related expenses. The parties to the Project Sublease agree that the proceeds of the Series 2006 Certificates will

be used to pay costs of completing the Project and to provide funds to satisfy a portion of the Certificate Reserve Fund Requirement.

Tax Covenants.

(a) The County will not take any action, or fail to take any action, if such action or failure to take such action would adversely affect the exclusion from gross income of the interest evidenced and represented by the Certificates and any Additional Certificates pursuant to Section 103 of the Code, and specifically the County will not directly or indirectly use or make any use of the proceeds of the Certificates and any Additional Certificates or any other funds of the County or take or omit to take any action that would cause the Certificates or any Additional Certificates to be "arbitrage bonds" subject to federal income taxation by reason of Section 148 of the Code or "private activity bonds" subject to federal income taxation by reason of Section 141(a) of the Code or obligations subject to federal income taxation because they are "federally guaranteed" as provided in Section 149(b) of the Code; and to that end the County, with respect to the proceeds of the Certificates and any Additional Certificates and such other funds, will comply with all requirements of such sections of the Code to the extent that such requirements are, at the time, applicable and in effect; *provided,* that if the County shall obtain an Opinion of Counsel to the effect that any action required under this section is no longer required, or to the effect that some further action is required, to maintain the exclusion from gross income of the interest evidenced and represented by the Certificates and any Additional Certificates pursuant to Section 103 of the Code, the County may rely conclusively on such opinion in complying with the provisions of the Project Sublease. In the event that at any time the County is of the opinion that for purposes of this section it is necessary to restrict or limit the yield on the investment of any moneys held by the Trustee under the Trust Agreement or otherwise the County shall so instruct the Trustee in writing, and the Trustee shall take such action in accordance with such instructions.

(b) To the ends covenanted in this section, the County specifically agrees to ensure that the following requirements are met:

(1) No more than five percent of the Project Property (determined both on the basis of space and on the basis of cost) shall be used in the trade or business of one or more nongovernmental persons (not including the portion of the proceeds properly allocable to facilities expected to be used by an organization described in Section 501(c)(3) of the Code).

(2) The County will not invest or allow to be invested proceeds of the Certificates or any Additional Certificates at a yield in excess of the yield on the Certificates and such Additional Certificates, except to the extent allowed under the Tax Certificate.

(3) The County will rebate or cause to be rebated any amounts due to the federal government, as provided in the Tax Certificate.

Rental Payments

Rental Payments. The County agrees to pay to the Corporation, its successors or assigns, without deduction or offset of any kind, as rental for the use and occupancy of the Project Property, the following amounts at the following times:

(a) *Base Rental*. Subject to the immediately following sentence, the County shall pay to the Corporation rental under the Project Sublease as Base Rental Payments with respect to the Project Property at the times and in the amounts set forth in the Base Rental Payment Schedule attached to the Project Sublease, and made a part thereof, a portion of which Base

Rental Payments shall constitute interest. Notwithstanding the foregoing or any other provision of the Project Sublease to the contrary, until such time as a Certificate of Completion has been delivered to the Trustee, the County's obligation to pay Base Rental Payments and Additional Rental shall be limited solely, in the case of Base Rental Payments, to amounts on deposit in the Interest Fund, (including (without limitation) the Capitalized Interest Account established therein) established pursuant to the Trust Agreement, and, if the Interest Fund is exhausted, the Certificate Reserve Fund, and, in the case of Additional Rent, the Cost of Issuance Fund, and the County shall have no obligation to make any Base Rental Payments or Additional Rental from any other source. Notwithstanding the dates designated for the payment of the Base Rental Payments in the Project Sublease, all Base Rental Payments due in any Fiscal Year shall be due and payable in one sum on July 5 of each year (or the next Business Day if July 5 does not fall on a Business Day), commencing on July 5, 2007 or, if the Certificate of Completion has not been delivered on or before July 5, 2007, commencing on the July 5 (or the next Business Day if July 5 does not fall on a Business Day) following the date of delivery of the Certificate of Completion to the Trustee; *provided, however,* that if a Certificate of Completion is delivered after July 5, 2007 and before February 1, 2008, then the County shall make the scheduled Base Rental Payments due on any Interest Payment Date following the date of the delivery of the Certificate of Completion and before July 5, 2008; *provided, further,* that if a Certificate of Completion is delivered after July 5, 2008 on any date in a Fiscal Year of the County after July 5 (or the next Business Day if July 5 does not fall on a Business Day) and before February 1 of that same Fiscal Year, then the County shall made the scheduled Base Rental Payments due on any Interest Payment Date in that Fiscal Year following the date of the delivery of the Certificate of Completion. Notwithstanding the foregoing, the County shall, on the Interest Payment Date immediately following the delivery of the Certificate of Completion to the Trustee, have no obligation to make that portion of the Base Rental Payments due on such Interest Payment Date equal to the product obtained by multiplying the aggregate Base Rental Payment due on such Interest Payment Date by a fraction, the numerator of which is the number of calendar days that elapsed from the Interest Payment Date immediately preceding the delivery of the Certificate of Completion to the Trustee until the date on which the Certificate of Completion was delivered to the Trustee and the denominator of which is 180. Failure of the County to comply with the provisions of this section shall constitute an event of default under the Project Sublease. The interest components of the Base Rental Payments shall be paid by the County as and constitute interest paid on the principal components of the Base Rental Payments to be paid by the County under the Project Sublease. The obligation to make the Base Rental Payments shall commence as of February 2, 2005. Notwithstanding the foregoing, each Base Rental Payment shall be paid by wire transfer to the Corporation or its assignee not later than one Business Day preceding its due date.

(b) *Additional Rental*. Subject to subsection (a) above, the County shall also pay, as rental under the Project Sublease in addition to the Base Rental Payments, to the Corporation or the Trustee, as provided in the Project Sublease, such amounts ("Additional Rental") in each year as shall be required for the payment of all costs and expenses incurred by the Corporation in connection with the execution, performance or enforcement of the Project Sublease or the assignment of the Project Sublease, the Trust Agreement or the respective interests in the Project Property and the lease of the Project Property by the Corporation to the County under the Project Sublease, including but not limited to all fees, costs and expenses and all administrative costs of the Corporation relating to the Project Property including, without limiting the generality of the foregoing, salaries and wages of employees, overhead, insurance premiums, taxes and assessments (if any), expenses, compensation and indemnification of the Trustee (to the extent not paid or otherwise provided for out of the proceeds of the sale of the Certificates or any Additional Certificates), fees of auditors, accountants, attorneys or engineers, insurance premiums, and all other reasonable and necessary administrative costs of the Corporation or

charges required to be paid by it to comply with the terms of the Certificates, any Additional Certificates or the Trust Agreement.

The foregoing Additional Rental shall be billed to the County by the Corporation or the Trustee from time to time, together with a statement certifying that the amount billed has been incurred or paid by the Corporation, the Trustee or the Trustee on behalf of the Corporation for one or more of the items above described, or that such amount is then so payable for such items. Amounts so billed shall be paid by the County not later than the latest time as such amounts may be paid without penalty or, if no penalty is associated with a late payment of such amounts, within 30 days after receipt of a bill by the County for such amounts.

The Corporation may enter into leases to finance facilities other than the Project Property. The administrative costs of the Corporation shall be allocated among said facilities and the Project Property, as hereinafter in this paragraph provided. Any taxes levied against the Corporation with respect to the Project Property, the fees of the Trustee, and any other expenses directly attributable to the Project Property shall be included in the Additional Rental payable under the Project Sublease. Any taxes levied against the Corporation with respect to real property other than the Project Property, the fees of any trustee or paying agent under any resolution securing bonds of the Corporation or any trust agreement other than the Trust Agreement, and any other expenses directly attributable to any facilities other than the Project Property shall not be included in the administrative costs of the Project Property and shall not be paid from the Additional Rental payable under the Project Sublease. Any expenses of the Corporation not directly attributable to any particular project of the Corporation shall be equitably allocated among all such projects, including the Project Property, in accordance with sound accounting practice. In the event of any question or dispute as to such allocation, the written opinion of an independent firm of certified public accountants, employed by the Corporation to consider the question and render an opinion thereon, shall be final and conclusive determination as to such allocation. The Trustee may conclusively rely upon a Certificate of the Corporation in making any determination that costs are payable as Additional Rental under the Project Sublease, and shall not be required to make any investigation as to whether or not the items so requested to be paid are expenses of operation of the Project Property.

(c) *Consideration*.

(i) Such payments of Base Rental Payments and Additional Rental for each Lease Year or portion thereof during the term of the Project Sublease shall constitute the total rental for such Lease Year or portion thereof and shall be paid or payable by the County for and in consideration of the right of the use and possession of, and the continued quiet use and enjoyment of, the Project Property. The parties to the Project Sublease have agreed and determined that the annual fair rental value of the Project Property is not less than the maximum Base Rental Payments payable under the Project Sublease in any year. In making such determinations of annual fair rental value, consideration has been given to a variety of factors including the replacement costs of the existing improvements on the Project Property, other obligations of the parties under the Project Sublease, the uses and purposes which may be served by the improvements on the Project Property and the benefits therefrom which will accrue to the County and the general public.

(ii) The parties to the Project Sublease acknowledge that the parties to the Project Sublease may amend the Project Sublease from time to time to increase the Base Rental Payments payable under the Project Sublease so that Additional Certificates may

be executed and delivered pursuant to the Project Sublease and the Trust Agreement. The proceeds of such Additional Certificates shall be used for any lawful purpose. Notwithstanding anything to the contrary contained in the Project Sublease, the Project Sublease may not be amended in a manner such that the sum of Base Rental Payments, including Base Rental Payments payable pursuant to such amendment, and Additional Rental with respect to the prorated portion of Outstanding Certificates and Additional Certificates secured by the Project Property in any year is in excess of the annual fair rental value of the Project Property and other land and improvements leased to the County under the Project Sublease.

Payment; Credit. Each installment of Base Rental Payments payable under the Project Sublease shall be paid in lawful money of the United States of America to or upon the order of the Corporation at the principal corporate trust office of the Trustee in Los Angeles, California, or such other place as the Corporation shall designate. Any such installment of rental accruing under the Project Sublease which shall not be paid when due shall remain due and payable until received by the Trustee, except as provided in the Trust Agreement, and to the extent permitted by law shall bear interest at the rate of ten percent per annum from the date when the same is due under the Project Sublease until the same shall be paid. Notwithstanding any dispute between the County and the Corporation, the County shall make all rental payments when due, without deduction or offset of any kind, and shall not withhold any rental payments pending the final resolution of any such dispute. In the event of a determination that the County was not liable for said rental payments or any portion thereof, said payments or excess of payments, as the case may be, shall, at the option of the County, be credited against subsequent rental payments due under the Project Sublease or be refunded at the time of such determination. Amounts required to be deposited by the County with the Trustee pursuant to the Project Sublease on any date shall be reduced to the extent of available amounts on deposit on such date in the Base Rental Payment Fund, the Interest Fund or the Principal Fund.

Annual Budgets; Reporting Requirements. The County covenants to take such action as may be necessary to include all Base Rental Payments and Additional Rental payments due under the Project Sublease in its operating budget for each fiscal year commencing after the date of the Project Sublease (an "Operating Budget") and to make all necessary appropriations for such Base Rental Payments and Additional Rental payments.

Application of Rental Payments. All Base Rental Payments received shall be applied first to the interest components of the Base Rental Payments due under the Project Sublease, then to the principal components (including any prepayment premium components) of the Base Rental Payments due under the Project Sublease and thereafter to all Additional Rental due under the Project Sublease, but no such application of any payments which are less than the total rental due and owing shall be deemed a waiver of any default under the Project Sublease.

Rental Abatement. Except to the extent of (a) amounts held by the Trustee in the Base Rental Payment Fund or in the Certificate Reserve Fund, (b) amounts received in respect of rental interruption insurance, and (c) amounts, if any, otherwise legally available to the Trustee for payments in respect of the Certificates, during any period in which, by reason of material damage, destruction, title defect, condemnation, there is substantial interference with the use and possession by the County of any portion of the Project Property, rental payments due under the Project Sublease with respect to the Project Property shall be abated to the extent that the annual fair rental value of the portion of the Project Property in respect of which there is no substantial interference is less than the annual Base Rental Payments and Additional Rental, in which case rental payments shall be abated only by an amount equal to the difference. In the event the County shall assign, transfer or sublease any or all of the Project Property or other rights under the Project Sublease, as permitted by the Project Sublease, for purposes of

determining the annual fair rental value available to pay Base Rental Payments and Additional Rental, annual fair rental value of the Project Property shall first be allocated to the Project Sublease as provided therein. Any abatement of rental payments pursuant to the Project Sublease shall not be considered an Event of Default as defined in the Project Sublease. The County waives the benefits of Civil Code Sections 1932(2) and 1933(4) and any and all other rights to terminate the Project Sublease by virtue of any such interference and the Project Sublease shall continue in full force and effect. Such abatement shall continue for the period commencing with the date of such damage, destruction, title defect or condemnation and ending with the substantial completion of the work of repair or replacement of the portions of the Project Property so damaged, destroyed, defective or condemned.

In the event that rental is abated, in whole or in part, pursuant to the Project Sublease due to damage, destruction, title defect or condemnation of any part of the Project Property and the County is unable to repair, replace or rebuild the Project Property from the proceeds of insurance, if any, the County agrees to apply for and to use its best efforts to obtain any appropriate state and/or federal disaster relief in order to obtain funds to repair, replace or rebuild the Project Property.

Prepayment of Rental Payments. The County may prepay, from eminent domain proceeds or net insurance proceeds received by it pursuant to Project Sublease, all or any portion of the components of Base Rental Payments payable under the Project Sublease relating to any portion of the Project Property then unpaid, in whole on any date, or in part on any date in integral multiples of an Authorized Denomination so that the aggregate annual amounts of principal components of Base Rental Payments payable under the Project Sublease and the Refunding Sublease represented by the Certificates and any Additional Certificates which shall be payable after such prepayment date shall each be in an integral multiple of an Authorized Denomination and shall be as nearly proportional as practicable to the aggregate annual amounts of principal components of Base Rental Payments payable under the Project Sublease and the Refunding Sublease represented by the Certificates and any Additional Certificates.

The County may prepay, from any source of available moneys pursuant to optional prepayment provisions of the Trust Agreement, all or any part (in an integral multiple of an Authorized Denomination) of the principal components of Base Rental Payments payable under the Project Sublease and the Refunding Sublease then unpaid so that the aggregate annual amounts of principal components of Base Rental Payments under the Project Sublease and the Refunding Sublease which shall be payable after such prepayment date shall be as nearly proportional as practicable to the aggregate annual amounts of principal components represented by the Certificates and any Additional Certificates unpaid prior to the prepayment date, at a prepayment amount equal to the principal component prepaid plus accrued interest thereon to the date of prepayment plus any applicable premium.

Before making any prepayment pursuant to the Project Sublease, at least 45 days before the prepayment date the County shall give written notice to the Corporation and the Trustee describing such event, specifying the order of Principal Payment Dates and specifying the date on which the prepayment will be made, which date shall be not less than 30 nor more than 60 days from the date such written notice is given to the Corporation and the Trustee.

Obligation to Make Rental Payments. The agreements and covenants on the part of the County contained in the Project Sublease shall be deemed to be and shall be construed to be duties imposed by law and it shall be the duty of each and every public official of the County to take such action and do such things as are required by law in the performance of the official duty of such officials to enable the County to carry out and perform the agreements and covenants contained in the Project Sublease agreed to be carried out and performed by the County.

THE OBLIGATION OF THE COUNTY TO MAKE BASE RENTAL PAYMENTS AND TO PAY ADDITIONAL RENT DOES NOT CONSTITUTE AN OBLIGATION OF THE COUNTY FOR WHICH THE COUNTY IS OBLIGATED TO LEVY OR PLEDGE ANY FORM OF TAXATION OR FOR WHICH THE COUNTY HAS LEVIED OR PLEDGED ANY FORM OF TAXATION. NEITHER THE CERTIFICATES NOR THE OBLIGATION TO MAKE RENTAL PAYMENTS AND TO PAY ADDITIONAL RENT CONSTITUTES AN INDEBTEDNESS OF THE COUNTY, THE STATE OF CALIFORNIA OR ANY POLITICAL SUBDIVISION THEREOF WITHIN THE MEANING OF ANY CONSTITUTIONAL OR STATUTORY DEBT LIMITATION OR RESTRICTION.

Additional Certificates. In addition to the Certificates to be executed and delivered under the Trust Agreement the County may, from time to time, but only upon satisfaction of the conditions to the execution and delivery of Additional Certificates set forth in the Trust Agreement, enter into a Supplemental Trust Agreement to execute and deliver Additional Certificates on a parity with the Certificates and any previously executed and delivered Additional Certificates (unless otherwise provided in the related Supplemental Trust Agreement), the proceeds of which may be used for any lawful purpose by the County, as provided in the Supplemental Trust Agreement; provided that prior to or concurrently with the execution and delivery of the Additional Certificates, the County and the Corporation shall have entered into an amendment to the Project Sublease, providing for an increase in the Base Rental Payments to be made under the Project Sublease subject to the limitations set forth in the Project Sublease.

Maintenance; Taxes; Insurance and other Charges

Maintenance of the Project Property by the County. The County agrees that, at all times during the term of the Project Sublease, it will, at its own cost and expense, maintain, preserve and keep the Project Property and every portion thereof in good repair, working order and condition and that it will from time to time make or cause to be made all necessary and proper repairs, replacements and renewals. The Corporation shall have no responsibility in any of these matters or for the making of additions or improvements to the Project Property.

Taxes, Other Governmental Charges and Utility Charges. The parties to the Project Sublease contemplate that the Project Property will be used for public purposes by the County and, therefore, that the Project Property will be exempt from all taxes presently assessed and levied with respect to real and personal property, respectively. In the event that the use, possession or acquisition by the County or the Corporation of the Project Property is found to be subject to taxation in any form, the County will pay during the term of the Project Sublease, as the same respectively become due, all taxes and governmental charges of any kind whatsoever that may at any time be lawfully assessed or levied against or with respect to the Project Property and any other property acquired by the County in substitution for, as a renewal or replacement of, or a modification, improvement or addition to, the Project Property, as well as all gas, water, steam, electricity, heat, power, air conditioning, telephone, utility and other charges incurred in the operation, maintenance, use, occupancy and upkeep of the Project Property; *provided,* that with respect to any governmental charges or taxes that may lawfully be paid in installments over a period of years, the County shall be obligated to pay only such installments as are accrued during such time as the Project Sublease is in effect.

Insurance. From and after the delivery to the Trustee of the Certificate of Completion, the County shall secure and maintain or cause to be secured and maintained at all time with insurers of recognized responsibility all coverage on the Project Property required by the Project Sublease. Such insurance shall consist of :

(1) A policy or policies of insurance against loss or damage to the Project Property known as "all risk," including flood, but excluding earthquake, which shall be maintained at any

time in an amount per occurrence at least equal to the lesser of (i) the cumulative replacement values of the Project Property and, in the case of a policy covering more than the Project Property, as permitted by the next succeeding sentence, any other property which is the subject of a lease, installment purchase agreement or other financing arrangement for which bonds, certificates of participation or other obligations shall have been issued ("Obligations") or (ii) the aggregate amount of the principal component of the then-remaining Base Rental Payments payable under the Project Sublease; *provided* that, with the consent of the Insurer, the amount of coverage required by this sentence may be reduced to a smaller amount if an insurance consultant or insurance broker retained by the County provides written advice to the Trustee that, based upon its evaluation of the County's maximum foreseeable loss in the event of a major conflagration, windstorm, explosion, riot, flood or similar event, a specified smaller amount is believed to be reasonable given the nature of the risks insured and the proximity of the insured properties to each other. Such insurance may be in the form of a policy which covers the Project Property and one or more additional parcels of real property leased or owned by the County which may be limited in an amount per occurrence in the aggregate to the amount required by the preceding sentence. Such insurance may at any time include a deductible clause providing for a deductible not to exceed $100,000 for any one loss (except for flood, in which case the deductible may not exceed $250,000 for any one loss). The County may obtain such coverage as a joint insured with one or more other public agencies located within or without the County of San Diego which may be limited in an amount per occurrence in the aggregate for all insureds as described in the first sentence of this paragraph (1) and which may be limited in a cumulative amount of claims during a 12-month period in the aggregate for all insureds in an amount not less than $500,000,000. Otherwise conforming policies satisfying the requirements of this paragraph (1) may provide that amounts payable as coverage under this paragraph (1) may be reduced by amounts payable under paragraph (3) for the same occurrence, and vice versa. The County is, however, under no obligation to provide insurance against loss or damage occasioned by the perils of earthquake.

(2) In the event that such coverage is not included in paragraph (1) above, boiler and machinery coverage against loss or damage by explosion of steam boilers, pressure vessels and similar apparatus now or hereafter installed on the Project Property in an amount not less than $75,000,000 per accident; *provided, however,* that the amount of coverage required by this sentence may be reduced to a smaller amount if an insurance consultant or insurance broker retained by the County provides written advice to the Trustee that, based upon its evaluation of the County's maximum foreseeable loss in the event of loss or damage by steam boilers, pressure vessels and similar apparatus now or hereafter installed on the Project Property, a specified smaller amount is believed to be reasonable. Such insurance may be in the form of a policy which covers the Project Property and one or more additional parcels of real property leased or owned by the County which may be limited in amount to $75,000,000 per accident. Such insurance may at any time include a deductible clause providing for a deductible not to exceed $100,000 for any one loss. The County may obtain such coverage as a joint insured with one or more public agencies located within or without the County of San Diego which may be limited in amount to $75,000,000 per accident. Otherwise conforming policies satisfying the requirements of this paragraph (2) may provide that amounts payable as coverage under this paragraph (2) may be reduced by amounts payable under paragraph (3) for the same occurrence, and vice versa.

(3) Rental interruption insurance to cover loss, total or partial, of the use of any part of the Project Property as a result of any of the hazards covered by the insurance required pursuant to paragraph (1) or (2) above, as the case may be, in an amount sufficient at all times to pay the total rent payable under the Project Sublease for a period of not less than two years' Base Rental Payments for the Project Property; provided that such rental interruption insurance may be

included in the policy or policies provided pursuant to paragraph (1) or (2) without increasing the aggregate limits for coverage with respect to any hazard covered thereby. Such insurance also may be in the form of a policy which covers the Project Property and one or more additional parcels of real property leased or owned by the County. The County also may obtain an otherwise conforming policy required by this paragraph (3) as a joint insured with one or more other public agencies within or without the County of San Diego which may, with respect to any hazard, be limited in aggregate amount for all insureds to the amount of the policy or policies required pursuant to paragraph (1) or (2) above, as the case may be, which insures against such hazard. Otherwise conforming policies satisfying the requirements of this paragraph (3) may provide that amounts payable as coverage under this paragraph (3) may be reduced by amounts payable under paragraph (1) or (2), as the case may be, for the same occurrence, and vice versa.

The County shall collect, adjust and receive all moneys which may become due and payable under any policies contemplated by paragraphs (1) and (2) above, and, may compromise any and all claims thereunder and shall transfer the net proceeds of such insurance as provided in the Project Sublease or in the Trust Agreement. The Trustee shall not be responsible for the sufficiency of any insurance required in the Project Sublease. The Trustee shall be fully protected in accepting payment on account of such insurance or any adjustment, compromise or settlement of any loss agreed to by the County.

Any insurance policy issued pursuant to paragraph (1) or (2) above shall be so written or endorsed as to make losses, if any, payable to the County, the Corporation and the Trustee as their respective interests may appear and the net proceeds of the insurance required by paragraphs (1) or (2) above shall be applied as provided in the Project Sublease. The net proceeds, if any, of the insurance policy described in paragraphs (1) and (2) above shall be payable to the County for deposit in the Insurance Proceeds and Condemnation Awards Fund. The net proceeds, if any, of the insurance policy described in paragraph (3) above shall be payable to the Trustee and deposited in the Base Rental Payment Fund. Each insurance policy provided for in the Project Sublease shall contain a provision to the effect that the insurance company shall not cancel the policy or modify it materially and adversely to the interests of the Corporation or the Trustee without first giving written notice thereof to the Corporation and the Trustee at least 30 days in advance of such intended cancellation or modification.

The County shall file a Certificate of the County with the Trustee not later than January 31 of each year certifying that the insurance policies required by the Project Sublease are in full force and effect and that the Corporation and/or the Trustee is named as a loss payee on each insurance policy which the Project Sublease requires to be so endorsed. The Trustee shall have no responsibility whatsoever for determining the adequacy of any insurance required under the Project Sublease.

