

**CITY AND COUNTY OF SAN FRANCISCO**  
**NOTES TO BASIC FINANCIAL STATEMENTS**  
**June 30, 2005**

**(1) THE FINANCIAL REPORTING ENTITY**

San Francisco is a city and county chartered by the State of California and as such can exercise the powers as both a city and a county under state law. As required by generally accepted accounting principles, the accompanying financial statements present the City and County of San Francisco (the City or Primary Government) and its component units. The component units discussed below are included in the City's reporting entity because of the significance of their operations or financial relationships with the City.

As a government agency, the City is exempt from both federal income taxes and California State franchise taxes.

***Blended Component Units***

Following is a description of those legally separate component units for which the City is financially accountable that are blended with the Primary Government because of their individual governance or financial relationships to the City.

*San Francisco County Transportation Authority (Authority)* - The voters of the City created the Authority in 1989 to impose a voter-approved sales and use tax of one-half of one percent to fund essential traffic and transportation projects. A Board consisting of the eleven members of the City's Board of Supervisors serving ex officio governs the Authority. The operations of the Authority are reported within other governmental funds. Financial statements for the Authority can be obtained from their administrative offices at 100 Van Ness Avenue, 25<sup>th</sup> Floor, San Francisco, CA 94102.

*San Francisco Finance Corporation (Finance Corporation)* - The Finance Corporation was created in 1990 by a vote of the electorate to allow the City to lease-purchase \$20 million (plus 5% per year growth) of equipment using tax-exempt obligations. Although legally separate from the City, the Finance Corporation is reported as if it were part of the primary government because its sole purpose is to provide lease financing to the City. The Finance Corporation is reported as an internal service fund. Financial statements for the Finance Corporation can be obtained from their administrative offices at City Hall, Room 336, 1 Dr. Carlton B. Goodlett Place, San Francisco, CA 94102.

*San Francisco Parking Authority (Parking Authority)* - The Parking Authority was created in October 1949 to provide services exclusively to the City. In accordance with Proposition D authorized by the City's electorate in November 1988, a City Charter amendment created the Parking and Traffic Commission (DPT). The DPT consists of five commissioners appointed by the mayor. Upon creation of the DPT, the responsibility to oversee the City's off-street parking operations was transferred from the Parking Authority to the DPT. The staff and fiscal operations of the Parking Authority were also incorporated into the DPT. Beginning on July 1, 2002, the responsibility for overseeing the operations of the DPT became the responsibility of the Municipal Transportation Agency (MTA) pursuant to Proposition E which was passed by the voters in November 1999. Separate financial statements are not prepared for the Parking Authority. Further information about the Parking Authority can be obtained from their administrative offices at 25 Van Ness Avenue, San Francisco, CA 94102.

***Discretely Presented Component Units***

*San Francisco Redevelopment Agency (Agency)* - The Agency is a public body, corporate and politic, organized and existing under the Community Redevelopment Law of the State of California. Seven commissioners who are appointed by the Mayor, subject to confirmation by the City's Board of Supervisors, govern it. The Agency has adopted as its mission the creation of affordable housing and economic development opportunities Citywide. Included in its financial data are the accounts of the San Francisco Redevelopment Financing Authority (SFRFA), a component unit of the Agency. The SFRFA is a separate joint-powers authority formed between the Agency and the City to facilitate the long-term financing of Agency activities. The Agency's governing commission serves as the Board of Directors of the SFRFA.

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In fiscal year 2001-2002, the Public Initiatives Development Corporation (PIDC) was formed to develop affordable housing on the Agency's behalf. The Board of PIDC is comprised of management of the Agency and other appointed individuals. Future funding will be dependent on the Agency and as such, PIDC is reported as a blended component unit of the Agency. Activities during the year are predevelopment activities including design and financing of a 106 affordable units mixed-use development, expected to be complete by December 2005.

The Agency's governing body is not substantively the same as that of the City, and the Agency does not provide services entirely or almost entirely to the City. The Agency is reported in a separate column to emphasize that it is legally separate from the City. The City is financially accountable for the Agency through the appointment of the Agency's Board and the ability of the City to approve the Agency's budget. Disclosures related to the Agency, where significant, are identified separately throughout these notes. Complete financial statements can be obtained from the Agency's administrative offices at 770 Golden Gate Avenue, San Francisco, CA 94102.

*Treasure Island Development Authority (TIDA)* - The TIDA is a nonprofit public benefit corporation. The TIDA was authorized in accordance with the Treasure Island Conversion Act of 1997 and designated as a redevelopment agency pursuant to Community Redevelopment Law of the State of California. Seven commissioners who are appointed by the Mayor, subject to confirmation by the City's Board of Supervisors, govern the TIDA. The specific purpose of the TIDA is to promote the planning, redevelopment, reconstruction, rehabilitation, reuse, and conversion of the property known as Naval Station Treasure Island for the public interest, convenience, welfare, and common benefit of the inhabitants of the City. The TIDA has adopted as its mission the creation of affordable housing and economic development opportunities on Treasure Island.

The TIDA's governing body is not substantively the same as that of the City it does not provide services entirely or almost entirely to the City. The TIDA is reported in a separate column to emphasize that it is legally separate from the City. The City is financially accountable for the TIDA through the appointment of the TIDA's Board and the ability of the City to approve the TIDA's budget. Disclosures related to the TIDA, where significant, are separately identified throughout these notes. Separate financial statements are not prepared for TIDA. Further information about TIDA can be obtained from their administrative offices at 410 Palm Avenue, Building 1, Room 223, Treasure Island, San Francisco, CA 94130.

***Non-Disclosed Organizations***

There are other governmental agencies that provide services within the City. These entities have independent governing boards and the City is not financially accountable for them. The City's basic financial statements, except for certain cash held by the City as an agent, do not reflect operations of the San Francisco Airport Improvement Corporation, San Francisco Health Authority, San Francisco Housing Authority, Private Industry Council of San Francisco, San Francisco Unified School District and San Francisco Community College District. The City is represented in two regional agencies, the Bay Area Rapid Transit District (BART) and the Bay Area Air Quality Management District (BAAQM), which are also excluded from the City's reporting entity.

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**(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**(a) Government-wide and fund financial statements**

The government-wide financial statements (i.e., the statement of net assets and the statement of changes in net assets) report information on all of the non-fiduciary activities of the primary government and its component units. For the most part, the effect of interfund activity has been removed from these statements. 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. Likewise, the primary government is reported separately from certain legally separate component units for which the primary government is financially accountable.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are 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.

Separate 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 basic financial statements include certain prior-year summarized comparative information. This information is presented only to facilitate financial analysis.

**(b) Measurement focus, basis of accounting, and financial statement presentation**

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting, as are the proprietary fund and fiduciary fund financial statements. Agency funds, however, report only assets and liabilities and cannot be said to have a measurement focus. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements have been met.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. The City considers property tax revenues to be available if they are collected within 60 days of the end of the current fiscal period. All other revenues are considered to be available if they are generally collected within 120 days of the end of the current fiscal period. It is the City's policy to submit reimbursement and claim requests for federal and state grant revenues within 30 days of the end of the program cycle and payment is generally received within the first or second quarter of the following fiscal year. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to vacation, sick leave, claims and judgments, are recorded only when payment is due.

Property taxes, other local taxes, grants and subventions, licenses, and interest associated with the current fiscal period are all considered susceptible to accrual and so have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when the City receives cash.

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The City reports the following major governmental fund:

The **General Fund** is the City's primary operating fund. It accounts for all financial resources of the City except those required to be accounted for in another fund.

The City reports the following major proprietary (enterprise) funds:

The **San Francisco International Airport Fund** accounts for the activities of the City-owned commercial service airport in the San Francisco Bay Area.

The **Water Department Fund** accounts for the activities of the San Francisco Water Department. The department is engaged in the distribution of water to the City and certain suburban areas.

The **Hetch Hetchy Water and Power Fund** accounts for the activities of Hetch Hetchy Water and Power Department (Hetch Hetchy). The department is engaged in the collection and conveyance of approximately 85% of the City's water supply and in the generation and transmission of electricity.

The **Municipal Transportation Agency Fund** accounts for the activities of the Municipal Transportation Agency (MTA). The MTA was established by Proposition E, passed by the City's voters in November 1999. The MTA includes the San Francisco Municipal Railway (MUNI), San Francisco Municipal Railway Improvement Corporation (SFMRIC), and the operations of the Parking and Traffic Commission (DPT), which includes the Parking Authority. MUNI was established in 1912 and is responsible for the operations of the City's public transportation system. SFMRIC is a nonprofit corporation established to provide capital financial assistance for the modernization of MUNI by acquiring, constructing, and financing improvements to the City's public transportation system. DPT is responsible for proposing and implementing street and traffic changes and oversees the City's off-street parking operations. DPT is a separate department of the MTA. The parking garages fund later accounted for the activities of various non-profit corporations formed by the Parking Authority to provide financial and other assistance to the City to acquire land, construct facilities, and manage various parking facilities.

The **General Hospital Medical Center Fund** accounts for the activities of the San Francisco General Hospital Medical Center, a City-owned acute care hospital.

The **Clean Water Program Fund** accounts for the activities of the Clean Water Program (CWP). It was created after the San Francisco voters approved a proposition in 1976, authorizing the City to issue \$240 million in bonds for the purpose of acquiring, construction, improving, and financing improvements to the City municipal sewage treatment and disposal system.

The **Port of San Francisco Fund** accounts for the activities of the Port of San Francisco. This was established in 1969 after the San Francisco voters approved a proposition to accept the transfer of the Harbor of San Francisco from the State of California.

The **Laguna Honda Hospital Fund** accounts for the activities of Laguna Honda Hospital, the City-owned skilled nursing facility which specializes in serving elderly and disabled residents.

Additionally, the City reports the following fund types:

The **Permanent Fund** accounts for resources that are legally restricted to the extent that only earnings, not principal, may be used for purposes that support specific programs.

The **Internal Service Funds** account for the financing of goods or services provided by one City department to another City department on a cost-reimbursement basis. Internal Service Funds account for the activities of the equipment maintenance services, centralized printing and mailing services, centralized telecommunications and information services, and lease financing through the Finance Corporation.

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The ***Pension and Other Employee Benefit Trust Funds*** reflect the activities of the Employees' Retirement System and the Health Service System. The Retirement System accounts for employee contributions, City contributions, and the earnings and profits from investments. It also accounts for the disbursements made for employee retirement benefits, withdrawals, disability and death benefits as well as administrative expenses. The Health Service System accounts for contributions from active and retired employees and surviving spouses, City contributions, and the earnings and profits from investments. It also accounts for the disbursements to various health plans and health care providers for the medical expenses of beneficiaries.

The ***Investment Trust Fund*** accounts for the external portion of the Treasurer's Office investment pool. The funds of the San Francisco Community College District, San Francisco Unified School District, and the Trial Courts are accounted for within the Investment Trust Fund.

The ***Agency Funds*** account for the resources held by the City in a custodial capacity on behalf of: the State of California, human welfare, community health and transportation programs.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in both the government-wide and proprietary fund financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. Governments also have the option of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The City has elected not to follow subsequent private-sector guidance.

In general, the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this rule are charges to other City Departments from the Water Department and Hetch Hetchy. These charges have not been eliminated because elimination would distort the direct costs and program revenues reported in the statement of activities.

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services in connection with the fund's principal ongoing operations. The principal operating revenues of the City's enterprise and internal service funds are charges for customer services including: water, sewer and power charges, public transportation fees, airline fees and charges, parking fees, hospital patient service fees, commercial and industrial rents, printing services, vehicle maintenance fees, and telecommunication and information system support charges. 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.

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

**(c) Budgetary Data**

The City adopts annual budgets for all governmental funds on a substantially modified accrual basis of accounting except for capital project funds and certain debt service funds which substantially adopt project length budgets.

The budget of the City is a detailed operating plan, which identifies estimated costs and results in relation to estimated revenues. The budget includes (1) the programs, projects, services, and activities to be provided during the fiscal year, (2) the estimated resources (inflows) available for appropriation, and (3) the estimated charges to appropriations. The budget represents a process through which policy decisions are deliberated, implemented, and controlled. The City Charter prohibits expending funds for which there is no legal appropriation.

The Administrative Code Chapter 3 outlines the City's general budgetary procedures, with Section 3.3 detailing the budget timeline. A summary of the key budgetary steps are summarized as follows:

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***Original Budget***

- (1) Departments and Commissions conduct hearings to obtain public comment on their proposed annual budgets beginning in December and submit their budget proposals to the Controller's Office no later than February 21.
- (2) The Controller's Office consolidates the budget estimates and transmits them to the Mayor's Office no later than the first working day of March. Staff of the Mayor's Office analyze, review and refine the budget estimates before transmitting the Mayor's Proposed Budget to the Board of Supervisors.
- (3) By the first working day of May, the Mayor submits the Proposed Budget for selected departments to the Board of Supervisors. The selected departments are determined by the Controller in consultation with the Board President and the Mayor's Budget Director. Criteria for selecting the departments include (1) that they are not supported by the City's General Fund or (2) that they do not rely on the State's budget submission in May for their revenue sources.
- (4) By the first working day of June, the Mayor submits the complete Proposed Budget to the Board of Supervisors along with a draft of the Annual Appropriation Ordinance prepared by the Controller's Office.
- (5) Within five working days of the Mayor's proposed budget transmission to the Board of Supervisors, the Controller reviews the estimated revenues and assumptions in the Mayor's Proposed Budget and provides an opinion as to their accuracy and reasonableness. The Controller also may make a recommendation regarding prudent reserves given the Mayor's proposed resources and expenditures.
- (6) The designated Committee (usually the Budget Committee) of the Board of Supervisors conducts hearings, hears public comment, and reviews the Mayor's Proposed Budget. The Committee recommends an interim budget reflecting the Mayor's budget transmittal and, by June 30, the Board of Supervisors passes an interim appropriation and salary ordinances.
- (7) Not later than the last working day of July, the Board of Supervisors adopts the budget through passage of the Annual Appropriation Ordinance, the legal authority for enactment of the budget.

***Final Budget***

The final budgetary data presented in the basic financial statements reflects the following changes to the original budget:

- (1) 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. In certain circumstances, other programs and regular annual appropriations may be carried forward after appropriate approval. Annually appropriated funds, not authorized to be carried forward, lapse at the end of the fiscal year. Appropriations carried forward from the prior year are included in the final budgetary data.
- (2) Appropriations may be adjusted during the year with the approval of the Mayor and the Board of Supervisors, e.g. supplemental appropriations. Additionally, the Controller is authorized to make certain transfers of surplus appropriations within a department. Such adjustments are reflected in the final budgetary data.

The Annual Appropriation Ordinance adopts the budget at the character level of expenditure within departments. As described above, the Controller is authorized to make certain transfers of appropriations within departments. Accordingly, the legal level of budgetary control by the Board of Supervisors is the department level.

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Budgetary data, as revised, is presented in the basic financial statements for the General Fund. Final budgetary data excludes the amount reserved for encumbrances for appropriate comparison to actual expenditures.

Generally, new or one-time federal and state grants, other capital projects, and debt issues are budgeted by the Mayor and the Board of Supervisors through a supplemental appropriation.

**(d) Deposits and Investments**

***Investment in the Treasurer's Pool***

The Treasurer invests on behalf of most funds of the City and external participants in accordance with the City's investment policy and the California State Government Code. The City Treasurer who reports on a monthly basis to the Board of Supervisors manages the Treasurer's pool. In addition, the function of the County Treasury Oversight Committee is to review and monitor the City's investment policy and to monitor compliance with the investment policy and reporting provisions of the law through an annual audit.

The Treasurer's investment pool consists of two components: 1) pooled deposits and investments and 2) dedicated investment funds. The dedicated investment funds represent restricted funds and relate to bond issuance of the Enterprise Funds and the General Fund's cash reserve requirement. In addition to the Treasurer's investment pool, the City has other funds that are held by trustees. These funds are related to the issuance of bonds and certain loan programs of the City. The investments of the Employees' Retirement System and deposits and investments of the Redevelopment Agency are held by trustees (note 5).

The San Francisco Unified School District, San Francisco Community College District, and the Trial Courts of the State of California are voluntary participants in the City's investment pool. As of June 30, 2005, \$321 million was held on behalf of these voluntary participants. The total percentage share of the Treasurer's pool that relates to these three external participants is 11.35%. The deposits held for these entities are included in the Investment Trust Fund. The City has not provided nor obtained any legally binding guarantees during the fiscal year ended June 30, 2005 to support the value of shares in the pool.

For reports on the external investment pool, contact the Office of the Treasurer, Room 140, City Hall, 1 Dr. Carlton B. Goodlett Place, San Francisco, CA 94102.

***Investment Valuation***

*Treasurer's Pool* - Substantially all investments are carried at fair value. The fair value of pooled investments is determined annually and is based on current market prices. The fair value of participants' position in the pool is the same as the value of the pool shares. The method used to determine the value of participants' equity withdrawn is based on the book value of the participants' percentage participation at the date of such withdrawal. In the event that a certain fund overdraws its share of pooled cash, the overdraft is reported as a due to the General Fund. Certain U.S. government securities that have a remaining maturity at time of purchase of one year or less are carried at amortized cost, which approximates market value.

*Employees' Retirement System (Retirement System)* - Investments are reported at fair value. Securities traded on national or international exchanges are valued at the last reported sales price at current exchange rates. Investments that do not have an established market price are reported at estimated fair value. Purchases and sales of investments are recorded on a trade date basis. The fair values of real estate holdings are estimated primarily on appraisals prepared by third-party appraisers. The fair values of venture capital investments are estimated based primarily on audited financial statements provided by the individual fund managers. Such market value estimates involve subjective judgments, and the actual market price of these investments can only be determined by negotiation between independent third parties in a sales transaction.

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The City Charter and Retirement System Board (Board) policies permit the Retirement System to use investments of the Retirement System's Pension Plan (the Plan) to enter into securities lending transactions. These are loans of securities to broker-dealers and other entities for collateral, with a simultaneous agreement to return collateral for the same securities in the future. Contracts with the lending agents require them to indemnify the Retirement System if the borrowers fail to return the securities (and if the collateral were inadequate to replace the securities lent) or if the borrowers fail to pay the Retirement System for income distributions by the securities issuers while the securities are on loan. Non-cash collateral cannot be pledged or sold unless the borrower defaults.

Either the Retirement System or the borrower can terminate all securities loans on demand, although the average term of the loans is sixty-five days. In lending domestic securities, cash collateral is invested in the lending agent's short-term investment pool, which at year-end had a weighted-average maturity of fifty-one days. In lending international securities, cash collateral is invested in a separate short-term investment pool, which at year-end had a weighted-average maturity of fourteen days. The relationship between the maturities of the investment pools and the Retirement System's loans is affected by the maturities of the securities loans made by other entities that use the agent's pool, which the Retirement System cannot determine. Cash collateral may also be invested separately in term loans, in which case the maturity of the loaned securities matches the term of the loan. Cash received as collateral on securities lending transactions is reported as an asset, and liabilities from these transactions are reported in the statement of net assets. Additionally, the costs of securities lending transactions, such as borrower rebates and fees, are recorded as expenses.

The City Charter and Board policies permit the Retirement System to use investments to enter into fixed coupon dollar repurchase agreements, that is, a sale of securities with a simultaneous agreement to repurchase similar securities in the future at a lower price that reflects a financing rate. The fair value of the securities underlying fixed coupon dollar repurchase agreements equals the cash received. If the dealers default on their obligations to resell these securities to the Retirement System at the agreed buy back price, the Retirement System could suffer an economic loss if the securities have to be purchased in the open market at a price higher than the agreed-upon buy back price. This credit exposure at June 30, 2005 was approximately \$95 thousand.

*Other funds* - Non-pooled investments are also generally carried at fair value. However, money market investments (such as short term, highly liquid debt instruments including commercial paper, bankers' acceptances, and U.S. Treasury and agency obligations), and participating interest-earning investment contracts (such as negotiable certificates of deposit, repurchase agreements and guaranteed or bank investment contracts) that have a remaining maturity at the time of purchase of one year or less are carried at amortized cost, which approximates market value. The fair value of non-pooled investments is determined annually and is based on current market prices. The fair value of investments in open-end mutual funds is determined based on the fund's current share price.

*Component Unit - San Francisco Redevelopment Agency* - Investments are stated at fair value except for money market investments with maturities of one year or less which have been stated at amortized cost. The fair value of investments has been obtained by using market quotes as of June 30, 2005.

***Investment Income***

Income from pooled investments is allocated at month end to the individual funds or external participants based on the fund or participant's average daily cash balance in relation to total pooled investments. City management has determined that the investment income related to certain funds should be allocated to the General Fund. On a budget basis, the interest income is recorded in the General Fund. On a generally accepted accounting principles (GAAP) basis, the income is reported in the fund where the related investments reside. A transfer is then recorded to transfer an amount equal to the interest earnings to the General Fund. This is the case for certain other governmental funds, Internal Service Funds, and Trust and Agency Funds.

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It is the City's policy to charge interest at month end to those funds that have a negative average daily cash balance. In certain instances, City management has determined that the interest expense related to the fund should be allocated to the General Fund. On a budget basis, the interest expense is recorded in the General Fund. On a GAAP basis, the interest expense is recorded in the fund and then a transfer from the General Fund for an amount equal to the interest expense is made to the fund. This is the case for certain other governmental funds, MTA, Laguna Honda Hospital, General Hospital Medical Center, and the Internal Service Funds.

Income from non-pooled investments is recorded based on the specific investments held by the fund. The interest income is recorded in the fund that earned the interest.

**(e) Loans Receivable**

For the purposes of the fund financial statements, the governmental funds expenditures relating to long-term loans arising from loan subsidy programs are charged to operations upon funding and the loans are recorded, net of an estimated allowance for potentially uncollectible loans, with an offset to a deferred credit account.

The Mayor's Office of Housing administers several housing programs and issues loans to qualified applicants. Many of these loans may be forgiven if certain terms and conditions of the loans are met. They are accounted for in the other governmental funds as long-term loans receivable with an allowance for forgivable loans, and an offsetting deferred credit account.

For purposes of the government-wide financial statements, long-term loans are not offset by deferred credit accounts.

**(f) Inventory**

Inventory recorded in the proprietary funds primarily consists of construction materials and maintenance supplies, as well as pharmaceutical supplies maintained by the hospitals. Generally, proprietary funds value inventory at cost or average cost and expense supply inventory as it is consumed. This is referred to as the consumption method of inventory accounting. The governmental fund types also use the purchase method to account for supply inventories, which are not material. This method records items as expenditures when they are acquired.

**(g) Redevelopment Agency Property Held for Resale**

Property held for resale is recorded as an asset at the lower of estimated cost or estimated conveyance value. Estimated conveyance value is management's estimate of net realizable value of a property based on current intended use.

**(h) Capital Assets**

Capital assets, which include land, facilities and improvements, machinery and equipment, and infrastructure assets, are reported in the applicable governmental or business-type activity columns in the government-wide financial statements. Capital assets are defined as assets with an initial individual cost of more than \$5,000 and an estimated useful life in excess of one year. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation. Capital outlay is recorded as expenditures of the General Fund and other governmental funds and as assets in the government-wide financial statements to the extent the City's capitalization threshold is met. Interest incurred during the construction phase of the capital assets of business-type activities is reflected in the capitalized value of the asset constructed, net of interest earned on the invested proceeds over the same period. Amortization of assets acquired under capital leases is included in depreciation and amortization. Facilities and improvements, infrastructure, machinery and equipment, and easements of the primary government, as well as the component units, are depreciated using the straight-line method over the following estimated useful lives:

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<u>Assets</u>	<u>Years</u>
Facilities and Improvements	15 to 175
Infrastructure	15 to 70
Machinery and Equipment	2 to 75
Easements	20

Works of art, historical treasures and zoological animals held for public exhibition, education, or research in furtherance of public service, rather than financial gain, are not capitalized. These items are protected, kept unencumbered, cared for and preserved by the City. It is the City's policy to utilize proceeds from the sale of these items for the acquisition of other items for collection and display.

**(i) Accrued Vacation and Sick Leave Pay**

Vacation pay, which may be accumulated up to ten weeks depending on an employee's length of service, is payable upon termination.

Sick leave may be accumulated up to six months, except for Local 21 members, who are all entitled to accumulate all unused sick leave. Unused amounts accumulated prior to December 6, 1978 are vested and payable upon termination of employment by retirement or disability caused by industrial accident or death. Effective July 1, 2002, the City established a pilot "Wellness Incentive Program" (the Program) to promote workforce attendance. The Program was initially negotiated as part of the July 1, 2001 to June 30, 2004 labor contract between the City and forty-one labor organizations, representing about 48% of the City's workforce. It is described in several Memorandums of Understanding (MOUs) dated since July 1, 2001, between the City and the affected labor organizations. Under the terms of these MOUs and the labor contracts, the Program is in effect from July 1, 2002 to at least June 30, 2005.

This Program provides:

Effective July 1, 2002, any full-time employee leaving the employment of the City upon service or disability retirement may receive payment for a portion of sick leave earned but unused at the time of separation. The amount of this payment shall be equal to 2.5% of sick leave balances earned but unused at the time of separation times the number of whole years of continuous employment times an employee's salary rate, exclusive of premiums or supplements, at the time of separation. Vested sick leave hours as described by Civil Service Commission rules, shall not be included in this computation.

The City accrues for all salary-related items, including the Program, in the government-wide and proprietary fund financial statements for which they are liable to make a payment directly and incrementally associated with payments made for compensated absences on termination. The City includes its share of social security and Medicare payments made on behalf of the employees in the accrual for vacation and sick leave pay.