Notwithstanding anything in the Project Sublease to the contrary, other than the following paragraph, none of the insurance provisions of the Project Sublease set forth above shall be binding on the County until the Certificate of Completion shall be delivered to the Trustee.

Advances. In the event the County shall fail to maintain the full insurance coverage required by the Project Sublease or shall fail to keep the Project Property in good repair and operating condition, the Corporation may (but shall be under no obligation to) purchase the required policies of insurance and pay the premiums on the same or may make such repairs or replacements as are necessary and provide for payment thereof; and all amounts so advanced therefor by the Corporation shall become Additional Rental, which amounts the County agrees to pay within 30 days of a written request therefor, together with interest thereon at the maximum rate allowed by law.

Title Insurance. The County covenants and agrees to deliver or cause to be delivered to the Trustee a CLTA leasehold owner's policy or policies, or a commitment for such policy or policies, with

respect to the Project Property with liability in the aggregate amount of the principal component of all Base Rental Payments payable under the Project Sublease. Such policy or policies, when issued, shall name the Trustee as the insured and shall insure the leasehold estate of the County in the Project Property subject only to such exceptions as do not materially affect the County's right to the use and occupancy of the Project Property.

Liquidated Damages under Construction Contract.

The County assigns and transfers to the Corporation all of the County's right, title, and interest in, to, and under any payments under the liquidated damage provisions of that certain Contract of Construction (the "Construction Contract"), by and between the County and Sundt Construction, Inc. ("Sundt") relating to the construction of the Project; *provided,* that the County only so assigns and transfers such rights, title, and interest as shall accrue on or after March 1, 2009.

The County agrees that, upon the written request of the Trustee, the County will take such actions as may be reasonably requested by the Trustee and to the extent permitted by law to enforce the obligations of Sundt under the liquidated damage provisions of the Construction Contract to the extent of the Trustee's or the Corporation's interest therein, including, but not limited, to bringing an action against Sundt for payments thereunder.

The County agrees that it will obtain from Sundt such evidence that the County deems reasonable under the circumstances to ensure that Sundt is complying with the insurance provisions of the Construction Contract.

Damage, Destruction, Title Defect and Condemnation

Damage, Destruction, Title Defect and Condemnation; Use of Net Proceeds. If prior to the termination of the term of the Project Sublease (a) the Project Property or any portion thereof is destroyed (in whole or in part) or is damaged by fire or other casualty; or (b) title to, or the temporary use of, the Project Property or any portion thereof or the estate of the County or the Corporation in the Project Property or any portion thereof is defective or shall be taken under the exercise of the power of eminent domain by any governmental body or by any person or firm or corporation acting under governmental authority, then the County and the Corporation will cause the net proceeds of any insurance claim or condemnation award to be applied to the prompt repair, restoration, modification, improvement or replacement of the damaged, destroyed, defective or condemned portion of the Project Property, and any balance of the net proceeds remaining after such work has been completed shall be paid to the County; *provided,* that the County, at its option and provided the proceeds of such insurance or condemnation award together with any other moneys then available for the purpose are at least sufficient to prepay the aggregate annual amounts of principal and interest components of the Base Rental Payments due under the Project Sublease attributable to the portion of the Project Property so destroyed, damaged, defective or condemned (determined by reference to the proportion which the annual fair rental value of the destroyed, damaged, defective or condemned portion thereof bears to the annual fair rental value of the Project Property), may elect not to repair, reconstruct or replace the damaged, destroyed, defective or condemned portion of the Project Property and thereupon shall cause said proceeds to be used for the prepayment of Outstanding Certificates and Additional Certificates pursuant to the optional prepayment provisions of the Trust Agreement. Notwithstanding any other provision in the Project Sublease, the County shall only prepay less than all of the principal component of the then-remaining Base Rental Payments if the annual fair rental value of the Project Property after such damage, destruction, title defect or condemnation is at least equal to the aggregate annual amount of the principal and interest components of the Base Rental Payments not being prepaid.

In the event that the proceeds, if any, of said insurance or condemnation award are insufficient either to (i) repair, rebuild or replace the Project Property so that the fair rental value of the Project Property would be at least equal to the Base Rental Payments or (ii) to prepay all the Outstanding Certificates and Additional Certificates, both as provided in the preceding paragraph, then the County may, in its sole discretion, budget and appropriate an amount necessary, but in no event more than the net proceeds available from any insurance claim or condemnation award described in the Project Sublease, to effect such repair, rebuilding or replacement or prepayment; provided that the failure of the County to so budget and/or appropriate shall not be a breach of or default under the Project Sublease.

Disclaimer of Warranties; Vendor's Warranties; Use of the Project Property

Disclaimer of Warranties. NEITHER THE TRUSTEE NOR THE CORPORATION MAKES ANY AGREEMENT, WARRANTY OR REPRESENTATION, EITHER EXPRESS OR IMPLIED, AS TO THE VALUE, DESIGN, CONDITION, MERCHANTABILITY OR FITNESS FOR PARTICULAR PURPOSE OR FITNESS FOR USE OF THE PROJECT PROPERTY, OR WARRANTY WITH RESPECT THERETO. THE COUNTY ACKNOWLEDGES THAT NEITHER THE TRUSTEE NOR THE CORPORATION IS A MANUFACTURER OF ANY PORTION OF THE PROJECT PROPERTY OR A DEALER THEREIN, THAT THE COUNTY LEASES THE PROJECT PROPERTY AS-IS, IT BEING AGREED THAT ALL OF THE AFOREMENTIONED RISKS ARE TO BE BORNE BY THE COUNTY. In no event shall the Corporation or the Trustee be liable for any incidental, indirect, special or consequential damage in connection with or arising out of the Project Sublease or the existence, furnishing, functioning or the County's use of the Project Property as provided by the Project Sublease.

Use of the Project Property; Improvements. The County will not use, operate or maintain the Project Property improperly, carelessly, in violation of any applicable law or in a manner contrary to that contemplated by the Project Sublease. The County shall provide all permits and licenses, if any, necessary for the use of the Project Property. In addition, the County agrees to comply in all respects (including, without limitation, with respect to the use, maintenance and operation of each portion of the Project Property) with all laws of the jurisdictions in which its operations involving any portion of the Project Property may extend and any legislative, executive, administrative or judicial body exercising any power or jurisdiction over the Project Property; *provided,* that the County may contest in good faith the validity or application of any such law or rule in any reasonable manner which does not, in the opinion of the County adversely affect the estate of the Corporation in and to the Project Property or its interest or rights under the Project Sublease.

Assignment and Indemnification

Assignment by Corporation. The parties understand that certain of the rights of the Corporation under the Project Sublease and under the Project Lease will be assigned to the Trustee pursuant to the Assignment Agreement, and accordingly the County agrees to make all payments due under the Project Sublease to the Trustee, notwithstanding any claim, defense, setoff or counterclaim whatsoever (whether arising from a breach of the Project Sublease or otherwise) that the County may from time to time have against the Corporation. The County agrees to execute all documents, including notices of assignment and chattel mortgages or financing statements, which may be reasonably requested by the Corporation or the Trustee to protect their interests in the Project Property during the term of the Project Sublease.

Assignment by County. The Project Sublease and the interest of the County in the Project Property may not be assigned or encumbered by the County except as permitted by the Project Sublease.

Indemnification. The County shall, to the full extent then permitted by law, indemnify, protect, hold harmless, save and keep harmless the Corporation and the Trustee and their respective directors,

officers and employees from and against any and all liability, obligations, losses, claims and damages whatsoever, regardless of the cause thereof, and expenses in connection therewith, including, without limitation, counsel fees and expenses, penalties and interest arising out of or as the result of the entering into of the Project Sublease, the acquisition, construction, installation and use of the Project Property and each portion thereof or any accident in connection with the operation, use, condition or possession of the Project Property or any portion thereof resulting in damage to property or injury to or death to any person including, without limitation, any claim alleging latent and other defects, whether or not discoverable by the County or the Corporation; any claim arising out of the use, presence, storage, disposal or release of any Hazardous Substances on or about the Project Property; any claim for patent, trademark or copyright infringement; and any claim arising out of strict liability in tort. The indemnification arising under the Project Sublease shall continue in full force and effect notwithstanding the full payment of all obligations under the Project Sublease or the termination of the Project Sublease for any reason. The County, the Trustee and the Corporation mutually agree to promptly give notice to each other of any claim or liability indemnified against by the Project Sublease following the learning thereof by such party.

Default

The following events shall be "Events of Default" under the Project Sublease and the terms "Event of Default" and "Default" shall mean, whenever they are used in the Project Sublease, any one or more of the following events:

(1) The County shall fail to deposit with the Trustee any Base Rental Payment required to be so deposited by the close of business on the day such deposit is required pursuant to the Project Sublease, provided, that the failure to deposit any Base Rental Payments abated pursuant to the Project Sublease shall not constitute an Event of Default;

(2) The County shall fail to pay any item of Additional Rental when the same shall become due and payable pursuant to the Project Sublease; or

(3) The County shall breach any other terms, covenants or conditions contained in the Project Sublease or in the Trust Agreement, and shall fail to remedy any such breach with all reasonable dispatch within a period of 30 days after written notice thereof from the Corporation to the County; *provided, however,* that if the failure stated in the notice cannot be corrected within such period, then the Corporation shall not unreasonably withhold its consent to an extension of such time if corrective action is instituted by the County within such period and is diligently pursued until the default is corrected.

Upon the happening of any of the Events of Default specified in the Project Sublease, it shall be lawful for the Corporation or its assignee, subject to the terms of the Project Sublease, and to the direction and control of the Insurer, so long as the Insurer is not in default under the Municipal Bond Insurance Policy, to exercise any and all remedies available or granted to it pursuant to law or under the Project Sublease.

Upon the occurrence of an Event of Default, the Corporation or its assignee must thereafter maintain the Project Sublease in full force and effect and may only recover rent and other monetary charges as they become due, all without terminating the County's right to possession of the Project Property, regardless of whether or not the County has abandoned the Project Property; **THIS SHALL BE THE SOLE AND EXCLUSIVE REMEDY AVAILABLE AGAINST THE COUNTY UNDER THIS PROJECT SUBLEASE OR OTHERWISE.** In such event, the County shall remain liable and agrees to keep or perform all covenants and conditions contained in the Project Sublease to be kept or performed by the County and, to pay the rent to the end of the term of the Project Sublease and further

agrees to pay said rent and/or rent deficiency punctually at the same time and in the same manner as provided in the Project Sublease for the payment of rent under the Project Sublease (without acceleration).

The Corporation expressly waives the right to receive any amount from the County pursuant to Section 1951.2(a)(3) of the California Civil Code.

In addition to any Event of Default resulting from breach by the County of any agreement, condition, covenant or term of the Project Sublease, if the County's interest in the Project Sublease or any part thereof assigned, sublet or transferred without the written consent of the Corporation (except as otherwise permitted by the Project Sublease), either voluntarily or by operation of law; or the County or any assignee shall file any petition or institute any proceedings under any act or acts, state or federal, dealing with or relating to the subject of bankruptcy or insolvency or under any amendment of such act or acts, either as a bankrupt or as an insolvent or as a debtor or in any similar capacity, wherein or whereby the County asks or seeks or prays to be adjudicated a bankrupt, or is to be discharged from any or all of its debts or obligations, or offers to its creditors to effect a composition or extension of time to pay its debts, or asks, seeks or prays for a reorganization or to effect a plan of reorganization or for a readjustment of its debts or for any other similar relief, or if the County shall make a general or any assignment for the benefit of its creditors; or the County shall abandon or vacate the Project Property or any portion thereof (except as permitted by the Project Sublease); then in each and every such case the County shall be deemed to be in default under the Project Sublease.

Neither the County nor the Corporation shall be in default in the performance of any of its obligations under the Project Sublease (except for the obligation to make Base Rental Payments pursuant to the Project Sublease) unless and until it shall have failed to perform such obligation within 30 days after notice by the County of the Corporation, as the case may be, to the other party properly specifying wherein it has failed to perform such obligation.

The County and Corporation and its successors and assigns shall honor the exclusive rights of the County to use the Project Property.

Miscellaneous

Trustee as Third Party Beneficiary. The Trustee is designated a third party beneficiary under the Project Sublease for the purpose of enforcing any of the rights under the Project Sublease assigned to the Trustee under the Assignment Agreement.

Net Lease. It is the purpose and intent of the Corporation and the County that lease payments under the Project Sublease shall be absolutely net to the Corporation so that the Project Sublease shall yield to the Corporation the lease payments, free of any charges, assessments or impositions of any kind charged, assessed or imposed on or against the Project Property, and without counterclaim, deduction, defense, deferment or set-off by the County except as specifically otherwise provided in the Project Sublease. The Corporation shall not be expected or required to pay any such charge, assessment or imposition, or be under any obligation or liability under the Project Sublease except as expressly set forth in the Project Sublease, and all costs, expenses and obligations of any kind relating to the maintenance and operation of the Project Property which may arise or become due during the term of the Project Sublease shall be paid by the County.

Amendments. The Project Sublease may be amended in writing as may be mutually agreed by the Corporation and the County, subject to the written approval of the Trustee; *provided,* that no such amendment which materially adversely affects the rights of the Owners shall be effective unless it shall

have been consented to by the Owners of more than 50% in principal amount of the Certificates and Additional Certificates Outstanding, and provided further, that no such amendment shall (a) extend the payment date of any Base Rental Payment, or reduce the interest, principal or prepayment premium component of any Base Rental Payment, without the prior written consent of the Owner of each Certificate and Additional Certificate so affected, or (b) reduce the percentage of the principal amount of the Certificates and Additional Certificates Outstanding the consent of the Owners of which is required for the execution of any amendment of the Project Sublease.

The Project Sublease and the rights and obligations of the Corporation and the County under the Project Sublease may also be amended or supplemented at any time by an amendment of the Project Sublease or supplement to the Project Sublease which shall become binding upon execution without the written consents of any Owners, but only to the extent permitted by law and only for any one or more of the following purposes:

(a) to add to the agreements, conditions, covenants and terms required by the Corporation or the County to be observed or performed in the Project Sublease and other agreements, conditions, covenants and terms thereafter to be observed or performed by the Corporation or the County, or to surrender any right or power reserved in the Project Sublease to or conferred in the Project Sublease on the Corporation or the County, and which in either case shall not materially adversely affect the interests of the Owners;

(b) to make such provisions for the purpose of curing any ambiguity or of correcting, curing or supplementing any defective provision contained in the Project Sublease or in regard to questions arising under the Project Sublease which the Corporation or the County may deem desirable or necessary and not inconsistent with the Project Sublease, and which shall not materially adversely affect the interests of the Owners;

(c) to effect a Substitution or Removal in accordance with the Project Sublease;

(d) to facilitate the issuance of Additional Certificates as provided in the Project Sublease; or

(e) to make any other addition, amendment or deletion which does not materially adversely affect the interests of the Owners or the Insurer.

Discharge of County. Upon the payment of all Base Rental Payments and Additional Rental payable under the Project Sublease, all of the obligations of the County under the Project Sublease shall thereupon cease, terminate and become void and shall be discharged and satisfied; *provided, however,* if any Outstanding Certificates and Additional Certificates shall be deemed to have been paid by virtue of a deposit of Base Rental Payments under the Project Sublease pursuant to the Trust Agreement, then the obligation of the County under the Project Sublease to make Base Rental Payments under the Project Sublease shall continue in full force and effect until the Outstanding Certificates and Additional Certificates so deemed paid have in fact been paid, but such payments shall be made solely and exclusively from moneys and securities deposited with the Trustee as contemplated by the Trust Agreement, and that shall be the sole source of satisfaction of the County's obligation to make Base Rental Payments. The time period for giving notice by the County to the Corporation and the Trustee specified in the Project Sublease shall not apply incident to the payment to the Owners of all Outstanding Certificates and Additional Certificates in accordance with the Trust Agreement.

California Law. The Project Sublease shall be governed by and construed and interpreted in accordance with the laws of the State of California.

Insurer Deemed Owner. For the purpose of (i) the giving of consents to amendments to the Project Sublease, (ii) the giving of any other consent of the Owners under the Project Sublease, and (iii) the control and direction of all rights and remedies upon the occurrence of an Event of Default, the Insurer shall be deemed to be the sole Owner of the Certificates for so long as it has not failed to comply with its payment obligations under the Municipal Bond Insurance Policy; *provided*, *however*, that, notwithstanding the foregoing, the Insurer shall not be deemed to be the Owner of the Certificates for any consent to an amendment to the Project Sublease that (a) extends the payment date of any Base Rental Payment, or reduces the interest, principal or prepayment premium component of any Base Rental Payment, or (b) reduces the percentage of the principal amount of the Certificates and Additional Certificates Outstanding the consent of the Owners of which is required for the execution of any amendment of the Project Sublease.

PROJECT LEASE

Project Property. The County leases to the Corporation and the Corporation rents and hires from the County, on the terms and conditions set forth in the Project Lease, the Project Property.

Term.

(a) The term of the Project Lease commenced on February 2, 2005 and shall end on the Expiry Date (as defined in the Project Sublease) unless such term is sooner terminated or is extended as provided in the Project Lease. If prior to the Expiry Date all Base Rental Payments under the Project Sublease shall have been paid, or provision therefor has been made in accordance with the Trust Agreement, the term of the Project Lease shall end simultaneously therewith.

(b) If the Project Sublease is extended beyond the Expiry Date pursuant to the terms thereof, the Project Lease shall also be extended to the day following the date of termination of the Project Sublease.

Rent. The Corporation shall pay to the County an advance rent of $1, which, together with the execution and delivery of the Project Sublease, shall constitute full consideration for the Project Lease over its term. The Corporation waives any right that it may have under the laws of the State of California to receive a rebate of such rent in full or in part in the event there is a substantial interference with the use and right of possession by the Corporation of the Project Property or portion thereof as a result of material damage, destruction or condemnation.

Purpose. The Corporation shall use the Project Property solely for the purpose of subleasing the same to the County; *provided,* that in the event of default by the County under the Project Sublease, the Corporation may exercise the remedies provided in the Project Sublease.

Owner in Fee. The County covenants that it is the owner of the Project Property free and clear of all liens, claims or encumbrances which affect marketability.

Assignments and Project Subleases. Unless the County shall be in default under the Project Sublease, the Corporation may not, without the prior written consent of the County, assign its rights under the Project Lease or sublet the Project Property except that the County expressly approves and consents to the assignment and transfer of the Corporation's right, title and interest in the Project Lease to the Trustee pursuant to the Assignment Agreement.

Right of Entry. The County reserves the right for any of its duly authorized representatives to enter upon the Project Property at any reasonable time to inspect the same or to make any repairs, improvements or changes necessary for the preservation thereof.

Termination. The Corporation agrees, upon the termination of the Project Lease, to quit and surrender the Project Property in the same good order and condition as the same was in at the time of commencement of the terms under the Project Lease, reasonable wear and tear excepted, and agrees that any permanent improvements to the Project Property at the time of the termination of the Project Lease shall remain thereon and title thereto shall vest in the County.

Default. In the event the Corporation shall be in default in the performance of any obligation on its part to be performed under the terms of the Project Lease, which default continues for thirty (30) days following notice and demand for correction thereof to the Corporation, the County may exercise any and all remedies granted by law, except that no merger of the Project Lease and of the Project Sublease shall be deemed to occur as a result thereof; *provided,* that so long as the Certificates executed and delivered pursuant to the Trust Agreement are Outstanding, the County shall have no power to terminate the Project Lease by reason of any default on the part of the Corporation, if such termination would affect or impair any assignment of the Project Sublease then in effect between the Corporation and the Trustee that executes and delivers the Certificates.

Eminent Domain. In the event the whole or any portion of the Project Property is taken by eminent domain proceedings, the interest of the Corporation shall be recognized and is determined to be the amount of the then unpaid Base Rental Payments payable under the Project Sublease, and the amount of the unpaid Additional Rental due under the Project Sublease, and the balance of the award, if any, shall be paid to the County.

Amendments. The Project Lease may be amended for the purpose of affecting a Substitution or Removal, as further described in the Project Sublease.

Governing Law. The Project Lease is made in the State of California under the Constitution and laws of the State of California and is to be so construed.

REFUNDING SUBLEASE

The Refunding Property

Lease of the Refunding Property. The Corporation leases to the County, and the County rents and hires from the Corporation, the Refunding Property on the conditions and terms set forth in the Refunding Sublease. The County agrees and covenants that during the term of the Refunding Sublease, except as provided in Refunding Sublease, it will use the Refunding Property for public purposes so as to afford the public the benefits contemplated by the Refunding Sublease and so as to permit the Corporation to carry out its agreements and covenants contained in the Refunding Sublease and in the Trust Agreement, and the County further agrees and covenants that during the term of the Refunding Sublease that it will not abandon or vacate the Refunding Property.

Quiet Enjoyment. The parties to the Refunding Sublease mutually covenant that the County, so long as it observes and performs the agreements, conditions, covenants and terms required to be observed or performed by it contained in the Refunding Sublease and is not in default under the Refunding Sublease, shall at all times during the term of the Refunding Sublease peaceably and quietly have, hold and enjoy the Refunding Property without suit, trouble or hindrance from the Corporation.

Right of Entry and Inspection. The Corporation shall have the right to enter the Refunding Property and inspect the Refunding Property during reasonable business hours (and in emergencies at all times) for any purpose connected with the Corporation's rights or obligations under the Refunding Sublease and for all other lawful purposes.

Prohibition Against Encumbrance or Sale. The County and the Corporation will not create or suffer to be created any mortgage, pledge, lien, charge or encumbrance upon the Refunding Property, except Permitted Encumbrances, and except incident to the execution and delivery of Additional Certificates as contemplated by the Refunding Sublease. The County and the Corporation will not sell or otherwise dispose of the Refunding Property or any property essential to the proper operation of the Refunding Property, except as otherwise provided in the Refunding Sublease. Notwithstanding anything to the contrary contained in the Refunding Sublease, with the consent of the Insurer, which will not be unreasonably withheld, the County may assign, transfer or sublease any and all of the Refunding Property or its other rights under the Refunding Sublease, provided that (a) the rights of any assignee, transferee or sublessee shall be subordinate to all rights of the Corporation under the Refunding Sublease, (b) no such assignment, transfer or sublease shall relieve the County of any of its obligations under the Refunding Sublease, (c) the assignment, transfer or sublease shall not result in a breach of any covenant of the County contained in the Refunding Sublease, (d) any such assignment, transfer or sublease shall by its terms expressly provide that the fair rental value of the Refunding Property for all purposes shall be first allocated to the Refunding Sublease, as the same may be amended from time to time before or after any such assignment, transfer or sublease and (e) no such assignment, transfer or sublease shall confer upon the parties thereto any remedy which allows reentry upon the Refunding Property unless concurrently with granting such remedy the same shall be also granted under the Refunding Sublease by an amendment to the Refunding Sublease which shall in all instances be prior to and superior to any such assignment, transfer or sublease.

Liens. In the event the County shall at any time during the term of the Refunding Sublease cause any improvements to the Refunding Property to be constructed or materials to be supplied in or upon or attached to the Refunding Property, the County shall pay or cause to be paid when due all sums of money that may become due or purporting to be due for any labor, services, materials, supplies or equipment furnished or alleged to have been furnished to or for the County in, upon, about or relating to the Refunding Property and shall keep the Refunding Property free of any and all liens against the Refunding Property or the Corporation's interest therein. In the event any such lien attaches to or is filed against the Refunding Property or the Corporation's interest therein, and the enforcement thereof is not stayed or if so stayed such stay thereafter expires, the County shall cause each such lien to be fully discharged and released at the time the performance of any obligation secured by any such lien matures or becomes due. If any such lien shall be reduced to final judgment and such judgment or any process as may be issued for the enforcement thereof is not promptly stayed, or if so stayed and such stay thereafter expires, the County shall forthwith pay and discharge or cause to be paid and discharged such judgment. The County shall, to the maximum extent permitted by law, indemnify and hold the Corporation and its assignee and its directors, officers and employees harmless from, and defend each of them against, any claim, demand, loss, damage, liability or expense (including attorneys' fees) as a result of any such lien or claim of lien against the Refunding Property or the Corporation's interest therein.

Substitution or Removal of Refunding Property.

(a) The County may amend the Refunding Sublease and the Refunding Lease to substitute other real property and/or improvements (the "Substituted Property") for existing Refunding Property and/or to remove real property (including undivided interests therein) and/or improvements from the definition of Refunding Property, with the consent of the Insurer, and upon compliance with all of the conditions set forth in subsection (b) below. After a Substitution or Removal, the part of the Refunding

Property for which the Substitution or Removal has been effected shall be released from the leasehold under the Refunding Sublease and under the Refunding Lease.

(b) No Substitution or Removal shall take place under the Refunding Sublease until the County delivers to the Corporation and the Trustee the following:

(1) A Certificate of the County containing a description of all or part of the Refunding Property to be released and, in the event of a Substitution, a description of the Substituted Property to be substituted in its place;

(2) A Certificate of the County (A) stating that the annual fair rental value of the Refunding Property after a Substitution or Removal, in each year during the remaining term of the Refunding Sublease, is at least equal to the maximum annual Base Rental Payments payable under the Refunding Sublease attributable to the Refunding Property prior to said Substitution or Removal, as determined by the County on the basis of an appraisal of the Refunding Property after said Substitution or Removal conducted by a member of the Appraisal Institute of America (MAI) designated by the County; (B) demonstrating that the useful life of the Refunding Property after Substitution or Removal equals or exceeds the remaining term of the Refunding Sublease; and (C) stating that the Refunding Property after a Substitution or Removal is as essential to the operations of the County as was the Refunding Property immediately prior to such Substitution or Removal;

(3) An Opinion of Counsel to the effect that the amendments to the Refunding Sublease and to the Refunding Lease contemplating Substitution or Removal have been duly authorized, executed and delivered and constitute the valid and binding obligations of the County and the Corporation enforceable in accordance with their terms;

(4) (A) In the event of a Substitution, a policy of title insurance in an amount equal to the principal portion of the then-remaining Base Rental Payments payable under the Refunding Sublease multiplied by a fraction, the numerator of which is that portion of the principal portion of the then-remaining Base Rental Payments payable under the Refunding Sublease attributable to the Substituted Property and the denominator of which is the principal portion of the then-remaining Base Rental Payments payable under the Refunding Sublease, insuring the County's leasehold interest in the Substituted Property (except any portion thereof which is not real property) subject only to Permitted Encumbrances, together with an endorsement thereto making said policy payable to the Trustee for the benefit of the Owners of the Certificates and any Additional Certificates, and (B) in the event of a partial Removal, evidence that the title insurance in effect immediately prior thereto is not affected;

(5) In the event of a Substitution, an opinion of the County Counsel of the County to the effect that the exceptions, if any, contained in the title insurance policy referred to in (4) above do not interfere with the beneficial use and occupancy of the Substituted Property described in such policy by the County for the purposes of leasing or using the Substituted Property;

(6) An Opinion of Counsel that the Substitution or Removal does not cause the interest with respect to the Certificates and any Additional Certificates to be includable in gross income of the Owners thereof for federal income tax purposes;

(7) Evidence that the County has complied with the covenants contained in the Refunding Sublease regarding insurance requirements with respect to the Substituted Property; and

(8) Evidence that the Substitution or Removal, in and of itself, has not or will not cause a downgrade or withdrawal of the then existing credit ratings on the Certificates and any Additional Certificates.

Term of the Sublease

Commencement of the Sublease. The effective date of the Refunding Sublease is February 2, 2005, and the term of the Refunding Sublease shall end on the Expiry Date, unless such term is extended or sooner terminated as provided in the Refunding Sublease. If on the Expiry Date, the rental payable under the Refunding Sublease shall not be fully paid and all Certificates and Additional Certificates shall not be fully paid and retired, or if the rental payable under the Refunding Sublease shall have been abated at any time and for any reason, then the term of the Refunding Sublease shall be extended until ten days after the rental payable under the Refunding Sublease shall be fully paid and all Certificates and Additional Certificates shall be fully paid, except that the term of the Refunding Sublease shall in no event be extended beyond February 1, 2024. If prior to the Expiry Date, the rental payable under the Refunding Sublease shall be fully paid and all Certificates and Additional Certificates shall have been fully paid, or deemed fully paid, in accordance with the Trust Agreement, the term of the Refunding Sublease shall end ten days thereafter or ten days after written notice by the County to the Corporation to the effect that the rental payable under the Refunding Sublease shall be fully paid and all Certificates and Additional Certificates have been fully paid, whichever is earlier, and the Refunding Sublease shall thereupon terminate.

Use of Proceeds; Tax Covenants

Use of Proceeds. The parties to the Refunding Sublease agree that the proceeds of the Certificates will be used to refund and defease the Prior Obligations, to pay Construction Costs with respect to the Project, and to pay the costs of executing and delivering the Certificates and incidental and related expenses.

Tax Covenants.

(a) The County will not take any action, or fail to take any action, if such action or failure to take such action would adversely affect the exclusion from gross income of the interest evidenced and represented by the Certificates and any Additional Certificates pursuant to Section 103 of the Code, and specifically the County will not directly or indirectly use or make any use of the proceeds of the Certificates and any Additional Certificates or any other funds of the County or take or omit to take any action that would cause the Certificates or any Additional Certificates to be "arbitrage bonds" subject to federal income taxation by reason of Section 148 of the Code or "private activity bonds" subject to federal income taxation by reason of Section 141(a) of the Code or obligations subject to federal income taxation because they are "federally guaranteed" as provided in Section 149(b) of the Code; and to that end the County, with respect to the proceeds of the Certificates and any Additional Certificates and such other funds, will comply with all requirements of such sections of the Code to the extent that such requirements are, at the time, applicable and in effect; *provided,* that if the County shall obtain an Opinion of Counsel to the effect that any action required under this section is no longer required, or to the effect that some further action is required, to maintain the exclusion from gross income of the interest evidenced and represented by the Certificates and any Additional Certificates pursuant to Section 103 of the Code, the County may rely conclusively on such opinion in complying with the provisions of the Refunding

Sublease. In the event that at any time the County is of the opinion that for purposes of this section it is necessary to restrict or limit the yield on the investment of any moneys held by the Trustee under the Trust Agreement or otherwise the County shall so instruct the Trustee in writing, and the Trustee shall take such action in accordance with such instructions.

(b) To the ends covenanted in this section, the County specifically agrees to ensure that the following requirements are met:

(1) The County will not invest or allow to be invested proceeds of the Certificates or any Additional Certificates at a yield in excess of the yield on the Certificates and such Additional Certificates, except to the extent allowed under the Tax Certificate.

(2) The County will rebate or cause to be rebated any amounts due to the federal government, as provided in the Tax Certificate.

Rental Payments

Rental Payments. The County agrees to pay to the Corporation, its successors or assigns, without deduction or offset of any kind, as rental for the use and occupancy of the Refunding Property, the following amounts at the following times:

(a) *Base Rental*. The County shall pay to the Corporation rental under the Refunding Sublease as Base Rental Payments with respect to the Refunding Property at the times and in the amounts set forth in the Base Rental Payment Schedules attached to the Refunding Sublease and made a part thereof, a portion of which Base Rental Payments shall constitute interest. Base Rental Payments specified in the Refunding Sublease shall be payable solely and exclusively from amounts deposited in the escrow fund established under the Prior Escrow Agreement. Notwithstanding the dates designated for the payment of the Base Rental Payments under the Refunding Sublease, all Base Rental Payments due in any Fiscal Year shall be due and payable in one sum on July 5 of each year (or the next Business Day if July 5 does not fall on a Business Day), commencing on July 5, 2005. Failure of the County to comply with the provisions of this section shall constitute an event of default under the Refunding Sublease. The interest components of the Base Rental Payments shall be paid by the County as and constitute interest paid on the principal components of the Base Rental Payments to be paid by the County under the Refunding Sublease. The obligation to make the Base Rental Payments under the Refunding Sublease commenced as of May 31, 1996. Notwithstanding the foregoing, each Base Rental Payment shall be paid by wire transfer to the Corporation or its assignee not later than one Business Day preceding its due date.

(b) *Additional Rental*. The County shall also pay, as rental under the Refunding Sublease in addition to the Base Rental Payments, to the Corporation or the Trustee, as provided in the Refunding Sublease, such amounts ("Additional Rental") in each year as shall be required for the payment of all costs and expenses incurred by the Corporation in connection with the execution, performance or enforcement of the Refunding Sublease or the assignment of the Refunding Sublease, the Trust Agreement or the respective interests in the Refunding Property and the lease of the Refunding Property by the Corporation to the County under the Refunding Sublease, including but not limited to all fees, costs and expenses and all administrative costs of the Corporation relating to the Refunding Property including, without limiting the generality of the foregoing, salaries and wages of employees, overhead, insurance premiums, taxes and assessments (if any), expenses, compensation and indemnification of the Trustee (to the extent not paid or otherwise provided for out of the proceeds of the sale of the Certificates or any

Additional Certificates), fees of auditors, accountants, attorneys or engineers, insurance premiums, and all other reasonable and necessary administrative costs of the Corporation or charges required to be paid by it to comply with the terms of the Certificates, any Additional Certificates or the Trust Agreement.

The foregoing Additional Rental shall be billed to the County by the Corporation or the Trustee from time to time, together with a statement certifying that the amount billed has been incurred or paid by the Corporation, the Trustee or the Trustee on behalf of the Corporation for one or more of the items above described, or that such amount is then so payable for such items. Amounts so billed shall be paid by the County not later than the latest time as such amounts may be paid without penalty or, if no penalty is associated with a late payment of such amounts, within 30 days after receipt of a bill by the County for such amounts.

The Corporation may enter into leases to finance facilities other than the Refunding Property. The administrative costs of the Corporation shall be allocated among said facilities and the Refunding Property, as hereinafter in this paragraph provided. Any taxes levied against the Corporation with respect to the Refunding Property, the fees of the Trustee, and any other expenses directly attributable to the Refunding Property shall be included in the Additional Rental payable under the Refunding Sublease. Any taxes levied against the Corporation with respect to real property other than the Refunding Property, the fees of any trustee or paying agent under any resolution securing bonds of the Corporation or any trust agreement other than the Trust Agreement, and any other expenses directly attributable to any facilities other than the Refunding Property shall not be included in the administrative costs of the Refunding Property and shall not be paid from the Additional Rental payable under the Refunding Sublease. Any expenses of the Corporation not directly attributable to any particular project of the Corporation shall be equitably allocated among all such projects, including the Refunding Property, in accordance with sound accounting practice. In the event of any question or dispute as to such allocation, the written opinion of an independent firm of certified public accountants, employed by the Corporation to consider the question and render an opinion thereon, shall be final and conclusive determination as to such allocation. The Trustee may conclusively rely upon a Certificate of the Corporation in making any determination that costs are payable as Additional Rental under the Refunding Sublease, and shall not be required to make any investigation as to whether or not the items so requested to be paid are expenses of operation of the Refunding Property.

(c) *Consideration.*

(i) Such payments of Base Rental Payments and Additional Rental for each Lease Year or portion thereof during the term of the Refunding Sublease shall constitute the total rental for such Lease Year or portion thereof and shall be paid or payable by the County for and in consideration of the right of the use and possession of, and the continued quiet use and enjoyment of, the Refunding Property. The parties to the Refunding Sublease have agreed and determined that the annual fair rental value of the Refunding Property is not less than the maximum Base Rental Payments payable under the Refunding Sublease in any year. In making such determinations of annual fair rental value, consideration has been given to a variety of factors including the replacement costs of the existing improvements on the Refunding Property, other obligations of the parties under the Refunding Sublease, the uses and purposes which may be served by the improvements on the Refunding Property and the benefits therefrom which will accrue to the County and the general public.

(ii) The parties to the Refunding Sublease acknowledge that the parties to the Refunding Sublease may amend the Refunding Sublease from time to time to increase the Base Rental Payments payable under the Refunding Sublease so that Additional Certificates may be executed and delivered pursuant to the Refunding Sublease and the Trust Agreement. The proceeds of such Additional Certificates shall be used for any lawful purpose. Notwithstanding anything to the contrary contained in the Refunding Sublease, the Refunding Sublease may not be amended in a manner such that the sum of Base Rental Payments, including Base Rental Payments payable pursuant to such amendment, and Additional Rental with respect to the prorated portion of Outstanding Certificates and Additional Certificates secured by the Refunding Property in any year is in excess of the annual fair rental value of the Refunding Property and other land and improvements leased to the County under the Refunding Sublease.

(d) *Payment*; *Credit*. Each installment of Base Rental Payments payable under the Refunding Sublease shall be paid in lawful money of the United States of America to or upon the order of the Corporation at the principal corporate trust office of the Trustee in Los Angeles, California, or such other place as the Corporation shall designate. Any such installment of rental accruing under the Refunding Sublease which shall not be paid when due shall remain due and payable until received by the Trustee, except as provided in the Refunding Sublease, and to the extent permitted by law shall bear interest at the rate of ten percent per annum from the date when the same is due under the Refunding Sublease until the same shall be paid. Notwithstanding any dispute between the County and the Corporation, the County shall make all rental payments when due, without deduction or offset of any kind, and shall not withhold any rental payments pending the final resolution of any such dispute. In the event of a determination that the County was not liable for said rental payments or any portion thereof, said payments or excess of payments, as the case may be, shall, at the option of the County, be credited against subsequent rental payments due under the Refunding Sublease or be refunded at the time of such determination. Amounts required to be deposited by the County with the Trustee pursuant to this paragraph on any date shall be reduced to the extent of available amounts on deposit on such date in the Base Rental Payment Fund, the Interest Fund or the Principal Fund.

Annual Budgets; Reporting Requirements. The County covenants to take such action as may be necessary to include all Base Rental Payments and Additional Rental payments due under the Refunding Sublease in its operating budget for each fiscal year commencing after the date of the Refunding Sublease (an "Operating Budget") and to make all necessary appropriations for such Base Rental Payments and Additional Rental payments.

Application of Rental Payments. All Base Rental Payments received shall be applied first to the interest components of the Base Rental Payments due under the Refunding Sublease, then to the principal components (including any prepayment premium components) of the Base Rental Payments due under the Refunding Sublease and thereafter to all Additional Rental due under the Refunding Sublease, but no such application of any payments which are less than the total rental due and owing shall be deemed a waiver of any default under the Refunding Sublease.

Rental Abatement. Except to the extent of (a) amounts held by the Trustee in the Base Rental Payment Fund or in the Certificate Reserve Fund, (b) amounts received in respect of rental interruption insurance, and (c) amounts, if any, otherwise legally available to the Trustee for payments in respect of the Certificates, during any period in which, by reason of material damage, destruction, title defect, condemnation, there is substantial interference with the use and possession by the County of any portion of the Refunding Property, rental payments due under the Refunding Sublease with respect to the Refunding Property shall be abated to the extent that the annual fair rental value of the portion of the

Refunding Property in respect of which there is no substantial interference is less than the annual Base Rental Payments and Additional Rental, in which case rental payments shall be abated only by an amount equal to the difference. In the event the County shall assign, transfer or sublease any or all of the Refunding Property or other rights under the Refunding Sublease, as permitted by the Refunding Sublease, for purposes of determining the annual fair rental value available to pay Base Rental Payments and Additional Rental, annual fair rental value of the Refunding Property shall first be allocated to the Refunding Sublease as provided in the Refunding Sublease. Any abatement of rental payments pursuant to the Refunding Sublease shall not be considered an Event of Default as defined in the Refunding Sublease. The County waives the benefits of Civil Code Sections 1932(2) and 1933(4) and any and all other rights to terminate the Refunding Sublease by virtue of any such interference and the Refunding Sublease shall continue in full force and effect. Such abatement shall continue for the period commencing with the date of such damage, destruction, title defect or condemnation and ending with the substantial completion of the work of repair or replacement of the portions of the Refunding Property so damaged, destroyed, defective or condemned.

In the event that rental is abated, in whole or in part, pursuant to the Refunding Sublease due to damage, destruction, title defect or condemnation of any part of the Refunding Property and the County is unable to repair, replace or rebuild the Refunding Property from the proceeds of insurance, if any, the County agrees to apply for and to use its best efforts to obtain any appropriate state and/or federal disaster relief in order to obtain funds to repair, replace or rebuild the Refunding Property.

Prepayment of Rental Payments. The County may prepay, from eminent domain proceeds or net insurance proceeds received by it pursuant to the Refunding Sublease, all or any portion of the components of Base Rental Payments payable under the Refunding Sublease relating to any portion of the Refunding Property then unpaid, in whole on any date, or in part on any date in integral multiples of an Authorized Denomination so that the aggregate annual amounts of principal components of Base Rental Payments payable under the Refunding Sublease and the Refunding Sublease represented by the Certificates and any Additional Certificates which shall be payable after such prepayment date shall each be in an integral multiple of an Authorized Denomination and shall be as nearly proportional as practicable to the aggregate annual amounts of principal components of Base Rental Payments payable under the Refunding Sublease and the Project Sublease represented by the Certificates and any Additional Certificates.

The County may prepay, from any source of available moneys pursuant to the Trust Agreement, all or any part (in an integral multiple of an Authorized Denomination) of the principal components of Base Rental Payments payable under the Refunding Sublease and the Project Sublease then unpaid so that the aggregate annual amounts of principal components of Base Rental Payments under the Refunding Sublease and the Project Sublease which shall be payable after such prepayment date shall be as nearly proportional as practicable to the aggregate annual amounts of principal components represented by the Certificates and any Additional Certificates unpaid prior to the prepayment date, at a prepayment amount equal to the principal component prepaid plus accrued interest thereon to the date of prepayment plus any applicable premium.

Before making any prepayment pursuant to this Section, at least 45 days before the prepayment date the County shall give written notice to the Corporation and the Trustee describing such event, specifying the order of Principal Payment Dates and specifying the date on which the prepayment will be made, which date shall be not less than 30 nor more than 60 days from the date such written notice is given to the Corporation and the Trustee.

Obligation to Make Rental Payments. The agreements and covenants on the part of the County contained in the Refunding Sublease shall be deemed to be and shall be construed to be duties imposed by

law and it shall be the duty of each and every public official of the County to take such action and do such things as are required by law in the performance of the official duty of such officials to enable the County to carry out and perform the agreements and covenants contained in the Refunding Sublease agreed to be carried out and performed by the County.

THE OBLIGATION OF THE COUNTY TO MAKE BASE RENTAL PAYMENTS AND TO PAY ADDITIONAL RENT DOES NOT CONSTITUTE AN OBLIGATION OF THE COUNTY FOR WHICH THE COUNTY IS OBLIGATED TO LEVY OR PLEDGE ANY FORM OF TAXATION OR FOR WHICH THE COUNTY HAS LEVIED OR PLEDGED ANY FORM OF TAXATION. NEITHER THE CERTIFICATES NOR THE OBLIGATION TO MAKE RENTAL PAYMENTS AND TO PAY ADDITIONAL RENT CONSTITUTES AN INDEBTEDNESS OF THE COUNTY, THE STATE OF CALIFORNIA OR ANY POLITICAL SUBDIVISION THEREOF WITHIN THE MEANING OF ANY CONSTITUTIONAL OR STATUTORY DEBT LIMITATION OR RESTRICTION.

Additional Certificates. In addition to the Certificates to be executed and delivered under the Trust Agreement the County may, from time to time, but only upon satisfaction of the conditions to the execution and delivery of Additional Certificates set forth in the Trust Agreement, enter into a Supplemental Trust Agreement to execute and deliver Additional Certificates on a parity with the Certificates and any previously executed and delivered Additional Certificates (unless otherwise provided in the related Supplemental Trust Agreement), the proceeds of which may be used for any lawful purpose by the County, as provided in the Supplemental Trust Agreement; provided that prior to or concurrently with the execution and delivery of the Additional Certificates, the County and the Corporation shall have entered into an amendment to the Refunding Sublease, providing for an increase in the Base Rental Payments to be made under the Refunding Sublease subject to the limitations set forth in Refunding Sublease.

Maintenance; Taxes; Insurance and other Charges

Maintenance of the Refunding Property by the County. The County agrees that, at all times during the term of the Refunding Sublease, it will, at its own cost and expense, maintain, preserve and keep the Refunding Property and every portion thereof in good repair, working order and condition and that it will from time to time make or cause to be made all necessary and proper repairs, replacements and renewals. The Corporation shall have no responsibility in any of these matters or for the making of additions or improvements to the Refunding Property.

Taxes, Other Governmental Charges and Utility Charges. The parties to the Refunding Sublease contemplate that the Refunding Property will be used for public purposes by the County and, therefore, that the Refunding Property will be exempt from all taxes presently assessed and levied with respect to real and personal property, respectively. In the event that the use, possession or acquisition by the County or the Corporation of the Refunding Property is found to be subject to taxation in any form, the County will pay during the term of the Refunding Sublease, as the same respectively become due, all taxes and governmental charges of any kind whatsoever that may at any time be lawfully assessed or levied against or with respect to the Refunding Property and any other property acquired by the County in substitution for, as a renewal or replacement of, or a modification, improvement or addition to, the Refunding Property, as well as all gas, water, steam, electricity, heat, power, air conditioning, telephone, utility and other charges incurred in the operation, maintenance, use, occupancy and upkeep of the Refunding Property; *provided,* that with respect to any governmental charges or taxes that may lawfully be paid in installments over a period of years, the County shall be obligated to pay only such installments as are accrued during such time as the Refunding Sublease is in effect.

Insurance. The County shall secure and maintain or cause to be secured and maintained at all time with insurers of recognized responsibility, all coverage on the Refunding Property required by the Refunding Sublease. Such insurance shall consist of :

(1) A policy or policies of insurance against loss or damage to the Refunding Property known as "all risk," including flood, but excluding earthquake, which shall be maintained at any time in an amount per occurrence at least equal to the lesser of (i) the cumulative replacement values of the Refunding Property and, in the case of a policy covering more than the Refunding Property, as permitted by the next succeeding sentence, any other property which is the subject of a lease, installment purchase agreement or other financing arrangement for which bonds, certificates of participation or other obligations shall have been issued ("Obligations") or (ii) the aggregate amount of the principal component of all then-remaining Base Rental Payments payable under the Refunding Sublease; *provided*, that with the consent of the Insurer, the amount of coverage required by this sentence may be reduced to a smaller amount if an insurance consultant or insurance broker retained by the County provides written advice to the Trustee that, based upon its evaluation of the County's maximum foreseeable loss in the event of a major conflagration, windstorm, explosion, riot, flood or similar event, a specified smaller amount is believed to be reasonable given the nature of the risks insured and the proximity of the insured properties to each other. Such insurance may be in the form of a policy which covers the Refunding Property and one or more additional parcels of real property leased or owned by the County which may be limited in an amount per occurrence in the aggregate to the amount required by the preceding sentence. Such insurance may at any time include a deductible clause providing for a deductible not to exceed $100,000 for any one loss (except for flood, in which case the deductible may not exceed $250,000 for any one loss). The County may obtain such coverage as a joint insured with one or more other public agencies located within or without the County of San Diego which may be limited in an amount per occurrence in the aggregate for all insureds as described in the first sentence of this paragraph (1) and which may be limited in a cumulative amount of claims during a 12-month period in the aggregate for all insureds in an amount not less than $500,000,000. Otherwise conforming policies satisfying the requirements of this paragraph (1) may provide that amounts payable as coverage under this paragraph (1) may be reduced by amounts payable under paragraph (3) for the same occurrence, and vice versa. The County is, however, under no obligation to provide insurance against loss or damage occasioned by the perils of earthquake.

(2) In the event that such coverage is not included in paragraph (1) above, boiler and machinery coverage against loss or damage by explosion of steam boilers, pressure vessels and similar apparatus now or hereafter installed on the Refunding Property in an amount not less than $75,000,000 per accident; *provided, however,* that the amount of coverage required by this sentence may be reduced to a smaller amount if an insurance consultant or insurance broker retained by the County provides written advice to the Trustee that, based upon its evaluation of the County's maximum foreseeable loss in the event of loss or damage by steam boilers, pressure vessels and similar apparatus now or hereafter installed on the Refunding Property, a specified smaller amount is believed to be reasonable. Such insurance may be in the form of a policy which covers the Refunding Property and one or more additional parcels of real property leased or owned by the County which may be limited in amount to $75,000,000 per accident. Such insurance may at any time include a deductible clause providing for a deductible not to exceed $100,000 for any one loss. The County may obtain such coverage as a joint insured with one or more public agencies located within or without the County of San Diego which may be limited in amount to $75,000,000 per accident. Otherwise conforming policies satisfying the requirements of this paragraph (2) may provide that amounts payable as coverage under this paragraph (2) may be reduced by amounts payable under paragraph (3) for the same occurrence, and *vice versa*.