**(j) Bond Issuance Costs, Premiums, Discounts and Interest Accretion**

In the government-wide financial statements and in the proprietary fund type 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 statement of net assets. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

In the fund financial statements, governmental funds recognize bond premiums and discounts as other financing sources and uses, respectively, and bond issuance costs as debt service expenditures. Issuance costs, whether or not withheld from the actual debt proceeds received are reported as debt service expenditures.

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Interest accreted on capital appreciation bonds is reported as accrued interest payable in the government-wide and proprietary fund financial statements.

**(k) Fund Equity**

***Reservations of Fund Equity***

Reservations of fund balances of the governmental funds indicate that portion of fund equity which is not available for appropriation for expenditure or is legally segregated for a specific future use. Following is a brief description of the nature of certain reserves.

*Reserve for rainy day* - The City's Charter requires that the City set aside funds into a reserve account in years in which revenue growth exceeds five percent compared to the year before. The City will be able to spend those funds in years in which revenues decline or grow by less than two percent.

*Reserve for assets not available for appropriation* - Certain assets, primarily cash and investments outside City Treasury and deferred charges, do not represent expendable available financial resources. Therefore, a portion of fund equity is reserved to offset the balance of these assets.

*Reserve for debt service* - The fund balance of the debt service funds is reserved for the payment of debt service in the subsequent year.

*Reserves for encumbrances* - Encumbrances are recorded as reservations of fund balances because they do not constitute expenditures or liabilities. In certain other governmental funds, this accounting treatment results in a deficit unreserved fund balance. This deficiency is carried forward to the next fiscal year where it is applied against estimated revenues in the year the commitments are expended.

*Reserve for appropriation carryforward* - At the end of the fiscal year, certain budgeted expenditures are authorized to be carried over and expended in the ensuing year. A reserve of fund balance is established in the amount of these budget authorizations.

*Reserve for subsequent years' budgets* - A portion of fund balance is reserved for subsequent years' budgets. This balance includes the reserve required by the City's Administrative Code for the budget incentive program for the purpose of making additional funds available for items and services that will improve the efficient operations of departments.

***Restricted Net Assets***

The government-wide and proprietary fund financial statements utilize a net assets presentation. Net assets are categorized as invested in capital assets (net of related debt), restricted, and unrestricted.

- *Invested in Capital Assets, Net of Related Debt* - This category groups all capital assets, including infrastructure, into one component of net assets. Accumulated depreciation and the outstanding balances of debt that are attributable to the acquisition, construction, or improvement of these assets reduce the balance in this category.
- *Restricted Net Assets* - This category represents net assets that have external restrictions imposed by creditors, grantors, contributors or laws or regulations of other governments and restrictions imposed by law through constitutional provisions or enabling legislation.
- *Unrestricted Net Assets* - This category represents net assets of the City, not restricted for any project or other purpose.

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***Designations of Fund Equity***

Designations of fund balances (note 4) indicate that portion of fund balance that is not available for appropriation based on management's plans for future use of the funds. Following is a brief description of the nature of the designation as of June 30, 2005.

*Designation for litigation and contingencies* - This designation represents management's estimate of anticipated legal settlements or contingencies to be paid in the subsequent fiscal year.

***Deficit Net Assets/Fund Balances***

The Telecommunications and Information Internal Service Fund had a \$2.1 million deficit in total net assets as of June 30, 2005. Approximately \$0.8 million of this deficit is due to current year depreciation that is not funded and will result in continuing deficits. The remaining portion of the deficit of total net assets relates to operations and is expected to be reduced in future years through anticipated rate increases or reductions in operating expenses.

The Central Shops Internal Service Fund had a \$0.3 million deficit as of June 30, 2005. The deficit is due to depreciation and certain non-current accrued expenses that are not funded and will result in continuing deficits in future years.

The Culture and Recreation Fund had a \$0.4 million deficit as of June 30, 2005. It is due to incurring costs for grant programs before receiving grant resources. It will be eliminated once the resources become available.

The Moscone Convention Center Fund had a \$5.2 million deficit as of June 30, 2005. The deficit will be covered as hotel tax revenues are realized.

**(l) Interfund Transfers**

Interfund transfers are generally recorded as transfers in (out) except for certain types of transactions that are described below.

- (1) Charges for services are recorded as revenues of the performing fund and expenditures of the requesting fund. Unbilled costs are recognized as an asset of the performing fund and a liability of the requesting fund at the end of the fiscal year.
- (2) Reimbursements for expenditures, initially made by one fund which are properly applicable to another fund, are recorded as expenditures in the reimbursing fund and as a reduction of expenditures in the fund that is reimbursed.

**(m) Refunding of Debt**

Gains or losses occurring from advance refundings, completed subsequent to June 30, 1993, are deferred and amortized into expense for both business-type activities and proprietary funds. For governmental activities, they are deferred and amortized into expense if they occurred subsequent to June 30, 2000.

**(n) Cash Flows**

Statements of cash flows are presented for proprietary fund types. Cash and cash equivalents include all unrestricted and restricted highly liquid investments with original purchase maturities of three months or less. Pooled cash and investments in the City's Treasury represent monies in a cash management pool and such accounts are similar in nature to demand deposits.

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**(o) Estimates**

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

**(p) Reclassifications**

Certain amounts presented as 2003-2004 Summarized Comparative Financial Information in the basic financial statements have been reclassified for comparative purposes to conform to the presentation in the 2004-2005 basic financial statements.

**(q) Effects of New Pronouncements**

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. The City implemented the new reporting requirements in the fiscal year 2004-2005 financial statements.

The City 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 City's fiscal year ending June 30, 2006. However, the Airport Enterprise Fund early implemented this statement in fiscal year 2004-2005 and reported an impairment loss of \$50 million.

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 City'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 City'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

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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 City'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*, which requires that limitations on the use of net assets imposed by enabling legislation be reported as restricted net assets. This statement clarifies that a legally enforceable enabling legislation restriction is one that a party external to a government – such as citizens, public interest groups, or the judiciary – can compel a government to honor. This statement also specifies the accounting and financial reporting requirements if new enabling legislation replaces existing enabling legislation or if legal enforceability is reevaluated. Finally, this statement requires governments to disclose the portion of total net assets that is restricted by enabling legislation. Application of this statement is effective for the City's fiscal year ending June 30, 2006.

In June 2004, GASB issued Statement No. 47, *Accounting for Termination Benefits*, which establishes accounting standards for termination benefits. More specifically, 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. Application of this statement is effective for the City in two parts. For termination benefits provided through an existing defined benefit OPEB plan, the provisions of this Statement will be implemented simultaneously with the requirements of statement 45, *Accounting and Financial Reporting by Employers for Post-employment Benefits Other Than Pensions*. For all other termination benefits, application of this statement is effective for the City's fiscal year ending June 30, 2006.

**(r) Restricted Assets**

Certain proceeds of the City's enterprise fund revenue bonds, as well as certain resources set aside for their repayment, are classified as restricted assets on the statement of net assets because the use of the proceeds is limited by applicable bond covenants and resolutions. Restricted assets account for the principal and interest amounts accumulated to pay debt service, unspent bond proceeds, and amounts restricted for future capital projects. In addition, certain grant proceeds are restricted by the granting agency.

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**(3) RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS**

**(a) Explanation of certain differences between the governmental fund balance sheet and the government-wide statement of net assets**

Total fund balances of the City's governmental funds, \$1,068,256, differ from net assets of governmental activities, \$1,501,082, reported in the statement of net assets. The difference primarily results from the long-term economic focus in the statement of net assets versus the current financial resources focus in the governmental fund balance sheets.

Balance Sheet/Statement of Net Assets (in thousands)

	Total Governmental Funds	Long-term Assets, Liabilities(1)	Internal Service Funds(2)	Reclassi- fications and Eliminations	Statement of Net Assets Totals
<b>Assets</b>					
Deposits and investments with City Treasury.....	\$ 1,230,154	\$ -	\$ 8,196	\$ -	\$ 1,238,350
Deposits and investments outside City Treasury.....	46,100	-	16,057	-	62,157
Receivables, net:					
Property taxes and penalties.....	33,031	-	-	-	33,031
Other local taxes.....	161,532	-	-	-	161,532
Federal and state grants and subventions.....	150,971	-	-	-	150,971
Charges for services.....	14,248	-	-	-	14,248
Interest and other.....	8,132	-	457	-	8,589
Due from other funds.....	42,046	-	2,301	(44,347)	-
Due from component unit.....	3,375	-	-	-	3,375
Loans receivable, net.....	242,902	-	-	-	242,902
Capital assets, net.....	-	2,367,571	4,155	-	2,371,726
Deferred charges and other assets.....	8,367	13,200	5,704	-	27,271
Total assets.....	<u>1,940,858</u>	<u>2,380,771</u>	<u>36,870</u>	<u>(44,347)</u>	<u>4,314,152</u>
<b>Liabilities</b>					
Accounts payable.....	135,859	-	7,237	-	143,096
Accrued payroll.....	48,541	-	1,385	-	49,926
Accrued vacation and sick leave pay.....	-	121,315	3,722	-	125,037
Accrued workers' compensation.....	-	213,654	1,151	-	214,805
Estimated claims payable.....	-	83,537	-	-	83,537
Accrued interest payable.....	-	6,517	1,082	-	7,599
Deferred tax, grant and subvention revenues.....	46,251	(42,680)	-	-	3,571
Due to other funds/internal balances.....	79,471	-	1,374	(44,347)	36,498
Deferred credits and other liabilities.....	412,480	(268,299)	1,205	-	145,386
Bonds, loans, capital leases, and other payables.....	150,000	1,622,283	231,332	-	2,003,615
Total Liabilities.....	<u>872,602</u>	<u>1,736,327</u>	<u>248,488</u>	<u>(44,347)</u>	<u>2,813,070</u>
<b>Fund balances/net assets</b>					
Total fund balances/net assets.....	1,068,256	644,444	(211,618)	-	1,501,082
Total liabilities and fund balances/net assets.....	<u>\$ 1,940,858</u>	<u>\$ 2,380,771</u>	<u>\$ 36,870</u>	<u>\$ (44,347)</u>	<u>\$ 4,314,152</u>

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- (1) When capital assets (land, infrastructure, buildings, and equipment) 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, net of accumulated depreciation, among the assets of the City as a whole.

Cost of capital assets.....	\$ 2,995,050
Accumulated depreciation.....	<u>(627,479)</u>
	<u>\$ 2,367,571</u>

Bond issuance costs are expended in governmental funds when paid and are capitalized and amortized over the life of the corresponding bonds for purposes of the statement of net assets.

\$ 13,200

Long-term liabilities applicable to the City's governmental activities are not due and payable in the current period and accordingly are not reported as fund liabilities. All liabilities, both current and long-term, are reported in the statement of net assets.

Accrued vacation and sick leave pay.....	\$ (121,315)
Accrued workers' compensation.....	(213,654)
Estimated claims payable.....	(83,537)
Bonds, loans, capital leases, and other payables.....	(1,622,283)
Deferred credits and other liabilities.....	<u>(97)</u>
	<u>\$ (2,040,886)</u>

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

\$ 6,517

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.

Deferred tax, grant and subvention revenue.....	\$ 42,680
Deferred credits and other liabilities.....	<u>268,396</u>
	<u>\$ 311,076</u>

- (2) Internal service funds are used by management to charge the costs of certain activities, such as capital lease financing, equipment maintenance, printing and mailing services, and telecommunications, to individual funds. The assets and liabilities of certain internal service funds are included in governmental activities in the statement of net assets.

Net deficit before adjustments.....	(1,477)
Adjustments for internal balances with San Francisco Finance Corporation:	
Capital lease receivables from other governmental and enterprise funds.....	(231,820)
Deferred charges and other assets.....	3,153
Deferred credits and other liabilities.....	<u>18,526</u>
	<u>\$ (211,618)</u>

In addition, intrafund receivables and payables among various internal service funds of \$0.4 million are eliminated.

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**(b) Explanation of certain differences between the governmental fund statement of revenues, expenditures, and changes in fund balances and the government-wide statement of activities**

The net change in fund balances for governmental funds, \$350,682, differs from the change in net assets for governmental activities \$194,341, reported in the statement of activities. The differences arise primarily from the long-term economic focus in the statement of activities versus the current financial resources focus in the governmental funds. The effect of the differences is illustrated below.

Statement of Revenues, Expenditures, and Changes in Fund Balances/Statement of Activities (in thousands)

	Total Governmental Funds	Long-term Revenues/ Expenses(3)	Capital- related Items(4)	Internal Service Funds(5)	Long-term Debt Transactions(6)	Statement of Activities Totals
<b>Revenues</b>						
Property taxes.....	\$ 918,645	\$ 1,669	\$ -	\$ -	\$ -	\$ 920,314
Business taxes.....	292,763	-	-	-	-	292,763
Other local taxes.....	538,085	-	-	-	-	538,085
Licenses, permits and franchises.....	25,942	-	-	-	-	25,942
Fines, forfeitures and penalties.....	12,509	-	-	-	-	12,509
Interest and investment income.....	28,268	971	-	251	-	29,490
Rents and concessions.....	49,450	1,880	-	-	-	51,330
Intergovernmental:						
Federal.....	348,764	-	-	-	-	348,764
State.....	522,937	763	-	-	-	523,700
Other.....	25,783	-	-	-	-	25,783
Charges for services.....	241,750	-	-	-	-	241,750
Other revenues.....	57,487	959	-	-	-	58,446
<b>Total revenues.....</b>	<b>3,062,383</b>	<b>6,242</b>	<b>-</b>	<b>251</b>	<b>-</b>	<b>3,068,876</b>
<b>Expenditures/Expenses</b>						
Current:						
Public protection.....	738,494	(5,200)	10,576	(5,182)	-	738,688
Public works, transportation and commerce.....	195,896	5,088	20,834	(8,483)	-	213,335
Human welfare and neighborhood development.....	644,899	(25,620)	581	(107)	-	619,753
Community health.....	501,050	1,252	957	-	-	503,259
Culture and recreation.....	239,022	11,438	27,684	(4,119)	(17,689)	256,336
General administration and finance.....	135,118	3,595	13,629	508	-	152,850
General City responsibilities.....	62,799	(3,278)	-	(1,049)	552	59,024
Debt service:						
Principal retirement.....	80,306	-	-	-	(80,306)	-
Interest and fiscal charges.....	61,524	-	-	6,523	21,643	89,690
Bond issuance costs.....	4,842	-	-	-	(4,842)	-
Capital outlay.....	130,224	-	(130,224)	-	-	-
<b>Total expenditures/expenses.....</b>	<b>2,794,174</b>	<b>(12,725)</b>	<b>(55,963)</b>	<b>(11,909)</b>	<b>(80,642)</b>	<b>2,632,935</b>
<b>Other financing sources (uses)/changes in net assets</b>						
Net transfers (to) from other funds.....	(241,870)	-	-	270	-	(241,600)
Issuance of bonds and loans:						
Face value of bonds issued.....	346,225	-	-	-	(346,225)	-
Face value of loans issued.....	500	-	-	-	(500)	-
Premium on issuance of bonds.....	11,989	-	-	-	(11,989)	-
Payment to escrow for refunded debt.....	(38,913)	-	-	-	38,913	-
Other financing sources - capital leases.....	4,542	-	-	(4,542)	-	-
<b>Total other financing sources (uses)/changes in net assets.....</b>	<b>82,473</b>	<b>-</b>	<b>-</b>	<b>(4,272)</b>	<b>(319,801)</b>	<b>(241,600)</b>
<b>Net change for the year.....</b>	<b>\$ 350,682</b>	<b>\$ 18,967</b>	<b>\$ 55,963</b>	<b>\$ 7,888</b>	<b>\$ (239,159)</b>	<b>\$ 194,341</b>

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(3) Because some property taxes will not be collected for several months after the City's fiscal year ends, they are not considered as available revenues in the governmental funds.	\$ 1,669
Some other revenues that do not provide current financial resources are not reported as revenues in the governmental funds but are recognized in the statement of activities.	<u>4,573</u>
	<u>\$ 6,242</u>
Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds. Certain long-term liabilities reported in the prior year statement of net assets were paid during the current period resulting in expenditures in the governmental funds. This is the amount by which the increase in long term liabilities exceeded expenses reported in the statement of activities that do not require the use of current financial resources.	\$ (1,553)
Some expenditures reported in the governmental funds pertain to the establishment of deferred credits on long-term loans since the loans are not considered "available" to pay current period expenditures. The deferred credits are not reported in the statement of net assets and, therefore, the related expenses are not reported in the statement of activities.	<u>14,278</u>
	<u>\$ 12,725</u>
(4) When capital assets that are to be used in governmental activities are purchased or constructed, the resources expended for those assets are reported as expenditures in governmental funds. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. As a result, fund balance decreases by the amount of financial resources expended, whereas net assets decrease by the amount of depreciation expense charged for the year, and the loss on disposal of capital assets.	
Capital expenditures.....	\$ 120,774
Depreciation expense.....	(64,797)
Loss on disposal of capital assets.....	(14)
Difference.....	<u>\$ 55,963</u>
(5) Internal service funds are used by management to charge the costs of certain activities, such as capital lease financing, equipment maintenance, printing and mailing services, 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.	<u>\$ 7,888</u>
(6) Lease payments on the Moscone Convention Center (note 8) are reported as a culture and recreation expenditure in the governmental funds and, thus, have the effect of reducing fund balance because current financial resources have been used. For the City as a whole, however, the principal payments reduce the liability in the statement of net assets and do not result in an expense in the statement of activities. The City's capital lease obligation was reduced because principal payments were made to lessee.	
Total property rent payments.....	<u>\$ 17,689</u>
Bond issuance costs are expended 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.....	\$ 4,842
Amortization of bond issuance costs.....	(552)
Difference.....	<u>\$ 4,290</u>
Bond premiums and discounts are expended in the governmental funds when the bonds are issued, and are capitalized in the statement of net assets. This is the amount of premiums capitalized during the current period.....	<u>\$ (11,989)</u>
Repayment of bond principal and the payment to escrow for refunding of debt are reported as expenditures in governmental funds and, thus, have the effect of reducing fund balance because current financial resources have been used. For the City as a whole, however, the principal payments and payment to escrow for refunded debt reduce the liabilities in the statement of net assets and do not result in expenses in the statement of activities. The City's bonded debt was reduced because principal payments were made to bond holders and payments were made to escrow for refunded debt.	
Principal payments made.....	\$ 80,306
Payments to escrow for refunded debt.....	38,913
	<u>\$ 119,219</u>

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Bond proceeds and capital leases are reported as other financing sources in governmental funds and thus contribute to the change in fund balance. In the government-wide statements, however, issuing debt and entering into capital lease arrangements increase long-term liabilities in the statement of net assets and do not affect the statement of activities. Proceeds were received from:

General obligation bonds.....	\$ (306,875)
Refunding certificate of participation.....	(39,350)
Loans.....	(500)
	(346,725)
	\$ (227,506)

Interest expense in the statement of activities differs from the amount reported in governmental funds because (1) additional accrued and accreted interest was calculated for bonds, notes payable and capital leases, (2) amortization of bond discounts, premiums and refunding losses which are expensed within the fund statements, and (3) additional interest expense was recognized on the accrual of an arbitrage rebate liability which will not be recognized in the governmental funds until the liability is due and payable.

Increase in accrued interest.....	\$ (318)
Interest payment on capital lease obligations on the Moscone Convention Center.....	(22,198)
Amortization of bond premiums, discounts and refunding losses.....	(214)
Reduction in arbitrage rebate liability.....	1,087
	\$ (21,643)

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**(4) BUDGETARY RESULTS RECONCILED TO RESULTS IN ACCORDANCE WITH GENERALLY ACCEPTED ACCOUNTING PRINCIPLES**

***Budgetary Results Reconciliation***

The budgetary process is based upon accounting for certain transactions on a basis other than GAAP basis. The results of operations are presented in the budget-to-actual comparison statement in accordance with the budgetary process (Budget basis) to provide a meaningful comparison with the budget.

The major differences between the Budget basis "actual" and GAAP basis are timing differences. Timing differences represent transactions that are accounted for in different periods for Budget basis and GAAP basis reporting. Certain revenues accrued on a Budget basis have been deferred for GAAP reporting. These primarily relate to the accounting for property tax revenues under the Teeter Plan (note 6).

The fund balance of the General Fund as of June 30, 2005 on a Budget basis is reconciled to the fund balance on a GAAP basis as follows (in thousands):

	General Fund
Fund Balance - Budget Basis.....	\$ 324,724
Unrealized Gains on Investments.....	224
Cumulative Excess Property Tax Revenues Recognized on a Budget Basis.....	(24,419)
Deferred Charges & Other.....	(1,880)
Reserved for Assets Not Available for Appropriation.....	9,031
Fund Balance - GAAP Basis.....	\$ 307,680

General Fund Budget basis fund balance at June 30, 2005 is composed of the following (in thousands):

Reserved for Rainy Day - Economic Stabilization Reserve.....	\$	48,139	
Reserved for Encumbrances.....		57,762	
Reserved for Appropriation Carryforward.....		36,198	
Reserved for Subsequent Years' Budgets:			
Baseline Appropriation Funding Mandates.....		6,223	
Budget Savings Incentive Program.....		2,628	
Budget Savings Incentive Program - Recreation & Park.....		3,075	
Salaries & benefits costs (MOU).....		9,150	
Total Reserved Fund Balance.....			\$ 163,175
Designated for Litigation and Contingencies.....		24,370	
Unreserved, Undesignated Fund Balance - Available for Appropriation.....		137,179	
Total Unreserved Amounts.....			161,549
Fund Balance, June 30, 2005 - Budget basis.....			\$ 324,724

Of the \$137.2 million unreserved, undesignated fund balance - available for appropriation, \$118 million has been subsequently appropriated as part of the General Fund budget for use in fiscal year 2005-2006.

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**(5) DEPOSITS AND INVESTMENTS**

**(a) Cash, Deposits and Investments Presentation**

Total City cash, deposits and investments, at fair value, are as follows (dollars in thousands):

	Primary Government				Component Units
	Governmental Activities	Business-type Activities	Fiduciary Funds	Total	
Deposits and investments with					
City Treasury.....	\$ 1,238,350 <sup>1</sup>	\$ 651,311	\$ 508,239 <sup>2</sup>	\$ 2,397,900	\$ 1,516
Deposits and investments outside					
City Treasury.....	62,157 <sup>3</sup>	8,017	13,230,007	13,300,181	157,675
Restricted assets:					
Deposits and investments with					
City Treasury.....	-	428,724	-	428,724	-
Deposits and investments outside					
City Treasury.....	-	268,437	-	268,437	91,089
Invested securities lending collateral			1,600,111	1,600,111	-
<b>Total deposits and investments.....</b>	<b>\$ 1,300,507</b>	<b>\$ 1,356,489</b>	<b>\$ 15,338,357</b>	<b>\$ 17,995,353</b>	<b>\$ 250,280</b>
Cash and deposits.....	\$ (70,123)	\$ 4,047	\$ 17,986	\$ (48,090)	\$ 1,056
Investments.....	1,370,630	1,352,442	15,320,371	18,043,443	249,224
<b>Total deposits and investments.....</b>	<b>\$ 1,300,507</b>	<b>\$ 1,356,489</b>	<b>\$ 15,338,357</b>	<b>\$ 17,995,353</b>	<b>\$ 250,280</b>

<sup>1</sup> Includes deposits and investments with the City Treasury of total governmental funds (\$1,230,154) and internal service funds (\$8,196).

<sup>2</sup> Includes deposits and investments with the City Treasury of pension and other employee benefit trust funds (\$76,672), investment trust fund (\$321,101) and agency funds (\$110,466).

<sup>3</sup> Includes deposits and investments outside the City Treasury of total governmental funds (\$46,100) and internal service funds (\$16,057).

**(b) Cash and Deposits**

The City had cash and deposits at June 30, 2005, as follows (in thousands):

	Primary Government						Component Units	
	Governmental Activities		Business-type Activities		Fiduciary Funds		Carrying Amount	Bank Balance
	Carrying Amount	Bank Balance	Carrying Amount	Bank Balance	Carrying Amount	Bank Balance		
Cash on hand.....	\$ 1,680	\$ -	\$ 483	\$ -	\$ -	\$ -	\$ 1	\$ -
Federally insured deposits....	500	500	377	828	100	100	268	468
Collateralized deposits*.....	(72,303)	32,873	170	60	3,752	3,752	787	2,002
Uninsured and uncollateralized.....	-	-	3,017	2,417	14,134	14,134	-	-
	<b>\$ (70,123)</b>	<b>\$ 33,373</b>	<b>\$ 4,047</b>	<b>\$ 3,305</b>	<b>\$ 17,986</b>	<b>\$ 17,986</b>	<b>\$ 1,056</b>	<b>\$ 2,470</b>

\* Under the City's cash management policy, investments are converted to cash as checks are presented for payment. At June 30, 2005, the carrying amount of collateralized deposits has been reduced by the amount of outstanding checks of approximately \$105.5 million. Of the \$105.5 million of outstanding checks, \$46.2 million relates to the San Francisco Unified School District and Community College District, which have been reflected in an investment trust fund.