(3) Rental interruption insurance to cover loss, total or partial, of the use of any part of the Refunding Property as a result of any of the hazards covered by the insurance required pursuant to paragraph (1) or (2) above, as the case may be, in an amount sufficient at all times to pay the total rent payable under the Refunding Sublease for a period of not less than two years' Base Rental Payments for the Refunding Property; provided that such rental interruption insurance may be included in the policy or policies provided pursuant to paragraph (1) or (2) without increasing the aggregate limits for coverage with respect to any hazard covered thereby. Such insurance also may be in the form of a policy which covers the Refunding Property and one or more additional parcels of real property leased or owned by the County. The County also may obtain an otherwise conforming policy required by this paragraph (3) as a joint insured with one or more other public agencies within or without the County of San Diego which may, with respect to any hazard, be limited in aggregate amount for all insureds to the amount of the policy or policies required pursuant to paragraph (1) or (2) above, as the case may be, which insures against such hazard. Otherwise conforming policies satisfying the requirements of this paragraph (3) may provide that amounts payable as coverage under this paragraph (3) may be reduced by amounts payable under paragraph (1) or (2), as the case may be, for the same occurrence, and *vice versa*.

The County shall collect, adjust and receive all moneys which may become due and payable under any policies contemplated by paragraphs (1) and (2) above, and, may compromise any and all claims thereunder and shall transfer the net proceeds of such insurance as provided in the Refunding Sublease or in the Trust Agreement. The Trustee shall not be responsible for the sufficiency of any insurance required in the Refunding Sublease. The Trustee shall be fully protected in accepting payment on account of such insurance or any adjustment, compromise or settlement of any loss agreed to by the County.

Any insurance policy issued pursuant to paragraph (1) or (2) above shall be so written or endorsed as to make losses, if any, payable to the County, the Corporation and the Trustee as their respective interests may appear and the net proceeds of the insurance required by paragraphs (1) or (2) above shall be applied as provided in the Refunding Sublease. The net proceeds, if any, of the insurance policy described in paragraphs (1) and (2) above shall be payable to the County for deposit in the Insurance Proceeds and Condemnation Awards Fund. The net proceeds, if any, of the insurance policy described in paragraph (3) above shall be payable to the Trustee and deposited in the Base Rental Payment Fund. Each insurance policy provided for in Refunding Sublease shall contain a provision to the effect that the insurance company shall not cancel the policy or modify it materially and adversely to the interests of the Corporation or the Trustee without first giving written notice thereof to the Corporation and the Trustee at least 30 days in advance of such intended cancellation or modification.

The County shall file a Certificate of the County with the Trustee not later than January 31 of each year certifying that the insurance policies required by the Refunding Sublease are in full force and effect and that the Corporation and/or the Trustee is named as a loss payee on each insurance policy which the Refunding Sublease requires to be so endorsed. The Trustee shall have no responsibility whatsoever for determining the adequacy of any insurance required under the Refunding Sublease.

Advances. In the event the County shall fail to maintain the full insurance coverage required by the Refunding Sublease or shall fail to keep the Refunding Property in good repair and operating condition, the Corporation may (but shall be under no obligation to) purchase the required policies of insurance and pay the premiums on the same or may make such repairs or replacements as are necessary and provide for payment thereof; and all amounts so advanced therefor by the Corporation shall become Additional Rental, which amounts the County agrees to pay within 30 days of a written request therefor, together with interest thereon at the maximum rate allowed by law.

Title Insurance. The County covenants and agrees to deliver or cause to be delivered to the Trustee a CLTA leasehold owner's policy or policies, or a commitment for such policy or policies, with respect to the Refunding Property with liability in the aggregate amount of the principal component of all Base Rental Payments payable under the Refunding Sublease. Such policy or policies, when issued, shall name the Trustee as the insured and shall insure the leasehold estate of the County in the Refunding Property subject only to such exceptions as do not materially affect the County's right to the use and occupancy of the Refunding Property.

Damage, Destruction, Title Defect and Condemnation

Damage, Destruction, Title Defect and Condemnation; Use of Net Proceeds. If prior to the termination of the term of the Refunding Sublease (a) the Refunding Property or any portion thereof is destroyed (in whole or in part) or is damaged by fire or other casualty; or (b) title to, or the temporary use of, the Refunding Property or any portion thereof or the estate of the County or the Corporation in the Refunding Property or any portion thereof is defective or shall be taken under the exercise of the power of eminent domain by any governmental body or by any person or firm or corporation acting under governmental authority, then the County and the Corporation will cause the net proceeds of any insurance claim or condemnation award to be applied to the prompt repair, restoration, modification, improvement or replacement of the damaged, destroyed, defective or condemned portion of the Refunding Property, and any balance of the net proceeds remaining after such work has been completed shall be paid to the County; *provided,* that the County, at its option and provided the proceeds of such insurance or condemnation award together with any other moneys then available for the purpose are at least sufficient to prepay the aggregate annual amounts of the principal and interest components of the Base Rental Payments due under the Refunding Sublease attributable to the portion of the Refunding Property so destroyed, damaged, defective or condemned (determined by reference to the proportion which the annual fair rental value of the destroyed, damaged, defective or condemned portion thereof bears to the annual fair rental value of the Refunding Property), may elect not to repair, reconstruct or replace the damaged, destroyed, defective or condemned portion of the Refunding Property and thereupon shall cause said proceeds to be used for the prepayment of Outstanding Certificates and Additional Certificates pursuant to the provisions of the Trust Agreement. Notwithstanding any other provision in the Refunding Sublease, the County shall only prepay less than all of the principal component of the then-remaining Base Rental Payments if the annual fair rental value of the Leased Refunding Property after such damage, destruction, title defect or condemnation is at least equal to the aggregate annual amount of the principal and interest components of the Base Rental Payments not being prepaid.

In the event that the proceeds, if any, of said insurance or condemnation award are insufficient either to (i) repair, rebuild or replace the Refunding Property so that the fair rental value of the Refunding Property would be at least equal to the Base Rental Payments or (ii) to prepay all the Outstanding Certificates and Additional Certificates, both as provided in the preceding paragraph, then the County may, in its sole discretion, budget and appropriate an amount necessary, but in no event more than the net proceeds available from any insurance claim or condemnation award described in the Refunding Sublease, to effect such repair, rebuilding or replacement or prepayment; provided that the failure of the County to so budget and/or appropriate shall not be a breach of or default under the Refunding Sublease.

Disclaimer of Warranties; Vendor's Warranties; Use of the Refunding Property

Disclaimer of Warranties. NEITHER THE TRUSTEE NOR THE CORPORATION MAKES ANY AGREEMENT, WARRANTY OR REPRESENTATION, EITHER EXPRESS OR IMPLIED, AS TO THE VALUE, DESIGN, CONDITION, MERCHANTABILITY OR FITNESS FOR PARTICULAR PURPOSE OR FITNESS FOR USE OF THE REFUNDING PROPERTY, OR WARRANTY WITH RESPECT THERETO. THE COUNTY ACKNOWLEDGES THAT NEITHER THE TRUSTEE NOR

THE CORPORATION IS A MANUFACTURER OF ANY PORTION OF THE REFUNDING PROPERTY OR A DEALER THEREIN, THAT THE COUNTY LEASES THE REFUNDING PROPERTY AS-IS, IT BEING AGREED THAT ALL OF THE AFOREMENTIONED RISKS ARE TO BE BORNE BY THE COUNTY. In no event shall the Corporation or the Trustee be liable for any incidental, indirect, special or consequential damage in connection with or arising out of the Refunding Sublease or the existence, furnishing, functioning or the County's use of the Refunding Property as provided by the Refunding Sublease.

Use of the Refunding Property; Improvements. The County will not use, operate or maintain the Refunding Property improperly, carelessly, in violation of any applicable law or in a manner contrary to that contemplated by the Refunding Sublease. The County shall provide all permits and licenses, if any, necessary for the use of the Refunding Property. In addition, the County agrees to comply in all respects (including, without limitation, with respect to the use, maintenance and operation of each portion of the Refunding Property) with all laws of the jurisdictions in which its operations involving any portion of the Refunding Property may extend and any legislative, executive, administrative or judicial body exercising any power or jurisdiction over the Refunding Property; *provided,* that the County may contest in good faith the validity or application of any such law or rule in any reasonable manner which does not, in the opinion of the County adversely affect the estate of the Corporation in and to the Refunding Property or its interest or rights under the Refunding Sublease.

Assignment and Indemnification

Assignment by Corporation. The parties understand that certain of the rights of the Corporation under the Refunding Sublease and under the Refunding Lease will be assigned to the Trustee pursuant to the Assignment Agreement, and accordingly the County agrees to make all payments due under the Refunding Sublease to the Trustee, notwithstanding any claim, defense, setoff or counterclaim whatsoever (whether arising from a breach of the Refunding Sublease or otherwise) that the County may from time to time have against the Corporation. The County agrees to execute all documents, including notices of assignment and chattel mortgages or financing statements, which may be reasonably requested by the Corporation or the Trustee to protect their interests in the Refunding Property during the term of the Refunding Sublease.

Assignment by County. The Refunding Sublease and the interest of the County in the Refunding Property may not be assigned or encumbered by the County except as permitted by the Refunding Sublease.

Indemnification. The County shall, to the full extent then permitted by law, indemnify, protect, hold harmless, save and keep harmless the Corporation and the Trustee and their respective directors, officers and employees from and against any and all liability, obligations, losses, claims and damages whatsoever, regardless of the cause thereof, and expenses in connection therewith, including, without limitation, counsel fees and expenses, penalties and interest arising out of or as the result of the entering into of the Refunding Sublease, the acquisition, construction, installation and use of the Refunding Property and each portion thereof or any accident in connection with the operation, use, condition or possession of the Refunding Property or any portion thereof resulting in damage to property or injury to or death to any person including, without limitation, any claim alleging latent and other defects, whether or not discoverable by the County or the Corporation; any claim arising out of the use, presence, storage, disposal or release of any Hazardous Substances on or about the Refunding Property; any claim for patent, trademark or copyright infringement; and any claim arising out of strict liability in tort. The indemnification arising under the Refunding Sublease shall continue in full force and effect notwithstanding the full payment of all obligations under the Refunding Sublease or the termination of the Refunding Sublease for any reason. The County, the Trustee and the Corporation mutually agree to

promptly give notice to each other of any claim or liability indemnified against by the Refunding Sublease following the learning thereof by such party.

Default

The following events shall be "Events of Default" under the Refunding Sublease and the terms "Event of Default" and "Default" shall mean, whenever they are used in the Refunding Sublease, any one or more of the following events:

(1) The County shall fail to deposit with the Trustee any Base Rental Payment required to be so deposited by the close of business on the day such deposit is required pursuant to the Refunding Sublease, provided, that the failure to deposit any Base Rental Payments abated pursuant to the Refunding Sublease shall not constitute an Event of Default;

(2) The County shall fail to pay any item of Additional Rental when the same shall become due and payable pursuant to the Refunding Sublease; or

(3) The County shall breach any other terms, covenants or conditions contained in the Refunding Sublease or in the Trust Agreement, and shall fail to remedy any such breach with all reasonable dispatch within a period of 30 days after written notice thereof from the Corporation to the County; *provided, however,* that if the failure stated in the notice cannot be corrected within such period, then the Corporation shall not unreasonably withhold its consent to an extension of such time if corrective action is instituted by the County within such period and is diligently pursued until the default is corrected.

Upon the happening of any of the Events of Default specified in the Refunding Sublease, it shall be lawful for the Corporation or its assignee, subject to the terms of the Refunding Sublease, and to the direction and control of the Insurer, so long as the Insurer is not in default under the Municipal Bond Insurance Policy, to exercise any and all remedies available or granted to it pursuant to law or under the Refunding Sublease.

Upon the occurrence of an Event of Default, the Corporation or its assignee must thereafter maintain the Refunding Sublease in full force and effect and may only recover rent and other monetary charges as they become due, all without terminating the County's right to possession of the Refunding Property, regardless of whether or not the County has abandoned the Refunding Property; **THIS SHALL BE THE SOLE AND EXCLUSIVE REMEDY AVAILABLE AGAINST THE COUNTY UNDER THIS SUBLEASE OR OTHERWISE**. In such event, the County shall remain liable and agrees to keep or perform all covenants and conditions in the Refunding Sublease contained to be kept or performed by the County and, to pay the rent to the end of the term of the Refunding Sublease and further agrees to pay said rent and/or rent deficiency punctually at the same time and in the same manner as provided in the Refunding Sublease for the payment of rent under the Refunding Sublease (without acceleration).

The Corporation expressly waives the right to receive any amount from the County pursuant to Section 1951.2(a)(3) of the California Civil Code.

In addition to any Event of Default resulting from breach by the County of any agreement, condition, covenant or term of the Refunding Sublease, if the County's interest in the Refunding Sublease or any part thereof assigned, sublet or transferred without the written consent of the Corporation (except as otherwise permitted by the Refunding Sublease), either voluntarily or by operation of law; or the County or any assignee shall file any petition or institute any proceedings under any act or acts, state or federal, dealing with or relating to the subject of bankruptcy or insolvency or under any amendment of

such act or acts, either as a bankrupt or as an insolvent or as a debtor or in any similar capacity, wherein or whereby the County asks or seeks or prays to be adjudicated a bankrupt, or is to be discharged from any or all of its debts or obligations, or offers to its creditors to effect a composition or extension of time to pay its debts, or asks, seeks or prays for a reorganization or to effect a plan of reorganization or for a readjustment of its debts or for any other similar relief, or if the County shall make a general or any assignment for the benefit of its creditors; or the County shall abandon or vacate the Refunding Property or any portion thereof (except as permitted by the Refunding Sublease); then in each and every such case the County shall be deemed to be in default under the Refunding Sublease.

Neither the County nor the Corporation shall be in default in the performance of any of its obligations under the Refunding Sublease (except for the obligation to make Base Rental Payments pursuant to the Refunding Sublease) unless and until it shall have failed to perform such obligation within 30 days after notice by the County of the Corporation, as the case may be, to the other party properly specifying wherein it has failed to perform such obligation.

The County and Corporation and its successors and assigns shall honor the exclusive rights of the County to use the Refunding Property.

Miscellaneous

Trustee as Third Party Beneficiary. The Trustee is designated a third party beneficiary under the Refunding Sublease for the purpose of enforcing any of the rights under the Refunding Sublease assigned to the Trustee under the Assignment Agreement.

Net Lease. It is the purpose and intent of the Corporation and the County that lease payments under the Refunding Sublease shall be absolutely net to the Corporation so that the Refunding Sublease shall yield to the Corporation the lease payments, free of any charges, assessments or impositions of any kind charged, assessed or imposed on or against the Refunding Property, and without counterclaim, deduction, defense, deferment or set-off by the County except as specifically otherwise provided in the Refunding Sublease. The Corporation shall not be expected or required to pay any such charge, assessment or imposition, or be under any obligation or liability under the Refunding Sublease except as expressly set forth in the Refunding Sublease, and all costs, expenses and obligations of any kind relating to the maintenance and operation of the Refunding Property which may arise or become due during the term of the Refunding Sublease shall be paid by the County.

Amendments. The Refunding Sublease may be amended in writing as may be mutually agreed by the Corporation and the County, subject to the written approval of the Trustee; *provided,* that no such amendment which materially adversely affects the rights of the Owners shall be effective unless it shall have been consented to by the Owners of more than 50% in principal amount of the Certificates and Additional Certificates Outstanding, and provided further, that no such amendment shall (a) extend the payment date of any Base Rental Payment, or reduce the interest, principal or prepayment premium component of any Base Rental Payment, without the prior written consent of the Owner of each Certificate and Additional Certificate so affected, or (b) reduce the percentage of the principal amount of the Certificates and Additional Certificates Outstanding the consent of the Owners of which is required for the execution of any amendment of the Refunding Sublease.

The Refunding Sublease and the rights and obligations of the Corporation and the County under the Refunding Sublease may also be amended or supplemented at any time by an amendment of the Refunding Sublease or supplement to the Trust Agreement which shall become binding upon execution without the written consents of any Owners, but only to the extent permitted by law and only for any one or more of the following purposes:

(a) to add to the agreements, conditions, covenants and terms required by the Corporation or the County to be observed or performed in the Refunding Sublease and other agreements, conditions, covenants and terms thereafter to be observed or performed by the Corporation or the County, or to surrender any right or power reserved in the Refunding Sublease to or conferred in the Refunding Sublease on the Corporation or the County, and which in either case shall not materially adversely affect the interests of the Owners;

(b) to make such provisions for the purpose of curing any ambiguity or of correcting, curing or supplementing any defective provision contained in the Refunding Sublease or in regard to questions arising under the Refunding Sublease which the Corporation or the County may deem desirable or necessary and not inconsistent with the Refunding Sublease, and which shall not materially adversely affect the interests of the Owners;

(c) to effect a Substitution or Removal in accordance with the Refunding Sublease;

(d) to facilitate the issuance of Additional Certificates as provided in the Refunding Sublease; or

(e) to make any other addition, amendment or deletion which does not materially adversely affect the interests of the Owners or the Insurer.

Discharge of County. Upon the payment of all Base Rental Payments and Additional Rental payable under the Refunding Sublease, all of the obligations of the County under the Refunding Sublease shall thereupon cease, terminate and become void and shall be discharged and satisfied; *provided, however,* if any Outstanding Certificates and Additional Certificates shall be deemed to have been paid by virtue of a deposit of Base Rental Payments under the Refunding Sublease pursuant to the Trust Agreement, then the obligation of the County under the Refunding Sublease to make Base Rental Payments under the Refunding Sublease shall continue in full force and effect until the Outstanding Certificates and Additional Certificates so deemed paid have in fact been paid, but such payments shall be made solely and exclusively from moneys and securities deposited with the Trustee as contemplated by the Trust Agreement, and that shall be the sole source of satisfaction of the County's obligation to make Base Rental Payments. The time period for giving notice by the County to the Corporation and the Trustee specified in the Refunding Sublease shall not apply incident to the payment to the Owners of all Outstanding Certificates and Additional Certificates in accordance with the Trust Agreement.

California Law. The Refunding Sublease shall be governed by and construed and interpreted in accordance with the laws of the State of California.

Insurer Deemed Owner. For the purpose of (i) the giving of consents to amendments to the Refunding Sublease, (ii) the giving of any other consent of the Owners under the Refunding Sublease, and (iii) the control and direction of all rights and remedies upon the occurrence of an Event of Default, the Insurer shall be deemed to be the sole Owner of the Certificates for so long as it has not failed to comply with its payment obligations under the Municipal Bond Insurance Policy; *provided*, *however*, that, notwithstanding the foregoing, the Insurer shall not be deemed to be the Owner of the Certificates for any consent to an amendment to the Refunding Sublease that (a) extends the payment date of any Base Rental Payment, or reduces the interest, principal or prepayment premium component of any Base Rental Payment, or (b) reduces the percentage of the principal amount of the Certificates and Additional Certificates Outstanding the consent of the Owners of which is required for the execution of any amendment of the Refunding Sublease.

REFUNDING LEASE

Refunding Property. The County leases to the Corporation and the Corporation rents and hires from the County, on the terms and conditions set forth in the Refunding Lease, the Refunding Property.

Term.

(a) The term of the Refunding Lease will commenced on February 2, 2005 and shall end on the Expiry Date (as defined in the Refunding Sublease) unless such term is sooner terminated or is extended as provided in the Refunding Lease. If prior to the Expiry Date all Base Rental Payments under the Refunding Sublease shall have been paid, or provision therefor has been made in accordance with the Trust Agreement, the term of the Refunding Lease shall end simultaneously therewith.

(b) If the Refunding Sublease is extended beyond the Expiry Date pursuant to the terms thereof, the Refunding Lease shall also be extended to the day following the date of termination of the Refunding Sublease.

Rent. The Corporation shall pay to the County an advance rent of $31,632,830.54, which, together with the execution and delivery of the Refunding Sublease, shall constitute full consideration for the Refunding Lease over its term. The Corporation waives any right that it may have under the laws of the State of California to receive a rebate of such rent in full or in part in the event there is a substantial interference with the use and right of possession by the Corporation of the Refunding Property or portion thereof as a result of material damage, destruction or condemnation.

Purpose. The Corporation shall use the Refunding Property solely for the purpose of subleasing the same to the County; *provided,* that in the event of default by the County under the Refunding Sublease, the Corporation may exercise the remedies provided in the Refunding Sublease.

Owner in Fee. The County covenants that it is the owner of the Refunding Property free and clear of all liens, claims or encumbrances which affect marketability.

Assignments and Project Subleases. Unless the County shall be in default under the Refunding Sublease, the Corporation may not, without the prior written consent of the County, assign its rights under the Refunding Lease or sublet the Refunding Property except that the County expressly approves and consents to the assignment and transfer of the Corporation's right, title and interest in the Refunding Lease to the Trustee pursuant to the Assignment Agreement.

Right of Entry. The County reserves the right for any of its duly authorized representatives to enter upon the Refunding Property at any reasonable time to inspect the same or to make any repairs, improvements or changes necessary for the preservation thereof.

Termination. The Corporation agrees, upon the termination of the Refunding Lease, to quit and surrender the Refunding Property in the same good order and condition as the same was in at the time of commencement of the terms under the Refunding Lease, reasonable wear and tear excepted, and agrees that any permanent improvements to the Refunding Property at the time of the termination of the Refunding Lease shall remain thereon and title thereto shall vest in the County.

Default. In the event the Corporation shall be in default in the performance of any obligation on its part to be performed under the terms of the Refunding Lease, which default continues for thirty (30) days following notice and demand for correction thereof to the Corporation, the County may exercise any and all remedies granted by law, except that no merger of the Refunding Lease and of the Refunding

Sublease shall be deemed to occur as a result thereof; *provided,* that so long as the Certificates executed and delivered pursuant to the Trust Agreement are Outstanding, the County shall have no power to terminate the Refunding Lease by reason of any default on the part of the Corporation, if such termination would affect or impair any assignment of the Refunding Sublease then in effect between the Corporation and the Trustee that executes and delivers the Certificates.

Eminent Domain. In the event the whole or any portion of the Refunding Property is taken by eminent domain proceedings, the interest of the Corporation shall be recognized and is determined to be the amount of the then unpaid Base Rental Payments payable under the Refunding Sublease, and the amount of the unpaid Additional Rental due under the Refunding Sublease, and the balance of the award, if any, shall be paid to the County.

Amendments. The Refunding Lease may be amended for the purpose of affecting a Substitution or Removal, as further described in the Refunding Sublease.

Governing Law. The Refunding Lease is made in the State of California under the Constitution and laws of the State of California and is to be so construed.

THE ASSIGNMENT AGREEMENT

Assignment. The Corporation, for good and valuable consideration, the receipt of which is acknowledged, does unconditionally grant, transfer and assign to the Trustee without recourse (a) all right, title and interest of the Corporation as lessee under the Leases; (b) all rights of the Corporation to receive the Base Rental Payments scheduled to be paid by the County under and pursuant to each of the Subleases for the benefit of the Owners of the Certificates; (c) all rents, profits and products from the Project Property and the Refunding Property to which the Corporation has any right or claim whatsoever under the Project Sublease and the Refunding Sublease, respectively; (d) the right to take all actions and give all consents under each of the Subleases; (e) the right of access more particularly described in each of the Subleases; and (f) any and all other rights and remedies of the Corporation in each of the Subleases as lessor thereunder for the purpose of (i) paying all sums due and owing to the Owners of the Certificates under the terms of the Trust Agreement, and (ii) performing and discharging each agreement, covenant and obligation of the County contained in each of the Subleases and in the Trust Agreement.

Acceptance. The Trustee accepts the foregoing assignment for the benefit of the Owners of the Certificates, subject to the conditions and terms of the Trust Agreement, and all such Base Rental Payments payable under both Subleases shall be applied and all such rights so assigned shall be exercised by the Trustee as provided in the Trust Agreement.

Payment of Rentals. Upon payment or provision for payment to the Trustee in full of all Base Rental Payments under the Project Sublease and under the Refunding Sublease and of all other amounts, including any additional rental or other amounts owed by the County under the Project Sublease, the Refunding Sublease or the Trust Agreement, the Assignment Agreement shall become and be void and of no effect with respect to the Project Sublease and the Refunding Sublease and, when the Certificates are no longer Outstanding (as defined in the Trust Agreement), the Trustee shall execute any and all documents or certificates reasonably requested by the Corporation to evidence the termination of the Assignment Agreement with respect to each of the Subleases.

Governing Law. The Assignment Agreement is made in the State of California under the Constitution and laws of the State of California and is to be so construed.

THE TRUST AGREEMENT

Terms and Conditions of Certificates

Dating of Certificates. The Series 2006 Certificates shall be dated as of their date of delivery. Each Series 2006 Certificate shall represent interest from the Interest Payment Date next preceding its date of execution to which interest has been paid in full, unless such date of execution shall be an Interest Payment Date, in which case such Series 2006 Certificate shall represent interest from the date of execution thereof, or unless such date of execution shall be after a Record Date and prior to the following Interest Payment Date, in which case such Series 2006 Certificate shall represent interest from such Interest Payment Date, or unless such date of execution shall be on or prior to July 15, 2007, in which case such Series 2006 Certificate shall represent interest from the Series 2006 Certificates Delivery Date. Notwithstanding the foregoing, if, as shown by the records of the Trustee, interest shall be in default, each Series 2006 Certificate shall represent interest from the last Interest Payment Date to which interest has been paid in full or duly provided for.

Method and Place of Payment. Except as otherwise provided in the Representation Letter, the interest represented by the Certificates shall be payable on each Interest Payment Date by check sent by first class mail by the Trustee to the respective Owners of the Certificates as of the Record Date for such Interest Payment Date at their addresses shown on the books required to be kept by the Trustee pursuant to the provisions of the Trust Agreement. Payments of defaulted interest with respect to any Certificate shall be paid by check to the Owner as of a special record date to be fixed by the Trustee, notice of which special record date shall be given to the Owner of the Certificate not less than ten days prior thereto. The principal and premium, if any, represented by the Certificates shall be payable upon presentation and surrender thereof on maturity or on prepayment prior thereto at the Principal Corporate Trust Office of the Trustee.

The Owner of $1,000,000 or more in aggregate principal amount represented by the Certificates may request in writing that the Trustee pay the interest represented by such Certificates by wire transfer to an account in the United States of America and the Trustee shall comply with such request for all Interest Payment Dates following the 15th day after receipt of such request.

Transfer and Payment of Certificates; Exchange of Certificates. All Certificates may be presented for transfer by the Owner thereof, in person or by his attorney duly authorized in writing, at the Principal Corporate Trust Office of the Trustee, on the books required to be kept by the Trustee pursuant to the provisions of the Trust Agreement, upon surrender of such Certificates for cancellation accompanied by delivery of a duly executed written instrument of transfer in a form acceptable to the Trustee. The Trustee may treat the Owner of any Certificate as the absolute owner of such Certificate for all purposes, whether or not such Certificate shall be overdue, and the Trustee shall not be affected by any knowledge or notice to the contrary; and payment of the interest and principal represented by such Certificate shall be made only to such Owner, which payments shall be valid and effectual to satisfy and discharge the liability represented by such Certificate to the extent of the sum or sums so paid.

Whenever any Certificate or Certificates shall be surrendered for transfer, the Trustee shall execute and deliver a new Certificate or Certificates representing the same principal amount in Authorized Denominations. The Trustee shall require the payment by any Owner requesting such transfer of any tax or other governmental charge required to be paid with respect to such transfer.

Certificates may be presented for exchange at the Principal Corporate Trust Office of the Trustee, for a like aggregate principal amount of Certificates of other Authorized Denominations. The Trustee

shall require the payment by the Owner requesting such exchange of any tax or other governmental charge required to be paid with respect to such exchange.

The Trustee shall not be required to transfer or exchange any Certificate during the period in which the Trustee is selecting Certificates for prepayment, nor shall the Trustee be required to transfer or exchange any Certificate or portion thereof selected for prepayment from and after the date of mailing the notice of prepayment thereof.

Certificate Registration Books. The Trustee will keep sufficient books for the registration and transfer of the Certificates, which books shall be available for inspection by the Corporation and the County at reasonable hours and under reasonable conditions; and upon presentation for such purpose the Trustee shall, under such reasonable regulations as it may prescribe, register or transfer the Certificates on such books as provided in the Trust Agreement. The Trustee will, upon written request, make copies of the foregoing available to any Owner of at least five percent in aggregate principal amount of Outstanding Certificates or his agent duly authorized in writing.

Temporary Certificates. The Certificates may be initially delivered in temporary form exchangeable for definitive Certificates when ready for delivery, which temporary Certificates shall be printed, lithographed or typewritten, shall be of such denominations as may be determined by the Trustee, shall be in fully registered form and shall contain such reference to any of the provisions of the Trust Agreement as may be appropriate. Every temporary Certificate shall be executed and delivered by the Trustee upon the same conditions and terms and in substantially the same manner as definitive Certificates. If the Trustee executes and delivers temporary Certificates, it will execute definitive Certificates without delay, and thereupon the temporary Certificates may be surrendered at the Principal Corporate Trust Office of the Trustee, in exchange for such definitive Certificates, and until so exchanged such temporary Certificates shall be entitled to the same benefits under the Trust Agreement as definitive Certificates executed and delivered under the Trust Agreement.

Certificates Mutilated, Lost, Destroyed or Stolen. If any Certificate shall become mutilated, the Trustee, at the expense of the Owner thereof, shall execute and deliver a new Certificate of like tenor, payment date in exchange and substitution for the Certificate so mutilated, but only upon surrender to the Trustee of the Certificate so mutilated. Every mutilated Certificate so surrendered to the Trustee shall be canceled by it. If any Certificate shall be lost, destroyed or stolen, evidence of such loss, destruction or theft may be submitted to the Trustee, and if such evidence is satisfactory to the Trustee and indemnity satisfactory to the Trustee shall be given, the Trustee, at the expense of the Owner thereof, shall execute and deliver a new Certificate of like tenor, numbered as the Trustee shall determine, in lieu of and in substitution for the Certificate so lost, destroyed or stolen. The Trustee shall require payment of a sum not exceeding the actual cost of preparing each new Certificate executed and delivered by it under the Trust Agreement and of the expenses which may be incurred by it under the Trust Agreement. Any Certificate executed and delivered under the provisions of the Trust Agreement in lieu of any Certificate alleged to be lost, destroyed or stolen shall be equally and proportionately entitled to the benefits of the Trust Agreement with all other Certificates secured by the Trust Agreement, and the Trustee shall not be required to treat both the original Certificate and any replacement Certificate as being Outstanding for the purpose of determining the amount of Certificates which may be executed and delivered under the Trust Agreement or for the purpose of determining any percentage of Certificates Outstanding under the Trust Agreement, but both the original and replacement Certificate shall be treated as one and the same. Notwithstanding any other provision of this paragraph, in lieu of executing and delivering a new Certificate for a Certificate which has been lost, destroyed or stolen and which has matured or will mature within 30 days after the Trustee has received all required indemnity and payments on account of a lost, destroyed or stolen Certificate, the Trustee may make payment of such Certificate to the Owner thereof on or after the maturity date.

Execution and Delivery of Additional Certificates. In addition to the County's Certificates of Participation (2005 Edgemoor Project and 1996 Regional Communications System Refunding), the County, the Corporation and the Trustee may, by execution of a Supplemental Trust Agreement without the consent of the Owners but with the consent of the Insurer (which consent shall not be unreasonably withheld), provide for the execution and delivery of Additional Certificates representing additional Base Rental Payments (which Additional Certificates shall not use the number "2005" in the title thereof). The Trustee may execute and deliver to or upon the request of the County such Additional Certificates, in such principal amount as shall reflect the additional principal components and interest components of the Base Rental Payments, and the proceeds of such Additional Certificates may be applied to any lawful purposes of the County or the Corporation, but such Additional Certificates may only be executed and delivered upon compliance by the County with the provisions of the Trust Agreement and subject to the following specific conditions, which are made conditions precedent to the execution and delivery of any such Additional Certificates:

(a) Neither of the County nor the Corporation shall be in default under the Trust Agreement or any Supplemental Trust Agreement or under either Lease or either Sublease;

(b) Said Supplemental Trust Agreement shall provide that from such proceeds or other sources an amount shall be deposited in the Certificate Reserve Fund so that following such deposit there shall be on deposit in the Certificate Reserve Fund an amount at least equal to the Certificate Reserve Fund Requirement;

(c) The Additional Certificates shall be payable as to principal only on a Principal Payment Date of each year in which principal components are due and shall be payable as to interest only on an Interest Payment Date of each year commencing with the first Interest Payment Date occurring after their date of execution and delivery;

(d) The interest with respect to the Additional Certificates shall be payable at a fixed rate;

(e) The aggregate principal amount of Certificates executed and delivered and at any time Outstanding under the Trust Agreement or under any Supplemental Trust Agreement shall not exceed any limit imposed by law, by the Trust Agreement or by any Supplemental Trust Agreement;

(f) Either the Project Lease and the Project Sublease or the Refunding Lease or the Refunding Sublease shall have been amended, to the extent necessary, so as to increase the Base Rental Payments payable by the County thereunder by an aggregate amount equal to the principal and interest represented by such Additional Certificates, payable at such times and in such manner as may be necessary to provide for the payment of the principal and interest represented by such Certificates; *provided, however*, that no such amendment shall be made such that Base Rental Payments shall be in any way conditioned upon an additional risk of construction or completion of any portion of the Project Property and that the sum of Base Rental Payments, including any such amendment, plus Additional Rental in any year shall be in excess of the annual fair rental value of the Project Property or the Refunding Property, as applicable, and evidence of the satisfaction of this condition shall be made by a Certificate of the County; and

(g) Said Supplemental Trust Agreement shall provide Principal Payment Dates and/or mandatory prepayments of Additional Certificates in amounts sufficient to provide for payment of the Additional Certificates when principal and interest components of Base Rental Payments are due.

Any Additional Certificates shall be on a parity with the Certificates and each Owner thereof shall have the same rights upon an Event of Default as the Owner of any other Certificates executed and delivered under the Trust Agreement, except as otherwise provided in the Supplemental Trust Agreement under which Additional Certificates are executed and delivered.

The County shall cause to be given to Fitch, Moody's and S&P, notice of any execution and delivery of Additional Certificates.

Proceedings for Authorization of Additional Certificates. Whenever the County and the Corporation shall determine to authorize the execution and delivery of any Additional Certificates pursuant to the Trust Agreement, the County, the Corporation and the Trustee shall enter into a Supplemental Trust Agreement without the consent of the Owners of any Certificates, providing for the execution and delivery of such Additional Certificates, specifying the maximum principal amount of such Additional Certificates and prescribing the terms and conditions of such Additional Certificates.

Such Supplemental Trust Agreement shall prescribe the form or forms of such Additional Certificates and, subject to the provisions of the Trust Agreement, shall provide for the distinctive designation, denominations, method of numbering, dates, Principal Payment Dates, interest rates, Interest Payment Dates, provisions for prepayment (if desired) and places of payment of principal and interest.

Before such Additional Certificates shall be executed and delivered, the County and the Corporation shall file or cause to be filed the following documents with the Trustee:

(a) An Opinion of Counsel setting forth (1) that such Counsel has examined the Supplemental Trust Agreement and the amendment, if any, to either the Project Lease and the Project Sublease or the Refunding Lease and the Refunding Sublease, as applicable, required by the Trust Agreement; (2) that the execution and delivery of the Additional Certificates have been sufficiently and duly authorized by the County and the Corporation; (3) that said amendments to the Project Lease and the Project Sublease or the Refunding Lease and the Refunding Sublease, as applicable, and the Supplemental Trust Agreement, when duly executed by the County and the Corporation, will be valid and binding obligations of the County and the Corporation; (4) that said amendments to the Project Lease and the Project Sublease or the Refunding Lease and the Refunding Sublease, as applicable, have been duly authorized, executed and delivered and have been duly recorded; and (5) that the amendments to the Project Lease and the Project Sublease or the Refunding Lease and the Refunding Sublease, as applicable, do not adversely affect the tax-exempt status of interest evidenced by Outstanding Certificates;

(b) A Certificate of the County that the requirements of the Trust Agreement have been met, which shall include a Certificate by the County as to the annual fair rental value of the Property;

(c) Certified copies of the resolutions of the County and the Corporation, authorizing the execution of the amendments to the Project Lease and Project Sublease or the Refunding Lease and the Refunding Sublease, as applicable, required by the Trust Agreement;

(d) An executed counterpart or duly authenticated copy of the amendments to the Project Lease and Project Sublease or the Refunding Lease and the Refunding Sublease, as applicable, required by the Trust Agreement;

(e) Certified copies of the policies of insurance required by the Project Sublease or the Refunding Sublease, as applicable, or certificates thereof, which shall evidence that the

amounts of the insurance required under the Project Sublease or the Refunding Sublease, as applicable, have been increased, if necessary, to cover the amount of such Additional Certificates; and

(f) A CLTA title insurance policy or other appropriate form of policy in the amount of the Additional Certificates of the type and with the endorsements described in the Project Sublease or the Refunding Sublease, as applicable.

Upon the delivery to the Trustee of the foregoing instruments so as to permit the execution and delivery of the Additional Certificates in accordance with the Supplemental Trust Agreement then delivered to the Trustee, the Trustee shall execute and deliver said Additional Certificates, in the aggregate principal amount specified in such Supplemental Trust Agreement, to, or upon the request of, the County.

Proceeds of Certificates

Construction Fund.

(a) The Trustee shall hold the moneys in the Construction Fund and shall disburse such moneys therefrom to pay Construction Costs. Such disbursements shall be made from time to time upon receipt of a Written Request of the County on behalf of the Corporation (in the form as set forth in Trust Agreement, signed by a Chief Financial Officer, County Treasurer-Tax Collector, the Capital Finance Manager or other officers who are specifically authorized by resolution of the Board of Supervisors of the County to sign or execute the same) which:

(i) states with respect to each disbursement to be made: (A) the requisition number, (B) the name and address of the person, firm or authority to whom payment is due, (C) the amount to be disbursed, and (D) that each obligation therein has been properly incurred, is a Construction Cost and is a proper charge against the Construction Fund and has not been the basis of any previous disbursement;

(ii) specifies in reasonable detail the nature of the obligation; and

(iii) is accompanied by a bill or statement of account for each obligation.

(b) If at any time there are insufficient moneys in the Costs of Issuance Fund to disburse moneys in accordance with the Trust Agreement, the Trustee shall disburse from the Construction Fund, subject to the Trust Agreement, such additional amounts as are necessary to pay such Costs of Issuance.

(c) Upon the delivery to the Trustee of a Certificate of Completion, the Trustee shall transfer any remaining balance of money in the Construction Fund, first, to County for deposit in the Excess Earnings Account to the extent the amount on deposit therein is less than the Rebate Requirement, second, to the Certificate Reserve Fund to the extent necessary to make the amount on deposit therein equal to the Certificate Reserve Fund Requirement, and third, the remainder to a separate subaccount within the Principal Account, which the Trustee shall establish and hold in trust, and which shall be entitled the "Surplus Subaccount." The moneys in the Surplus Subaccount shall be applied (unless some other application of such moneys would not, in the opinion of Bond Counsel, adversely affect the tax-exempt status of interest on the Certificates) as directed in writing by the County to pay principal on the Certificates as such principal becomes due and payable, in annual amounts which bear the same ratio to the principal amount of Certificates maturing in such year that the amount deposited in the Surplus Subaccount bears to the original principal amount of Certificates. The moneys in the Surplus Subaccount

shall be invested at a yield no higher than the yield on the Outstanding Certificates (unless, in the opinion of Bond Counsel, investment at a higher yield would not adversely affect the tax-exempt status of interest on the Certificates), and all such investment income shall be deposited in the Surplus Subaccount and expended or reinvested as provided above.

Certificate Reserve Fund.

(a) There is established in trust a special fund designated as the "Certificate Reserve Fund" which shall be held by the Trustee and which shall be kept separate and apart from all other funds held by the Trustee. Moneys in the Certificate Reserve Fund shall be in the amount of the Certificate Reserve Fund Requirement and shall be used and withdrawn by the Trustee solely for the purposes set forth in the Trust Agreement.

(i) If, on any Interest Payment Date (or on any earlier date as specified in a Reserve Fund Credit Facility or Certificate Reserve Fund investment), the amount on deposit in the Interest Fund is insufficient to pay the interest due with respect to the Certificates and any Additional Certificates on such Interest Payment Date, the Trustee shall transfer from the Certificate Reserve Fund and deposit in the Interest Fund an amount sufficient to make up such deficiency.

(ii) If, on any Principal Payment Date or any Mandatory Sinking Account Payment Date (or on any earlier date as specified in a Reserve Fund Credit Facility or Certificate Reserve Fund investment), the amount on deposit in the Principal Fund is insufficient to pay the principal due with respect to the Certificates and any Additional Certificates on such Principal Payment Date or Mandatory Sinking Account Payment Date, the Trustee shall transfer from the Certificate Reserve Fund and deposit in the Principal Fund an amount sufficient to make up such deficiency.

(iii) Monies on deposit in the Certificate Reserve Fund shall be withdrawn and transferred by the Trustee to be applied for the final payment on the Certificates and any Additional Certificates.

In the event of any withdrawal or transfer from the Certificate Reserve Fund, the Trustee shall, within five days thereafter, provide written notice to the County of the amount and the date of such transfer. If at any time the balance in the Certificate Reserve Fund shall be reduced below the Certificate Reserve Fund Requirement, the first of Base Rental Payments thereafter payable by the County under the Subleases and not needed to pay the interest and principal components of Base Rental Payments payable by the County under the Subleases to the Owners on the next Interest Payment Date, Principal Payment Date or Mandatory Sinking Account Payment Date shall be used to increase the balance in the Certificate Reserve Fund to the Certificate Reserve Fund Requirement. If after the payment of principal and interest on any Interest Payment Date the balance in the Certificate Reserve Fund shall be in excess of the Certificate Reserve Fund Requirement the Trustee shall, upon Written Request of the County, transfer such excess first to the Excess Earnings Account to the extent the amount on deposit therein is less than the Rebate Requirement, then to the County for deposit in the Administrative Expense Fund to the extent needed to pay reasonable and necessary operating expenses of the County relating to the Certificates and thereafter to the Principal Fund. At the termination of both Subleases in accordance with their respective terms, any balance remaining in the Certificate Reserve Fund shall be released and may be transferred to such other fund or account of the County, or otherwise used by the County for any other lawful purposes, as the County may direct in writing. For purposes of determining the amount on deposit in the Certificate Reserve Fund, all investments shall be valued annually at the amortized cost thereof (exclusive of accrued but unpaid interest, but inclusive of commissions). Investments in the Certificate Reserve Fund shall

mature, or be subject to tender, redemption or withdrawal at the option of the holder thereof, not later than five years from the date of investment.

(b) At the option of the County, one or more Reserve Fund Credit Facilities may be substituted for the funds held by the Trustee in the Certificate Reserve Fund such that the amount available to be drawn under such Reserve Fund Credit Facilities together with funds remaining in the Certificate Reserve Fund satisfies the Certificate Reserve Fund Requirement.

If the County exercises its option to substitute a Reserve Fund Credit Facility for all or a portion of the moneys held by the Trustee in the Certificate Reserve Fund, then such moneys, on or after the date that the Reserve Fund Credit Facility becomes effective, at the option of the County, shall be transferred (A) to the Base Rental Payment Fund and on each applicable Principal Payment Date a pro rata portion thereof shall be transferred to the Principal Fund and used to pay a portion of the principal with respect to the Certificates due on such Principal Payment Date, or (B) to a construction fund to be held by the County and used for capital projects of the County in accordance with the Tax Certificate. Neither the County nor the Trustee may invest such amounts transferred so as to produce a yield greater than the yield permitted under the Tax Certificate. In the event any Reserve Fund Credit Facility is scheduled to terminate prior to the final maturity date of the Certificates and any Additional Certificates and such Reserve Fund Credit Facility is not extended, renewed or replaced with another Reserve Fund Credit Facility or with cash or Permitted Investments in the amount of such Reserve Fund Credit Facility, the Trustee shall draw on or make a claim under such Reserve Fund Credit Facility ten days prior to the date of such expiration in an amount equal to the lesser of (i) the maximum amount available thereunder or (ii) the Certificate Reserve Fund Requirement, in either case for deposit into the Certificate Reserve Fund.

In the event a Reserve Fund Credit Facility is substituted for all or a portion of the moneys held by the Trustee in the Certificate Reserve Fund pursuant to the terms of the Trust Agreement, then, notwithstanding any other provision of the Trust Agreement, (1) the Trustee shall draw upon the Reserve Fund Credit Facility for amounts which the terms of the Trust Agreement require to be transferred from the Certificate Reserve Fund; provided that the Trustee shall first draw upon any cash or Permitted Investments on deposit in the Certificate Reserve Fund before drawing upon any Reserve Fund Credit Facility, and thereafter shall draw upon all such Reserve Fund Credit Facilities on a pro rata basis, and (2) amounts required by the terms of the Trust Agreement to be deposited or transferred to the Certificate Reserve Fund (a) in the event the Reserve Fund Credit Facility has been drawn upon, shall be first paid to the provider of such Reserve Fund Credit Facility if the County has an outstanding reimbursement obligation to such provider resulting from such draw, which payment shall result in an increase in the amount then available under the Reserve Fund Credit Facility equal to such payment and (b) to the extent all such draws on Reserve Fund Credit Facilities have been paid, then, second, shall be transferred or deposited to the Certificate Reserve Fund in amount such that after giving effect to the deposit the amount on deposit in the Certificate Reserve Fund is equal to the Certificate Reserve Fund Requirement.

The County shall be permitted to make use of a Reserve Fund Credit Facility pursuant to the Trust Agreement at any time.

The term "substitution" as used above shall include such initial funding of the Certificate Reserve Fund Requirement by means of a Reserve Fund Credit Facility instead of by deposit of moneys, and shall not be read to mean that the County must first make an initial cash deposit in the Certificate Reserve Fund before invoking the provisions of the Trust Agreement relating to Reserve Fund Credit Facilities and satisfying the Certificate Reserve Fund Requirement by securing and implementing a Reserve Fund Credit Facility.

Cost of Issuance Fund. There is established in trust a special fund designated as the "Cost of Issuance Fund" which shall be held by the County and which shall be kept separate and apart from all other funds held by the County. The County shall disburse moneys from the Cost of Issuance Fund on such dates and in such amounts as are necessary to pay Costs of Issuance in accordance with the Tax Certificate. On or before June 1, 2007, the Trustee shall transfer any amounts then remaining in the Cost of Issuance Fund first to the Excess Earnings Account to the extent the amount on deposit therein is less than the Rebate Requirement, then to the Certificate Reserve Fund to the extent the amount on deposit therein is less than the Certificate Reserve Fund Requirement, then to the County for deposit in the Administrative Expense Fund to the extent that the amount on deposit therein is less than $20,000, and thereafter to the Interest Fund.

Administrative Expense Fund.

(a) There is established in trust a special fund designated as the "Administrative Expense Fund" which shall be held by the County and which shall be kept separate and apart from all other funds held by the County.

(b) Amounts in the Administrative Expense Fund shall be paid out from time to time by the County for reasonable and necessary operating expenses of the County relating to the Certificates including, without limitation, expenses incidentally incurred in connection with the purchase or prepayment of any Certificates, which expenses shall not include the payment of principal or interest with respect to any Certificates.

(c) Amounts in the Administrative Expense Fund which the County at any time determines to be in excess of $20,000 shall be transferred to the Trustee for deposit in the Principal Fund.

Earnings Fund. There is established under the Trust Agreement in trust a special fund designated as the "Earnings Fund" which shall be held by the Trustee and which shall be kept separate and apart from all other funds held by the Trustee. The Trsutee shall administer the Earnings Fund as provided in the Trust Agreement.

The Trustee shall establish and maintain in the Earnings Fund a separate account designated as the "Investment Earnings Account," and a separate account designated as the "Excess Earnings Account." All moneys in the Investment Earnings Account and the Excess Earnings Account shall be held by the Trustee in trust and shall be kept separate and apart from all other funds and money held by the Trustee. All investment earnings on the funds and accounts (other than the Excess Earnings Account, the Construction Fund, and the Surplus Subaccount) established under the Trust Agreement shall be deposited into the Investment Earnings Account. All investment earnings on the Construction Fund and the Surplus Subaccount shall be retained therein. Amounts on deposit in the Investment Earnings Account shall be transferred to the Excess Earnings Account in accordance with the provisions of the Tax Certificate.