**Custodial Credit Risk - Deposits**

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, the City will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The California Government Code, the City's investment policy and the Retirement System's investment policy do not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits, other than the following provision. The

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California Government Code requires that a financial institution secure deposits made by state or local governmental units by pledging securities in an undivided collateral pool held by a depository regulated under state law (unless so waived by the governmental unit). The market value of the pledged securities in the collateral pool must equal at least 110% of the total amount deposited by the public agencies. California law also allows financial institutions to secure City deposits by pledging first trust deed mortgage notes having a value of 150% of the secured public deposits. In addition, the City's investment policy states that mortgage-backed collateral will not be accepted. As of June 30, 2005, \$2.4 million and \$14.1 million of the business-type activities and the Retirement System's bank balances, respectively, were exposed to custodial credit risk by not being insured or collateralized.

**(c) Investment Policies**

***Treasurer's Pool***

The City's investment policy addresses the soundness of financial institutions in which the City will deposit funds, types of investment instruments as permitted by the California Government Code, and the percentage of the portfolio which may be invested in certain instruments with longer terms to maturity. The objectives of the policy, in order of priority, are preservation of capital, liquidity, and yield. The City has established a Treasury Oversight Committee (Oversight Committee), comprised of various City officials and representatives of agencies with large cash balances, to monitor and review the management of public funds maintained in the investment pool in accordance with Sections 27130 to 27137 of the California Government Code. The Treasurer prepares and submits a comprehensive investment report to the members of the Oversight Committee and the investment pool participants every month. The report covers the type of investments in the pool, maturity dates, par value, actual cost, and fair value.

Although the California Government Code and the City's investment policy do not limit the amount of City funds that may be invested in treasury bills and treasury notes, the investment policy requires the consideration of the City's anticipated cash requirements when purchasing treasury notes of longer maturities. Also, treasury notes with maturities that exceed five years are restricted to a maximum of 10 percent of the total portfolio at the time of purchase. In addition, purchases of treasury bonds are subject to an analysis of cash requirements and restricted to a maximum of five percent of the total portfolio at the time of purchase.

Further, the California Government Code does not limit the amount of City funds that may be invested in federal agency instruments. However, the City's investment policy requires that investments in federal agencies should neither exceed 60 percent of the total portfolio at the time of purchase nor have a weighted average maturity in excess of 270 days. If it exceeds 270 days, the total should not exceed 30 percent of the total par value of the portfolio. The investment policy also limits each type of agency instrument.

The City's investment policy also limits the purchase of negotiable certificates of deposit to the five largest domestic commercial banks that have demonstrated profitability in their most recent audited financial statements at the time of purchase. In addition, the investment policy requires that public time deposits be made only at approved financial institutions with at least one full service branch within the geographical boundaries of the City, and that they yield a minimum of 0.125% higher than equal maturity U.S. Treasury instruments. The investment policy restricts exposure to \$100,000 for all savings institutions and requires that each deposit be fully guaranteed by the Federal Deposit Insurance Corporation. The investment policy also requires that commercial bank deposits be made on a competitive basis with risk exposure based on financial statements and related information gathered on each individual bank.

Also, the California State Government Code requires that the Treasurer purchase only domestic commercial paper with maturities not to exceed 270 days and that the issuer must be rated in the highest ranking by at least one of the national rating agencies. However, the Treasurer's investment policy is more restrictive in that it requires that the Treasurer purchase only domestic commercial paper with maturities not to exceed 180 days.

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The table below identifies the investment types that are authorized for the City, along with the related interest rate risk and concentration of credit risk.

<u>Authorized Investment Type</u>	<u>Maximum Maturity</u>	<u>Maximum Percentage of Portfolio</u>	<u>Maximum Investment in One Issuer</u>
U.S. Treasury Obligations	N/A	None	None
U.S. Agency Securities	N/A	60%	None
Commercial Paper Discounts	180 days	15%	10%
Negotiable Certificates of Deposit	5 years	30%	None
Public Time Deposit	1 year	None	\$100,000
Public Demand Accounts	N/A	None	None
Bankers Acceptances	180 days	40%	30%
Repurchase Agreements	30 days	None	None
Reverse Repurchase Agreements	45 days	None	\$75 million

The Treasurer also holds for safekeeping bequests, trust funds, and lease deposits for other City departments. The bequests and trust funds consist of stocks and debentures. Those instruments are valued at par, cost, or market value at the time of donation.

***Other Funds***

Other funds consist primarily of deposits and investments with trustees related to the issuance of bonds and to certain loan programs operated by the City. These funds are invested either in accordance with bond covenants and are pledged for payment of principal, interest, and specified capital improvements or in accordance with grant agreements and may be restricted for the issuance of loans.

***Employees' Retirement System***

The Retirement System's investments are invested pursuant to investment policy guidelines as established by the Retirement Board. The objective of the policy is to maximize the expected return of the fund at an acceptable level of risk. The Retirement Board has established percentage guidelines for types of investments to ensure the portfolio is diversified.

***Redevelopment Agency***

The investment policy of the Redevelopment Agency is governed by Article 2 of the California Government Code (Code). Investments are restricted to certain types of instruments and certain of these instruments are only allowed within limits. The Code permits repurchase agreements, but reverse repurchase agreements require the prior approval of the Agency Commission. The Agency does not participate in reverse repurchase agreements or other high-risk investments as defined by the Agency's investment policy. It is the Agency's intention to hold investments until maturity, unless earlier liquidation would result in an investment gain.

Certain investments of the Redevelopment Agency are in the Local Agency Investment Fund (LAIF). LAIF is sponsored by the State Treasurer and prepares its market value report detailing the carrying cost and the estimated market value for the entire pool. The Agency has used a multiplier provided by LAIF to determine estimated market values. In addition, the Redevelopment Agency has investments with trustees. These investments are restricted by various bond covenants and are pledged for payment of principal, interest and specified capital improvements.

**(d) *Investment Risks***

**Interest rate risk** is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. The following schedule indicates the interest rate risk of the City's

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investments as of June 30, 2005 (in thousands). The Employees' Retirement System's interest rate risk information begins on page 68.

	Fair Value	Investment Maturities		
		Less than 1 year	1 to 5 years	More than 10 years
<b>Primary Government:</b>				
Investments in City Treasury:				
U.S. Treasury Bills	\$ 682,030	\$ 682,030	\$ -	\$ -
U.S. Treasury Notes	54,791	-	54,791	-
U.S. Agencies - Coupon	1,431,791	1,431,791	-	-
Commercial paper	377,888	377,888	-	-
Negotiable certificates of deposits	357,975	357,975	-	-
Nonnegotiable certificates of deposits	100	100	-	-
Less: Treasure Island Development Authority Investments with City Treasury	(1,516)	(1,516)	-	-
Subtotal investments in City Treasury	2,903,059	\$ 2,848,268	\$ 54,791	\$ -
Investments Outside City Treasury: (Governmental and Business-Type)				
U.S. Treasury Notes	4,896	\$ -	\$ 4,896	\$ -
U.S. Treasury Bills	23,892	23,892	-	-
U.S. Agencies - Coupon	28,407	23,034	5,373	-
U.S. Agencies - Discount	222,700	222,700	-	-
Money market mutual funds	46,791	46,791	-	-
Equity securities	828	828	-	-
Commercial paper	738	738	-	-
Subtotal investments outside City Treasury	328,252	\$ 317,983	\$ 10,269	\$ -
Employees' Retirement System investments	14,812,132			
<b>Total Primary Government</b>	<b>18,043,443</b>			
<b>Component Units:</b>				
Redevelopment Agency:				
U.S. Agencies - Coupon	52,154	\$ -	\$ 52,154	\$ -
U.S. Agencies - Discount	19,057	19,057	-	-
Commercial paper	13,981	13,981	-	-
Medium-term corporate notes	1,990	1,990	-	-
Repurchase agreements	1,834	1,834	-	-
State Local Agency Investment Fund	64,477	64,477	-	-
Money market mutual funds	71,324	71,324	-	-
Guaranteed investment contracts	22,705	-	988	21,717
Subtotal Redevelopment Agency	247,522	\$ 172,663	\$ 53,142	\$ 21,717
Treasure Island Development Authority:				
Investments with City Treasury	1,516	\$ 1,516	\$ -	\$ -
Investments Outside City Treasury:				
Certificates of deposits	186	186	-	-
Subtotal Treasure Island Development Authority	1,702	\$ 1,702	\$ -	\$ -
<b>Total Component Units</b>	<b>249,224</b>			
<b>Total Investments</b>	<b>\$ 18,292,667</b>			

One of the ways that the Treasurer manages its exposure to interest rate risk is by purchasing a combination of shorter term and longer term investments and by timing cash flows from maturities so that a portion of the portfolio is maturing or coming close to maturity evenly over time as necessary to provide the cash flow and liquidity needed for operations.

As a means of limiting its exposure to fair value losses arising from rising interest rates, the Agency's investment policy limits investments to securities with short maturities, such as the following:

- The maximum maturity of commercial paper 180 days. Investment in commercial paper will comprise not more than 30% of the Agency's portfolio if average maturity is no more than 31 days or 15% if average maturity is more than 31 days.
- The maximum maturity of corporate notes is five years. Investment in corporate notes may not exceed 15% of the Agency's portfolio.

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**Credit risk** is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization.

Presented below is the minimum rating required by the California Government Code and the City's investment policy and the actual rating as of June 30, 2005 for each investment type.

<u>Investment Type</u>	<u>Minimum Legal Rating</u>	<u>Standard &amp; Poor's Rating</u>	<u>Total Investment Portfolio</u>
U.S. Treasury Bills	N/A	A-1+	24%
U.S. Treasury Notes	N/A	A-1	2%
U.S. Agencies	N/A	A-1+	18%
U.S. Agencies	N/A	A-1	31%
Commercial Paper	A-1	A-1	13%
Negotiable Certificates of Deposits	N/A	A-1+	12%

As a means of limiting its exposure to credit risk, the Agency's investment policy limits investments to high-quality securities with an investment grade of A or better, and maintaining a portfolio diversified by type and issuer.

<u>Investment Type</u>	<u>Credit Ratings</u>	<u>Total Investment Portfolio</u>
U.S. Agencies - Coupon	AAA	21%
U.S. Agencies - Discount	AAA	8%
Commercial paper	A-1/P-1	6%
Medium-term corporate notes	AAA	1%
Repurchase agreements	Not rated	1%
State Local Agency Investment Fund	Not rated	26%
Money market mutual funds	AAA	28%
Guaranteed investment contracts	AA or Higher	9%

**Custodial credit risk** for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The California Government Code and the City's investment policy do not contain legal or policy requirements that would limit the exposure to custodial credit risk for investments; however, it is the practice of the City Treasurer that all investments are insured, registered or held by the Treasurer's custodial agent in the City's name.

The Agency does not have a formal investment policy for custodial credit risk for investments. As of June 30, 2005, \$1.8 million of the Agency's investments are uninsured and unregistered.

**Concentration of Credit Risk**

The City diversifies its portfolio by limiting the percentage of the portfolio that can be invested in any one issuer's name. U.S. Treasury and Agency securities are not subject to this limitation. More than 5 percent of the City's investments with City Treasurer are in the Federal Home Loan Mortgage Corporation, Federal Home Loan Bank, and the Federal National Mortgage Association. These investments represent 15.4 percent, 16.2 percent, and 17.7 percent, respectively, of the City's investments with the City Treasurer. In addition, more than five percent of the Airport's investments with its trustees are in Federal Home Loan Bank and Federal Nation Mortgage Association. These investments represent 51 percent and 48 percent, respectively, of the Airport's investments with its trustees. The Finance Corporation's investments with its trustee are held in Federal Home Loan Bank for 19 percent and Federal Nation Mortgage Association for 20 percent.

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**(e) Investment Gain**

The types of investments made during the year were substantially the same as those held as of June 30, 2005. Fair value fluctuates with interest rates, and increasing rates could cause fair value to decline below original cost. City management believes the liquidity in the portfolio is sufficient to meet cash flow requirements and to preclude the City from having to sell investments below original cost for that purpose. The interest and net investment gain is comprised of the following at June 30, 2005 (in thousands):

Interest and dividends, net of amounts capitalized	\$ 377,976
Net increase in the fair value of investments	<u>1,244,537</u>
Total investment gain	<u><u>\$ 1,622,513</u></u>

The net increase in the fair value of investments takes into account all changes in fair value (including purchases and sales) that occurred during the year. The primary component of this figure is the net increase in fair value of pension investments.

The earned yield, which includes net gains on investments sold, on all investments held by the City Treasurer for the fiscal year ended June 30, 2005 was 2.31%.

**(f) Treasurer's Pool**

The following represents a condensed statement of net assets and changes in net assets for the Treasurer's Pool as of June 30, 2005 (in thousands):

<b>Statement of Net Assets</b>	
Net assets held in trust for all pool participants.....	<u>\$ 2,828,140</u>
Equity of internal pool participants.....	2,507,655
Equity of external pool participants.....	<u>320,485</u>
Total equity.....	<u><u>\$ 2,828,140</u></u>
 <b>Statement of Changes in Net Assets</b>	
Net assets at July 1, 2004.....	\$ 2,222,788
Net change in investments by pool participants.....	<u>605,352</u>
Net assets at June 30, 2005.....	<u><u>\$ 2,828,140</u></u>

The following provides a summary of key investment information for the Treasurer's Pool as of June 30, 2005 (in thousands):

Types of Investment	Rates	Maturities	Par Value	Carrying Value
U.S. government securities.....	2.64% - 4.56%	07/07/05-06/15/10	\$ 745,000	\$ 736,821
Federal agencies.....	2.91% - 3.27%	07/05/05-10/18/05	1,442,000	1,431,791
Negotiable certificate of deposits.....	3.09% - 3.31%	07/11/05-08/30/05	358,000	357,975
Commercial paper.....	3.04% - 3.29%	07/05/05-08/29/05	380,000	377,888
Public time deposits.....	3.00%	07/16/05	<u>100</u>	<u>100</u>
			<u><u>\$ 2,925,100</u></u>	2,904,575
Carrying amount of deposits in Treasurer's Pool.....				<u>(76,435)</u>
Total cash and investments in Treasurer's Pool.....				<u><u>\$ 2,828,140</u></u>

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**(g) Retirement System Investments**

The Retirement System's investments as of June 30, 2005 are summarized as follows (in thousands):

Fixed Income Investments:	
Short-term bills and notes	\$ 622,621
Debt securities:	
U.S. Government and agencies	1,372,895
U.S. Corporate	1,773,910
International government	319,682
International corporate	162,740
Subtotal debt securities	<u>3,629,227</u>
Total fixed income investments	<u>4,251,848</u>
Equity securities:	
Domestic	4,225,420
International	2,199,917
Total equity securities	<u>6,425,337</u>
Real estate holdings	1,084,786
Venture capital	1,436,796
Foreign currency contracts, net	13,254
Investment in lending agent's short-term investment pool	1,600,111
<b>Total Retirement System Investments</b>	<u><u>\$ 14,812,132</u></u>

**Interest Rate Risk**

The Retirement System does not have a specific policy to manage interest rate risk, but requires investment managers to diversify by issue, maturity, sector, coupon and geography. Investment managers retained by the Retirement System follow specific investment guidelines and are evaluated against specific market benchmarks that represent their investment style. Any exemption from general guidelines requires approval from the Retirement Board.

As of June 30, 2005, the Retirement System had the following fixed income investments subject to interest rate risk (amounts in thousands):

<u>Investment Type</u>	<u>Fair Value</u>	<u>Weighted Average Maturity (in Years)</u>
Asset Backed Securities	\$ 136,564	0.791
Commercial Mortgage-Backed Securities	378,542	1.861
Corporate Bonds	1,302,916	1.175
Corporate Convertible Bonds	166,487	0.693
Government Agencies	45,552	0.143
Government Bonds	1,166,117	1.984
Government Mortgage-Backed Securities	395,979	1.669
Index Linked Government Bonds	75,017	0.310
Mortgages	10,207	0.023
Municipal/Provincial Bonds	11,041	0.015
Non-Government Backed Collateralized Mortgage Obligations	104,484	0.635
Other Fixed Income	3,000	0.001
Short-term Bills and Notes	94,678	0.003
Short-term Investment Funds	297,936	0.000
<b>Total</b>	<u><u>\$ 4,188,520</u></u>	<u><u>9.303</u></u>

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The 9.3 year weighted average maturity of the Retirement System's fixed income investments is based on the final maturity dates of all of the securities listed in the table. However, it is estimated that approximately 30% of the securities in the table contain embedded call options. Some of these "put back" options are explicit (such as call features attached to corporate bonds) and others are implicit (such as prepayment options on mortgage backed securities) which makes the expected life of these investments shorter than the stated maturity. For these reasons, actual maturities might differ from those reflected in the table.

**Credit Risk**

The Retirement System's fixed income managers are limited within their portfolios to no more than 10% exposure in any single security, with the exception of United States Treasury and government agencies. The following table illustrates the Retirement System's exposure to credit risk excluding obligations of the U.S. government and those explicitly guaranteed by the U.S. government as of June 30, 2005 (amounts in thousands):

<u>Investment Type</u>	<u>Fair Value</u>	<u>A</u>	<u>AA</u>	<u>AAA</u>	<u>B</u>	<u>BB</u>	<u>BBB</u>	<u>C</u>	<u>Not Rated</u>
Asset Backed Securities	\$ 136,564	\$ 77	\$ -	\$ 68,303	\$ 2,346	\$ 24,481	\$ 33,008	\$ 3,075	\$ 5,274
Commercial Mortgage-Backed	378,542	1,842	19,186	117,862	17,214	101,633	36,209	3,889	80,707
Corporate Bonds	1,302,916	49,302	35,147	27,763	213,866	138,113	62,395	33,960	742,370
Corporate Convertible Bonds	166,487	18,548	3,592	-	21,411	36,457	65,683	3,068	17,728
Government Agencies	45,552	2,218	8,112	35,222	-	-	-	-	-
Government Bonds	296,424	72,018	27,837	79,718	41,783	14,056	51,523	170	9,319
Government Mortgage-Backed Securities	373,445	-	-	-	568	783	-	-	372,094
Index Linked Government Bonds	11,288	-	-	11,288	-	-	-	-	-
Mortgages	10,207	-	-	-	-	-	-	-	10,207
Municipal/Provincial Bonds	11,041	205	10,836	-	-	-	-	-	-
Non-Government Backed Collateralized Mortgage Obligations	104,484	1,048	490	53,784	14,630	11,276	3,491	514	19,251
Other fixed Income	3,000	-	3,000	-	-	-	-	-	-
Short-term bills and notes	89,082	-	-	-	-	-	-	-	89,082
<b>Total</b>	<b>\$ 2,929,032</b>	<b>\$ 145,258</b>	<b>\$ 108,200</b>	<b>\$ 393,940</b>	<b>\$ 311,818</b>	<b>\$ 326,799</b>	<b>\$ 252,309</b>	<b>\$ 44,676</b>	<b>\$ 1,346,032</b>

The ratings are the lower of the ratings by Moody's Investors Service (Moody's) and Standard & Poor's (S&P). Investments not rated by either Moody's or S&P are shown as not rated in the above table.

**Custodial Credit Risk**

The Retirement System does not have a specific policy addressing custodial credit risk for investments, but it is the practice of the Retirement System that all investments are insured, registered, or held by the Retirement System or its agent in the Retirement System's name. As of June 30, 2005, \$9,967 of the Retirement System's investments were exposed to custodial credit risk because they were not insured or registered in the name of the Retirement System, and were held by the counterparty's trust department or agent but not in the Retirement System's name.

Cash received as securities lending collateral is invested in a securities lending collateral investment pool and is not exposed to custodial credit risk.

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**Foreign Currency Risk**

Foreign currency risk is the risk that changes in foreign exchange rates will adversely affect the fair value of investments. As of June 30, 2005, the Retirement System was subjected to foreign currency risk. To mitigate this risk, the Retirement System's investment policy allows international managers to enter into foreign currency exchange contracts limited to hedging currency exposure existing in the portfolio. The Retirement System's exposure to foreign currency risk derives from its positions in foreign currency denominated international equity and fixed income investments. The Retirement System's net exposure to foreign currency risk is as follows (in thousands):

<u>Currency</u>	<u>Cash</u>	<u>Fixed Income Securities</u>	<u>Equity Securities</u>	<u>Real Estate</u>	<u>Venture Capital</u>	<u>Total</u>
Australian dollar	\$ 39,325	\$ -	\$ 54,475	\$ -	\$ -	\$ 93,800
Brazilian real	14,862	-	2,418	-	-	17,280
British pound sterling	29,845	12,584	357,972	-	3,660	404,061
Canadian dollar	(26,841)	12,853	58,149	-	-	44,161
Chilean peso	3,166	-	-	-	-	3,166
Chinese yuan renminbi	(3,266)	-	-	-	-	(3,266)
Danish krone	(778)	835	13,652	-	-	13,709
Egyptian pound	2,212	2,977	-	-	-	5,189
Euro currency	(471,992)	296,870	582,913	-	97,811	505,602
Hong Kong dollar	467	-	44,459	-	-	44,926
Hungarian forint	5,565	-	-	-	-	5,565
Iceland krona	(4,710)	6,548	-	-	-	1,838
Indian rupee	2,264	-	-	-	-	2,264
Japanese yen	(45,532)	95,978	404,855	5,048	-	460,349
Malaysian ringgit	6,146	-	-	-	-	6,146
Mexican peso	13,881	-	-	-	-	13,881
New Israeli shekel	-	2,741	-	-	-	2,741
Taiwan dollar	3,298	-	-	-	-	3,298
New Zealand dollar	(9,759)	7,996	5,085	-	-	3,322
Norwegian krone	674	-	11,918	-	-	12,592
Philippine peso	4,319	-	-	-	-	4,319
Polish zloty	10,298	-	-	-	-	10,298
Russian ruble (new)	13,366	6,076	-	-	-	19,442
Singapore dollar	8,870	-	15,215	-	-	24,085
Slovak koruna	7,942	-	-	-	-	7,942
South African rand	4,948	-	3,809	-	-	8,757
South Korean won	8,414	1,728	31,237	-	-	41,379
Swedish krona	3,878	2,575	32,741	-	-	39,194
Swiss franc	6,039	-	119,178	-	-	125,217
Turkish lira	1,523	15,366	-	-	-	16,889
Ukrainian hryvnia	2,404	3,115	-	-	-	5,519
Uruguayan peso	45	2,601	-	-	-	2,646
<b>Total</b>	<b>\$ (369,127)</b>	<b>\$ 470,843</b>	<b>\$ 1,738,076</b>	<b>\$ 5,048</b>	<b>\$ 101,471</b>	<b>\$ 1,946,311</b>

Investments in forward currency contract investments are commitments to purchase or sell stated amounts of foreign currency. Changes in market value of open contracts are immediately recognized as gains or losses. The market values of forward currency contracts are determined by quoted currency prices from national exchanges. As of June 30, 2005, the fair value of open contracts can be summarized as follows (in thousands):

Purchase contracts	\$ 1,132,367
Sales contracts	(1,119,113)
Net fair value	<u>\$ 13,254</u>

The Retirement System utilized these contracts to hedge (or decrease) the currency risk of foreign investments, to increase investment exposure in foreign currencies beyond the amounts reported as international investment securities, or to settle trades. Additionally, contracts may be used to effectively

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cancel previous contracts. The impact on market risk of these contracts can be summarized as follows (in thousands):

Contracts used to hedge or to settle trades, net	\$ (509,479)
Contracts used to increase investment exposure in a foreign currency or to settle trades, net	522,733
Net fair value	\$ 13,254

**Securities Lending**

The Retirement System 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 securities at 105% of the fair market value of domestic securities and non-domestic securities lent. 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 said collateral.

The Retirement System lent \$1,932,450 in securities and received collateral of \$391,580 and \$1,600,111 in securities and cash, respectively, from borrowers. The Retirement System's securities lending transactions as of June 30, 2005, are summarized in the following table (in thousands):

Security Type	Fair Value of Loaned Securities	Cash Collateral	Fair Value of Non-Cash Collateral
Securities Loaned for Cash Collateral:			
International Corporate Fixed	\$ 2,001	\$ 2,092	\$ -
International Equities	216,236	226,926	-
International Government Fixed	19,307	20,306	-
U.S. Agencies	605	616	-
U.S. Corporate Fixed	182,593	186,989	-
U.S. Equities	248,102	254,608	-
U.S. Government Fixed	888,303	908,574	-
Securities Loaned with Non-Cash Collateral:			
International Equities	268,163	-	281,856
International Government Fixed	10,611	-	11,008
International UK Gilt	11,069	-	11,414
U.S. Agencies	6,408	-	6,570
U.S. Corporate Fixed	18,988	-	19,401
U.S. Equities	1,289	-	1,319
U.S. Government Fixed	58,775	-	60,012
<b>Total</b>	<b>\$ 1,932,450</b>	<b>\$ 1,600,111</b>	<b>\$ 391,580</b>

The Retirement System does not have the ability to pledge or sell collateral securities unless a borrower defaults. As of June 30, 2005, the Retirement System has no credit risk exposure to borrowers because the amounts the Retirement System owes them exceed the amounts they owe the Retirement System. As with other extensions of credit, the Retirement System may bear the risk of delay in recovery or of rights in the collateral should the borrower of securities fail financially. In addition, the lending agent indemnifies the Retirement System against all borrower defaults.

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**(h) Supplemental disclosure of non-cash investing and financing activities**

San Francisco International Airport

During the fiscal year 2004-2005, the San Francisco International Airport (SFO) issued Second Series Revenue Bonds Issue 31F and Issue 32 to refund previously issued debt. The \$109.1 million in proceeds from Issue 31F and the \$197.7 million in proceeds from Issue 32 were deposited immediately into irrevocable trusts for the defeasance of \$306.8 million of Second Series Refunding Bonds.

Bond issuance costs of \$8.4 million that were deducted from the proceeds of the Second Series Revenue Bonds were capitalized and will be amortized over the debt repayment period.

**Other Non-Cash Transactions**

The following represents the other non-cash transactions as of June 30, 2005 (in thousands):

	General Hospital Medical Center	Port of San Francisco	Laguna Honda Hospital	Internal Service Funds	Total	
					2005	2004
Loss on abandonment of property and equipment.....	\$ -	\$ 11	\$ -	\$ -	\$ 11	\$ 39
Acquisition of capital assets on accounts payable and capital leases.....	958	2,313	409	313	3,993	3,750
Donated surplus.....	-	5,000	-	-	5,000	-
Total	<u>\$ 958</u>	<u>\$ 7,324</u>	<u>\$ 409</u>	<u>\$ 313</u>	<u>\$ 9,004</u>	<u>\$ 3,789</u>

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**(6) PROPERTY TAXES**

The City is responsible for assessing, collecting and distributing property taxes in accordance with enabling state law. Property taxes are levied on both real and personal property. Liens for secured property taxes attach on January 1<sup>st</sup> preceding the fiscal year for which taxes are levied. Secured property taxes are levied on the first business day of September and are payable in two equal installments: the first is due on November 1<sup>st</sup> and delinquent with penalties after December 10<sup>th</sup>; the second is due February 1<sup>st</sup> and delinquent with penalties after April 10<sup>th</sup>. Secured property taxes that are delinquent and unpaid as of June 30<sup>th</sup> are subject to redemption penalties, costs, and interest when paid. If not paid at the end of five years, the property may be sold at public auction and the proceeds used to pay delinquent amounts due. Any excess is remitted, if claimed, to the taxpayer. Unsecured personal property taxes do not represent a lien on real property. Those taxes are due on January 1<sup>st</sup> and become delinquent with penalties after August 31<sup>st</sup>. Supplemental property tax assessments associated with changes in the assessed valuation due to transfer of ownership in property or upon completion of new construction are levied in two equal installments and have variable due dates based on the dates of the underlying transaction.

Since the passage of California's Proposition 13, beginning with fiscal year 1978-1979, general property taxes are based either on a flat 1% rate applied to the 1975-1976 full value of the property or on 1% of the sales price of the property on sales transactions or construction value added after the 1975-1976 valuation. Taxable values on properties (exclusive of increases related to sales and construction) can rise at the lesser of 2% per year or inflation.

The Proposition 13 limitations on general property taxes do not limit taxes levied to pay the interest and redemption charges on any indebtedness approved by the voters prior to June 6, 1978 (the date of passage of Proposition 13). Proposition 13 was amended in 1986 to allow property taxes in excess of the 1% tax rate limit to fund general obligation bond debt service when such bonds are approved by two-thirds of the local voters. In 2000, California voters approved Proposition 39 which set the approval threshold at 55% for school facilities-related bonds. These "override" taxes for debt service amounted to approximately \$130 million for the year ended June 30, 2005.

Taxable valuation for the year ended June 30, 2005 (net of non-reimbursable exemptions, reimbursable exemptions, and tax increment allocations to the Redevelopment Agency) was approximately \$100.6 billion, an increase of 5.5%. The secured tax rate was \$1.144 per \$100 of assessed valuation. After adjusting for a State mandated property tax shift to schools, the tax rate is comprised of: \$0.65 for general government, \$0.35 for other taxing entities including the San Francisco Unified School District, San Francisco Community College District, the Bay Area Air Quality Management District and the Bay Area Rapid Transit District, and also \$0.144 for bond debt service. Delinquencies in the current year on secured taxes and unsecured taxes amounted to 1.36% and 2.53%, respectively, of the current year tax levy, for an average delinquency rate of 1.44% of the current year tax levy.

As established by the Teeter Plan, the Controller allocates to the City 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 tax amounts in the Agency Fund. To the extent the Agency Fund balances are higher than required, transfers may be made to benefit the City's General Fund on a budgetary basis. The balance of the tax loss reserve, as of June 30, 2005 was \$11.3 million, which is included in the Agency Fund for reporting purposes. The City has funded payment of accrued and current delinquencies, together with the required reserve, from interfund borrowing.

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**(7) CAPITAL ASSETS**

**Primary Government**

Capital asset activity of the primary government for the year ended June 30, 2005, was as follows (in thousands):

**Governmental Activities:**

	Balance July 1, 2004	Increases	Decreases	Balance June 30, 2005
Capital assets, not being depreciated:				
Land.....	\$ 143,640	\$ -	\$ -	\$ 143,640
Construction in progress.....	245,677	112,520	(66,157)	292,040
Total capital assets, not being depreciated.....	389,317	112,520	(66,157)	435,680
Capital assets, being depreciated:				
Facilities and improvements.....	2,092,382	48,216	-	2,140,598
Machinery and equipment.....	244,119	14,868	(2,550)	256,437
Infrastructure.....	180,976	13,490	-	194,466
Property held under lease.....	4,816	-	-	4,816
Total capital assets, being depreciated.....	2,522,293	76,574	(2,550)	2,596,317
Less accumulated depreciation for:				
Facilities and improvements.....	397,184	39,148	-	436,332
Machinery and equipment.....	191,445	21,507	(2,536)	210,416
Infrastructure.....	4,138	5,105	-	9,243
Property held under lease.....	4,280	-	-	4,280
Total accumulated depreciation.....	597,047	65,760	(2,536)	660,271
Total capital assets, being depreciated, net.....	1,925,246	10,814	(14)	1,936,046
Governmental activities capital assets, net.....	<u>\$ 2,314,563</u>	<u>\$ 123,334</u>	<u>\$ (66,171)</u>	<u>\$ 2,371,726</u>

**Business-type Activities:**

Capital asset activity of the business enterprises for the year ended June 30, 2005, was as follows (in thousands):

**San Francisco International Airport**

	Balance July 1, 2004	Increases	Decreases	Balance June 30, 2005
Capital assets, not being depreciated:				
Land.....	\$ 2,316	\$ -	\$ -	\$ 2,316
Construction in progress.....	126,574	77,399	(158,931)	45,042
Total capital assets, not being depreciated.....	128,890	77,399	(158,931)	47,358
Capital assets, being depreciated:				
Facilities and improvements.....	4,670,864	102,009	(3,329)	4,769,544
Machinery and equipment.....	70,207	739	(5,077)	65,869
Easements.....	135,598	3,011	-	138,609
Total capital assets, being depreciated.....	4,876,669	105,759	(8,406)	4,974,022
Less accumulated depreciation for:.....				
Facilities and improvements.....	998,507	150,311	-	1,148,818
Machinery and equipment.....	59,702	4,700	(4,938)	59,464
Easements.....	46,445	6,630	-	53,075
Total accumulated depreciation.....	1,104,654	161,641	(4,938)	1,261,357
Total capital assets, being depreciated, net.....	3,772,015	(55,882)	(3,468)	3,712,665
Capital assets, net.....	<u>\$ 3,900,905</u>	<u>\$ 21,517</u>	<u>\$ (162,399)</u>	<u>\$ 3,760,023</u>

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**Water Department**

	Balance July 1, 2004	Increases	Decreases	Balance June 30, 2005
<b>Capital assets, not being depreciated:</b>				
Land.....	\$ 17,929	\$ -	\$ -	\$ 17,929
Construction in progress.....	85,755	110,342	(74,234)	121,863
<b>Total capital assets, not being depreciated.....</b>	<b>103,684</b>	<b>110,342</b>	<b>(74,234)</b>	<b>139,792</b>
<b>Capital assets, being depreciated:</b>				
Facilities and improvements.....	968,502	59,334	-	1,027,836
Machinery and equipment.....	99,905	4,704	(415)	104,194
<b>Total capital assets, being depreciated.....</b>	<b>1,068,407</b>	<b>64,038</b>	<b>(415)</b>	<b>1,132,030</b>
<b>Less accumulated depreciation for:</b>				
Facilities and improvements.....	359,118	32,088	-	391,206
Machinery and equipment.....	60,806	8,024	(379)	68,451
<b>Total accumulated depreciation.....</b>	<b>419,924</b>	<b>40,112</b>	<b>(379)</b>	<b>459,657</b>
<b>Total capital assets, being depreciated, net.....</b>	<b>648,483</b>	<b>23,926</b>	<b>(36)</b>	<b>672,373</b>
<b>Capital assets, net.....</b>	<b>\$ 752,167</b>	<b>\$ 134,268</b>	<b>\$ (74,270)</b>	<b>\$ 812,165</b>

**Hetch Hetchy Water and Power**

	Balance July 1, 2004	Increases	Decreases	Balance June 30, 2005
<b>Capital assets, not being depreciated:</b>				
Land.....	\$ 4,215	\$ -	\$ -	\$ 4,215
Construction in progress.....	51,097	19,941	(20,132)	50,906
<b>Total capital assets, not being depreciated.....</b>	<b>55,312</b>	<b>19,941</b>	<b>(20,132)</b>	<b>55,121</b>
<b>Capital assets, being depreciated:</b>				
Facilities and improvements.....	426,665	16,707	-	443,372
Machinery and equipment.....	38,156	1,002	(100)	39,058
<b>Total capital assets, being depreciated.....</b>	<b>464,821</b>	<b>17,709</b>	<b>(100)</b>	<b>482,430</b>
<b>Less accumulated depreciation for:</b>				
Facilities and improvements.....	234,066	9,197	-	243,263
Machinery and equipment.....	25,806	1,562	(89)	27,279
<b>Total accumulated depreciation.....</b>	<b>259,872</b>	<b>10,759</b>	<b>(89)</b>	<b>270,542</b>
<b>Total capital assets, being depreciated, net.....</b>	<b>204,949</b>	<b>6,950</b>	<b>(11)</b>	<b>211,888</b>
<b>Capital assets, net.....</b>	<b>\$ 260,261</b>	<b>\$ 26,891</b>	<b>\$ (20,143)</b>	<b>\$ 267,009</b>

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**Municipal Transportation Agency**

	Balance July 1, 2004	Increases	Decreases	Balance June 30, 2005
Capital assets, not being depreciated:				
Land.....	\$ 26,245	\$ -	\$ -	\$ 26,245
Construction in progress.....	282,779	101,762	(5,338)	379,203
Total capital assets, not being depreciated.....	<u>309,024</u>	<u>101,762</u>	<u>(5,338)</u>	<u>405,448</u>
Capital assets, being depreciated:				
Facilities and improvements.....	376,851	6,746	-	383,597
Machinery and equipment.....	1,088,637	5,652	(5,023)	1,089,266
Infrastructure.....	703,673	13,052	-	716,725
Total capital assets, being depreciated.....	<u>2,169,161</u>	<u>25,450</u>	<u>(5,023)</u>	<u>2,189,588</u>
Less accumulated depreciation for:				
Facilities and improvements.....	123,396	32,317	-	155,713
Machinery and equipment.....	257,450	63,424	(4,461)	316,413
Infrastructure.....	209,003	22,680	-	231,683
Total accumulated depreciation.....	<u>589,849</u>	<u>118,421</u>	<u>(4,461)</u>	<u>703,809</u>
Total capital assets, being depreciated, net.....	<u>1,579,312</u>	<u>(92,971)</u>	<u>(562)</u>	<u>1,485,779</u>
Capital assets, net.....	<u>\$ 1,888,336</u>	<u>\$ 8,791</u>	<u>\$ (5,900)</u>	<u>\$ 1,891,227</u>

**General Hospital Medical Center**

	Balance July 1, 2004	Increases	Decreases	Balance June 30, 2005
Capital assets, not being depreciated:				
Land.....	\$ 542	\$ -	\$ -	\$ 542
Construction in progress.....	3,555	717	(1,589)	2,683
Total capital assets, not being depreciated.....	<u>4,097</u>	<u>717</u>	<u>(1,589)</u>	<u>3,225</u>
Capital assets, being depreciated:				
Facilities and improvements.....	125,903	2,529	-	128,432
Machinery and equipment.....	45,930	2,512	-	48,442
Total capital assets, being depreciated.....	<u>171,833</u>	<u>5,041</u>	<u>-</u>	<u>176,874</u>
Less accumulated depreciation for:				
Facilities and improvements.....	83,369	4,248	-	87,617
Machinery and equipment.....	36,625	2,407	-	39,032
Total accumulated depreciation.....	<u>119,994</u>	<u>6,655</u>	<u>-</u>	<u>126,649</u>
Total capital assets, being depreciated, net.....	<u>51,839</u>	<u>(1,614)</u>	<u>-</u>	<u>50,225</u>
Capital assets, net.....	<u>\$ 55,936</u>	<u>\$ (897)</u>	<u>\$ (1,589)</u>	<u>\$ 53,450</u>

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**Clean Water Program**

	Balance July 1, 2004	Increases	Decreases	Balance June 30, 2005
Capital assets, not being depreciated:				
Land.....	\$ 22,168	\$ -	\$ -	\$ 22,168
Construction in progress.....	22,379	27,560	(16,381)	33,558
Total capital assets, not being depreciated.....	<u>44,547</u>	<u>27,560</u>	<u>(16,381)</u>	<u>55,726</u>
Capital assets, being depreciated:				
Facilities and improvements.....	1,923,515	13,891	-	1,937,406
Machinery and equipment.....	24,203	2,513	-	26,716
Total capital assets, being depreciated.....	<u>1,947,718</u>	<u>16,404</u>	<u>-</u>	<u>1,964,122</u>
Less accumulated depreciation for:				
Facilities and improvements.....	662,932	36,704	-	699,636
Machinery and equipment.....	20,171	1,096	-	21,267
Total accumulated depreciation.....	<u>683,103</u>	<u>37,800</u>	<u>-</u>	<u>720,903</u>
Total capital assets, being depreciated, net.....	<u>1,264,615</u>	<u>(21,396)</u>	<u>-</u>	<u>1,243,219</u>
Capital assets, net.....	<u>\$ 1,309,162</u>	<u>\$ 6,164</u>	<u>\$ (16,381)</u>	<u>\$ 1,298,945</u>

**Port of San Francisco**

	Balance July 1, 2004	Increases	Decreases	Balance June 30, 2005
Capital assets, not being depreciated:				
Land.....	\$ 119,452	\$ -	\$ -	\$ 119,452
Construction in progress.....	12,056	12,250	(3,912)	20,394
Total capital assets, not being depreciated.....	<u>131,508</u>	<u>12,250</u>	<u>(3,912)</u>	<u>139,846</u>
Capital assets, being depreciated:				
Facilities and improvements.....	265,826	8,243	(790)	273,279
Machinery and equipment.....	13,368	921	(812)	13,477
Total capital assets, being depreciated.....	<u>279,194</u>	<u>9,164</u>	<u>(1,602)</u>	<u>286,756</u>
Less accumulated depreciation for:				
Facilities and improvements.....	157,300	8,963	(790)	165,473
Machinery and equipment.....	7,957	1,004	(803)	8,158
Total accumulated depreciation.....	<u>165,257</u>	<u>9,967</u>	<u>(1,593)</u>	<u>173,631</u>
Total capital assets, being depreciated, net.....	<u>113,937</u>	<u>(803)</u>	<u>(9)</u>	<u>113,125</u>
Capital assets, net.....	<u>\$ 245,445</u>	<u>\$ 11,447</u>	<u>\$ (3,921)</u>	<u>\$ 252,971</u>

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**Laguna Honda Hospital**

	Balance July 1, 2004	Increases *	Decreases *	Balance June 30, 2005
Capital assets, not being depreciated:				
Land.....	\$ 914	\$ -	\$ -	\$ 914
Construction in progress.....	56,574	11,345	-	67,919
Total capital assets, not being depreciated.....	<u>57,488</u>	<u>11,345</u>	<u>-</u>	<u>68,833</u>
Capital assets, being depreciated:				
Facilities and improvements.....	27,388	-	-	27,388
Machinery and equipment.....	12,619	288	-	12,907
Property held under lease.....	2,294	508	-	2,802
Total capital assets, being depreciated.....	<u>42,301</u>	<u>796</u>	<u>-</u>	<u>43,097</u>
Less accumulated depreciation for:				
Facilities and improvements.....	22,056	779	-	22,835
Machinery and equipment.....	11,830	155	-	11,985
Property held under lease.....	46	89	-	135
Total accumulated depreciation.....	<u>33,932</u>	<u>1,023</u>	<u>-</u>	<u>34,955</u>
Total capital assets, being depreciated, net	<u>8,369</u>	<u>(227)</u>	<u>-</u>	<u>8,142</u>
Capital assets, net.....	<u>\$ 65,857</u>	<u>\$ 11,118</u>	<u>\$ -</u>	<u>\$ 76,975</u>

**Other Fund - San Francisco Market Corporation**

	Balance July 1, 2004	Increases	Decreases	Balance June 30, 2005
Capital assets, being depreciated:				
Facilities and improvements.....	\$ 9,483	\$ 48	\$ -	\$ 9,531
Machinery and equipment.....	29	26	-	55
Total capital assets, being depreciated.....	<u>9,512</u>	<u>74</u>	<u>-</u>	<u>9,586</u>
Less accumulated depreciation for:				
Facilities and improvements.....	4,256	282	-	4,538
Machinery and equipment.....	-	-	-	-
Total accumulated depreciation.....	<u>4,256</u>	<u>282</u>	<u>-</u>	<u>4,538</u>
Total capital assets, being depreciated, net.....	<u>5,256</u>	<u>(208)</u>	<u>-</u>	<u>5,048</u>
Capital assets, net.....	<u>\$ 5,256</u>	<u>\$ (208)</u>	<u>\$ -</u>	<u>\$ 5,048</u>

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**Total Business-type Activities**

	Balance July 1, 2004	Increases *	Decreases *	Balance June 30, 2005
Capital assets, not being depreciated:				
Land.....	\$ 193,781	\$ -	\$ -	\$ 193,781
Construction in progress.....	640,769	361,316	(280,517)	721,568
Total capital assets, not being depreciated.....	834,550	361,316	(280,517)	915,349
Capital assets, being depreciated:				
Facilities and improvements.....	8,794,997	209,507	(4,119)	9,000,385
Machinery and equipment.....	1,393,054	18,357	(11,427)	1,399,984
Infrastructure.....	703,673	13,052	-	716,725
Property held under lease.....	2,294	508	-	2,802
Easements.....	135,598	3,011	-	138,609
Total capital assets, being depreciated.....	11,029,616	244,435	(15,546)	11,258,505
Less accumulated depreciation for:				
Facilities and improvements.....	2,645,001	274,889	(790)	2,919,100
Machinery and equipment.....	480,347	82,372	(10,670)	552,049
Infrastructure.....	209,002	22,680	-	231,682
Property held under lease.....	46	89	-	135
Easements.....	46,445	6,630	-	53,075
Total accumulated depreciation.....	3,380,841	386,660	(11,460)	3,756,041
Total capital assets, being depreciated, net.....	7,648,775	(142,225)	(4,086)	7,502,464
Capital assets, net.....	\$ 8,483,325	\$ 219,091	\$ (284,603)	\$ 8,417,813

\* The increases and decreases include transfers of categories of fixed assets from properties held under lease to facilities and improvements.

Depreciation expense was charged to functions/programs of the primary government as follows (in thousands):

<b>Governmental Activities</b>	
Public protection.....	\$ 10,224
Public works, transportation, and commerce.....	15,693
Human welfare and neighborhood development.....	551
Community health.....	916
Culture and recreation.....	23,915
General administration and finance.....	13,498
Capital assets held by the City's internal service funds charged to the various functions on a prorated basis.....	963
Total depreciation expense - governmental activities	\$ 65,760
<b>Business-type activities:</b>	
Airport.....	\$ 161,641
Transportation.....	118,421
Port.....	9,967
Water.....	40,112
Power.....	10,759
Hospitals.....	7,678
Sewer.....	37,800
Market.....	282
Total depreciation expense - business-type activities.....	\$ 386,660

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Equipment is generally estimated to have useful lives of 2 to 40 years, except for certain equipment of the Water Department that has an estimated useful life of up to 75 years. Facilities and improvements are generally estimated to have useful lives from 15 to 50 years, except for utility type assets of the Water Department (Water), Hetch Hetchy Water and Power (Hetch Hetchy), the Clean Water Program (CWP), the Municipal Transportation Agency (MTA), Laguna Honda Hospital (LHH), and the Port of San Francisco (Port) that have estimated useful lives from 51 to 175 years. These long-lived assets include reservoirs, aqueducts, pumping stations of Hetch Hetchy, Cable Car Barn facilities and structures of MTA, building and structures of LHH, and pier substructures of the Port and totaled \$1.5 billion as of June 30, 2005. In addition, the Water Department had utility type assets with useful lives over 100 years, which totaled \$4.5 million as of June 30, 2005.

During the fiscal year ended June 30, 2005, the City's enterprise funds incurred total interest expense and interest income of approximately \$268 million and \$33.3 million, respectively. Of these amounts, interest expense of approximately \$8.3 million was capitalized, while no interest income was received as part of the cost of constructing proprietary capital assets.

During fiscal year ended June 30, 2005, Water, Hetch Hetchy, and CWP expensed \$14.1 million, \$3.3 million, and \$1.7 million, respectively, related to capitalized design and planning costs on certain projects that were discontinued. The amounts of the write-off were recognized as other operating expense in the accompanying financial statements.

Special items identify significant transactions or events within the control of management that are either unusual in nature or infrequent in occurrence. During fiscal year ended June 30, 2005, the Airport recognized a loss due to asset impairment of approximately \$50 million (including capitalized interest of \$5 million) relating to potential runway reconfigurations, construction methods, and materials.

**Component Unit - Redevelopment Agency**

Capital asset activity of the Redevelopment Agency for the year ended June 30, 2005 was as follows (in thousands):

	Balance July 1, 2004	Increases	Decreases	Balance June 30, 2005
Capital assets, not being depreciated:				
Property held under lease.....	\$ 82,692	\$ 22,276	\$ -	\$ 104,968
Construction in progress.....	31,568	17,494	(26,770)	22,292
Total capital assets, not being depreciated/amortized.....	<u>114,260</u>	<u>39,770</u>	<u>(26,770)</u>	<u>127,260</u>
Capital assets, being depreciated:				
Facilities and improvements.....	137,212	24,227	-	161,439
Leasehold improvements.....	21,602	-	-	21,602
Machinery and equipment.....	7,759	68	-	7,827
Total capital assets, being depreciated.....	<u>166,573</u>	<u>24,295</u>	<u>-</u>	<u>190,868</u>
Less accumulated depreciation and amortization for:				
Facilities and improvements.....	32,332	3,683	-	36,015
Leasehold improvements.....	7,354	432	-	7,786
Machinery and equipment.....	7,157	283	-	7,440
Total accumulated depreciation and amortization.....	<u>46,843</u>	<u>4,398</u>	<u>-</u>	<u>51,241</u>
Total capital assets, being depreciated, net.....	<u>119,730</u>	<u>19,897</u>	<u>-</u>	<u>139,627</u>
Redevelopment Agency capital assets, net.....	<u>\$ 233,990</u>	<u>\$ 59,667</u>	<u>\$ (26,770)</u>	<u>\$ 266,887</u>

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**(8) BONDS, LOANS, CAPITAL LEASES AND OTHER PAYABLES**

The following is a summary of long-term obligations of the City as of June 30, 2005 (in thousands):

<b>GOVERNMENTAL ACTIVITIES</b>			
<u>Type of Obligation and Purpose</u>	<u>Final Maturity Date</u>	<u>Remaining Interest Rates</u>	<u>Amount</u>
<b>GENERAL OBLIGATION BONDS (a):</b>			
Affordable housing.....	2021	4.0 to 7.05%	\$ 84,030
California Academy of Sciences.....	2024	3.0 to 5.25%	7,805
Library.....	2022	2.5 to 5.0%	35,940
Laguna Honda Hospital.....	2030	3.25 to 5.0%*	230,000
Museums.....	2019	4.5 to 5.5%	13,345
Parks and playgrounds.....	2024	2.4 to 5.75%	135,570
Schools.....	2023	2.4 to 5.75%	131,760
Zoo facilities.....	2022	2.5 to 5.75%	33,525
Refunding.....	2016	3.0 to 5.75%	<u>414,380</u>
General obligation bonds - governmental activities.....			<u>1,086,355</u>
<b>LEASE REVENUE BONDS:</b>			
San Francisco Finance Corporation (b) & (e).....	2030	2.0 to 5.5%**	<u>230,620</u>
Lease revenue bonds - governmental activities.....			<u>230,620</u>
<b>OTHER LONG-TERM OBLIGATIONS:</b>			
Certificates of participation (c) & (d).....	2034	3.0 to 5.3%	283,320
Commercial Paper (c).....	2006	1.85 to 2.85%	150,000
Loans (c), (d) & (f).....	2015	2.0 to 6.7%	7,961
Capital leases payable (c) & (f).....	2024	1.5 to 7.05%	198,703
Settlement Obligation Bonds (d).....	2011	2.4 to 3.05%	38,670
Accrued vacation and sick leave (d) & (f).....			125,037
Accrued workers' compensation (d) & (f).....			214,805
Estimated claims payable (d) & (f).....			<u>83,537</u>
Other long-term obligations - governmental activities.....			<u>1,102,033</u>
<b>DEFERRED AMOUNTS:</b>			
Bond issuance premiums.....			16,254
Bond issuance discounts.....			(2,425)
Bond refunding.....			<u>(5,843)</u>
Deferred amounts.....			<u>7,986</u>
Governmental activities total long-term obligations.....			<u>\$ 2,426,994</u>

Debt service payments are made from the following sources:

- (a) Property tax recorded in the Debt Service Fund.
- (b) Lease revenues from participating departments in the General, Special Revenue and Enterprise Funds.
- (c) Revenues recorded in the Special Revenue Funds.
- (d) Revenues recorded in the General Fund.
- (e) Hotel taxes and other revenues recorded in the General and Special Revenue Funds.
- (f) User-charge reimbursements from the General, Special Revenue and Enterprise Funds.