Upon each transfer, any amount remaining in the Earnings Fund or any amount on deposit in the Excess Earnings Account which exceeds the amount required to be maintained therein pursuant to the provision of the Tax Certificate shall be transferred first, to the Certificate Reserve Fund so that following such deposit there shall be on deposit in the Certificate Reserve Fund an amount at least equal to the Certificate Reserve Fund Requirement, second, before the delivery of a Certificate of Completion to the Trustee, to the Construction Fund, and, after the delivery of a Certificate of Completion to the Trustee, for deposit in the Base Rental Payment Fund. Except as set forth in the proceeding sentence, amounts on deposit in the Excess Earnings Account shall only be applied to payments made to the United States in accordance with written instructions of the County.

Rental Payments

Pledge of Base Rental Payments and Additional Rental; Base Rental Payment Fund.

(a) There is established a special fund designated as the "Base Rental Payment Fund" which shall be held by the Trustee and which shall be kept separate and apart from all other funds and moneys held by the Trustee. The County irrevocably pledges and transfers to the Trustee, for the benefit of the Owners, all of its right, title and interest in and to all amounts on deposit from time to time in the funds and accounts established under the Trust Agreement and in and to the Base Rental Payments, which shall be used for the punctual payment of the interest and principal represented by the Certificates and any Additional Certificates and the Base Rental Payments shall not be used for any other purpose while any of the Certificates or Additional Certificates remain Outstanding. It is the intent of the parties to the Trust Agreement that the Corporation shall not have any right, title, in or to the Base Rental Payments. In the event, however, that it should be determined that the Corporation has any right, title or interest in or to the Base Rental Payments, then the Corporation irrevocably pledge and transfer to the Trustee, for the benefit of the Owners, all of such right, title and interest, which shall be used for the punctual payment of the interest and principal represented by the Certificates and any Additional Certificates. These pledges shall constitute a first and exclusive lien on the funds established under the Trust Agreement and the Base Rental Payments in accordance with the terms of the Trust Agreement subject in all events to the power of the County to cause the execution and delivery of Additional Certificates pursuant to the Trust Agreement which shall be on a parity with the Certificates and any Additional Certificates Outstanding.

(b) All Base Rental Payments shall be paid directly by the County to the Trustee, and if received by the Corporation at any time shall be deposited by the Corporation, as the case may be, with the Trustee within one Business Day after the receipt thereof. All Base Rental Payments, the proceeds of rental interruption insurance, liquidated damages, if any, and any payments made under the liquidated damage provisions the Construction Contract (as such term is defined in the Project Sublease) shall be deposited by the Trustee in the Base Rental Payment Fund and all amounts on deposit therein shall be held in trust by the Trustee, which fund the Trustee agrees to establish and maintain for the benefit of the Owners until all required Base Rental Payments are paid in full pursuant to both Subleases or until such date as the Certificates and any Additional Certificates are no longer Outstanding; *provided, however,* and notwithstanding the foregoing, if the Trustee receives a Base Rental Payment amount in excess of the amount necessary to pay the amount due and owing on the next Interest Payment Date, Principal Payment Date or Mandatory Sinking Account Payment Date, as the case may be, after giving effect to the funds then on deposit in the Base Rental Payment Fund not needed for any other purpose under the Trust Agreement, and if the amount then in the Certificate Reserve Fund is at least equal to the Certificate Reserve Fund Requirement and there exists no Event of Default under the Trust Agreement, then amounts in the Base Rental Payment Fund not needed to make such payments may be utilized by the Trustee, as directed in writing by the County, to make any regular periodic payment due to provider of a Reserve Fund Credit Facility or a Certificate Reserve Fund investment which provides for such payments, if any, or for any other purpose.

Deposit of Base Rental Payments. Except as otherwise provided in the Trust Agreement, the Trustee shall deposit the amounts in the Base Rental Payment Fund at the time and in the priority and manner provided in the Trust Agreement in the following respective funds, each of which the Trustee agrees to establish and maintain until all required Base Rental Payments are paid in full pursuant to both Subleases or until such date as the Certificates and any Additional Certificates are no longer Outstanding, and the moneys in each of such funds shall be disbursed only for the purposes and uses authorized in the Trust Agreement. The Trustee shall establish and maintain the Capitalized Interest Account within the Interest Fund until the date all amounts are transferred therefrom in accordance with the Trust Agreement.

(a) *Interest Fund and Capitalized Interest Account*. The Trustee, on each Interest Payment Date, shall deposit in the Interest Fund a sufficient amount of money such that the aggregate of amounts therein equal the portion of the Base Rental Payments designated as the interest component coming due on such Interest Payment Date; *provided, however,* that on each Interest Payment Date occurring on or before the later of July 1, 2007 or the delivery to the Trustee of the Certificate of Completion, before making said deposit, if and to the extent available in the Capitalized Interest Account within the Interest Fund, an amount equal to the difference between (1) the aggregate amount of interest component coming due on such Interest Payment Date and (2) the aggregate amount of the interest component of any Base Rental Payments payable under the Refunding Sublease, shall be transferred from the Capitalized Interest Account within the Interest Fund to the Interest Fund. Moneys in the Interest Fund shall be used by the Trustee for the purpose of paying the interest evidenced by the Certificates and the Additional Certificates when due and payable. Upon the later of July 1, 2007 or the delivery to the Trustee of the Certificate of Completion, the Trustee shall transfer any amounts then remaining in the Capitalized Interest Account to the Interest Fund.

(b) *Principal Fund*. The Trustee, on each Principal Payment Date and Mandatory Sinking Account Payment Date, shall deposit in the Principal Fund a sufficient amount of money such that the aggregate of amounts therein equal the portion of the Base Rental Payments designated as the principal component coming due on such Principal Payment Date or Mandatory Sinking Account Payment Date. Monies in the Principal Fund shall be used and withdrawn by the Trustee for the purpose of paying the principal represented by the Certificates and any Additional Certificates when due and payable at maturity or upon earlier prepayment from Mandatory Sinking Account Payments.

(c) *Prepayment Fund*. The Trustee, on the prepayment date specified in the Written Request of the County filed with the Trustee at the time that any prepaid Base Rental Payment is paid to the Trustee pursuant to each of the Subleases, shall deposit in the Prepayment Fund that amount of moneys representing the portion of the Base Rental Payments designated as prepaid Base Rental Payments. Monies in the Prepayment Fund shall be used and withdrawn by the Trustee for the purpose of paying the principal, premium, if any, and interest represented by the Certificates and any Additional Certificates to be prepaid.

Application of Insurance Proceeds and Condemnation Awards. The Trustee shall not be responsible for the sufficiency of any insurance required by either Sublease and shall be fully protected in accepting payment on account of such insurance or any adjustment, compromise or settlement of any loss agreed to by the County or the Corporation. Delivery to the Trustee of the schedule of insurance policies under the Subleases shall not confer responsibility upon the Trustee as to the sufficiency of coverage or amounts of such policies.

Except as provided in the Trust Agreement, in the event of any damage to or destruction of any part of the Project Property, caused by the perils covered by the policies of insurance required to be maintained by the County pursuant to the Project Sublease or, in the event of any damage to or destruction of any part of the Refunding Property, caused by the perils covered by the policies of insurance required to be maintained by the County pursuant to the Refunding Sublease, the County and the Corporation shall cause the proceeds of such insurance (other than rental interruption insurance which is to be placed in the Base Rental Payment Fund) to be used in accordance with the Project Sublease or the Refunding Sublease, as applicable. The Trustee shall hold said proceeds in a separate fund to be established and maintained by the Trustee and designated the "Insurance Proceeds and Condemnation Awards Fund." The Trustee shall only make disbursements from the Insurance Proceeds and Condemnation Awards Fund upon receipt of a Written Request of the County on behalf of the

Corporation, signed by a Chief Financial Officer, County Treasurer-Tax Collector, the Capital Finance Manager or other officers who are specifically authorized by resolution of the Board of Supervisors of the County to sign or execute the same) which (i) states with respect to each disbursement to be made: (A) the requisition number, (B) the name and address of the person, firm or authority to whom payment is due, (C) the amount to be disbursed, and (D) that each obligation therein has been properly incurred for the purpose of repair, reconstruction or replacement of the Project Property or the Refunding Property, as applicable, to at least the same good order, repair and condition as it was in prior to the damage or destruction, insofar as the same may be accomplished by the use of said proceeds and is a proper charge against the Insurance Proceeds and Condemnation Awards Fund and has not been the basis of any previous disbursement; (ii) specifies in reasonable detail the nature of the obligation; and (iii) is accompanied by a bill or statement of account for each obligation. Any balance of said proceeds not required for such repair, reconstruction or replacement as evidenced by a Certificate of the County to the effect that such repair, reconstruction or replacement has been completed and all amounts owing therefor have been paid or provision for the payment therefor has been made shall be transferred by the Trustee to Prepayment Fund and applied in the manner provided by the Trust Agreement. Alternatively, the County, at its option, and if the proceeds of such insurance together with any other moneys then available for the purpose are at least sufficient to prepay all Outstanding Certificates and Additional Certificates, may elect not to repair, reconstruct or replace the damaged or destroyed portion of the Property and thereupon shall cause said proceeds to be transferred to the Prepayment Fund and used for the prepayment of Outstanding Certificates and Additional Certificates pursuant to the Trust Agreement; provided, that if the County elects to so prepay the Outstanding Certificates and Additional Certificates, then the County shall make said election within 45 days after the damage to or destruction of the Project Property or the Refunding Property, as applicable. Notwithstanding any other provision in the Trust Agreement, the County shall only prepay less than all of the Outstanding Certificates and Additional Certificates if the annual fair rental value of the Property after such damage, destruction or condemnation is at least equal to the aggregate annual amount of principal and interest represented by the Outstanding Certificates and Additional Certificates not being prepaid.

The proceeds of any award in eminent domain shall be transferred by the County to the Trustee for deposit in the Prepayment Fund and applied to the prepayment of Outstanding Certificates and Additional Certificates pursuant to the Trust Agreement.

Title Insurance. Proceeds of any policy of title insurance received by the County, the Corporation or the Trustee in respect of the Property shall be applied and disbursed by the County, the Corporation or the Trustee as follows:

(a) If the County determines that the title defect giving rise to such proceeds has not materially affected the operation of the Property and will not result in an abatement of Rental Payments payable by the County under the applicable Sublease, such proceeds shall be deposited first in the Excess Earnings Account to the extent the amount on deposit therein is less than the Rebate Requirement, then in the Certificate Reserve Fund to the extent that the amount therein is less than the Certificate Reserve Fund Requirement, then in the Administrative Expense Fund to the extent needed to pay reasonable and necessary operating expenses of the County with respect to the Certificates, and thereafter amounts not required to be so deposited shall be remitted to the County and used for any lawful purpose thereof; or

(b) If any portion of the Property has been affected by such title defect, and if the County determines that such title defect will result in an abatement of Rental Payments payable by the County under the applicable Sublease, then the County, the Corporation or the Trustee shall immediately deposit such proceeds in the Prepayment Fund and such proceeds shall be applied to the prepayment of Certificates and Additional Certificates in the manner provided in the Trust Agreement.

Covenants

Compliance with Trust Agreement. The Trustee will not execute or deliver any Certificates or Additional Certificates in any manner other than in accordance with the provisions of the Trust Agreement, and neither of the County or the Corporation will suffer or permit any default by them to occur under the Trust Agreement, but will faithfully comply with, keep, observe and perform all the agreements, conditions, covenants and terms of the Trust Agreement required to be complied with, kept, observed and performed by them.

Compliance with Leases and Subleases. The County and the Corporation will faithfully comply with, keep, observe and perform all the agreements, conditions, covenants and terms contained in the Leases and Subleases required to be complied with, kept, observed and performed by them and, together with the Trustee, will enforce the Leases and Subleases against the other party thereto in accordance with their respective terms.

Observance of Laws and Regulations. The Trustee, the County and the Corporation will faithfully comply with, keep, observe and perform all valid and lawful obligations or regulations now or hereafter imposed on them by contract, or prescribed by any law of the United States of America or of the State of California, or by any officer, board or commission having jurisdiction or control, as a condition of the continued enjoyment of each and every franchise, right or privilege now owned or hereafter acquired by them, including their right to exist and carry on their respective businesses, to the end that such franchises, rights and privileges shall be maintained and preserved and shall not become abandoned, forfeited or in any manner impaired.

Other Liens. The County will keep the Property and all parts thereof free from judgments and materialmen's and mechanics' liens and free from all claims, demands, encumbrances and other liens of whatever nature or character, other than Permitted Encumbrances (with respect to the Project Property, as such term is defined in the Project Sublease, and, with respect to the Refunding Property, as such term is defined in the Refunding Sublease) and free from any claim or liability which materially impairs the County in conducting its business or utilizing the Property, and the Trustee at its option (after first giving the County ten days' written notice to comply therewith and failure of the County to take any necessary steps to defend against or to so comply within such ten-day period) may defend against any and all actions or proceedings in which the validity of the Trust Agreement is or might be questioned, or may pay or compromise any claim or demand asserted in any such actions or proceedings; *provided, however,* that, in defending against any such actions or proceedings or in paying or compromising any such claims or demands, the Trustee shall not in any event be deemed to have waived or released the County from liability for or on account of any of its agreements and covenants contained in the Trust Agreement, or from its liability under the Trust Agreement to defend the validity of the Trust Agreement and to perform such agreements and covenants. The Trustee shall have no liability with respect to any determination made in good faith to proceed or decline to defend, pay or compromise any such claim or demand.

So long as any Certificates or Additional Certificates are Outstanding, neither the County nor the Corporation will create or suffer to be created any pledge of or lien on the Base Rental Payments other than as provided or permitted under the Trust Agreement.

Prosecution and Defense of Suits. The County will promptly take such action from time to time as may be necessary or proper, in its reasonable discretion, to remedy or cure any known cloud upon or defect in the title to the Property or any portion thereof, whether now existing or hereafter developing, and will prosecute all actions, suits or other proceedings as may be appropriate for such purpose.

Accounting Records and Statements. The Trustee will keep proper accounting records in which complete and correct entries shall be made of all transactions made by it relating to the receipt, deposit and disbursement of the Base Rental Payments, and such accounting records shall be available for inspection by the County or the Corporation at reasonable hours, under reasonable conditions and with reasonable notice. The Trustee shall deliver a monthly accounting to the County; provided that the Trustee shall not be obligated to report as to any fund or account that (a) has a balance of zero and (b) has not had any activity since the last reporting date.

Recordation and Filing. The Corporation will file, record, register, renew, refile and rerecord all such documents, including financing statements (or continuation statements in connection therewith), as may be required by law in order to maintain the Lease, Sublease, Assignment Agreement and the Trust Agreement at all times as a security interest in the Base Rental Payments, all in such manner, at such times and in such places as may be required and to the extent permitted by law in order to perfect, preserve and protect fully the security of the Owners and the rights and security interests of the Trustee, and the Corporation will do whatever else may be necessary or be reasonably required in order to perfect and continue the liens of the Leases, Subleases, Assignment Agreement and the Trust Agreement.

Further Assurances. Whenever and so often as requested to do so by the Trustee or any Owner, the County and the Corporation will promptly execute and deliver or cause to be executed and delivered all such other and further assurances, documents or instruments and promptly do or cause to be done all such other and further things as may be necessary or reasonably required in order to further and more fully vest in the Trustee and the Owners all advantages, benefits, interests, powers, privileges and rights conferred or intended to be conferred upon them by the Trust Agreement or by the Assignment Agreement, Subleases or Leases.

Excess Earnings Account of the Earnings Fund; Tax Covenants. (a) The Trustee shall establish and maintain an account separate from any other fund or account established and maintained under the Trust Agreement designated as the "Excess Earnings Account." There shall be deposited in the Excess Earnings Account such amounts as are required to be deposited therein pursuant to the Tax Certificate. All money at any time deposited in the Excess Earnings Account shall be held by the Trustee in trust, to the extent required to satisfy the Rebate Requirement, for payment to the United States of America. Notwithstanding defeasance of the Certificates and the Additional Certificates pursuant to the Trust Agreement or anything to the contrary contained in the Trust Agreement, all amounts required to be deposited into or on deposit in the Excess Earnings Account shall be governed exclusively by the provisions of the Trust Agreement described under this caption and by the Tax Certificate (which is incorporated in the Trust Agreement by reference). The Trustee shall have no duty or obligation to monitor the compliance by the County with the requirements of the Tax Certificate.

(b) Any funds remaining in the Excess Earnings Account after payment in full of all of the Certificates and any Additional Certificates and after payment of any amounts described in the provisions of the Trust Agreement described under the caption "—Excess Earnings Account of the Earnings Fund; Tax Covenants", shall be transferred to the County to be used for any lawful purpose.

Continuing Disclosure. The County and the Trustee, in its capacity as dissemination agent, covenant and agree that they will comply with and carry out all of the provisions of the Continuing Disclosure Agreement. Notwithstanding any other provision of the Trust Agreement, failure of the County or the Trustee to comply with the Continuing Disclosure Agreement shall not be considered an Event of Default; however, the Trustee may (and, at the request of the Purchasers or the Owners of at least 25% aggregate principal amount of Outstanding Certificates, shall) or any Owner or Beneficial Owner of Certificates may take such actions as may be necessary and appropriate, including seeking mandate or specific performance by court order, to cause the County or the Trustee, as the case may be, to

comply with its obligations under this paragraph; *provided*, that the Trustee shall only be required to take an action under this paragraph to the extent funds have been provided to it or it has been otherwise indemnified to its reasonable satisfaction from any cost, liability, expense or additional charges of the Trustee whatsoever, including, without limitation, fees and expenses of its attorneys.

Default and Limitations of Liability

Events of Default. The following events shall be Events of Default:

(a) default in the due and punctual payment of the principal of or premium, if any, on any Certificate or Additional Certificate when and as the same shall become due and payable, whether at maturity as therein expressed, by proceedings for prepayment, by declaration or otherwise;

(b) default in the due and punctual payment of any installment of interest on any Certificate or Additional Certificate when and as such interest installment shall become due and payable;

(c) default by the County in the observance of any of the covenants, agreements or conditions on its part in the Trust Agreement contained, if such default shall have continued for a period of 30 days after written notice thereof, specifying such default and requiring the same to be remedied, shall have been given to the County and the Corporation by the Trustee, or to the County, the Corporation and the Trustee by the Owners of not less than 25% in aggregate principal amount of the Certificates and Additional Certificates at the time Outstanding; *provided, however,* that if such default can be remedied but not within such 30-day period and if the County has taken all action reasonably possible to remedy such default within such 30-day period, such default shall not become an Event of Default for so long as the County shall diligently proceed to remedy the same in accordance with and subject to any directions or limitations of time reasonably established by the Trustee; or

(d) an event of default shall have occurred and be continuing under either Sublease.

Action on Default. Subject to the Trust Agreement, in each and every case during the continuance of an Event of Default, the Trustee or the Owners of not less than a majority in aggregate principal amount represented by the Certificates and any Additional Certificates at the time Outstanding (subject to the provisions of the Trust Agreement) shall be entitled, upon notice in writing to the County and the Corporation to exercise any of the remedies granted to the County under the Leases, to the Corporation under the Subleases, and in addition, to take whatever action at law or in equity may appear necessary or desirable to enforce its rights as assignee pursuant to the Assignment Agreement or to protect and enforce any of the rights vested in the Trustee or the Owners by the Trust Agreement or by the Certificates and any Additional Certificates, either at law or in equity or in bankruptcy or otherwise, whether for the specific enforcement of any covenant or agreement or for the enforcement of any other legal or equitable right, including any one or more of the applicable remedies set forth in the Trust Agreement.

Other Remedies of the Trustee. The Trustee shall have the right:

(a) by mandamus or other action or proceeding or suit at law or in equity to enforce its rights against the County, the Corporation or any director, officer or employee thereof, and to compel the County or the Corporation or any such director, officer or employee to perform or

carry out its or his or her duties under law and the agreements and covenants required to be performed by it or him or her contained in the Trust Agreement;

(b) by suit in equity to enjoin any acts or things which are unlawful or violate the rights of the Trustee; or

(c) by suit in equity upon the happening of any default under the Trust Agreement to require the County and the Corporation to account as the trustee of an express trust.

Non-Waiver. A waiver of any default or breach of duty or contract by the Trustee shall not affect any subsequent default or breach of duty or contract or impair any rights or remedies on any such subsequent default or breach of duty or contract. No delay or omission by the Trustee to exercise any right or remedy accruing upon any default or breach of duty or contract shall impair any such right or remedy or shall be construed to be a waiver of any such default or breach of duty or contract or an acquiescence therein, and every right or remedy conferred upon the Trustee by law or by the Trust Agreement may be enforced and exercised from time to time and as often the Trustee shall deem expedient.

If any action, proceeding or suit to enforce any right or to exercise any remedy is abandoned or determined adversely to the Trustee or any Owner or Owners, then subject to any adverse determination, the Trustee or such Owner or Owners and the County and the Corporation shall be restored to their former positions, rights and remedies as if such action, proceeding or suit had not been brought or taken.

Remedies Not Exclusive. No remedy conferred upon or reserved to the Trustee in the Trust Agreement is intended to be exclusive of any other remedy, and each such remedy shall be cumulative and shall be in addition to every other remedy given under the Trust Agreement or now or hereafter existing at law or in equity or by statute or otherwise and may be exercised without exhausting and without regard to any other remedy conferred by any law. The assertion or employment of any right or remedy under the Trust Agreement, or otherwise, shall not prevent the concurrent assertion or employment of any other appropriate right or remedy.

No Liability by the Corporation or the County to the Owners. Except as expressly provided in the Trust Agreement, the Corporation shall have no obligation or liability to the Owners with respect to the payment when due of the Base Rental Payments by the County, or with respect to the performance by the County of the other agreements and covenants required to be performed by it contained in the Project Sublease, the Refunding Sublease or in the Trust Agreement, or with respect to the performance by the Trustee of any right or obligation required to be performed by it contained in the Trust Agreement.

No Liability by the County to the Owners. Except for the payment when due of the Base Rental Payments and the performance of the other agreements and covenants required to be performed by it contained in the Project Sublease, the Refunding Sublease or in the Trust Agreement, the County shall not have any obligation or liability to the Owners with respect to the Trust Agreement or the preparation, execution, delivery or transfer of the Certificates or the disbursement of the Base Rental Payments by the Trustee to the Owners, or with respect to the performance by the Trustee of any right or obligation required to be performed by it contained in the Trust Agreement.

No Liability by the Trustee to the Owners. Except as expressly provided in the Trust Agreement, the Trustee shall not have any obligation or liability to the Owners with respect to the payment when due of the Base Rental Payments by the County, or with respect to the performance by the County or the Corporation of the other agreements and covenants required to be performed by them, respectively contained in the Leases or Subleases or in the Trust Agreement.

Application of Amounts After Default. Notwithstanding anything to the contrary contained in the Trust Agreement, after a default by the County, all funds and accounts held by the Trustee and all payments received by the Trustee with respect to the rental of the Property after a default by the County pursuant to the Project Sublease or the Refunding Sublease, and all damages or other payments received by the Trustee for the enforcement of any rights and powers of the Trustee under the Project Sublease or the Refunding Sublease, shall be deposited into the Base Rental Payment Fund and as soon as practicable thereafter applied:

(a) to the payment of all amounts due the Trustee under the Trust Agreement; and

(b) to the payment of all amounts then due as interest with respect to the Certificates and any Additional Certificates, and thereafter to the payment of all amounts due as principal with respect to the Certificates and any Additional Certificates, in respect of which or for the benefit of which, money has been collected (other than Certificates and any Additional Certificates which have matured or otherwise become payable prior to such Event of Default and money for the payment of which is held by the Trustee), ratably without preference or priority of any kind, according to the amounts due and payable with respect to such Certificates and Additional Certificates.

Trustee May Enforce Claims Without Possession of Certificates. All rights of action and claims under the Trust Agreement or the Certificates and any Additional Certificates may be prosecuted and enforced by the Trustee without the possession of any of the Certificates or Additional Certificates or the production thereof in any proceeding relating thereto, and any such proceeding instituted by the Trustee shall be brought in its own name as trustee of an express trust, and any recovery of judgment shall, after provision for the payment of the reasonable compensation, expenses, disbursements and advances of the Trustee, its agents and counsel, be for the ratable benefit of the Owners of the Certificates or Additional Certificates in respect of which such judgment has been recovered.