Internal Service Funds serve primarily the governmental funds. Accordingly, long-term liabilities for the Internal Service Funds are included in the above amounts.

\* Laguna Honda Hospital General Obligation Bonds Series 2005 A are fixed rate bonds and Series 2005 B, C and D are variable rate bonds that reset weekly. The remaining interest rates stated are for Series 2005 A. The average interest rate for the variable rate bonds from issuance date of May 26, 2005 through June 30, 2005 was 2.42%. The rate at June 30, 2005 was 2.20%.

\*\* Includes the Moscone Center West Expansion Project, which was financed with variable rate bonds that reset weekly. The average interest rate from issuance date of November 2, 2000 through June 30, 2005 was 1.57%. The rate at June 30, 2005 was 2.21%.

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**BUSINESS-TYPE ACTIVITIES**

Entity and Type of Obligation	Final Maturity Date	Remaining Interest Rates	Amount
San Francisco International Airport:			
Revenue bonds.....	2032	1.55 to 8.0%*	\$ 4,114,431
Water Department:			
Revenue bonds.....	2032	3.0 to 7.0%	486,970
Commercial paper.....	2006	2.58 to 2.75%	80,000
Accreted interest.....	2019	7.0%	2,749
Hetch Hetchy Water and Power:			
Notes, loans and other payables.....	2010	3.0%	595
Municipal Transportation Agency:			
Parking and Traffic			
Revenue bonds.....	2020	4.0 to 5.0%	21,170
Lease revenue bonds.....	2022	3.7 to 6.0%	10,465
Capital leases.....	2008	3.41 to 5.11%	195
Notes, loans and other payables**.....	2010	3.0 to 5.25%	20,266
Downtown Parking - parking revenue refunding bonds.....	2018	3.0 to 5.375%	11,440
Ellis-O'Farrell - parking revenue refunding bonds.....	2017	3.5 to 4.7%	5,315
Japan Center Garage Corporation - notes, loans and other payables.....	2008	6.75%	309
Uptown Parking - revenue bonds.....	2031	4.5 to 6.0%	18,425
General Hospital Medical Center:			
Capital leases.....	2010	5.7 to 8.5%	2,519
Clean Water Program:			
Revenue bonds.....	2026	3.0 to 5.25%	396,270
State of California - Revolving fund loans.....	2021	2.8 to 3.5%	134,783
Port of San Francisco:			
Revenue bonds.....	2010	2.25 to 4.0%	19,940
Notes, loans and other payables.....	2029	4.5%	3,359
Laguna Honda Hospital:			
Capital leases.....	2009	3.465%	2,040
Accrued vacation and sick leave.....			75,318
Accrued workers' compensation.....			176,623
Estimated claims payable.....			68,718
Deferred Amounts:			
Bond issuance premiums.....			45,420
Bond issuance discounts.....			(20,108)
Bond refunding.....			(92,446)
Business-type activities total long-term obligations.....			<u>\$ 5,584,766</u>

\* Includes Second Series Revenue Bonds Issue 31 and 32, which were issued in an auction mode. The average interest rates on the Issue 31 and 32 bonds were 1.8% and 2.36%, respectively, from the dates of issuance through June 30, 2005.

\*\* Includes an unamortized loan premium of \$0.9 million for Parking and Traffic.

Sources of funds to meet debt service requirements are revenues derived from user fees and charges for services recorded in their respective Enterprise Funds.

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**COMPONENT UNITS**

<u>Type of Obligation</u>	<u>Final Maturity Date</u>	<u>Remaining Interest Rates</u>	<u>Amount</u>
SAN FRANCISCO REDEVELOPMENT AGENCY AND FINANCING AUTHORITY:			
Lease Revenue Bonds:			
Moscone Convention Center (a).....	2025	2.0 to 7.05%	\$ 138,155
Hotel Tax Revenue Bonds (b).....	2025	4.25 to 6.94%	67,220
Financing Authority Bonds:			
Tax Allocation Revenue Bonds (c).....	2031	2.0 to 8.3%	469,671
South Beach Harbor Variable Rate			
Refunding Bonds (d).....	2017	Variable (2.4% at 6/30/05)	10,000
Less deferred amounts:			
Bond issuance premiums.....			8,966
Refunding loss.....			<u>(3,042)</u>
Sub-total.....			690,970
California Department of Boating and			
Waterways Loan (e).....	2037	4.5%	8,000
Accrued interest payable.....			77,025
Accrued vacation and sick leave pay.....			<u>2,701</u>
Component unit total long-term obligations.....			<u>\$ 778,696</u>

Debt service payments are made from the following sources:

- (a) Hotel taxes and operating revenues recorded in the Convention Facilities Special Revenue Fund and existing debt service/escrow trust funds.
- (b) Hotel taxes from hotels located in the Redevelopment Project Areas.
- (c) Property taxes allocated to the Redevelopment Agency based on increased assessed valuations in project areas (note 12) and existing debt service/escrow trust funds.
- (d) South Beach Harbor Project cash reserves, property tax increments and project revenues.
- (e) South Beach Harbor Project revenues (subordinated to Refunding Bonds).

Debt Compliance

There are a number of limitations and restrictions contained in the various bond indentures. The City believes it is in compliance with all significant limitations and restrictions.

Legal Debt Limit and Legal Debt Margin

As of June 30, 2005, the City's debt limit (3% of valuation subject to taxation) was \$3.2 billion. The total amount of debt applicable to the debt limit was \$1.1 billion, net of certain assets in other non-major governmental funds, and other deductions allowed by law. The resulting legal debt margin was \$2.1 billion.

Arbitrage

Under U.S. Treasury Department regulations, all governmental tax-exempt debt issued after August 31, 1986 is subject to arbitrage rebate requirements. The requirements stipulate, in general, that the earnings from the investment of tax exempt bond proceeds, which exceed related interest expenditures on the bonds, must be remitted to the Federal government on every fifth anniversary of each bond issue. The City has evaluated each general obligation bond and has recognized an arbitrage liability of \$0.4 million as of June 30, 2005. This arbitrage liability is reported in deferred credits and other liabilities in the governmental activities of the statement of net assets. The Finance Corporation has evaluated their lease revenue bonds, and a liability of \$0.2 million was reported in the deferred credits and other liabilities in the Internal Service Fund as of June 30, 2005. Each Enterprise Fund has performed a similar analysis of its debt which is subject to arbitrage rebate requirements. Any material arbitrage liability related to the

**CITY AND COUNTY OF SAN FRANCISCO**  
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debt of the Enterprise Funds has been recorded as a liability in the respective fund. In addition, the Redevelopment Agency records any arbitrage liability in deferred credits and other liabilities.

Assessment District

During June 1996, the City issued \$1 million of Limited Obligation Improvement Bonds for the Bayshore Hester Assessment District No. 95-1. These bonds were issued pursuant to the Improvement Bond Act of 1915. The proceeds were used to finance the construction of a new public right-of-way. The bonds began to mature during the fiscal year ended June 30, 1999 and continue through 2026 bearing interest from 6.0% to 6.85%. These bonds do not represent obligations of the City. Neither the faith and credit nor the taxing power of the City is pledged to the payment of the bonds. Accordingly, the debt has not been included in the basic financial statements. Assessments collected for repayment of this debt are received in the Tax Collection Agency Fund. Unpaid assessments constitute fixed liens on the lots and parcels assessed within the Bayshore-Hester Assessment District and do not constitute a personal indebtedness of the respective owners of such lots and parcels.

Mortgage Revenue Bonds

In order to facilitate affordable housing, the City issues mortgage revenue bonds for the financing of multifamily rental housing and for below-market rate mortgage financing for first time homebuyers. These obligations are secured by the related mortgage indebtedness and are not obligations of the City. As of June 30, 2005, the aggregate outstanding obligation of such bonds was \$130 million.

**Changes in Long-Term Obligations**

The changes in long-term obligations for governmental activities for the year ended June 30, 2005, are as follows (in thousands):

	July 1, 2004	Additional Obligations, Interest Accretion and Net Increases	Current Maturities Retirements, and Net Decreases	June 30, 2005	Amounts Due Within One Year
<b>Governmental activities:</b>					
Bonds payable:					
General obligation bonds.....	\$ 844,350	\$ 306,875	\$ (64,870)	\$ 1,086,355	\$ 67,805
Lease revenue bonds.....	245,680	-	(15,060)	230,620	17,780
Certificates of participation.....	290,635	39,350	(46,665)	283,320	7,160
Settlement obligation bond.....	44,275	-	(5,605)	38,670	5,715
Less deferred amounts:					
For issuance premiums.....	4,912	11,989	(647)	16,254	-
For issuance discounts.....	(2,509)	-	84	(2,425)	-
On refunding.....	(6,339)	(253)	749	(5,843)	-
Total Bonds payable.....	1,421,004	357,961	(132,014)	1,646,951	98,460
Commercial Paper.....	50,000	100,000	-	150,000	150,000
Loans.....	9,515	500	(2,054)	7,961	943
Capital leases.....	194,815	6,364	(2,476)	198,703	14,888
Accrued vacation and sick leave pay.....	128,417	72,900	(76,280)	125,037	63,098
Accrued workers' compensation.....	213,630	34,042	(32,867)	214,805	44,624
Estimated claims payable.....	79,805	29,360	(25,628)	83,537	37,487
Governmental activities long-term obligations..	<u>\$ 2,097,186</u>	<u>\$ 601,127</u>	<u>\$ (271,319)</u>	<u>\$ 2,426,994</u>	<u>\$ 409,500</u>

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Internal Service Funds serve primarily the governmental funds, the long-term liabilities of which are included as part of the above totals for governmental activities. At the year ended June 30, 2005, \$230.7 million of lease revenue bonds, \$0.5 million of capital leases, \$0.1 million of loans, \$3.7 million of accrued vacation and sick leave pay and \$1.2 million of accrued workers' compensation are included in the above amounts. Also, for the governmental activities, claims and judgments and compensated absences are generally liquidated by the general fund.

The changes in long-term obligations for each enterprise fund for the year ended June 30, 2005, are as follows (in thousands):

	July 1, 2004	Additional Obligations, Interest Accretion and Net Increases	Current Maturities Retirements, and Net Decreases	June 30, 2005	Amounts Due Within One Year
<b>San Francisco International Airport</b>					
Bonds payable:					
Revenue bonds.....	\$ 4,173,170	\$ 311,596	\$ (370,335)	\$ 4,114,431	\$ 79,126
Less deferred amounts:					
For issuance premiums.....	17,544	-	(435)	17,109	-
For issuance discounts.....	(19,059)	-	1,709	(17,350)	-
On refunding.....	(53,004)	(13,281)	5,695	(60,590)	-
Total bonds payable.....	4,118,651	298,315	(363,366)	4,053,600	79,126
Accrued vacation and sick leave pay.....	11,576	7,788	(7,874)	11,490	5,928
Accrued workers' compensation.....	5,155	2,316	(2,352)	5,119	1,339
Estimated claims payable.....	459	575	(189)	845	812
Long-term obligations.....	<u>\$ 4,135,841</u>	<u>\$ 308,994</u>	<u>\$ (373,781)</u>	<u>\$ 4,071,054</u>	<u>\$ 87,205</u>

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The changes in long-term obligations for each enterprise fund for the year ended June 30, 2005, are as follows (in thousands) - continued:

	July 1, 2004	Additional Obligations, Interest Accretion and Net Increases	Current Maturities Retirements, and Net Decreases	June 30, 2005	Amounts Due Within One Year
<b>Water Department</b>					
Bonds payable:					
Revenue bonds.....	\$ 501,025	\$ -	\$ (14,055)	\$ 486,970	\$ 14,790
Less deferred amounts:					
For issuance premiums.....	6,932	-	(245)	6,687	-
For issuance discounts.....	(2,709)	-	(49)	(2,758)	-
On refunding.....	(7,885)	-	474	(7,411)	-
Total bonds payable.....	497,363	-	(13,875)	483,488	14,790
Accreted interest payable.....	2,567	182	-	2,749	-
Commercial paper.....	25,000	55,000	-	80,000	80,000
Accrued vacation and sick leave pay.....	9,130	6,176	(5,722)	9,584	4,755
Accrued workers' compensation.....	11,695	669	(2,013)	10,351	2,159
Estimated claims payable.....	6,111	1,385	(2,210)	5,286	1,225
Long-term obligations.....	\$ 551,866	\$ 63,412	\$ (23,820)	\$ 591,458	\$ 102,929
<b>Hetch Hetchy Water and Power</b>					
Notes, loans, and other payables.....	\$ 693	\$ -	\$ (98)	\$ 595	\$ 101
Accrued vacation and sick leave pay.....	1,798	973	(902)	1,869	988
Accrued workers' compensation.....	2,276	463	(289)	2,450	500
Estimated claims payable.....	169	3,702	(1,869)	2,002	432
Long-term obligations.....	\$ 4,936	\$ 5,138	\$ (3,158)	\$ 6,916	\$ 2,021
<b>Municipal Transportation Agency</b>					
Bonds payable:					
Revenue bonds.....	\$ 58,420	\$ -	\$ (2,070)	\$ 56,350	\$ 2,365
Lease revenue bonds.....	11,425	-	(960)	10,465	1,010
Less deferred amounts:					
For issuance premiums.....	969	-	(29)	940	-
Total bonds payable.....	70,814	-	(3,059)	67,755	3,375
Notes, loans, and other payables.....	24,299	335	(4,059)	20,575 *	4,124
Capital leases.....	561	91	(457)	195	138
Accrued vacation and sick leave pay.....	24,219	19,077	(19,196)	24,100	13,810
Accrued workers' compensation.....	119,440	17,443	(21,531)	115,352	25,289
Estimated claims payable.....	33,844	23,602	(7,680)	49,766	16,836
Long-term obligations.....	\$ 273,177	\$ 60,548	\$ (55,982)	\$ 277,743	\$ 63,572
* Includes an unamortized loan premium of \$0.9 million for Parking and Traffic.					
<b>General Hospital Medical Center</b>					
Capital leases.....	\$ 2,205	\$ 959	\$ (645)	\$ 2,519	\$ 653
Accrued vacation and sick leave pay.....	13,564	10,231	(9,559)	14,236	8,167
Accrued workers' compensation.....	22,993	4,199	(4,293)	22,899	4,550
Long-term obligations.....	\$ 38,762	\$ 15,389	\$ (14,497)	\$ 39,654	\$ 13,370

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The changes in long-term obligations for all enterprise funds for the year ended June 30, 2005, are as follows (in thousands) - continued:

	July 1, 2004	Additional Obligations, Interest Accretion and Net Increases	Current Maturities Retirements, and Net Decreases	June 30, 2005	Amounts Due Within One Year
<b>Clean Water Program</b>					
Bonds payable:					
Revenue bonds.....	\$ 396,270	\$ -	\$ -	\$ 396,270	\$ -
Less deferred amounts:					
For issuance premiums.....	21,386	-	(1,005)	20,381	-
On refunding.....	(25,124)	-	1,727	(23,397)	-
Total bonds payable.....	392,532	-	722	393,254	-
State of California - Revolving fund loans.....	150,196	-	(15,413)	134,783	15,914
Accrued vacation and sick leave pay.....	3,756	2,208	(1,869)	4,095	2,173
Accrued workers' compensation.....	4,800	721	(847)	4,674	967
Estimated claims payable.....	4,761	4,779	(448)	9,092	2,241
Long-term obligations.....	<u>\$ 556,045</u>	<u>\$ 7,708</u>	<u>\$ (17,855)</u>	<u>\$ 545,898</u>	<u>\$ 21,295</u>
<b>Port of San Francisco</b>					
Bonds payable:					
General obligation bonds.....	\$ 400	\$ -	\$ (400)	\$ -	\$ -
Revenue bonds.....	27,095	19,940	(27,095)	19,940	3,390
Less deferred amounts:					
For issuance premiums.....	216	159	(72)	303	-
On refunding.....	(788)	(510)	250	(1,048)	-
Total bonds payable.....	26,923	19,589	(27,317)	19,195	3,390
Notes, loans, and other payables.....	3,436	-	(77)	3,359	80
Capital leases.....	23	-	(23)	-	-
Accrued vacation and sick leave pay.....	1,839	1,431	(1,578)	1,692	922
Accrued workers' compensation.....	3,113	417	(804)	2,726	547
Estimated claims payable.....	2,287	300	(860)	1,727	957
Long-term obligations.....	<u>\$ 37,621</u>	<u>\$ 21,737</u>	<u>\$ (30,659)</u>	<u>\$ 28,699</u>	<u>\$ 5,896</u>
<b>Laguna Honda Hospital</b>					
Capital leases.....	\$ 2,102	\$ 409	\$ (471)	\$ 2,040	\$ 499
Accrued vacation and sick leave pay.....	8,008	6,290	(6,046)	8,252	4,881
Accrued workers' compensation.....	14,024	27,088	(28,060)	13,052	2,654
Long-term obligations.....	<u>\$ 24,134</u>	<u>\$ 33,787</u>	<u>\$ (34,577)</u>	<u>\$ 23,344</u>	<u>\$ 8,034</u>

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A summary of the changes in long-term obligations for all enterprise funds for the year ended June 30, 2005, is as follows (in thousands):

	July 1, 2004	Additional Obligations, Interest Accretion and Net Increases	Current Maturities Retirements, and Net Decreases	June 30, 2005	Amounts Due Within One Year
<b>Total Business-type Activities:</b>					
Bonds payable:					
General obligation bonds.....	\$ 400	\$ -	\$ (400)	\$ -	\$ -
Revenue bonds.....	5,155,980	331,536	(413,555)	5,073,961	99,671
Lease revenue bonds.....	11,425	-	(960)	10,465	1,010
Less deferred amounts:					
For issuance premiums.....	47,047	159	(1,786)	45,420	-
For issuance discounts.....	(21,768)	-	1,660	(20,108)	-
On refunding.....	(86,801)	(13,791)	8,146	(92,446)	-
Total bonds payable.....	5,106,283	317,904	(406,895)	5,017,292	100,681
Accreted interest payable.....	2,567	182	-	2,749	-
Commercial paper.....	25,000	55,000	-	80,000	80,000
State of California - Revolving fund loans.....	150,196	-	(15,413)	134,783	15,914
Notes, loans, and other payables.....	28,428	335	(4,234)	24,529	4,305
Capital leases.....	4,891	1,482	(1,619)	4,754	1,290
Accrued vacation and sick leave pay.....	73,890	54,174	(52,746)	75,318	41,624
Accrued workers' compensation.....	183,496	53,330	(60,203)	176,623	38,005
Estimated claims payable.....	47,631	34,324	(13,237)	68,718	22,503
Business-type activities long term obligations....	<u>\$ 5,622,382</u>	<u>\$ 516,731</u>	<u>\$ (554,347)</u>	<u>\$ 5,584,766</u>	<u>\$ 304,322</u>

The changes in long term obligations for the component unit for the year ended June 30, 2005, are as follows (in thousands):

	July 1, 2004	Additional Obligations, Interest Accretion and Net Increases	Current Maturities Retirements, and Net Decreases	June 30, 2005	Amounts Due Within One Year
<b>Component Unit:</b>					
<b>Redevelopment Agency</b>					
Bonds payable:					
Revenue bonds.....	\$ 727,713	\$ -	\$ (52,667)	\$ 675,046	\$ 28,581
Refunding bonds.....	11,500	-	(1,500)	10,000	-
Less deferred amounts:					
For issuance premiums.....	9,641	-	(675)	8,966	-
On refunding.....	(3,263)	-	221	(3,042)	-
Total bonds payable.....	745,591	-	(54,621)	690,970	28,581
Accreted interest payable.....	142,388	9,167	(74,530)	77,025	2,084 (1)
Notes, loans, and other payables.....	8,000	-	-	8,000	-
Accrued vacation and sick leave pay.....	2,733	6	(38)	2,701	1,092
Component unit - long term obligations.....	<u>\$ 898,712</u>	<u>\$ 9,173</u>	<u>\$ (129,189)</u>	<u>\$ 778,696</u>	<u>\$ 31,757</u>

(1) This amount is included in accrued interest payable in the accompanying Statement of Net Assets.

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Annual debt service requirements to maturity for all bonds and loans outstanding as of June 30, 2005, for governmental activities are as follows (in thousands):

Fiscal Year Ending June 30	Governmental Activities <sup>(1) (2) (3)</sup>							
	General Obligation Bonds		Lease Revenue Bonds		Other Long-Term Obligations		Total	
	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest
2006.....	\$ 67,805	\$ 50,878	\$ 17,780	\$ 6,979	\$ 13,818	\$ 14,788	\$ 99,403	\$ 72,645
2007.....	70,795	47,346	15,805	6,424	15,977	14,269	102,577	68,039
2008.....	78,090	43,871	13,955	5,928	15,863	13,723	107,908	63,522
2009.....	81,715	40,079	12,565	5,469	16,427	13,165	110,707	58,713
2010.....	82,495	36,070	7,180	5,019	16,921	12,609	106,596	53,698
2011-2015..	327,125	123,872	35,670	21,438	61,520	54,236	424,315	199,546
2016-2020..	209,045	56,107	36,995	15,651	48,745	41,711	294,785	113,469
2021-2025..	99,385	17,084	42,970	9,631	43,265	30,636	185,620	57,351
2026-2030..	69,900	5,279	47,700	3,686	51,050	18,860	168,650	27,825
2031-2035..	-	-	-	-	46,365	4,894	46,365	4,894
Total.....	<u>\$1,086,355</u>	<u>\$ 420,586</u>	<u>\$ 230,620</u>	<u>\$ 80,225</u>	<u>\$ 329,951</u>	<u>\$ 218,891</u>	<u>\$ 1,646,926</u>	<u>\$ 719,702</u>

- (1) The specific year for payment of estimated claims payable, accrued vacation and sick leave pay and accrued workers' compensation is not practicable to determine.
- (2) The payment stream for principal and interest on commercial paper is not practicable to determine because the timing of the issuance and payment is based on project expenditures.
- (3) Includes the following variable rate demand notes, Moscone Center Expansion Project Lease Revenue Bonds and Laguna Honda Hospital General Obligation Bonds. Currently, they bear interest at a weekly rate of 2.21% and 2.2% respectively, at June 30, 2005.

The annual debt service requirement to maturity for all bonds and loans outstanding as of June 30, 2005, for each enterprise fund is as follows (in thousands):

Fiscal Year Ending June 30	San Francisco International Airport <sup>(1)</sup>					
	Revenue Bonds		Other Long-Term Obligations		Total	
	Principal	Interest	Principal	Interest	Principal	Interest
2006.....	\$ 79,126	\$ 201,214	\$ -	\$ -	\$ 79,126	\$ 201,214
2007.....	86,505	198,119	-	-	86,505	198,119
2008.....	105,720	192,997	-	-	105,720	192,997
2009.....	110,865	188,512	-	-	110,865	188,512
2010.....	118,795	182,488	-	-	118,795	182,488
2011-2015..	759,270	816,444	-	-	759,270	816,444
2016-2020..	940,920	614,584	-	-	940,920	614,584
2021-2025..	1,116,380	368,838	-	-	1,116,380	368,838
2026-2030..	742,520	122,053	-	-	742,520	122,053
2031-2035..	54,330	3,637	-	-	54,330	3,637
Total.....	<u>\$ 4,114,431</u>	<u>\$ 2,888,886</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 4,114,431</u>	<u>\$ 2,888,886</u>

- (1) The specific year for payment of estimated claims payable, accrued vacation and sick leave pay and accrued workers' compensation is not practicable to determine.

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The annual debt service requirement to maturity for all bonds and loans outstanding as of June 30, 2005, for each enterprise fund is as follows (in thousands) - continued:

Water Department <sup>(1)(2)</sup>						
Fiscal Year Ending	Revenue Bonds		Other Long-Term Obligations		Total	
	Principal	Interest	Principal	Interest	Principal	Interest
June 30						
2006.....	\$ 14,790	\$ 23,315	\$ -	\$ -	\$ 14,790	\$ 23,315
2007.....	15,450	22,666	-	-	15,450	22,666
2008.....	16,225	21,921	-	-	16,225	21,921
2009.....	17,035	21,131	-	-	17,035	21,131
2010.....	17,805	20,370	-	-	17,805	20,370
2011-2015...	102,670	88,254	-	-	102,670	88,254
2016-2020...	85,815	64,100	-	-	85,815	64,100
2021-2025...	84,165	43,683	-	-	84,165	43,683
2026-2030...	86,095	22,183	-	-	86,095	22,183
2031-2035...	46,920	3,142	-	-	46,920	3,142
Total.....	\$ 486,970	\$ 330,765	\$ -	\$ -	\$ 486,970	\$ 330,765

Hetch Hetchy Water and Power <sup>(1)</sup>						
Fiscal Year Ending	Revenue Bonds		Other Long-Term Obligations		Total	
	Principal	Interest	Principal	Interest	Principal	Interest
June 30						
2006.....	\$ -	\$ -	\$ 101	\$ 17	\$ 101	\$ 17
2007.....	-	-	104	14	104	14
2008.....	-	-	107	11	107	11
2009.....	-	-	110	8	110	8
2010.....	-	-	115	4	115	4
2011-2015...	-	-	58	1	58	1
Total.....	\$ -	\$ -	\$ 595	\$ 55	\$ 595	\$ 55

Municipal Transportation Agency <sup>(1)(3)</sup>						
Fiscal Year Ending	Revenue and Lease Revenue Bonds		Other Long-Term Obligations		Total	
	Principal	Interest	Principal	Interest	Principal	Interest
June 30						
2006.....	\$ 3,375	\$ 3,281	\$ 4,123	\$ 931	\$ 7,498	\$ 4,212
2007.....	3,500	3,147	4,331	723	7,831	3,870
2008.....	3,650	3,003	4,519	505	8,169	3,508
2009.....	3,810	2,851	6,381	283	10,191	3,134
2010.....	3,125	2,707	279	61	3,404	2,768
2011-2015...	15,715	11,221	-	-	15,715	11,221
2016-2020...	18,405	6,420	-	-	18,405	6,420
2021-2025...	4,315	2,914	-	-	4,315	2,914
2026-2030...	-	1,420	-	-	-	1,420
2031-2035...	10,920	78	-	-	10,920	78
Total.....	\$ 66,815	\$ 37,042	\$ 19,633	\$ 2,503	\$ 86,448	\$ 39,545

- (1) The specific year for payment of accreted interest payable (Water Department), estimated claims payable, accrued vacation and sick leave pay and accrued workers' compensation is not practicable to determine.
- (2) The payment stream for principal and interest on commercial paper is not practicable to determine because the timing of the issuance and payment is based on project expenditures.
- (3) Unamortized loan premiums of \$0.9 million (MTA) are not included in principal payments.

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The annual debt service requirement to maturity for all bonds and loans outstanding as of June 30, 2005, for each enterprise fund is as follows (in thousands) - continued:

Clean Water Program <sup>(1)</sup>						
Fiscal Year Ending	Revenue Bonds		Other Long-Term Obligations		Total	
	Principal	Interest	Principal	Interest	Principal	Interest
June 30						
2006.....	\$ -	\$ 17,219	\$ 15,914	\$ 4,218	\$ 15,914	\$ 21,437
2007.....	33,445	16,718	16,430	3,701	49,875	20,419
2008.....	34,500	15,698	13,337	3,168	47,837	18,866
2009.....	35,665	14,646	13,761	2,744	49,426	17,390
2010.....	37,130	13,183	14,199	2,307	51,329	15,490
2011-2015...	121,610	48,948	46,444	5,795	168,054	54,743
2016-2020...	79,255	22,653	12,996	1,145	92,251	23,798
2021-2025...	51,155	5,310	1,702	49	52,857	5,359
2026-2030...	3,510	83	-	-	3,510	83
Total.....	\$ 396,270	\$ 154,458	\$ 134,783	\$ 23,127	\$ 531,053	\$ 177,585

Port of San Francisco <sup>(1)</sup>						
Fiscal Year Ending	Revenue Bonds		Other Long-Term Obligations		Total	
	Principal	Interest	Principal	Interest	Principal	Interest
June 30,						
2006.....	\$ 3,390	\$ 554	\$ 80	\$ 151	\$ 3,470	\$ 705
2007.....	3,975	453	84	148	4,059	601
2008.....	4,070	348	88	144	4,158	492
2009.....	4,185	222	92	140	4,277	362
2010.....	4,320	75	96	136	4,416	211
2011-2015...	-	-	549	609	549	609
2016-2020...	-	-	685	474	685	474
2021-2025...	-	-	853	305	853	305
2026-2030...	-	-	832	95	832	95
Total.....	\$ 19,940	\$ 1,652	\$ 3,359	\$ 2,202	\$ 23,299	\$ 3,854

A summary of the annual debt service requirement to maturity for all bonds and loans outstanding as of June 30, 2005, for business type activities is as follows (in thousands):

Total Business-type Activities <sup>(1) (2) (3)</sup>						
Fiscal Year Ending	Revenue Bonds		Other Long-Term Obligations		Total	
	Principal	Interest	Principal	Interest	Principal	Interest
June 30						
2006.....	\$ 100,681	\$ 245,583	\$ 20,218	\$ 5,317	\$ 120,899	\$ 250,900
2007.....	142,875	241,103	20,949	4,586	163,824	245,689
2008.....	164,165	233,967	18,051	3,828	182,216	237,795
2009.....	171,560	227,362	20,344	3,175	191,904	230,537
2010.....	181,175	218,823	14,689	2,508	195,864	221,331
2011-2015...	999,265	964,867	47,051	6,405	1,046,316	971,272
2016-2020...	1,124,395	707,757	13,681	1,619	1,138,076	709,376
2021-2025...	1,256,015	420,745	2,555	354	1,258,570	421,099
2026-2030...	832,125	145,739	832	95	832,957	145,834
2031-2035...	112,170	6,857	-	-	112,170	6,857
Total.....	\$ 5,084,426	\$ 3,412,803	\$ 158,370	\$ 27,887	\$ 5,242,796	\$ 3,440,690

- (1) The specific year for payment of accreted interest payable (Water Department), estimated claims payable, accrued vacation and sick leave pay and accrued workers' compensation is not practicable to determine.
- (2) The payment stream for principal and interest on commercial paper is not practicable to determine because the timing of the issuance and payment is based on project expenditures.
- (3) Unamortized loan premiums of \$0.9 million (MTA) are not included in principal payments.

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The annual debt service requirement to maturity for all bonds and loans outstanding as of June 30, 2005, for the component unit are as follows (in thousands):

Component Unit: Redevelopment Agency <sup>(1)</sup>								
Fiscal Year Ending June 30	Lease Revenue Bonds		Tax Revenue Bonds		Other Long-Term Obligations		Total	
	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest
2006.....	\$ 5,510	\$ 12,361	\$ 23,071	\$ 27,856	\$ -	\$ 786	\$ 28,581	\$ 41,003
2007.....	5,146	12,728	24,639	26,934	1	785	29,786	40,447
2008.....	5,544	13,027	27,018	24,141	882	779	33,444	37,947
2009.....	5,350	13,289	26,212	24,627	1,107	757	32,669	38,673
2010.....	5,152	13,565	27,051	23,529	1,169	668	33,372	37,762
2011-2015..	28,933	65,698	160,515	90,251	7,767	2,379	197,215	158,328
2016-2020..	68,040	11,171	170,492	41,755	1,190	1,489	239,722	54,415
2021-2025..	14,480	1,953	62,742	43,001	1,483	1,196	78,705	46,150
2026-2030..	-	-	13,275	1,899	1,849	831	15,124	2,730
2031-2035..	-	-	1,876	54	2,304	376	4,180	430
2036-2040..	-	-	-	-	248	12	248	12
Total.....	<u>\$ 138,155</u>	<u>\$ 143,792</u>	<u>\$ 536,891</u>	<u>\$ 304,047</u>	<u>\$ 18,000</u>	<u>\$ 10,058</u>	<u>\$ 693,046</u>	<u>\$ 457,897</u>

(1) The specific year for payment of accreted interest payable and accrued vacation and sick leave pay is not practicable to determine.

**Governmental Activities Long-term Liabilities**

General Obligation Bonds

The City issues general obligation bonds to provide funds for the acquisition or improvement of real property and construction of affordable housing. General obligation bonds have been issued for both governmental and business-type activities. The net authorized and unissued governmental activities general obligation bonds for the fiscal year ended June 30, 2005, are as follows (in thousands):

**Governmental Activities - General Obligation Bonds  
(in thousands)**

Authorized and unissued as of June 30, 2004.....	\$ 872,060
Bonds issued:	
Series 2004A, Neighborhood Recreation and Park Facilities Improvement Bonds.....	(68,800)
Series 2004B, California Academy of Sciences Improvement Bonds.....	(8,075)
Series 2005A, Laguna Honda Hospital.....	(110,000)
Series 2005B, C & D, Laguna Honda Hospital.....	<u>(120,000)</u>
Net authorized and unissued as of June 30, 2005.....	<u>\$ 565,185</u>

There were no new authorizations on general obligation bonds in the year ended June 30, 2005.

In October 2004, the City issued General Obligation Bonds, Neighborhood Recreation and Park Facilities Improvement Bonds, Series 2004A in the amount of \$68.8 million. Interest rates range from 3.0% to 5.0%. The bonds mature from June 2005 through June 2024. The bonds were issued to provide funds to finance the acquisition, construction and/or reconstruction of certain improvements to recreation and park facilities in the City, and all other works, property and structures necessary or convenient for these purposes. Debt service payments are funded through ad valorem taxes on property.

**CITY AND COUNTY OF SAN FRANCISCO  
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In October 2004, the City issued General Obligation Bonds, California Academy of Sciences Improvement Bonds, Series 2004B in the amount of \$8.1 million. Interest rates range from 3.0% to 5.0%. The bonds mature from June 2005 through June 2024. The bonds were issued to provide funds to finance the acquisition, construction, and/or reconstruction of certain improvements to the California Academy of Sciences, and all other works, property and structures necessary or convenient for these purposes. Debt service payments are funded through ad valorem taxes on property.

In May 2005, the City issued General Obligation Bonds, Laguna Honda Hospital, Series 2005A, in the amount of \$110 million and Series 2005B, C and D in the amount of \$40 million each, totaling \$120 million. Interest rates for Series 2005A ranges from 3.25% to 5.0%. The Bonds mature from June 2005 through June 2021. Series B, C & D Bonds are variable rate demand and interest rate resets weekly. The bonds mature from June 2021 through June 2030. The bonds were issued to provide funds to finance the acquisition, improvement, construction, and/or reconstruction of a new health care, assisted living and/or other type of continuing care facility or facilities to replace Laguna Honda Hospital. Debt service payments are funded through ad valorem taxes on property.

**Lease Revenue Bonds**

The changes in governmental activities - lease revenue bonds for the year ended June 30, 2005 were as follows:

**Governmental Activities - Lease Revenue Bonds  
(in thousands)**

Authorized and unissued as of June 30, 2004.....	\$ 125,218
Increase in authorization in this fiscal year:	
Current year annual increase in Finance Corporation's equipment program.....	1,886
Current year maturities in Finance Corporation's equipment program.....	8,450
Net authorized and unissued as of June 30, 2005.....	\$ 135,554

**Finance Corporation**

The purpose of the Finance Corporation is to provide a means to publicly finance through lease financings, the acquisition, construction and installation of facilities, equipment and other tangible real and personal property for the City's general governmental purposes.

The Finance Corporation uses lease revenue bonds to finance the purchase or construction of property and equipment, which are in turn leased to the City under the terms of an Indenture and Equipment Lease Agreement. These assets are then recorded in the basic financial statements of the City. Since the sole purpose of the bond proceeds is to provide lease financing to the City, any amounts that are not applied towards the acquisition or construction of real and personal property such as unapplied acquisition funds, bond issue costs, amounts withheld pursuant to reserve fund requirements, and amounts designated for capitalized interest are recorded as deferred credits until such time as they are used for their intended purposes.

**(a) Equipment Lease Program**

In the June 5, 1990 election, the voters of the City approved Proposition C, which amended the City Charter to allow the City to lease-purchase up to \$20 million of equipment through a non-profit corporation using tax-exempt obligations.

Beginning July 1, 1991, the Finance Corporation was authorized to issue lease revenue bonds up to \$20 million in aggregate principal amount outstanding plus 5% annual adjustment each July 1. As of

**CITY AND COUNTY OF SAN FRANCISCO**  
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June 30, 2005, the total authorized amount is \$39.6 million. The total accumulated annual authorization since 1990 is \$19.6 million of which \$1.9 million is new annual authorization for the fiscal year ended June 30, 2005.

The equipment lease program functions as a revolving bond authorization fund. That is, for each dollar in bond principal that is repaid, a new dollar can be issued. The Finance Corporation has issued \$104 million in equipment lease revenue bonds since 1991. As of June 30, 2005, \$85.8 million has been repaid leaving \$18.2 million in equipment lease revenue bonds outstanding and \$21.4 million available for new issuance.

The Lease Revenue Bonds, Series 2005A were originally scheduled for issuance in the fiscal year 2004-2005. In anticipation of the issuance of the Lease Revenue Bonds, Series 2005A, expenditures in the total amount of \$2.3 million for equipment were incurred in fiscal year 2004-2005. The Lease Revenue Bonds, Series 2005A were subsequently issued in October 2005 in the aggregate principal amount of \$9.4 million (see note 17). The issuance of the Lease Revenue Bonds, Series 2005A was delayed due to the budget constraints to alleviate the City's general fund of lease payment in fiscal year 2005-2006.

**(b) City-wide Communication System**

In 1993, the voters approved the issuance of up to \$50 million in lease revenue bonds to finance the acquisition and construction of a citywide emergency radio communication system (800 MHz). The Finance Corporation issued two series in January 1998 and January 1999 for \$31.2 million and \$18.7 million, respectively. As of June 30, 2005, the amount authorized and unissued was \$0.1 million. Further, in 1994, the voters approved the issuance of up to \$60 million in lease revenue bonds to finance the acquisition and construction of a combined emergency communication center to house the City's 911-emergency communication system. The Finance Corporation issued two series in June 1997 and in June 1998 for \$22.6 million and \$23.3 million, respectively. As of June 30, 2005, the amount authorized and unissued was \$14.1 million.

**(c) Moscone Center West Expansion Project**

In 1996, the voters approved the issuance of up to \$157.5 million in lease revenue bonds for the purpose of financing a portion of the costs of acquiring, constructing, and improving a free-standing expansion to the City's Moscone Convention Center. On November 2, 2000, Series 2000-1, 2000-2 and 2000-3 totaling \$157.5 million were issued. Each series of bonds may bear interest at a different rate and in a different interest rate mode from other series of bonds. Currently, the bonds bear interest at a weekly rate.

In March 2005, the Corporation revised the mandatory sinking fund schedules set forth in the Indenture of Trust dated November 1, 2000. The First Supplemental Indenture of Trust dated March 1, 2005 revised the mandatory sinking fund by spreading the principal amount of \$3 million that would otherwise have been paid on April 1, 2005 over the remaining terms of the financing through March 1, 2030. The revision of the mandatory sinking fund was due to budget constraints, which resulted in \$3 million savings for lease payment for Lease Revenue Bonds, Series 2000-1, -2, -3 in fiscal year 2004-2005.

**Refunding Certificates of Participation**

In July 2004, the City issued \$39.4 million Refunding Certificates of Participation, Series 2004-R1 (San Francisco Courthouse Project) to refinance an existing City courthouse building located at 400 McAllister in the City by refunding in whole a series of certificates of participation executed and delivered to finance the construction, furnishing, and equipping of the said building, \$40.6 million of which were outstanding.

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The Series 2004-R1 were issued with interest rates ranging from 3.0% to 4.5% and mature from April 2007 through April 2021.

The net proceeds of \$39.3 million (including original issue premium of \$0.5 million, and after payment of \$0.6 million in underwriting fees and other issuance costs), together with funds from the existing debt service reserves, were used to refund in whole a series of Certificates of Participation (San Francisco Courthouse Project), Series 1995. Although the refund resulted in the recognition of an accounting loss of \$0.3 million for the year ended June 30, 2005, the City in effect reduced its aggregate debt service payment by \$7.4 million over the next 16 years, and obtained an economic gain of \$2.3 million.

Facades Improvement Revolving Fund Loan

In January 2005, the City through the Mayor's Office of Community Development entered into a loan agreement with Wells Fargo Community Development Corporation. Under the Agreement, Wells Fargo advanced a principal sum of \$0.5 million to the City for operating and managing a revolving loan program (Loan) to assist small businesses in improving their storefront facades in targeted neighborhoods representing distressed or underserved areas of the city, including the Mission District, South of Market, Tenderloin, Chinatown, Bayview, Mid-Market, Excelsior (Outer Mission), and Ocean Avenue.

The City agrees to repay the Loan, together with interest at an initial fixed rate of 2% on the principal sum outstanding for the first ten years of the Loan and a fixed rate of 6% thereafter until the Loan is fully paid or the agreement is terminated. The principal is due and payable in the year 2015, subject to one mandatory extension for one year, provided the City continues to satisfactorily perform all its obligations under the agreement and annually thereafter at the discretion of Wells Fargo.

San Francisco County Transportation Authority Commercial Paper Notes

In March 2004, the San Francisco County Transportation Authority authorized the issuance of an initial tranche of up to \$50 million and in September 2004, the Authority authorized the second tranche of \$100 million of a programmed \$200 million aggregate principal amount of Commercial Paper Notes (Limited Tax Bonds), Series A and B. The Commercial Paper Notes are issued to provide an interim source of financing for the Authority's New Transportation Expenditure Plan until a permanent financing plan is finalized and implemented. Under this program, the Authority is able to issue commercial paper notes at prevailing interest rates not to exceed 12% per annum. The maximum maturity of the notes is 270 days. The principal amount of the commercial paper notes plus interest thereon is backed as to credit and liquidity by an irrevocable Letter of Credit (LOC), issued by Landesbank Baden-Württemberg, New York Branch in the amount up to \$217.8 million, with an expiration date of April 14, 2007. The expiration date of the irrevocable letter of credit was extended through Authority Board Resolution 06-01 on July 12, 2005 to December 29, 2015. The commercial paper notes are secured by a first lien gross pledge of the Authority's ability to levy a half-cent sales tax collected by the California State Board of Equalization. The principal and interest on the commercial paper notes will be payable at each maturity.

As of June 30, 2005, \$150 million in commercial paper notes was outstanding and maturing within 6 to 130 days after year-end with interest rates ranging from 1.85% to 2.85%.

**CITY AND COUNTY OF SAN FRANCISCO  
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***Business-Type Activities Long-Term Liabilities***

The following provides a brief description of the current year additions to the long-term debt of the business-type activities.

San Francisco International Airport

In January 2005, the San Francisco International Airport (SFO or Airport) issued Second Series Revenue Bonds Issue 31F in the amount of \$111.7 million with interest rates ranging from 3.95% to 4.91%. Proceeds from Issue 31F were deposited into an irrevocable trust with an escrow agent to advance refund certain of the SFO's Second Series Revenue Bonds as follows (in thousands):

	<u>Amount Refunded</u>	<u>Interest Rate</u>	<u>Call Price</u>
<u>Second Series Revenue Bond Issuance:</u>			
Issue 13.....	\$ 100,400	6.75% - 7.13%	\$ 102,000

The refunded Second Series Revenue Bonds have final maturity dates ranging from May 1, 2009 to May 1, 2026 and a call date of May 1, 2006.

The net proceeds of \$109.1 million (after payment of \$2.6 million in underwriting fees, insurance, surety, premium and cost of issuance account) were used to purchase U.S. Treasury Securities. The securities were deposited in an irrevocable trust with an escrow agent to provide debt service payment on the refunded bond identified above until called on May 1, 2006. The refunded bonds are considered legally defeased where the debt is legally satisfied based on certain provisions in the debt instrument even though the debt is still outstanding. Accordingly, the liability for the refunded bonds has been removed from the Statements of Net Assets. Although the advance refunding resulted in the recognition of a deferred accounting loss of \$8.2 million for the year ended June 30, 2005, SFO in effect reduced its aggregate debt service payments by approximately \$47 million over the next 22 years and obtained an economic gain (the difference between the present values of the old and new debt service payments) of \$19.8 million.

The Issue 31 bonds were initially issued, and remain in Auction Mode, subject to conversion by the Airport Commission (Commission) to another interest rate mode. The initial interest was established by the Commission for the interest rate period commencing March 25, 2004 for each series of Issue 31 bonds.

Each series of Issue 31 auction rate bonds may bear a different interest rate and is subject to different auction periods. As of June 30, 2005, series Issue 31A was in a 343 days auction period, series 31B, 31C, and 31D were in a 35 days auction period, and series 31E was in a 7 days auction period. For the period July 1, 2004 through June 30, 2005, the average interest rate on the Issue 31 was 1.805%.

In February 2005, SFO issued Second Series Variable Rate Revenue Refunding Bonds Issue 32 in the amount of \$199.9 million. The Issue 32 Bonds were initially issued in an auction mode, subject to conversion by the Commission to another interest rate mode. The initial interest rate was established by the Commission for the initial interest rate period commencing February 10, 2005 for each series of Issue 32 Bonds. Thereafter, each series of Issue 32 bonds will bear interest at an auction rate resulting from an auction conducted for each auction period.

Each series of Issue 32 Bonds may bear a different auction rate and are subject to a different auction period. As of June 30, 2005, Series 32A, 32B, 32C, 32D and 32E were in 7 days, 35 days, 35 days, 35 days and 7 days auction periods, respectively. For the period of February 10, 2005 to June 30, 2005, the average interest rate for the Issue 32 Bonds was 2.36%.

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During fiscal year 2004-2005, the Airport issued Second Series Revenue Bonds Issue 31F and Issue 32 to refund previously issued debt. The \$109.1 million in proceeds from Issue 31F and the \$197.7 million in proceeds from Issue 32 were deposited immediately into irrevocable trusts for the defeasance of \$291.8 million of Second Series Revenue Bonds.

Proceeds of the Issue 32 were deposited into an irrevocable trust with an escrow agent to advance refund certain of SFO's Second Series Revenue Bonds as follows (in thousands):

	<u>Amount Refunded</u>	<u>Interest Rate</u>	<u>Call Price</u>
<u>Second Series Revenue Bond Issuance:</u>			
Issue 9.....	\$ 191,380	5.0% - 5.9%	\$ 101,000

The refunded Second Series Revenue Bonds have final maturity dates ranging from May 1, 2006 to May 1, 2025 and a call date of May 1, 2005. The net proceeds of \$197.7 million (after payment of \$5.8 million in underwriting fees, insurance, surety premium, and cost of issuance account) plus an additional \$3.6 million of available debt service funds were used to purchase U.S. Treasury Securities – State and Local Government Series. These securities were deposited in an irrevocable trust with an escrow agent to provide debt service payments on the refunded bonds identified above until called on May 1, 2005. The refunded bonds are considered legally defeased where the debt is legally satisfied based on certain provisions in the debt instrument, even though the debt is still outstanding. Accordingly, the liability for the refunded bonds has been removed from the Statements of Net Assets. Although the advance refunding resulted in the recognition of a deferred accounting loss of \$5.1 million for the year ended June 30, 2005, SFO in effect reduced its aggregate debt service payment by approximately \$11.7 million (based on an assumed interest rate of 3.44%) over the next 22 years and obtained an economic gain (the difference between the present values of the old and new debt service payments), of \$30.3 million.

SFO entered into seven forward-starting interest rate swaps in December 2004 in connection with the anticipated issuance of its Second Series Variable Rate Revenue Refunding Bonds, Issue 32, on February 10, 2005, and its Variable Rate Refunding Bonds, Issue 33, on February 15, 2006. Pursuant to these interest rate swaps, SFO will receive a monthly variable rate payment from each counterparty approximate to the variable interest rate SFO will pay on the Issue 32 and 33 Bonds. SFO will then make a monthly fixed rate payment to the counterparties. The objective of the swaps is to achieve a synthetic fixed rate with respect to Issue 32 and 33 Bonds.

The four interest rate swaps relating to the Issue 32 Bonds went into effect on February 10, 2005, the date of the issuance of the Issue 32 Bonds, and the first payment commenced on March 1, 2005. The remaining three interest rate swaps relating to the Issue 33 Bonds are expected to go into effect concurrently with the issuance of the Issue 33 Bonds on February 15, 2006, with the first payment commencing on March 1, 2006. All of the interest rate swaps are terminable at any time at the option of SFO at their fair market value.

The interest rate swaps relating to the Issue 32 Bonds terminate by their terms on May 1, 2026, the final maturity date for the Issue 32 Bonds. The following is additional information regarding each swap and the counterparties as of June 30, 2005:

<u>Counterparty/guarantor</u>	<u>Initial notional amount</u>	<u>Counterparty credit ratings (S&amp;P/Moody's)</u>	<u>Fixed rate payable by Commission</u>	<u>Fair value to Commission</u>
J.P. Morgan Chase Bank, N.A.	\$ 70,000,000	AA-/Aa2	3.444%	\$ (2,485,569)
Bear Sterns Capital Markets, Inc.	30,000,000	A/A1	3.444%	(1,065,244)
J.P. Morgan Chase Bank, N.A.	69,930,000	AA-/Aa2	3.445%	(2,491,182)
Bear Sterns Capital Markets, Inc.	29,970,000	A/A1	3.445%	(1,067,650)
(Aggregate notional amount)	<u>\$ 199,900,000</u>			<u>\$ (7,109,645)</u>

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The interest rate swaps relating to the Issue 33 Bonds terminate by their terms on May 1, 2019, the final maturity date for the Issue 33 Bonds. The following is additional information regarding each swap and counterparties as of June 30, 2005:

<u>Counterparty/guarantor</u>	<u>Initial notional amount</u>	<u>Counterparty credit ratings (S&amp;P/Moody's)</u>	<u>Fixed rate payable by Commission</u>	<u>Fair value to Commission</u>
Lehman Brothers Special Financial Inc.	\$ 73,570,000	A/A1	3.393%	\$ (1,889,060)
Bear Sterns Capital Markets, Inc.	31,530,000	A/A1	3.393%	(809,597)
Lehman Brothers Special Financial Inc.	100,000,000	A/A1	3.379%	(2,460,207)
(Aggregate notional amount)	<u>\$ 205,100,000</u>			<u>\$ (5,158,864)</u>

**Risks Disclosure**

The aggregate fair value to the Airport from time to time, if any, of the interest rate swaps with any single counterparty is the maximum amount of credit exposure the Commission will have to that counterparty. The Airport has limited counterparty credit risk by limiting its exposure to any one counterparty. Under the terms of the swaps, counterparties are required to post collateral consisting of specified U.S. Treasury and Agency securities for the fair value of a swap that exceeds specified thresholds which are linked to the counterparty's credit ratings. Any such collateral will be held by the Airport's custodial bank. There is limited basis risk with respect to the interest rate swaps, as the Airport has chosen a variable rate index designed to closely approximate the variable rates payable on the Issue 32 and 33 Bonds. The Airport has limited termination risk with respect to the interest rate swaps. That risk would arise primarily from certain credit-related events or events of default on the part of the Commission, the municipal swap insurer, or the counterparty. The Airport has secured municipal swap insurance for its payments due under each interest rate swaps, as the Airport has secured a forward municipal bond insurance commitment from an insurer currently rated AAA/Aaa with respect to the Issue 33 Bonds.