Limitation on Suits. No Owner of any Certificate or Additional Certificate shall have any right to institute any proceeding, judicial or otherwise, with respect to the Trust Agreement, or for the appointment of a receiver or trustee, or for any other remedy under the Trust Agreement, unless such Owner has previously given written notice to the Trustee of a continuing Event of Default; the Owners of not less than 25% in principal amount of the Outstanding Certificates and Additional Certificates shall have made written request to the Trustee to institute proceedings in respect of such Event of Default in its own name as Trustee under the Trust Agreement; such Owner or Owners have afforded to the Trustee indemnity reasonably satisfactory to the Trustee against the costs, expenses and liabilities to be incurred in compliance with such request; the Trustee for 60 days after its receipt of such notice, request and offer of indemnity has failed to institute any such proceedings; and no direction inconsistent with such written request has been given to the Trustee during such 60-day period by the Owners of a majority in principal amount of the Outstanding Certificates and Additional Certificates; it being understood and intended that no one or more Owners of Certificates and Additional Certificates shall have any right in any manner whatever by virtue of, or by availing of, any provision of the Trust Agreement to affect, disturb or prejudice the rights of any other Owner of Certificates or Additional Certificates, or to obtain or seek to obtain priority or preference over any other Owner or to enforce any right under the Trust Agreement, except in the manner provided in the Trust Agreement and for the equal and ratable benefit of all the Owners of Certificates and Additional Certificates. Nothing in the Trust Agreement contained shall, however, affect or impair the right of any Owner to enforce the payment of the principal component of or the prepayment price of and the interest component of the Base Rental Payments represented by any Certificate or Additional Certificate at and after the maturity or earlier prepayment.

The Trustee

Employment of the Trustee. The County and the Corporation appoint and employ the Trustee to receive, deposit and disburse the Rental Payments, to prepare, execute, deliver and transfer the Certificates and Additional Certificates and to perform the other functions contained in the Trust Agreement; all in the manner provided in the Trust Agreement and subject to the conditions and terms of the Trust Agreement. By executing and delivering the Trust Agreement, the Trustee accepts the appointment and employment referred to in the Trust Agreement and accepts the rights and obligations of the Trustee provided in the Trust Agreement, subject to the conditions and terms of the Trust Agreement. The Trustee undertakes to perform such duties and only such duties as are specifically set forth in the Trust Agreement, and no implied covenants or obligations shall be read into the Trust Agreement against the Trustee. In case an Event of Default has occurred and is continuing, the Trustee shall exercise such of the rights and powers vested in it by the Trust Agreement, and use the same degree of care and skill in their exercise, as a prudent person would exercise or use under the circumstances in the conduct of his own affairs.

Duties, Removal and Resignation of the Trustee. The County and the Corporation may, by an instrument in writing and upon 30 days written notice remove the Trustee initially a party to the Trust Agreement and any successor thereto unless an Event of Default shall have occurred and then be continuing, and shall remove the Trustee initially a party to the Trust Agreement and any successor thereto if at any time requested to do so by an instrument or concurrent instruments in writing signed by the Owners of a majority in aggregate principal amount represented by the Certificates and Additional Certificates at the time Outstanding (or their attorneys duly authorized in writing), but any such successor Trustee shall be a bank with trust powers or trust company doing business and having a principal corporate trust office in California or New York, having (or if such bank or trust company is a member of a bank holding company system, its bank holding company has) a combined capital (exclusive of borrowed capital) and surplus of at least seventy-five million dollars ($75,000,000) and subject to supervision or examination by federal or state authorities. If such bank or trust company publishes a report of condition at least annually, pursuant to law or to the requirements of any supervising or examining authority above referred to, then for the purposes of the Trust Agreement the combined capital and surplus of such bank or trust company shall be deemed to be its combined capital and surplus as set forth in its most recent report of condition so published.

The Trustee may at any time resign by giving written notice of such resignation to the County, the Corporation and the Insurer and by mailing notice, first class, postage prepaid, of such resignation to the Owners at their addresses appearing on the books required to be kept by the Trustee pursuant to the provisions of the Trust Agreement. Upon receiving such notice of resignation, the County and the Corporation shall promptly appoint a successor Trustee by an instrument in writing; provided, however, that in the event the County and the Corporation do not appoint a successor Trustee within 30 days following receipt of such notice of resignation, the resigning Trustee may, at the expense of the County, petition the appropriate court having jurisdiction to appoint a successor Trustee. Any resignation or removal of a Trustee and appointment of a successor Trustee shall become effective only upon acceptance of appointment by the successor Trustee.

For such time as the Financial Guaranty Insurance Policy shall be in full force and effect and so long as the Insurer is not in default under its Financial Guaranty Insurance Policy (1) the Trustee may be removed at any time, at the request of the Insurer, for any breach of the trust set forth in the Trust Agreement, (2) the Insurer shall receive prior written notice of any Trustee resignation, (3) every successor Trustee appointed pursuant to this Section shall be a trust company or bank in good standing located in or incorporated under the laws of the State, duly authorized to exercise trust powers and subject to examination by federal or state authority, having a reported capital and surplus of not less than

$75,000,000 and acceptable to the Insurer, and (4) no removal, resignation or termination of the Trustee shall take effect until a successor, acceptable to the Insurer, shall be appointed.

Compensation and Indemnification of the Trustee. The County shall from time to time, subject to any written agreement then in effect with the Trustee, pay the Trustee reasonable compensation for all its services rendered under the Trust Agreement and reimburse the Trustee for all its advances and expenditures under the Trust Agreement, including but not limited to payments due any provider of a Reserve Fund Credit Facility or Certificate Reserve Fund investment which provides for such payments, advances to and fees and expenses of accountants, agents, appraisers, consultants or other experts, and counsel not directly employed by the Trustee but an attorney or firm of attorneys retained by the Trustee, employed by it in the exercise and performance of its rights and obligations under the Trust Agreement; *provided, however,* that the Trustee shall not have any lien for such compensation or reimbursement against any moneys held by it in any of the funds or accounts established under the Trust Agreement or under either Sublease (except that such compensation or reimbursement may be made from the Cost of Issuance Fund held by the County to the extent provided in the Trust Agreement or as provided in the Trust Agreement). The Trustee may take whatever legal actions are lawfully available to it directly against the County or the Corporation. The rights of the Trustee under the Trust Agreement are in addition to the rights granted to the Trustee pursuant to the Subleases.

Except as otherwise expressly provided in the Trust Agreement, no provision of the Trust Agreement shall require the Trustee to expend or risk its own funds or otherwise incur any financial liability in the performance of any of its duties under the Trust Agreement or in the exercise of any of its rights or powers under the Trust Agreement.

The County covenants and agrees to indemnify and save the Trustee and its officers, directors, agents and employees, harmless against any loss, expense and liabilities which it may incur arising out of or in the exercise and performance of its powers and duties under the Trust Agreement, including the costs of expenses of defending against any claim of liability including, without limitation, any claim arising out of the use, presence, storage, disposal or release of any Hazardous Substances on or about the Property, but excluding any and all losses, expenses and liabilities which are due to the negligence or intentional misconduct of the Trustee, its officers, directors, agents or employees. Such indemnity shall survive the discharge of the Trust Agreement or the resignation or removal of the Trustee.

Protection of the Trustee. The Trustee shall be protected and shall incur no liability in acting or proceeding in good faith upon any affidavit, bond, certificate, consent, opinion, notice, request, requisition, resolution, direction, instruction, statement, telegram, voucher, waiver or other paper or document which it shall in good faith believe to be genuine and to have been adopted, executed or delivered by the proper party or pursuant to any of the provisions of the Trust Agreement, and the Trustee shall be under no duty to make any investigation or inquiry as to any statements contained or matters referred to in any such instrument, but may accept and rely upon the same as conclusive evidence of the truth and accuracy of such statements. The Trustee shall not be bound to recognize any person as an Owner of any Certificate or Additional Certificate or to take any action at the request of any such person unless such Certificate or Additional Certificate shall be deposited with the Trustee or satisfactory evidence of the ownership of such Certificate or Additional Certificate shall be furnished to the Trustee. The Trustee shall be under no obligation to exercise any of the rights or powers vested in it by the Trust Agreement at the request or direction of any of the Owners of the Certificates or Additional Certificates pursuant to the Trust Agreement, unless such Owners shall have offered to the Trustee security or indemnity reasonably satisfactory to the Trustee, against the costs, expenses and liabilities which might be incurred by it in compliance with such request or direction. The Trustee may consult with counsel, who may be counsel to the County or the Corporation, with regard to legal questions, and the opinion of such counsel shall be full and complete authorization and protection in respect to any action taken or suffered

by it under the Trust Agreement in good faith in accordance therewith. If requested by the County, counsel to the Trustee shall be of recognized national standing in the field of law relating to municipal bonds.

The Trustee shall not be responsible for the sufficiency or adequacy of the Certificates or any Additional Certificates, the Leases, the Subleases, or of the assignment made to it by the Assignment Agreement, or for statements made in the preliminary or final official statement relating to the Certificates or any Additional Certificates, or of the title to or value of the Property.

The Trustee shall not be required to take notice or be deemed to have notice of any default or Event of Default under the Trust Agreement or an Event of Default under the Trust Agreement, except failure of any of the payments to be made to the Trustee required to be made under the Trust Agreement unless the Trustee shall be specifically notified in writing of such default or Event of Default by the County, the Corporation or by the Owners of not less than 25% in aggregate principal amount represented by the Certificates and Additional Certificates then Outstanding.

Whenever in the administration of its rights and obligations under the Trust Agreement the Trustee shall deem it necessary or desirable that a matter be proved or established prior to taking or suffering any action under the Trust Agreement, such matter (unless other evidence in respect thereof be specifically prescribed in the Trust Agreement) may be deemed to be conclusively proved and established by a Certificate of the County, and such certificate shall be full warrant to the Trustee for any action taken or suffered under the provisions of the Trust Agreement upon the faith thereof, but in its discretion the Trustee may, in lieu thereof, accept other evidence of such matter or may require such additional evidence as to it may seem reasonable.

The Trustee may buy, sell, own, hold and deal in any of the Certificates and Additional Certificates and may join in any action which any Owner may be entitled to take with like effect as if the Trustee were not a party to the Trust Agreement. The Trustee, either as principal or agent, may also engage in or be interested in any financial or other transaction with the County or the Corporation, and may act as agent, depository or trustee for any committee or body of Owners or of owners of obligations of the Corporation or the County as freely as if it were not the Trustee under the Trust Agreement.

The Trustee may, to the extent reasonably necessary, execute any of the trusts or powers of the Trust Agreement and perform any rights and obligations required of it under the Trust Agreement by or through agents, attorneys or receivers, and shall be entitled to advice of counsel concerning all matters of trust and its rights and obligations under the Trust Agreement, and the Trustee shall not be answerable for the default or misconduct of any such agent, attorney or receiver selected by it with reasonable care. The Trustee shall not be liable for any error of judgment made by it in good faith unless it shall be proved that the Trustee was negligent in ascertaining the pertinent facts.

The Trustee shall not be answerable for the exercise of any trusts or powers under the Trust Agreement or for anything whatsoever in connection with the funds established under the Trust Agreement, except only for its own willful misconduct or negligence.

The Trustee shall not be liable with respect to any action taken or omitted to be taken by it in accordance with the direction of the Owners of not less than a majority (or other percentage provided for in the Trust Agreement) in aggregate principal amount of the Certificates at the time Outstanding relating to the exercise of any right or remedy available to the Trustee under the Trust Agreement.

The Trustee makes no representation or warranty, express or implied as to the title, value, design, compliance with specifications or legal requirements, quality, durability, operation, condition,

merchantability or fitness for any particular purpose or fitness for the use contemplated by the County of the Property. In no event shall the Trustee be liable for incidental, indirect, special or consequential damages in connection with or arising from the Subleases, the Leases or the Trust Agreement for the existence, furnishing or use of the Property.

Every provision of the Trust Agreement, the Leases, the Subleases and the Assignment Agreement relating to the conduct or liability of the Trustee shall be subject to the provisions of the Trust Agreement.

In acting as Trustee under the Trust Agreement, the Trustee acts solely in its capacity as Trustee for the Owners and not in its individual or personal capacity, and all persons, including without limitation, the Owners, the County and the Corporation, having any claim against the Trustee shall look only to the funds and accounts held by the Trustee under the Trust Agreement for payment, except as otherwise specifically provided in the Trust Agreement. Under no circumstances shall the Trustee be liable in its individual capacity for the obligations evidenced by the Certificates.

The recitals of facts, covenants and agreements in the Trust Agreement and in the Certificates shall be taken as statements, covenants and agreements of the County or the Corporation, as the case may be, and the Trustee assumes no responsibility for the correctness of the same.

Amendment of or Supplement to Trust Agreement

Amendment or Supplement. The Trust Agreement and the rights and obligations of the County, the Corporation, the Owners and the Trustee under the Trust Agreement may be amended or supplemented at any time by an amendment of the Trust Agreement or supplement to the Trust Agreement which shall become binding when the written consents of the Owners of a majority in aggregate principal amount of the Certificates and Additional Certificates then Outstanding, exclusive of Certificates and Additional Certificates disqualified as provided in the Trust Agreement, are filed with the Trustee. No such amendment or supplement shall (1) extend the Principal Payment Date of any Certificate or Additional Certificate or reduce the rate of interest represented thereby or extend the time of payment of such interest or reduce the amount of principal represented thereby or reduce the amount of any Mandatory Sinking Account Payment without the prior written consent of the Owner of each Certificate and Additional Certificate so affected, or (2) reduce the percentage of Owners whose consent is required for the execution of any amendment of the Trust Agreement or supplement to the Trust Agreement without the prior written consent of the Owners of all Certificates or Additional Certificates then Outstanding, or (3) modify any of the rights or obligations of the Trustee without its prior written consent thereto, (4) modify any provision of the Trust Agreement expressly recognizing or granting rights in or to the Insurer in any manner which affects the rights of the Insurer under the Trust Agreement without its prior written assent thereto or (5) amend the provisions of the Trust Agreement described by the provisions of the Trust Agreement described under the caption "—Amendment or Supplement" without the prior written consent of the Owners of all Certificates or Additional Certificates then Outstanding.

The Trust Agreement and the rights and obligations of the County, the Corporation, the Owners and the Trustee under the Trust Agreement may also be amended or supplemented at any time by an amendment of the Trust Agreement or supplement to the Trust Agreement which shall become binding upon execution, but without the written consents of any Owners, but only to the extent permitted by law and after receipt of an unqualified approving Opinion of Counsel and only for any one or more of the following purposes:

(a) to add to the agreements, conditions, covenants and terms required to be observed or performed in the Trust Agreement by the County or the Corporation, or to surrender any right or power reserved in the Trust Agreement to or conferred in the Trust Agreement on the County or the Corporation, and which in either case shall not materially adversely affect the interests of the Owners; or

(b) to provide for additional or substitute Property as may be requested from time to time by the County in accordance with the Sublease; or

(c) to make such provisions for the purpose of curing any ambiguity or of correcting, curing or supplementing any defective provision contained in the Trust Agreement or in regard to questions arising under the Trust Agreement which the County or the Corporation may deem desirable or necessary and not inconsistent with the Trust Agreement, and which shall not materially adversely affect the interests of the Owners; or

(d) to provide for the execution and delivery of Additional Certificates in accordance with the Trust Agreement; or

(e) for any other reason, provided such amendment or supplement does not materially adversely affect the interests of the Owners or the Insurer, provided further that the County, the Corporation and the Trustee may rely in entering into any such amendment or supplement upon an Opinion of Counsel stating that the requirements of this subsection (e) have been met with respect to such amendment or supplement.

Any provision of the Trust Agreement expressly recognizing or granting rights in or to the Insurer may not be amended in any manner which affects the rights of the Insurer under the Trust Agreement without the prior written consent of the Insurer.

Disqualified Certificates. Certificates and Additional Certificates actually known by the Trustee to be owned or held by or for the account of the County (but excluding Certificates and Additional Certificates held in any pension or retirement fund of the County) shall not be deemed Outstanding for the purpose of any consent or other action or any calculation of Outstanding Certificates and Additional Certificates provided in the Trust Agreement, and shall not be entitled to consent to or take any other action provided in this Article, and the Trustee may adopt appropriate regulations to require each Owner, before his consent provided for in the Trust Agreement shall be deemed effective, to reveal if the Certificates and Additional Certificates as to which such consent is given are disqualified as provided in this paragraph.

Endorsement or Replacement of Certificates After Amendment or Supplement. After the effective date of any action taken as provided in the Trust Agreement, the Trustee may determine that the Certificates and Additional Certificates may bear a notation by endorsement in form approved by the Trustee as to such action, and in that case upon demand of the Owner of any Outstanding Certificate or Additional Certificate and presentation of such Certificate or Additional Certificate for such purpose at the Principal Corporate Trust Office of the Trustee a suitable notation as to such action shall be made on such Certificate or Additional Certificate. If the Trustee shall receive an Opinion of Counsel advising that new Certificates or Additional Certificates modified to conform to such action are necessary, modified Certificates or Additional Certificates shall be prepared, and in that case upon demand of the Owner of any Outstanding Certificates or Additional Certificates such new Certificates or Additional Certificates shall be exchanged at the Principal Corporate Trust Office of the Trustee, without cost to each Owner for Certificates or Additional Certificates then Outstanding upon surrender of such Outstanding Certificates or Additional Certificates.

Amendment by Mutual Consent. The amendment provisions of the Trust Agreement shall not prevent any Owner from accepting any amendment as to the particular Certificates or Additional Certificates owned by him, provided that due notation thereof is made on such Certificates or Additional Certificates.

Opinion of Counsel. In executing any amendment or supplement to the Trust Agreement, the Trustee may conclusively rely upon an Opinion of Counsel to the effect that all conditions precedent for the execution of an amendment or supplement to the Trust Agreement have been satisfied.

Defeasance

Discharge of Certificates and Trust Agreement. (a) If the Trustee shall pay or cause to be paid or there shall otherwise be paid to the Owners of all Outstanding Certificates and Additional Certificates the interest and principal represented thereby at the times and in the manner stipulated therein, then such Owners shall cease to be entitled to the pledge of and lien on the Base Rental Payments as provided in the Trust Agreement, and all agreements and covenants of the County, the Corporation and the Trustee to such Owners under the Trust Agreement shall thereupon cease, terminate and become void and shall be discharged and satisfied.

(b) Any Outstanding Certificates or Additional Certificates shall, prior to the maturity or prepayment date thereof, be deemed to have been paid within the meaning and with the effect expressed in the Trust Agreement if (i) in case said Certificates or Additional Certificates are to be prepaid on any date prior to their maturity, the County shall have given to the Trustee in form satisfactory to the Trustee irrevocable instructions to mail, in accordance with the provisions of the Trust Agreement, notice of prepayment of such Certificates or Additional Certificates on said prepayment date, (ii) there shall have been deposited with the Trustee either moneys in an amount which shall be sufficient, or Defeasance Securities which are not callable or subject to prepayment prior to their respective maturity dates, the principal of and the interest on which when due, and without any reinvestment thereof, will provide moneys which, together with the moneys, if any, deposited with or held by the Trustee at the same time, shall be sufficient (as verified by a report of an independent certified public accountant or other independent financial consultant), to pay when due the principal or prepayment price (if applicable) of, and interest due and to become due on, said Certificates or Additional Certificates on and prior to the prepayment date or maturity date thereof, as the case may be, and (iii) in the event any of said Certificates or Additional Certificates are not to be prepaid within the next succeeding 60 days, the County shall have given the Trustee in form satisfactory to the Trustee irrevocable instructions to mail, as soon as practicable in the same manner as a notice of prepayment is mailed pursuant to the Trust Agreement, a notice to the Owners of such Certificates or Additional Certificates and to the securities depositories and information services specified in the Trust Agreement that the deposit required by (ii) above has been made with the Trustee and that said Certificates or Additional Certificates are deemed to have been paid in accordance with the Trust Agreement and stating such maturity or prepayment dates upon which moneys are to be available for the payment of the principal or prepayment price (if applicable) of said Certificates or Additional Certificates. Neither the securities nor moneys deposited with the Trustee pursuant to this paragraph nor principal or interest payments on any such securities shall be withdrawn or used for any purpose other than, and shall be held in trust for, the payment of the principal or prepayment price (if applicable) of, and interest on said Certificates or Additional Certificates; provided that Defeasance Securities deposited with the Trustee pursuant to this paragraph may be sold upon the written request of the County and the proceeds concurrently reinvested in other Defeasance Securities which satisfy the conditions of (ii) above provided that the Trustee receives an Opinion of Counsel to the effect that such sale and reinvestment does not adversely affect the exclusion of interest on the Certificates and Additional Certificates from federal income taxes, and provided further that any cash received from such principal or interest payments on such obligations deposited with the Trustee, if not then needed for such

purpose, shall, to the extent practicable, and at the direction of the County, be reinvested in Defeasance Securities maturing at times and in amounts, together with the other moneys and payments with respect to securities then held by the Trustee pursuant to this paragraph, sufficient to pay when due the principal or prepayment price (if applicable) of, and interest to become due with respect to said Certificates or Additional Certificates on and prior to such prepayment date or maturity date thereof, as the case may be, and interest earned from such reinvestments shall, upon receipt by the Trustee of a Written Request of the County, be paid over to the County, as received by the Trustee, free and clear of any trust, lien or pledge. Nothing in this paragraph shall preclude prepayments pursuant to the Trust Agreement.

Any release under this subsection (b) shall be without prejudice to the right of the Trustee to be paid reasonable compensation for all services rendered by it under the Trust Agreement and all its reasonable expenses, charges and other disbursements and those of its attorneys, agents and employees, incurred on and about the administration of trusts by the Trust Agreement created and the performance of its powers and duties under the Trust Agreement; provided however, that the Trustee shall have no right, title or interest in, or lien on, any moneys or securities deposited pursuant to the Trust Agreement.

(c) After the payment or deemed payment of all the interest and principal represented by all Outstanding Certificates and Additional Certificates as provided in the Trust Agreement, the Trustee shall execute and deliver to the Corporation and the County all such instruments as may be necessary or desirable to evidence the discharge and satisfaction of the Trust Agreement, and the Trustee shall pay over or deliver to the County all moneys or securities held by it pursuant to the Trust Agreement which are not required for the payment of the interest and principal represented by such Certificates and Additional Certificates. Notwithstanding the discharge and satisfaction of the Trust Agreement, Owners of Certificates and Additional Certificates shall thereafter be entitled to payments due under the Certificates and Additional Certificates pursuant to the Subleases, but only from amounts deposited pursuant to the Trust Agreement and from no other source.

(d) In the event that the principal, interest, or both due on the Certificates shall be paid by the Insurer pursuant to the Financial Guaranty Insurance Policy, the Certificates shall not be considered paid by the County or the Corporation under the Trust Agreement, and all covenants, agreements and other obligations of the Corporation and the County to the benefit of the Owners shall continue to exist and shall run to the benefit of the Insurer and the Insurer shall be subrogated to the rights of the Owners.

Unclaimed Moneys. Anything contained in the Trust Agreement to the contrary notwithstanding, any moneys held by the Trustee in trust for the payment and discharge of the interest or principal represented by any of the Certificates or Additional Certificates which remain unclaimed for two years after the date when the payments represented by such Certificates or Additional Certificates have become payable, if such moneys were held by the Trustee at such date, or for two years after the date of deposit of such moneys if deposited with the Trustee after the date when the interest and principal represented by such Certificates or Additional Certificates have become payable, shall be repaid by the Trustee to the County as its absolute property free from trust, and the Trustee shall thereupon be released and discharged with respect thereto and the Owners shall look only to the County for the payment of the interest and principal represented by such Certificates or Additional Certificates; *provided, however,* that before being required to make any such payment to the County, the Trustee shall mail a notice to the Owner that such unclaimed funds shall be returned to the County within 30 days.

Municipal Bond Insurance Policy

Insurer Deemed Owner. For the purposes of (i) the giving of consents to amendments to the Trust Agreement, (ii) the giving of any other consent of the Owners under the Trust Agreement, and (iii) the control and direction of all rights and remedies upon the occurrence of an Event of Default, the

Insurer shall be deemed to be the sole Owner of the Certificates for so long as it has not failed to comply with its payment obligations under the Financial Guaranty Insurance Policy; provided, however, that, notwithstanding the foregoing, the Insurer shall not be deemed to be the Owner of the Certificates for any consent to an amendment to the Trust Agreement that (1) extends the Principal Payment Date of any Certificate or reduces the rate of interest represented thereby or extends the time of payment of such interest or reduces the amount of principal represented thereby or reduces the amount of any Mandatory Sinking Account Payment, (2) reduces the percentage of Owners whose consent is required for the execution of any amendment of or supplement to the Trust Agreement, or (3) amends the provisions of the Trust Agreement under the caption "—Amendment of or Supplement to Trust Agreement."