Water Department

In November 1997, the voters approved Propositions A and B, authorizing up to \$304 million in Water Revenue Bonds to fund capital improvements for the Water Enterprise. In May and June 1999, the San Francisco Public Utilities Commission (the Commission) and the Board of Supervisors, respectively, approved a commercial paper program to provide short-term financing for capital improvement projects funded under the \$304 million Water Revenue Bond Program. In October 2000, the Commission and the Board of Supervisors approved the expansion of the commercial paper program to up to \$250 million.

As of June 30, 2005, the Water Department had \$80 million in commercial paper notes outstanding. The interest rates ranged from 2.58% to 2.75%.

Municipal Transportation Agency

In fiscal year 2004-2005, the Japan Center Garage Corporation (the Corporation) entered into an unsecured small business banking agreement for \$0.3 million to partially finance the purchase of certain garage equipment. Under the terms of the agreement, the Corporation is required to make 36 monthly payments of \$10 thousand including interest at 6.75% per annum.

San Francisco Clean Water Program

During the fiscal year 2002-2003, the San Francisco Clean Water Program (the Program) issued 2003 Refunding Series A Bonds in the amount of \$396 million with interest rates ranging from 3.0% to 5.25%. During the fiscal year 2004-2005, the Program substituted cash and equivalents held in the Bond Reserve Fund with a surety bond reserve fund policy of \$34 million, which was the largest reserve

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requirement pursuant to the Indenture. The cash released by the substitution will be used for improvements to capital projects within the Program in accordance with the Indenture.

The Program has entered into several contracts with the State Water Resources Control Board (SWRCB) under which the Program borrowed up to prescribed maximum amounts to finance the construction of certain facilities. Interest rates range from 2.8% to 3.5% and mature from April 2007 through January 2021.

Port of San Francisco

In August 2004, the Port Commission issued Revenue Refunding Bonds, Series 2004 in the amount of \$19.9 million with an average interest rate of 3.16%. The bonds were issued to refund \$23.2 million of outstanding Series 1994 Revenue Bonds with an average interest rate of 5.84%. Net proceeds from the new bonds plus an additional \$3.9 million of Series 1994 debt service monies were used to defease the 1994 bonds. Although the refunding resulted in the recognition of an accounting loss of \$0.5 million, the Port in effect reduced its aggregate debt service payment over the next five years by \$1.6 million and obtained an economic gain of \$1.2 million. The 1994 bonds refunded \$50 million of outstanding 1984 Revenue Bonds, Series A, B and C with an average rate of 8.4%.

The refunding resulted in a difference between the reacquisition price (principal of the old debt plus 2% call premium) and the net carrying amount of the old debt of \$0.5 million. The previous 1994 refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of \$2.36 million. The total difference, reported in the accompanying financial statements as a deduction from bonds payable, is being charged to operations through the fiscal year 2010 using the straight line method.

***Component Unit Debt - Redevelopment Agency***

The current year debt activities of the Redevelopment Agency are discussed in note 12.

**(9) EMPLOYEE BENEFIT PROGRAMS**

**(a) Retirement Plans**

The City maintains a single-employer, defined benefit pension plan (the Plan) which covers substantially all of its employees, and certain classified and certified employees of the San Francisco Community College District and Unified School District. The Plan is administered by the San Francisco City and County Employees' Retirement System (the Retirement System). Some City employees participate in the California Public Employees Retirement System (PERS), an agent multiple-employer, public employee pension plan which covers certain employees in public safety functions, the Port, SFO and the Redevelopment Agency.

***Employees' Retirement System***

Plan Description - Substantially all full-time employees of the City participate in the Plan. The Plan provides basic service retirement, disability and death benefits based on specified percentages of defined final average monthly salary and provides annual cost-of-living adjustments after retirement. The Plan also provides pension continuation benefits to qualified survivors. The San Francisco City and County Charter and Administrative Code is the authority which establishes and amends the benefit provisions and employer obligations of the Plan. The retirement related payroll for employees covered by the Retirement System for the year ended June 30, 2005 was approximately \$2.155 billion. The Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for the Plan. That report may be obtained by writing to the San Francisco City

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and County Employees' Retirement System, 30 Van Ness, Suite 3000, San Francisco, CA 94102 or by calling (415) 487-7020.

Membership

Membership of the Retirement System at July 1, 2004, the date of the latest actuarial valuation is:

	<u>Police</u>	<u>Fire</u>	<u>Others</u>	<u>Total</u>
Retirees and beneficiaries currently receiving benefits....	<u>2,050</u>	<u>1,856</u>	<u>15,175</u>	<u>19,081</u>
Active members:				
Vested.....	1,843	1,344	20,807	23,994
Nonvested.....	340	319	6,998	7,657
Subtotal.....	<u>2,183</u>	<u>1,663</u>	<u>27,805</u>	<u>31,651</u>
Total.....	<u><u>4,233</u></u>	<u><u>3,519</u></u>	<u><u>42,980</u></u>	<u><u>50,732</u></u>

As of July 1, 2004, there were 996 terminated members entitled to, but not yet receiving benefits.

Plan member contributions are recognized in the period in which the contributions are due. Benefits and refunds are recognized when due and payable in accordance with the terms of the Plan.

Funding Policy - Contributions are made to the basic plan by both the City and the participating employees. Employee contributions are mandatory. Employee contribution rates for fiscal year 2004-2005 varied from 7% to 8% as a percentage of gross salary. The City is required to contribute at an actuarially determined rate. Based on the July 1, 2004 actuarial report, the required employer contribution for fiscal year 2004-05 was 4.48 percent. In collective bargaining during the year ended June 30, 1994, the City and County agreed to pay a portion of the employee contributions on behalf of employees. From 1994 through June 2003, the City and County portion of these contributions has been negotiated through the various unions on a member group basis, and did not exceed 8% of base salary. For fiscal year ended June 30, 2005, most employee groups agreed through collective bargaining for employees to contribute the full amount of the employee contributions on a pretax basis.

Employer contributions and member contributions made by the employer to the Plan are recognized when due and the employer has made a formal commitment to provide the contributions.

Annual Pension Cost - The annual required contribution for the current year was determined as part of an actuarial valuation performed as of July 1, 2004. The actuarial method used was the entry age normal cost method. The significant actuarial assumptions include: (1) annual rate of return on investments of 8%; (2) inflation element in wage increases of 3.5%; and (3) salary merit increases of 4.5%. Unfunded liabilities are amortized using the level percentage of payroll method. Changes in actuarial gains and loss assumptions and purchasable services are amortized as a level percentage of pay over a closed 15 year period. Plan amendments are amortized over 20 years.

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Three-year trend information is as follows (amounts in thousands):

<u>Fiscal Year Ended</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>
6/30/2003	\$ -	N/A	\$ -
6/30/2004	-	N/A	-
6/30/2005	83,664	100%	-

***California Public Employees' Retirement System***

Various City public safety, Port, and all Redevelopment Agency employees are eligible to participate in PERS. Disclosures for the Redevelopment Agency are included in the separately issued financial statements.

Plan Description - The City contributes to PERS, an agent multiple-employer public employee defined benefit pension plan. PERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. PERS acts as a common investment and administrative agent for participating public entities within the State of California. Benefit provisions and all other requirements are established by state statute and City ordinance. Copies of PERS' annual financial report may be obtained from their executive office: 400 P Street, Sacramento, CA 95814. A separate report for the City's plan within PERS is not available.

***Miscellaneous Plan***

Funding Policy - Miscellaneous plan - Participants are required to contribute 7% of their annual covered salary. The City is required to contribute at an actuarially determined rate. For the miscellaneous plan, the fiscal year 2004-2005 contribution rate is 0% of annual covered payroll because the City is funded at 145.7% at June 30, 2002. The contribution requirements of plan members and the City are established and may be amended by PERS.

Annual Pension Cost – Miscellaneous plan - cost for PERS for fiscal year 2004-2005 was equal to the City's required and actual contributions which was determined as part of the June 30, 2002 actuarial valuation using the entry age actuarial cost method. The assumptions included in the June 30, 2002 actuarial valuation were: (a) 8.25% investment rate of return (net of administrative expenses), (b) 3.75% to 14.2% projected annual salary increases that vary by age, service, and type of employment, and (c) 3.75% per year cost-of-living adjustments. Both (a) and (b) included an inflation component of 3.5%. The actuarial value of PERS assets was determined using techniques that smooth the effects of short-term volatility in the market value of investments. Changes in unfunded liability/(excess assets) due to changes in actuarial methods or assumptions or changes in plan benefits are amortized, as a level percentage of pay, over a closed 20 year period. Actuarial gains and losses are first offset against one another and then 10% of the net unamortized gain/loss is recognized.

Three-year trend information is as follows (amounts in thousands):

<u>Fiscal Year Ended</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>
6/30/2003	\$ -	N/A	\$ -
6/30/2004	-	N/A	-
6/30/2005	-	N/A	-

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**Safety Plan**

Funding Policy – Safety plan - Participants are required to contribute 9% of their annual covered salary. The City makes the contributions required of City employees on their behalf and for their account. The City is required to contribute at an actuarially determined rate. For the safety plan, the fiscal year contribution rate is 20.801% because the City is funded at 103%. The contribution requirements of plan members and the City are established and may be amended by PERS.

Annual Pension Cost – Safety Plan - cost for PERS for fiscal year 2004-2005 was equal to the City's required and actual contributions which was determined as part of the June 30, 2002 actuarial valuation using the entry age actuarial cost method. The assumptions included in the June 30, 2002 actuarial valuation were: (a) 8.25% investment rate of return (net of administrative expenses), (b) 4.27% to 11.59% projected annual salary increases that vary by age, service and type of employment, and (c) 3.75% per year cost-of-living adjustments. Both (a) and (b) included an inflation component of 3.5%. The actuarial value of PERS assets was determined using techniques that smooth the effects of short-term volatility in the market value of investments. Changes in unfunded liability/(excess assets) due to changes in actuarial methods or assumptions or changes in plan benefits are amortized over as a level percentage of pay over a closed 20 year period. Actuarial gains and losses are first offset against one another and then 10% of the net unamortized gain/loss is recognized.

Three-year trend information is as follows (amounts in thousands):

<u>Fiscal Year Ended</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>
6/30/2003	\$ -	100%	\$ -
6/30/2004	5,606	100%	-
6/30/2005	3,689	100%	-

**(b) Deferred Compensation Plan**

The City offers its employees a deferred compensation plan in accordance with Internal Revenue Code (IRC) Section 457. The plan, available to all employees, permits them to defer a portion of their salary until future years. The deferred compensation is not available to employees or other beneficiaries until termination, retirement, death, or unforeseeable emergency.

The City has no administrative involvement and does not perform the investing function. The City has no fiduciary accountability for the plan and, accordingly, the plan assets and related liabilities to plan participants are not included in the basic financial statements.

**(c) Health Service System**

The Health Service System was established in 1937. Health care benefits of employees, retired employees and surviving spouses are financed by beneficiaries and by the City through the Health Service System. The employers' contribution, which includes the San Francisco Community College District and Unified School District, amounted to approximately \$382.2 million in fiscal year 2005. The employers' contribution is mandated and determined by Charter provision based on similar contributions made by the ten most populous counties in California. Included in this amount is \$113.7 million to provide post-employment health care benefits for 19,755 retired employees. The City's liability for both current employee and post-employment health care benefits is limited to its annual contribution. The City's contribution is paid out of current available resources and funded on a pay-as-you-go basis. The Health Service System issues a publicly available financial report that includes financial statements and required

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supplementary information for the health care benefits. That report may be obtained by writing to the San Francisco Health Service System, 1145 Market Street, Suite 200, San Francisco, CA 94103 or by calling (800) 541-2266.

**(10) SAN FRANCISCO COUNTY TRANSPORTATION AUTHORITY**

The San Francisco County Transportation Authority (the Authority) was established in 1989 by the voters of the City and County of San Francisco pursuant to State Code Section 131.000. The purpose of the Authority is to impose the voter-approved transactions and use tax of one-half of one percent to fund essential traffic and transportation projects, as set forth in the San Francisco County Transportation Expenditure Plan, for a period not to exceed 20 years. The principal focus of the Authority's Expenditure Plan is to define a program of prioritized projects to ensure that funding is allocated across major transportation categories. The City accounts for these activities in the other governmental funds.

In June 1992, the Authority was designated by the Board of Supervisors as the overall program manager for the Local Guarantee share of transportation funds available through the "Transportation Fund for Clean Air" Program (AB 434) which is administered by the Bay Area Air Quality Management District. The source of funds is a \$4.00 surcharge on the vehicle registration fee.

The Authority serves as the Congestion Management Agency under state laws, and in that capacity prioritizes state and federal transportation funds for San Francisco. The funding is administered by the Metropolitan Transportation Commission in accordance with the Federal Surface Transportation Program for congestion management activities.

In April 1998, the Authority signed a memorandum of understanding with the State of California Department of Transportation (Caltrans) to serve as the lead agency for the environmental impact research and study and the preliminary design for the Doyle Drive Replacement Project for which Caltrans was awarded \$6 million in federal grant funds.

In November 2003, the City voters approved Proposition K amending the City Business and Tax Code to extend the sunset date to 2034 from 2010, continue the existing half-cent sales tax, and replace the 1989 Proposition B Expenditure Plan with a new 30-year Expenditure Plan. The new Expenditure Plan includes investments in four major categories: Transit, Streets and Roads (including street resurfacing, and bicycle and pedestrian improvements); Paratransit services for seniors and disabled people; Transportation System Management/Strategic Initiatives, to fund neighborhood parking management, land use coordination, and beautification efforts; and Major Capital Projects. The major capital projects to be funded by the new Expenditure Plan are development of the Bus Rapid Transit/MUNI Metro Network, construction of the MUNI Central Subway (Third Street Light Rail Project – Phase 2), construction of the CalTrain Downtown Extension to a rebuilt Transbay Terminal and replacement of the South Access to the Golden Gate Bridge (Doyle Drive). The Authority may modify the Expenditure Plan with voter approval, and the half-cent sales tax would continue as long as a new or modified plan is in effect. Under the current Proposition K legislation, the Authority directs the use of the sales tax and may spend up to \$485.2 million per year and issue up to \$1.9 billion in bonds, to be repaid from the half-cent sales tax.

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Following is a summary of the Authority's financial position and changes in financial position as of and for the year ended June 30, 2005 (in thousands):

<b>ASSETS</b>		<b>OPERATIONS</b>	
Deposits and investments.....	\$ 257,933	Revenues:	
Receivables and other assets.....	<u>17,747</u>	Sales tax.....	\$ 66,762
Total assets.....	<u>\$ 275,680</u>	Interest and investment income.....	5,398
		Intergovernmental.....	3,131
		Other.....	<u>408</u>
			75,699
<b>LIABILITIES AND FUND BALANCE</b>			
Due to other funds.....	\$ 45,881	Expenditures and other financing uses:	
Other liabilities.....	<u>155,202</u>	Public works, transportation, and commerce....	41,734
Total liabilities.....	<u>201,083</u>	Transfer to other funds.....	<u>94,834</u>
Fund balance:			<u>136,568</u>
Reserved for debt service.....	931	Deficiency of revenues under expenditures and other financing uses.....	(60,869)
Reserved for encumbrances.....	1,747	Fund balance at the beginning of year.....	<u>135,466</u>
Reserved for appropriation carryforward...	<u>71,919</u>	Fund balance at end of year.....	<u>\$ 74,597</u>
Total fund balance.....	<u>74,597</u>		
Total liabilities and fund balance.....	<u>\$ 275,680</u>		

**(11) DETAILED INFORMATION FOR ENTERPRISE FUNDS**

**(a) San Francisco International Airport**

San Francisco International Airport (SFO), which is owned and operated by the City, is the principal commercial service airport for the San Francisco Bay Area. A five member Commission is responsible for the operation and management of SFO. SFO is located 14 miles south of downtown San Francisco in an unincorporated area of San Mateo County between the Bayshore Freeway (U.S. Highway 101) and the San Francisco Bay. According to final data for calendar year 2004 from the Airports Council International (the ACI), SFO is one of the largest airports in the United States both in terms of passengers (12th) and air cargo (14th). SFO is also a major origin and destination point and one of the nation's principal gateways for Pacific traffic.

The San Francisco Bay Area Rapid Transit District (BART) extension to SFO creates a convenient connection between SFO and the greater San Francisco Bay Area. An intermodal station in the City of Millbrae provides a direct link to Caltrain offering additional transit options and connections to the southern parts of the Bay Area. Access from the BART station throughout SFO is enhanced by the AirTrain system, a shuttle train that connects airport terminals. The AirTrain system provides transit service over a "terminal loop" to serve the terminal complex and over a "north corridor loop" to serve the rental car facility and other locations situated north of the terminal complex.

SFO has developed a revised Capital Plan to better fit the changes in the aviation industry. The revised Capital Plan was approved in March 2005 and included projects related to improvements to the airfield, groundside activities and customer service functions, environmental mitigation, utilities infrastructure upgrades, seismic retrofit of certain facilities, health, safety and security enhancements, and cost savings and revenue generating enhancements.

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In May 2002, SFO obtained a standby letter of credit with a maximum stated principal amount of \$200 million. The subordinate Lien Resolution authorizes a maximum principal amount of notes of \$400 million. There were no commercial borrowings during the year ended June 30, 2005.

In addition to the long-term obligations discussed above, there is \$115 million and \$118 million in Special Facilities Lease Revenue Bonds outstanding at June 30, 2005 and June 30, 2004, respectively, for SFO Fuel. SFO Fuel is required to pay facilities rent to SFO in an amount equal to debt service payments and required bond reserve account deposits on the bonds. The principal and interest on the bonds will be paid solely from the facilities rent payable by SFO Fuel to SFO. SFO assigned its right to receive the facilities rent to the bond trustee to pay and secure the payment of the bonds. Neither SFO nor the City is obligated in any manner for the repayment of these obligations, and as such, they are not reported in the accompanying financial statements.

In July 2001, the Federal Aviation Administration (FAA) approved SFO's first Passenger Facility Charge application (PFC#1) to impose and use a \$4.50 Passenger Facility Charge (PFC) per enplaning passenger from October 1, 2001 through June 1, 2003, to pay for approximately \$113 million in PFC eligible project development activities and studies associated with the potential runway reconfiguration. In March 2002, the FAA approved SFO's PFC Application Number 2 (PFC#2) to impose and use a \$4.50 PFC per enplaning passenger from June 1, 2003 through April 1, 2008, to pay for approximately \$224 million in the principal and interest on bonds issued for certain eligible costs relating to the new International Terminal Complex.

In March 2003, as a result of decrease in enplanement, SFO notified PFC-collecting carriers of the intent to extend the PFC#1 collection period, thereby revising the current PFC#1 charge expiration date from June 1, 2003 to January 1, 2004. With the PFC#1 collection period extension in place, the PFC#2 effective date changed from June 1, 2003 to January 1, 2004. Automatically, the PFC#2 expiration date changed from April 1, 2008 to November 1, 2008. During the extended collection period, the PFC is maintained at \$4.50.

In November 2003, the FAA approved SFO's third PFC application (PFC#3) to impose and use a \$4.50 PFC per enplaning passenger for approximately \$539 million to pay for debt service costs related to the construction of the new international terminal and boarding areas A and G. The collection period for PFC #3, as originally approved, was from November 1, 2008 to November 1, 2018.

In January 2004, the FAA approved SFO's amendment to delete PFC#1. The receipts from PFC#1 were applied to PFC#2 and the FAA revised PFC#2 and PFC#3 collection periods to expire in January 1, 2006 and January 1, 2016, respectively.

In June 2005, the Airport Commission authorized the fourth PFC application (PFC#4) for approximately \$70 million.

For the year ended June 30, 2005, SFO reported approximately \$61.4 million of PFC revenue, which is included in other non-operating revenues in the accompanying basic financial statements. SFO designated \$68.4 million of PFC revenues as "Revenues" under the 1991 Master Bond Resolution for the purpose of paying debt service in fiscal year 2004-2005.

Due to SFO's noise mitigation efforts, significant progress has been made in reducing the impact of aircraft noise on the communities surrounding the Airport through the implementation of (1) noise abatement flight procedures, (2) an aircraft noise insulation program, (3) community outreach through the Airport Community Roundtable, and (4) requests that certain surrounding communities adopt ordinances to protect new purchasers of homes within their community.

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Pursuant to an agreement with certain airlines, SFO makes an annual payment to the City's General Fund equal to 15% of concession revenue, but not less than \$5 million per fiscal year. The amount transferred to the General Fund during the year ended June 30, 2005 was \$19.7 million.

Purchase commitments for construction, material and services as of June 30, 2005 are as follows (in thousands):

Construction.....	\$ 17,224
Operating.....	<u>13,091</u>
Total	<u><u>\$ 30,315</u></u>

SFO has a Memorandum of Understanding with various surrounding communities to insulate residential and nonresidential structures such as schools, churches and hospitals. The total estimated funding for this program is approximately \$154 million funded by bond proceeds, by federal grant reimbursements to the local communities, and by operating and other internally generated funds. As of June 30, 2005, approximately \$123.6 million has been disbursed under this program.

SFO leases facilities to the airlines pursuant to the Lease and Use Agreements and to other businesses to operate concessions at SFO. During the year ended June 30, 2005, revenues realized from the following SFO tenants exceeded five percent of SFO's total operating revenues:

United Airlines.....	26.0%
AMPCO Parking Systems.....	10.2%
American Airlines.....	5.1%

**(b) Port of San Francisco**

A five-member Port Commission is responsible for the operation, development, and maintenance activities of the Port of San Francisco (Port). Prior to 1969, the Port was owned by the State of California. At that time the Port was transferred in trust to the City under the terms and conditions of legislation as ratified by the electorate of the City. The State retains the right to amend, modify or revoke the transfer of lands in trust provided that it assumes all lawful obligations related to such lands.

In 1996, the Department of Parking and Traffic (DPT) entered into an Annual Payment Agreement with the Port to resolve a dispute concerning the City's collection of parking fine revenues from Port property. Among other things, DPT agreed to pay the Port a guaranteed annual payment of \$1.2 million for 20 years commencing on July 1, 1997, for parking fine revenues collected from Port property. Thereafter, amounts remitted to the Port are based on actual ticket collections, net of administrative costs.

In connection with a mixed-use cruise terminal development project at Piers 30-32, and as approved by state legislation in 2001 (Assembly Bill No. 1389), a portion of Seawall Lot No. 330 was sold to a developer in 2004. The land was sold for \$9.3 million, slightly above its appraised fair value. Certain proceeds from the land sale (\$9 million) are restricted for the construction of a public plaza area called Brannan Street Wharf. The remainder of the proceeds from the land sale, together with certain residual receipts from the future sale of residential condominium units built on the land sold, is restricted for the construction of the cruise terminal.

The Port is presently planning various development projects that involve a commitment to expend significant funds. Purchase commitments at June 30, 2005 were \$14.5 million for capital projects and \$1.1 million for general operating costs. Under an agreement with the San Francisco Bay Conservation and Development Commission (BCDC), the Port is committed to fund and expend up to \$30 million over a 20 year period for pier removal, parks and plazas and other public access improvements. As of June

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30, 2005, \$16.5 million has been appropriated and \$1.6 million has been expended for projects under the agreement.

Special items identify significant transactions or events within the control of management that are either unusual in nature or infrequent in occurrence. In 2001, the Port entered into an agreement giving the San Francisco Municipal Transportation Agency (MUNI) the permanent right to use certain land for its Metro East Maintenance and Operations Facility. MUNI paid a total use fee of \$29.7 million for these property rights. A portion of the fee (\$4 million) was restricted for the construction of a new rail bridge. Construction on the bridge commenced during 2005 and approximately \$3.7 million of deferred revenue was recognized as of June 30, 2005.

**(c) Water Department**

The Water Department was established in 1930. The Water Department, which consists of a system of reservoirs, storage tanks, water treatment plants, pump stations, and pipelines, is engaged in the collection, transmission and distribution of water to the City and certain suburban areas. The Water Department delivers water, approximately 88,686 million gallons annually, to a total population of approximately 2.4 million people who reside primarily in four Bay Area counties (San Francisco, San Mateo, Santa Clara and Alameda).

The Commission, established in 1932, provides the operational oversight for the Water Department, Hetch Hetchy, and the Clean Water Program. The Commission consists of five members appointed by the Mayor who are responsible for determining such matters as the rates and charges for services, approval of contracts, and organizational policy.

The Water Department purchases water from Hetch Hetchy. This amount, totaling approximately \$19.0 million, is included in the charges for services provided by other departments in the accompanying financial statements.

During fiscal year 2004-2005, water sales to suburban resale customers were \$104 million. As of June 30, 2005, the Water Department owed suburban resale customers approximately \$8 million under the Suburban Water Rate Agreement.