Consent of Insurer in the Event of Insolvency. So long as the Insurer is not in default under the Financial Guaranty Insurance Policy, any reorganization or liquidation plan with respect to the County must be acceptable to the Insurer. In the event of any reorganization or liquidation, the Insurer shall have the right to vote on behalf of all Owners who hold Certificates absent a default under the Financial Guaranty Insurance Policy.

Exercise of Remedies Upon Default. Notwithstanding anything to the contrary in the Trust Agreement, so long as the Insurer is not in default under the Financial Guaranty Insurance Policy, upon the occurrence and continuance of an Event of Default as defined in the Trust Agreement, the Insurer shall be entitled to control and direct the enforcement of all rights and remedies granted to the Owners or the Trustee for the benefit of the Owners under the Trust Agreement.

Limitation on Modification. Any provision of the Trust Agreement expressly recognizing or granting rights in or to the Insurer may not be amended in a manner which affects the rights of the Insurer under the Trust Agreement without the prior written consent of the Insurer.

Effect of Financial Guaranty Insurance Policy. Notwithstanding any other provision of the Trust Agreement, in determining whether any actions taken pursuant to the terms and provisions of the Trust Agreement or under either Sublease are adverse to the interests of the Owners of the Certificates, the effect on the Owners shall be considered as if there were no Financial Guaranty Insurance Policy.

Insurer as Third Party Beneficiary. To the extent that the Trust Agreement confers upon or gives or grants to the Insurer any right, remedy or claim under or by reason of the Trust Agreement, the Insurer is explicitly recognized as being a third-party beneficiary under the Trust Agreement and may enforce any such right, remedy or claim conferred, given or granted under the Trust Agreement.

Miscellaneous

Benefits of Trust Agreement Limited to Parties. Nothing contained in the Trust Agreement, expressed or implied, is intended or shall be construed to confer upon, or to give or grant to, any person or entity other than the County, the Corporation, the Trustee, the Insurer and the Owners, any right, remedy or claim under or by reason of the Trust Agreement or any covenant, condition or stipulation of the Trust Agreement, and all covenants, stipulations, promises and agreements in the Trust Agreement contained by and on behalf of the County or the Corporation shall be for the sole and exclusive benefit of the County, the Corporation, the Trustee, the Insurer and the Owners.

Execution of Documents by Owners. Any declaration, request or other instrument which is permitted or required in the Trust Agreement to be executed by Owners may be in one or more instruments of similar tenor and may be executed by Owners in person or by their attorneys appointed in writing. The fact and date of the execution by any Owner or his attorney of any declaration, request or other instrument or of any writing appointing such attorney may be proved by the certificate of any notary

public or other officer authorized to take acknowledgments of deeds to be recorded in the state or territory in which he purports to act that the person signing such declaration, request or other instrument or writing acknowledged to him the execution thereof, or by an affidavit of a witness of such execution duly sworn to before such notary public or other officer, or by such other proof as the Trustee may accept which it may deem sufficient.

The ownership of any Certificate or Additional Certificate and the amount, payment date, number and date of owning the same may be proved by the books required to be kept by the Trustee pursuant to the provisions of the Trust Agreement.

Any declaration, consent, request or other instrument in writing of the Owner of any Certificate or Additional Certificate shall bind all future Owners of such Certificate or Additional Certificate with respect to anything done or suffered to be done by the County, the Corporation or the Trustee in good faith and in accordance therewith.

Waiver of Personal Liability. Notwithstanding anything contained in the Trust Agreement to the contrary, no member, officer, employee or agent of the County, the Corporation or the Trustee shall be individually or personally liable for the payment of any moneys, including without limitation, the interest or principal represented by the Certificates and Additional Certificates, but nothing contained in the Trust Agreement shall relieve any member, officer, employee or agent of the County from the performance of any official duty provided by any applicable provisions of law or by the Leases, the Subleases or the Trust Agreement.

Acquisition of Certificates by County. All Certificates and Additional Certificates acquired by the County, whether by purchase or gift or otherwise, shall be surrendered to the Trustee for cancellation.

Content of Certificates. Every Certificate of the County or Corporation with respect to compliance with any agreement, condition, covenant or term contained in the Trust Agreement shall include (a) a statement that the person or persons making or giving such certificate have read such agreement, condition, covenant or term and the definitions in the Trust Agreement relating thereto; (b) a brief statement as to the nature and scope of the examination or investigation upon which the statements contained in such certificate are based; (c) a statement that, in the opinion of the signers, they have made or caused to be made such examination or investigation as is necessary to enable them to express an informed opinion as to whether or not such agreement, condition, covenant or term has been complied with; and (d) a statement as to whether, in the opinion of the signers, such agreement, condition, covenant or term has been complied with.

Any Certificate of the County or the Corporation may be based, insofar as it relates to legal matters, upon an Opinion of Counsel unless the person making or giving such certificate knows that the Opinion of Counsel with respect to the matters upon which his certificate may be based, as aforesaid, is erroneous, or in the exercise of reasonable care should have known that the same was erroneous. Any Opinion of Counsel may be based, insofar as it relates to factual matters, upon information with respect to which is in the possession of the County upon a representation by an officer or officers of the County, unless the counsel executing such Opinion of Counsel knows that the representation with respect to the matters upon which his opinion may be based, as aforesaid, is erroneous, or in the exercise of reasonable care should have known that the same was erroneous.

Publication for Successive Weeks. Any publication required to be made under the Trust Agreement for two successive weeks in a Financial Newspaper may be made in each instance upon any Business Day of the first week and need not be made on the same Business Day of any succeeding week

or in the same Financial Newspaper for any subsequent publication, but may be made on different Business Days or in different Financial Newspapers, as the case may be.

Funds. Any fund required to be established and maintained in the Trust Agreement by the County or the Trustee may be established and maintained in the accounting records of the County or the Trustee either as an account or a fund, and may, for the purposes of such accounting records, any audits thereof and any reports or statements with respect thereto, be treated either as an account or a fund; but all such records with respect to all such funds shall at all times be maintained in accordance with sound accounting practice and with due regard for the protection of the security of the Certificates and the rights of the Owners. The Trustee may establish such funds and accounts as it deems necessary to perform its obligations under the Trust Agreement.

The County and the Trustee may commingle any of the moneys held by it under the Trust Agreement for investment purposes only; *provided, however,* that the County and the Trustee shall account separately for the moneys in each fund or account established pursuant to the Trust Agreement.

Investments. Any moneys held by the County in the funds and accounts established under the Trust Agreement shall be invested only in Permitted Investments. Any moneys held by the Trustee in the funds and accounts established under the Trust Agreement shall be invested by the Trustee upon the written request of the County Treasurer only in Permitted Investments. In the absence of such direction, moneys shall be invested by the Trustee solely in Permitted Investments set forth in clause (6) of the definition thereof. The Trustee shall not be liable or responsible for any loss suffered in connection with any such investment made by it under the terms of and in accordance with this paragraph. The Trustee may sell or present for redemption any obligations so purchased whenever it shall be necessary in order to provide moneys to meet any payment of the funds so invested, and the Trustee shall not be liable or responsible for any losses resulting from any such investment sold or presented for redemption. Any interest or profits on such investments in any funds and accounts (other than the Excess Earnings Account, the Construction Fund, and the Surplus Subaccount) established under the Trust Agreement shall be deposited in the Earnings Fund and are to be transferred as provided in the Trust Agreement. All investment earnings on the Construction Fund and the Surplus Subaccount shall be retained therein. For purposes of determining the amount on deposit in any fund or account under the Trust Agreement, all investments shall be valued annually at the amortized cost thereof (exclusive of accrued but unpaid interest, but inclusive of commissions). Investments in the Certificate Reserve Fund shall mature, or be subject to tender, redemption or withdrawal at the option of the holder thereof, not later than five years from the date of investment. Any Permitted Investments that are registrable securities shall be registered in the name of the Trustee, as trustee under the Trust Agreement.

California Law. The Trust Agreement shall be construed and governed in accordance with the laws of the State of California.

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APPENDIX D

BOOK-ENTRY SYSTEM

THE INFORMATION IN THIS APPENDIX D CONCERNING THE DEPOSITORY TRUST COMPANY, NEW YORK, NEW YORK AND ITS BOOK-ENTRY SYSTEM HAS BEEN OBTAINED FROM SOURCES THAT THE COUNTY AND THE CORPORATION BELIEVE TO BE RELIABLE, BUT THE COUNTY AND THE CORPORATION TAKE NO RESPONSIBILITY FOR THE ACCURACY THEREOF.

The Depository Trust Company, New York, New York ("DTC"), will act as securities depository for the Series 2006 Certificates. The Series 2006 Certificates will be issued as fully-registered securities registered in the name of Cede & Co. (DTC's partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered bond certificate will be issued for each maturity of the Series 2006 Certificates, each in the aggregate principal amount of such maturity, and will be deposited with DTC.

DTC is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of the New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934, as amended. DTC holds and provides asset servicing for over 2.2 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments from over 85 countries that DTC's participants ("Direct Participants") deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants' accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, credit providers, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation ("DTCC"). DTCC, in turn, is owned by a number of Direct Participants of DTC and Members of the National Securities Clearing Corporation, Government Securities Clearing Corporation, MBS Clearing Corporation, and Emerging Markets Clearing Corporation, ("NSCC," "GSCC," "MBSCC" and "EMCC," also subsidiaries of DTCC), as well as by the New York Stock Exchange, Inc., the American Stock Exchange LLC, and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, credit providers, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). DTC has Standard & Poor's highest rating: "AAA." The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtcc.com.

Purchases of Certificates under the DTC system must be made by or through Direct Participants, which will receive a credit for the Series 2006 Certificates on DTC's records. The ownership interest of each actual purchaser of each Series 2006 Certificate ("Beneficial Owner") is in turn to be recorded on the Direct and Indirect Participants' records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmation providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Series 2006 Certificates are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in the Series 2006 Certificates, except in the event that use of the book-entry system for the Series 2006 Certificates is discontinued.

To facilitate subsequent transfers, all Certificates deposited by Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of Certificates with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Series 2006 Certificates: DTC records reflect only the identity of the Direct Participants to whose accounts such Certificates are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time. The County, the Corporation, the Trustee and the Underwriters will not have any responsibility or obligation to such Direct Participants and Indirect Participants or the persons for whom they act as nominees with respect to the Series 2006 Certificates. Beneficial Owners of Certificates may wish to take certain steps to augment the transmission to them of notices of significant events with respect to the Series 2006 Certificates, such as redemptions, defaults, and proposed amendments to the bond documents. Beneficial Owners may wish to provide their names and addresses to the registrar and request that copies of notices be provided directly to them.

Redemption notices will be sent to DTC. If less than all of the Series 2006 Certificates within a maturity are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such issue to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to the Series 2006 Certificates unless authorized by a Direct Participant in accordance with DTC's Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the Trustee as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts the Series 2006 Certificates are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Principal and Interest payments on the Series 2006 Certificates will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the Trustee, on payable dates in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC nor its nominee, or the Trustee, subject to any statutory, or regulatory requirements as may be in effect from time to time. Payment of principal and interest to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the Trustee, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

DTC may discontinue providing its services as securities depository with respect to the Series 2006 Certificates at any time by giving reasonable notice to the Trustee. Under such circumstances, in the event that a successor securities depository is not obtained, bond certificates are required to be printed and delivered. The Corporation may decide to discontinue use of the system of book-entry-only transfers through DTC (or a successor securities depository). In that event, bond certificates will be printed and delivered to DTC.

THE COUNTY, THE CORPORATION, THE TRUSTEE AND THE UNDERWRITERS CANNOT AND DO NOT GIVE ANY ASSURANCES THAT DTC, DIRECT PARTICIPANTS OR INDIRECT PARTICIPANTS OF DTC WILL DISTRIBUTE TO THE BENEFICIAL OWNERS OF THE SERIES 2006 CERTIFICATES (I) PAYMENTS OF PRINCIPAL OF AND INTEREST ON THE SERIES 2006 CERTIFICATES (II) CONFIRMATIONS OF THEIR OWNERSHIP INTERESTS IN THE SERIES 2006 CERTIFICATES OR (III) OTHER NOTICES SENT TO DTC OR CEDE & CO., ITS PARTNERSHIP NOMINEE, AS THE REGISTERED OWNER OF THE SERIES 2006 CERTIFICATES, OR THAT THEY WILL DO SO ON A TIMELY BASIS, OR THAT DTC, DIRECT PARTICIPANTS OR INDIRECT PARTICIPANTS WILL SERVE AND ACT IN THE MANNER DESCRIBED IN THIS OFFICIAL STATEMENT.

NEITHER THE COUNTY, THE CORPORATION, THE TRUSTEE NOR THE UNDERWRITERS WILL HAVE ANY RESPONSIBILITY OR OBLIGATIONS TO DTC, THE DIRECT PARTICIPANTS, THE INDIRECT PARTICIPANTS OF DTC OR THE BENEFICIAL OWNERS WITH RESPECT TO (1) THE ACCURACY OF ANY RECORDS MAINTAINED BY DTC OR ANY DIRECT PARTICIPANTS OR INDIRECT PARTICIPANTS OF DTC; (2) THE PAYMENT BY DTC OR ANY DIRECT PARTICIPANTS OR INDIRECT PARTICIPANTS OF DTC OF ANY AMOUNT DUE TO ANY BENEFICIAL OWNER IN RESPECT OF THE PRINCIPAL AMOUNT OF OR INTEREST ON SERIES 2006 CERTIFICATES; (3) THE DELIVERY BY DTC OR ANY DIRECT PARTICIPANTS OR INDIRECT PARTICIPANTS OF DTC OF ANY NOTICE TO ANY BENEFICIAL OWNER THAT IS REQUIRED OR PERMITTED TO BE GIVEN TO OWNERS UNDER THE TERMS OF THE INDENTURE; OR (4) ANY CONSENT GIVEN OR OTHER ACTION TAKEN BY DTC AS OWNER OF THE SERIES 2006 CERTIFICATES.

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APPENDIX E

FORM OF SPECIAL COUNSEL OPINION

_____, 2006

County of San Diego
1600 Pacific Highway
San Diego, California 92101

County of San Diego
Certificates of Participation
(2006 Edgemoor Completion Project)
(Final Opinion)

Ladies and Gentlemen:

We have acted as special counsel to the County of San Diego (the "County") in connection with the execution and delivery of $42,390,000 aggregate principal amount of County of San Diego Certificates of Participation (2006 Edgemoor Completion Project) (the "Certificates"). In such connection, we have reviewed a Project Lease, dated as of February 1, 2005 (the "Project Lease") between the County and the San Diego County Capital Asset Leasing Corporation (the "Corporation"), a Project Sublease, dated as of February 1, 2005, as amended by a First Amendment to Project Sublease (the "First Amendment to Project Sublease"), dated as of December 1, 2006 (collectively, the "Project Sublease"), between the County and the Corporation, a Trust Agreement, dated as of February 1, 2005, as supplemented by a First Supplemental Trust Agreement (the "First Supplemental Trust Agreement"), dated as of December 1, 2006 (collectively, the "Trust Agreement"), among Zions First National Bank, as trustee (the "Trustee"), the County and the Corporation, a Tax Certificate of the County, dated the date hereof (the "Tax Certificate"), and an Assignment Agreement, dated as of February 1, 2005, as amended by a First Amendment to Assignment Agreement, dated as of December 1, 2006 (collectively, the "Assignment Agreement"), between the County and the Trustee, opinions of counsel to the County, the Corporation and the Trustee, certificates of the County, the Corporation, the Trustee and others and such other documents, opinions and matters to the extent we deemed necessary to render the opinions set forth herein. Capitalized terms not otherwise defined herein shall have the meanings ascribed thereto in the Trust Agreement.

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

The opinions expressed herein are based on an analysis of existing laws, regulations, rulings and court decisions and cover certain matters not directly addressed by such authorities. Such opinions may be affected

by actions taken or omitted or events occurring after the date hereof. We have not undertaken to determine, or to inform any person, whether any such actions are taken or omitted or events do occur or any other matters come to our attention after the date hereof. Our engagement with respect to the Certificates has concluded with their execution and delivery, and we disclaim any obligation to update this letter. We have assumed the genuineness of all documents and signatures presented to us (whether as originals or as copies) and the due and legal execution and delivery thereof by, and validity against, any parties other than the County. We have assumed, without undertaking to verify, the accuracy of the factual matters represented, warranted or certified in the documents, and of the legal conclusions contained in the opinions, referred to in the first paragraph hereof. Furthermore, we have assumed compliance with all covenants and agreements contained in the Trust Agreement, the Project Lease, the Project Sublease, the Assignment Agreement and the Tax Certificate, including (without limitation) covenants and agreements compliance with which is necessary to assure that future actions, omissions or events will not cause the interest portion of Base Rental Payments to be included in gross income for federal income tax purposes. We call attention to the fact that the rights and obligations under the Certificates, the Project Lease, the Project Sublease, the Trust Agreement, the Assignment Agreement, the Tax Certificate and their enforceability may be subject to bankruptcy, insolvency, reorganization, arrangement, fraudulent conveyance, moratorium and other laws relating to or affecting creditors' rights, to the application of equitable principles, to the exercise of judicial discretion in appropriate cases and to the limitations on legal remedies against counties in the State of California. We express no opinion with respect to any indemnification, contribution, penalty, choice of law, choice of forum, choice of venue, waiver or severability provisions contained in the foregoing documents, nor do we express any opinion with respect to the state or quality of title to or interest in any of the real or personal property described in or as subject to the liens of the Project Lease, the Project Sublease or the Trust Agreement or the accuracy or sufficiency of the description contained therein of, or the remedies available to enforce liens on, any such property. Finally, we undertake no responsibility for the accuracy, completeness or fairness of the Official Statement or other offering material relating to the Certificates and express no opinion with respect thereto.

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

1. The First Amendment to Project Sublease and the First Supplemental Trust Agreement have been duly executed and delivered by, and constitute valid and binding obligations of, the County.

2. The obligation of the County to make the Base Rental Payments during the term of the Project Sublease constitutes a valid and binding obligation of the County, payable from funds of the County lawfully available therefor.

3. Assuming due authorization, execution and delivery of the Trust Agreement and the Certificates by the Trustee, the Certificates are entitled to the benefits of the Trust Agreement.

4. The portion of each Base Rental Payment designated as and constituting interest paid by the County under the Project Sublease and received by the Owners of the Certificates is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986 and is exempt from State of California personal income taxes. Such interest is not a specific preference item for purposes of the federal individual or corporate alternative minimum taxes, although we observe that it is included in adjusted current earnings when calculating corporate alternative minimum taxable income. We express no opinion regarding other tax consequences related to the ownership or disposition of, or the accrual or receipt of such interest on, the Certificates.

Faithfully yours,

ORRICK, HERRINGTON & SUTCLIFFE LLP

per

APPENDIX F

SPECIMEN FINANCIAL GUARANTY INSURANCE POLICY

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Ambac

Financial Guaranty Insurance Policy

Ambac Assurance Corporation
One State Street Plaza, 15th Floor
New York, New York 10004
Telephone: (212) 668-0340

Obligor:

Policy Number:

Obligations:

Premium:

Ambac Assurance Corporation (Ambac), a Wisconsin stock insurance corporation, in consideration of the payment of the premium and subject to the terms of this Policy, hereby agrees to pay to The Bank of New York, as trustee, or its successor (the "Insurance Trustee"), for the benefit of the Holders, that portion of the principal of and interest on the above-described obligations (the "Obligations") which shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Obligor.

Ambac will make such payments to the Insurance Trustee within one (1) business day following written notification to Ambac of Nonpayment. Upon a Holder's presentation and surrender to the Insurance Trustee of such unpaid Obligations or related coupons, uncanceled and in bearer form and free of any adverse claim, the Insurance Trustee will disburse to the Holder the amount of principal and interest which is then Due for Payment but is unpaid. Upon such disbursement, Ambac shall become the owner of the surrendered Obligations and/or coupons and shall be fully subrogated to all of the Holder's rights to payment thereon.

In cases where the Obligations are issued in registered form, the Insurance Trustee shall disburse principal to a Holder only upon presentation and surrender to the Insurance Trustee of the unpaid Obligation, uncanceled and free of any adverse claim, together with an instrument of assignment, in form satisfactory to Ambac and the Insurance Trustee duly executed by the Holder or such Holder's duly authorized representative, so as to permit ownership of such Obligation to be registered in the name of Ambac or its nominee. The Insurance Trustee shall disburse interest to a Holder of a registered Obligation only upon presentation to the Insurance Trustee of proof that the claimant is the person entitled to the payment of interest on the Obligation and delivery to the Insurance Trustee of an instrument of assignment, in form satisfactory to Ambac and the Insurance Trustee, duly executed by the Holder or such Holder's duly authorized representative, transferring to Ambac all rights under such Obligation to receive the interest in respect of which the insurance disbursement was made. Ambac shall be subrogated to all of the Holders' rights to payment on registered Obligations to the extent of any insurance disbursements so made.

In the event that a trustee or paying agent for the Obligations has notice that any payment of principal of or interest on an Obligation which has become Due for Payment and which is made to a Holder by or on behalf of the Obligor has been deemed a preferential transfer and theretofore recovered from the Holder pursuant to the United States Bankruptcy Code in accordance with a final, nonappealable order of a court of competent jurisdiction, such Holder will be entitled to payment from Ambac to the extent of such recovery if sufficient funds are not otherwise available.

As used herein, the term "Holder" means any person other than (i) the Obligor or (ii) any person whose obligations constitute the underlying security or source of payment for the Obligations who, at the time of Nonpayment, is the owner of an Obligation or of a coupon relating to an Obligation. As used herein, "Due for Payment", when referring to the principal of Obligations, is when the scheduled maturity date or mandatory redemption date for the application of a required sinking fund installment has been reached and does not refer to any earlier date on which payment is due by reason of call for redemption (other than by application of required sinking fund installments), acceleration or other advancement of maturity; and, when referring to interest on the Obligations, is when the scheduled date for payment of interest has been reached. As used herein, "Nonpayment" means the failure of the Obligor to have provided sufficient funds to the trustee or paying agent for payment in full of all principal of and interest on the Obligations which are Due for Payment.

This Policy is noncancelable. The premium on this Policy is not refundable for any reason, including payment of the Obligations prior to maturity. This Policy does not insure against loss of any prepayment or other acceleration payment which at any time may become due in respect of any Obligation, other than at the sole option of Ambac, nor against any risk other than Nonpayment.

In witness whereof, Ambac has caused this Policy to be affixed with a facsimile of its corporate seal and to be signed by its duly authorized officers in facsimile to become effective as its original seal and signatures and binding upon Ambac by virtue of the countersignature of its duly authorized representative.

President

AMBAC ASSURANCE CORPORATION
CORPORATE
SEAL
WISCONSIN

Secretary

Effective Date:

Authorized Representative

THE BANK OF NEW YORK acknowledges that it has agreed to perform the duties of Insurance Trustee under this Policy.

Form No.: 2B-0012 (1/01)

Authorized Officer of Insurance Trustee

SPECIMEN

Ambac

Ambac Assurance Corporation
One State Street Plaza, 15th Floor
New York, New York 10004
Telephone: (212) 668-0340

Endorsement

Policy for:

Attached to and forming part of Policy No.:

Effective Date of Endorsement:

SPECIMEN

In the event that Ambac Assurance Corporation were to become insolvent, any claims arising under the Policy would be excluded from coverage by the California Insurance Guaranty Association, established pursuant to the laws of the State of California.

Nothing herein contained shall be held to vary, alter, waive or extend any of the terms, conditions, provisions, agreements or limitations of the above mentioned Policy other than as above stated.

In Witness Whereof, Ambac has caused this Endorsement to be affixed with a facsimile of its corporate seal and to be signed by its duly authorized officers in facsimile to become effective as its original seal and signatures and binding upon Ambac by virtue of the countersignature of its duly authorized representative.

Ambac Assurance Corporation

President

AMBAC ASSURANCE CORPORATION
CORPORATE
SEAL
WISCONSIN

Secretary

Authorized Representative

Form No.: 2B-0015 (7/97)

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COUNTY OF SAN DIEGO • CERTIFICATES OF PARTICIPATION (2006 EDGEMOOR COMPLETION PROJECT)

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