As of June 30, 2005, the Water Department had outstanding commitments with third parties of \$72.6 million for various capital projects and for materials and supplies.

In July 1999, the California Regional Water Quality Control Board (CRWQCB) issued a directive instructing the Water Department to develop a remedial action plan (Plan) that addresses environmental contamination at certain real property owned by the Water Department. In response to the directive, the Commission developed a remedial action plan and in August 2001 received the final directive from the CRWQCB to execute the plan. The cost of cleanup associated with the Plan was estimated to be \$22.7 million and was accrued in fiscal year 2000-2001. At June 30, 2005, the outstanding estimated liability is \$7.7 million.

**(d) Hetch Hetchy Water and Power**

Hetch Hetchy was established as a result of the Raker Act of 1913, which granted water and power resources rights-of-way on the Tuolumne River in Yosemite National Park to the City. Hetch Hetchy is engaged in the collection and conveyance of approximately 85% of the City's water supply and in the generation and transmission of electricity from that resource. Approximately one-third of the electricity is used by the City's municipal customers (e.g., the San Francisco Municipal Railway, the Recreation and Parks Department, San Francisco International Airport, the Port of San Francisco, San Francisco County hospitals, street lighting, Moscone Center, and the water and sewer utilities). The balance of the power generated is sold to other publicly owned utilities, such as the Modesto and Turlock Irrigation Districts (the Districts).

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Hetch Hetchy consists of a system of reservoirs, hydroelectric power plants, aqueducts, pipelines, and transmission lines. This system carries water and power more than 165 miles from the Sierra Nevada Mountains to customers in the City and portions of the surrounding San Francisco Bay Area.

Hetch Hetchy also purchases wholesale electric power from various energy providers that are used in conjunction with owned hydro resources to meet the power requirements of its customers. Operations and business decisions can be greatly influenced by state and federal power matters before the California Public Utilities Commission (CPUC) and the Federal Energy Regulatory Commission (FERC). Therefore, Hetch Hetchy serves as the City's representative at both CPUC and FERC forums and continues to monitor regulatory proceedings.

Charges for services for the year ended June 30, 2005 include \$57.3 million in sales of power by Hetch Hetchy to other City Departments. Income from Hetch Hetchy is available for certain operations of the City.

As of June 30, 2005, Hetch Hetchy had outstanding commitments with third parties of \$16 million for various capital projects and other purchase agreements for materials and services.

Hetch Hetchy facilitates all electric and gas service connections between Pacific Gas and Electric Company (PG&E) and City Departments. In this capacity, Hetch Hetchy, as a pass-through agent on behalf of the City departments, coordinates the payment for the service connections that are performed by PG&E. As of June 30, 2005, there were no outstanding amounts from City departments related to this work.

Hetch Hetchy receives title to the underlying assets of certain completed projects on behalf of the City and assumes responsibility for their maintenance, repair and replacement following their initial year of operation.

The Commission has contracted with PG&E to provide transmission capacity on PG&E's system where needed to deliver Hetch Hetchy's power to its customers. In addition, the PG&E agreement provides backup power and other support services to Hetch Hetchy. The PG&E agreement allows PG&E to review past billings paid by Hetch Hetchy and to retroactively adjust these payments to actual backup power, transmission, and other charges as finally determined by PG&E. During fiscal year 2004-2005, Hetch Hetchy purchased \$16.4 million of transmission services, backup power, and other support services from PG&E under the terms of the agreement.

To meet certain requirements of the Don Pedro Reservoir operating license, the City entered into an agreement with the Districts in which they would be responsible for an increase in water flow releases from the reservoir in exchange for annual payments of \$3.5 million from the City. The payments are to be made for the duration of the license, but may be terminated with one year's prior written notice after 2001. The City and the Districts have also agreed to monitor the fisheries in the lower Tuolumne River for the duration of the license. A maximum monitoring expense of \$1.4 million is to be shared between the City and the Districts over the term of the license. The City's share of the monitoring costs is 52% and the Districts are responsible for 48% of the costs.

In April 1988, Hetch Hetchy entered into a long-term power sales agreement (the Agreement) with the Districts. The Agreement expires in 2015 and requires that Hetch Hetchy provide, as generated, an amount equivalent to the difference between 260 megawatts and the amount required to meet the City's demand. In June 2003, Hetch Hetchy amended the terms of the Agreement with the Modesto Irrigation District (MID). Under the terms of the amended and restated long-term power sales agreement, which became effective on January 1, 2003, the expiration date was shortened to 2007, the existing pricing structure was modified, and Hetch Hetchy's firm obligation to provide power to the MID was relaxed. For fiscal year 2004-2005, power sales to the Districts totaled 965,348 MWhrs or \$25.7 million.

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On May 9, 2001, Hetch Hetchy entered into a fixed price, forward contract (the Contract) to purchase 2.19 million MWhrs of electric energy from a third party energy provider with scheduled future delivery over a five-year period beginning July 1, 2001. Effective March 9, 2003, Hetch Hetchy executed an amended and restated transaction confirmation with the third party energy provider to amend and retroactively restate the terms of the original agreement entered into on May 9, 2001 in its entirety, to settle any pending disputes brought forth by Hetch Hetchy. Under this amended take or pay contract, Hetch Hetchy is obligated to pay for a minimum amount of electricity even if the electricity is not required for operations. Commitments related to this contract total \$86.1 million from July 1, 2003 through June 30, 2006. Expenses under this contract totaled \$30.4 million in fiscal year 2004-2005.

In December 2002, the City entered into an agreement (the Power Purchase Agreement) with the California Department of Water Resources in anticipation of the settlement and implementation agreements. Under the terms of the Power Purchase Agreement, the California Department of Water Resources has agreed to purchase power and rated capacity from the City at rates that will essentially provide for the full recovery of the City's costs incurred in the construction of a power generating facility (The Facility) over a ten year period from the date in which the California Department of Water Resources accepts the City's certification that the Facility meets all requirements of commercial operation as set forth in the Power Purchase Agreement (Commercial Operation Date).

The City may terminate the Power Purchase Agreement at any time from and after the fifth anniversary of the Commercial Operation Date upon providing a one-year notice to the California Department of Water Resources, and the California Department of Water Resources may terminate the Power Purchase Agreement at such time that there is no longer a debt service component within the capacity payment.

On January 21, 2003, the City's Board of Supervisors authorized the settlement of a lawsuit filed in January 2001 by the City, on behalf of the people of the State of California (the State), against certain energy companies. Under the terms of the settlement, the City received or is to receive (i) four gas turbine generator sets valued at approximately \$33 million for use within the City, (ii) future funding from a State administered fund (the Fund) to assist with the costs of sitting and developing electric generating equipment in the City, and (iii) payment to the City of \$0.5 million for attorney's fees and other expenses of litigation.

Effective January 23, 2003, the City entered into an implementation agreement with the Attorney General of the State of California (the Attorney General), the California Consumer Power and Conservation Financing Authority (the Financing Authority), and the California Department of Water Resources, outlining the terms of execution of the settlement agreement.

In conjunction with the execution of the settlement agreement, the Attorney General has received the first \$7.6 million from the defendants, and deposited that amount into the Fund. The City has eligible costs incurred in the development of the facility of about \$3.8 million. As of June 30, 2005, the City has requested and received a total of \$2.0 million for reimbursement from the Fund. Under the terms of the Agreement, the City only has claim to the proceeds held by the Fund to the extent that eligible costs are incurred in the development of the Facility. As such, the corresponding revenue will be recognized as eligible costs. Hetch Hetchy has recognized \$2.0 million of revenue from the Fund as of June 30, 2005.

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**(e) Municipal Transportation Agency**

The Municipal Transportation Agency (MTA) is responsible for overseeing the City's public transportation operations, including those of the San Francisco Municipal Railway (MUNI), the San Francisco Municipal Railway Improvement Corporation (SFMRIC), and the Department of Parking and Traffic (DPT), which includes the Parking Authority and its five parking garages operated by separate nonprofit corporations organized by the City. Created in November 1999, with the passage of Proposition E, by the voters, the MTA replaced the San Francisco Public Transportation Commission as the oversight agency for the operations of MUNI and SFMRIC, and effective July 1, 2002, the MTA also assumed responsibility for overseeing the operations of DPT.

The tables below reflect the financial information of MUNI, DPT, and the parking garages that are reported within the MTA (in thousands), net of \$0.7 million interagency accounts payables and receivables.

	MUNI	DPT	Parking Garages	Total
<b>Assets</b>				
Current assets.....	\$ 151,742	\$ 21,761	\$ 2,928	\$ 176,431
Noncurrent assets.....	1,820,024	43,003	95,059	1,958,086
<b>Total Assets.....</b>	<b>1,971,766</b>	<b>64,764</b>	<b>97,987</b>	<b>2,134,517</b>
<b>Liabilities</b>				
Current liabilities.....	97,207	18,443	20,852	136,502
Liabilities payable from restricted assets.....	861	-	-	861
Noncurrent liabilities.....	153,188	60,246	34,997	248,431
<b>Total liabilities.....</b>	<b>251,256</b>	<b>78,689</b>	<b>55,849</b>	<b>385,794</b>
<b>Net assets</b>				
Invested in capital assets, net of related debt.....	1,778,547	(12,001)	35,384	1,801,930
Restricted net assets.....	40,616	6,608	22,971	70,195
Unrestricted net assets (deficit).....	(98,653)	(8,532)	(16,217)	(123,402)
<b>Total net assets (deficit).....</b>	<b>\$ 1,720,510</b>	<b>\$ (13,925)</b>	<b>\$ 42,138</b>	<b>\$ 1,748,723</b>
	MUNI	DPT	Parking Garages	Total
Operating revenues.....	\$ 127,431	\$ 24,009	\$ 36,473	\$ 187,913
Operating expenses.....	579,065	70,686	57,298	707,049
Net operating income (loss).....	(451,634)	(46,677)	(20,825)	(519,136)
Nonoperating Income (loss).....	229,652	20,734	(1,684)	248,702
Capital contributions.....	45,330	-	-	45,330
Transfers in.....	196,610	36,066	-	232,676
Transfers out.....	-	(12,298)	-	(12,298)
Change in net assets.....	19,958	(2,175)	(22,509)	(4,726)
Net assets (deficit) at beginning of year.....	1,700,552	(11,750)	64,647	1,753,449
<b>Net assets (deficit) at end of year.....</b>	<b>\$ 1,720,510</b>	<b>\$ (13,925)</b>	<b>\$ 42,138</b>	<b>\$ 1,748,723</b>

The City's Annual Appropriation Ordinance provides funds to subsidize the operating deficits of MUNI and DPT determined by the City's budgetary accounting procedures, subject to the appropriation process. The amount of General Fund subsidy to the MTA was \$138 million (\$102 million for MUNI and \$36 million for DPT).

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Municipal Railway

MUNI receives capital grants from various federal, state, and local agencies to finance transit related property and equipment purchases. As of June 30, 2005, MUNI had approved capital grants with unused balances amounting to \$278 million. Capital grants receivable as of June 30, 2005 totaled \$47 million.

MUNI also receives operating assistance from various federal, state, and local sources, including Transit Development Act funds and sales tax allocations. As of June 30, 2005, MUNI had various operating grants receivable of \$26.4 million.

These capital grants and operating assistance include funds from the San Francisco Transportation Authority (SFCTA). During the year ended June 30, 2005, the SFCTA approved \$81 million in new capital grants and \$17 million in new operating grants for MUNI. During the same period, MUNI received total payments of \$87 million for capital grants and \$19 million in operating grants from the Authority. As of June 30, 2005, MUNI had \$24 million due from the SFCTA for capital grants and \$3 million due from the SFCTA for operating grants reported in due from other funds.

The State Public Utilities Code requires that fare revenues must equal or exceed 33% of operating costs in order to qualify for an allocation of certain sales tax revenues available for public transit. Transit operators may add local support to fare revenues in order to calculate the fare recovery ratio. The City provides significant local support to MUNI from parking revenues and the General Fund.

MUNI has outstanding contract commitments of approximately \$50 million with third parties for various capital projects. Grant funding is available for a majority of this amount. MUNI also has outstanding commitments of approximately \$7 million for non-capital expenditures. Various local funding sources are used to finance these expenditures. MUNI is committed to numerous capital projects for which it anticipates that federal and state grants will be the primary source of funding. The San Francisco Municipal Railway Improvement Corporation's (SMFRIC) Board of Directors has authorized SMFRIC to extend financial guarantees to MUNI for certain projects totaling \$4.3 million.

Given that the proposed Metro East light Rail Vehicle Maintenance and Operating Facility (Metro East) is an integral part of the Third Street Light Rail Project and is vital for relieving overcrowded conditions at MUNI's existing light rail facility, MUNI identified a 17-acre site of the Western Pacific Railroad under the jurisdiction of the Port of San Francisco (Port) as the best location for the Metro East Facility.

In March 2001, MUNI and the Port entered in to a Memorandum of Understanding (MOU) under which MUNI may use the Metro East site in perpetuity for rail vehicle maintenance, operations and other operational needs at a cost of \$25.7 million. The MOU also required MUNI to pay the Port an additional \$4 million to construct the Illinois Street Bridge over Islais Creek. Construction of this bridge will mitigate traffic in the area and improve coordination with MUNI's Metro East and Third Street Light Rail Project. In the event the Port fails to expend the money toward construction of the bridge within three years after the effective date of the MOU, the Port shall return the \$4 million to MUNI. MUNI has agreed to reasonably extend this deadline up to March 2006 provided the Port has demonstrated good faith efforts toward construction of the bridge. The Port started construction of the Illinois Street Bridge in May 2005 with substantial completion scheduled by the end of July 2006. As of June 30, 2005, the \$4 million is reflected as nonoperating revenues and expenses.

Leveraged Lease-Leaseback with BREDA Vehicles

**Tranche 1**

The Municipal Transportation Agency board of directors authorized the Director of Transportation to solicit proposals regarding a leveraged lease-leaseback transaction involving up to 150 BREDA light rail vehicles. The transaction would not involve financing or procurement of any new vehicles. Rather, MUNI's intention was to obtain an upfront economic benefit in return for entering into a lease-leaseback

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transaction involving the Breda light rail vehicles, without impairing the day-to-day operations of the transit system.

In April 2002, MUNI entered into the leveraged lease-leaseback transaction over 118 Breda light rail vehicles (the Tranche 1 Equipment). The transaction was structured as a head lease of the Tranche 1 Equipment to separate special purpose trusts and a sublease of the Tranche 1 Equipment back from such trusts. The sublease provides MUNI with an option to purchase the Tranche 1 Equipment in approximately 27 years, the scheduled completion date of the sublease. During the term of the sublease, MUNI maintains custody of the Tranche 1 Equipment and is obligated to insure and maintain the Tranche 1 Equipment throughout the life of the sublease.

MUNI received an aggregate of \$388.2 million from the equity investors in full prepayment of the head lease. MUNI deposited \$352.7 million of this head lease payment into two escrows. One escrow was deposited with a debt payment undertaker whose repayment obligations are guaranteed by Financial Security Assurance, an "Aaa/AAA" rated bond insurance company. The other escrow was invested in U.S. government bonds with maturity dates that match the completion of the sublease. Payments under these escrows are to be made at such times and in such amounts so as to fund MUNI's scheduled payments under the sublease as well as to provide a source of funding for MUNI's purchase option if it chooses to exercise it. Although these escrows do not represent a legal defeasance of MUNI's obligations under the sublease, management believes that the creditworthiness of these escrows is such that they will fund MUNI's obligations under the sublease and that the possibility that MUNI will need to access other monies to make sublease payments is remote. Therefore, the trust assets and the sublease obligations are not recorded on the financial statements of MUNI as of June 30, 2005.

As a result of the cash transactions above, MUNI recorded deferred revenue in fiscal year 2001-2002 of \$35.5 million for the difference between the amount received of \$388.2 million and the amount paid to the escrows of \$352.7 million. The deferred revenue will be amortized over the life of the sublease. The deferred revenue amortized amounts were \$1.3 million for fiscal year 2004-2005.

As of June 30, 2005, the outstanding payments to be made on the sublease through 2027 are \$295.7 million and the payments to be made on the purchase option of the Tranche 1 Equipment would be \$643.1 million, if exercised. All of these payments are to be funded from the amounts in escrow. If MUNI does not exercise the purchase option, MUNI would be required to either: 1) pay service and maintenance costs related to the continued operation and use of the vehicles beyond the term of the sublease; or 2) arrange for another party to be the "service recipient," under a "service contract," and to perhaps guarantee the obligations of that party under the service contract if the replacement service recipient does not meet specified credit or net worth criteria.

## **Tranche 2**

In September 2003, after obtaining final approval from the Municipal Transportation Agency's Board of Directors and the City's Board of Supervisors, MUNI entered into a second leveraged lease-leaseback transaction over 21 Breda light rail vehicles (the Equipment). The transaction was structured as a head lease of the Equipment to one separate special purpose trust (formed on behalf of a certain equity investor) and a sublease of the Equipment back from such trust. The sublease provides MUNI with an option to purchase the Equipment in approximately 26 years, the scheduled completion date of the sublease. During the term of the sublease, MUNI maintains custody of the Equipment and is obligated to insure and maintain the Equipment throughout the life of the sublease.

MUNI received an aggregate of \$72.6 million from the equity investors in full prepayment of the head lease. MUNI deposited approximately \$67.5 million of this head lease payment into two escrows. One escrow was deposited with a debt payment undertaker whose repayment obligations are guaranteed by Financial Security Assurance, an "Aaa/AAA" rated bond insurance company. The other escrow was invested in U.S. government bonds with maturity dates that match the completion of the sublease. Payments under these escrows are to be made at such times and in such amounts so as to fund MUNI's scheduled payments under the sublease as well as to provide a source of funding for MUNI's purchase

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option if it chooses to exercise it. Although these escrows do not represent a legal defeasance of MUNI's obligations under the sublease, management believes that the creditworthiness of these escrows is such that they will fund MUNI's obligations under the sublease and that the possibility that MUNI will need to access other monies to make sublease payments is remote.

As a result of the cash transactions above, MUNI recorded deferred revenue in fiscal year 2004 of \$4.4 million for the difference between the amount received of \$72.6 million and the amount paid to the escrows of \$67.5 million (minus \$0.7 million for certain transaction expenses). The deferred revenue will be amortized over the life of the sublease. The deferred revenue amortized in fiscal year 2004-2005 amounted to \$168 thousand.

As of June 30, 2005, the outstanding payments to be made on the sublease through 2029 are \$59.7 million and the payments to be made on the purchase option of the Equipment would be \$198.5 million, if exercised. All of these payments are to be funded from the amounts in escrow. If MUNI does not exercise the purchase option, MUNI would be required to either: 1) pay service and maintenance costs related to the continued operation and use of the vehicles beyond the term of the sublease; or 2) arrange for another party to be the "service recipient," under a "service contract," and to perhaps guarantee the obligations of that party under the service contract if the replacement service recipient does not meet specified credit or net worth criteria.

The data below reflect the operations of the five parking garages operated by separate nonprofit corporations organized by the City, which are under the Parking Authority. Information about these nonprofit corporations for the year ended June 30, 2005 follows (in thousands), including \$0.7 million accounts payable to MUNI:

	Downtown Parking	Uptown Parking	Japan Center Garage	Ellis- O'Farrell Parking	Portsmouth Plaza Parking	Total
Operating revenues.....	\$ 11,319	\$ 14,903	\$ 2,437	\$ 4,658	\$ 3,156	\$ 36,473
Depreciation.....	737	11,979	4,363	8,412	129	25,620
Operating income.....	593	(9,861)	(4,110)	(7,521)	74	(20,825)
Interest and other non-operating revenues (expenses).....	(442)	(1,059)	(5)	(194)	16	(1,684)
Change in net assets.....	151	(10,920)	(4,115)	(7,715)	90	(22,509)
Capital assets, additions.....	-	-	-	-	246	246
Capital assets, deletions.....	(433)	(11,979)	(3,694)	(7,994)	-	(24,100)
Net working capital (deficit).....	(7,280)	(8,626)	21	(1,486)	791	(16,580)
Total assets.....	29,155	49,675	3,805	11,991	3,361	97,987
Total liabilities.....	19,136	28,989	576	6,536	612	55,849
Net assets.....	10,019	20,686	3,229	5,455	2,749	42,138
Total debt outstanding.....	\$ 11,665	\$ 19,095	\$ 309	\$ 5,323	\$ -	\$ 36,392

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**(f) Laguna Honda Hospital**

The Laguna Honda Hospital (LHH) is a skilled nursing facility which specializes in serving elderly and disabled residents. The operations of LHH are subsidized by the City. It is the City's policy to fund operating deficits of the enterprise on a budgetary basis; however, the amount of operating subsidy provided is limited to the amount budgeted by the City. Accordingly, depreciation and certain non-current accrued expenses are not funded, resulting in continuing deficits on a budget basis. In those circumstances, the City allows the enterprise to show a deficit on a budget basis. For the fiscal year ended June 30, 2005, the subsidy for LHH was approximately \$39 million.

	(in thousands)
Changes in net assets of LHH on a GAAP basis	\$ 18,502
Transfer to General Fund	79
Net income on specific/donor restricted funds	(17,598)
Operating subsidy from City General Fund	<u>(39,239)</u>
Net loss on LHH on a GAAP basis before operating subsidy	<u>(38,256)</u>
Expenses which require budgetary funding but are not GAAP basis expenses:	
Capitalized services and other asset purchases	1,339
Change in encumbrances and appropriation carryforward	(2,503)
Expenses which do not require budgetary funding but are GAAP basis expenses:	
Depreciation and other expenses	<u>181</u>
Net loss of LHH requiring General Fund subsidy on a budget basis	<u><u>\$ (39,239)</u></u>

LHH has agreements with third-party payors that provide for reimbursement to LHH at amounts different from its established rates. Contractual adjustments under third-party reimbursement programs represent the difference between the hospital's established rate for services and amounts reimbursed by third-party payors. Medicare and Medi-Cal are the major third-party payors with whom such agreements have been established. During the fiscal year ended June 30, 2005, Medicare and Medi-Cal charges for services amounted to approximately \$4 million and \$107 million, respectively. As of June 30, 2005, LHH had net patient receivables from Medicare of \$1.3 million and net patient receivables from Medi-Cal of \$21.7 million.

During fiscal year ended June 30, 2005, LHH received approximately \$15 million in payments as a result of matching federal funds to local funds, which provided a Medi-Cal supplemental in the form of quarterly payments effective August 1, 2001.

In November 1999, San Francisco voters approved Proposition A, a ballot measure authorizing the City to issue general obligation bonds to finance the acquisition, improvement, construction and/or reconstruction of a new health care, assisted living and/or other type of continuing care facility or facilities to replace Laguna Honda Hospital (the Replacement Project). Proposition A requires an increase in property taxes to pay for the bonds. In addition, Proposition A stipulates that \$100 million of tobacco settlement funds received by the City, excluding \$1 million set aside each year for smoking education and prevention programs, may be used to pay for some construction of the Replacement Project, as well as to offset the cost to property owners of repaying the bonds. As of June 30, 2005, bonds have been sold to fund the Replacement Project. LHH is actively involved in the planning and design phase and construction of the Replacement Project.

The California Hospital Facilities Safety Act (SB 1953) specifies certain requirements that must be met at various dates in order to increase the probability that LHH could maintain uninterrupted operations following major earthquakes. By January 1, 2008, all general acute care buildings must be life safe. By

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January 1, 2030, all general acute care inpatient buildings must be operational after an earthquake. In December 2001, LHH finalized and submitted a plan to the State of California indicating that the Laguna Honda Hospital Replacement Project will be fully operational by 2013 and thereby in full compliance with the 2030 requirements. A five-year extension for the January 2008 deadline was requested and granted, postponing the deadline to 2013.

LHH received a report initiated by the California Integrated Waste Management Board declaring an old dumpsite on hospital property a "hazardous waste site" under California hazardous waste statute. The San Francisco Department of Public Health, as the local enforcement agency, has been designated to oversee and certify the future abatement of the dumpsite. LHH management has subsequently received a number of estimates to remedy this situation, ranging from approximately \$0.8 million to \$2.5 million. The hospital and the San Francisco Department of Public Health are evaluating the bids submitted. The State has mentioned that this particular hazardous waste site is classified as a low priority considering the other more hazardous waste sites within the State. The specific site has been contained and secured for the safety of the general public.

As of June 30, 2005, LHH has entered into various purchase contracts totaling approximately \$11.6 million that are related to future construction for the Replacement Project.

**(g) General Hospital Medical Center**

The San Francisco General Hospital Medical Center (SFGH) is an acute care hospital. The operations of SFGH are subsidized by the City. It is the City's policy to fully fund enterprise operations on a budgetary basis; however, the amount of operating subsidy provided is limited to the amount budgeted by the City. Accordingly, depreciation and certain non-current accrued expenses are not funded, resulting in continuing deficits on a budget basis. In those circumstances, the City allows the enterprise to show a deficit on a budget basis. For the year ended June 30, 2005, the subsidy for SFGH was \$78 million.

	(in thousands)
Income before transfers of SFGH on a GAAP basis	\$ 14,516
Reimbursement to City General Fund for SB 855 matching program	(80,683)
Transfers from City General Fund to support SFGH on:	
Other Program Support	1,374
Interest expense on the over draft funds with the City Treasury	(684)
Transfers from SFGH to City facility projects	(350)
Transfers from SFGH to Jail Health	(620)
Transfers from SFGH to Laguna Honda	(2,032)
Expenses which require budgetary funding but are not GAAP basis expenses:	
Capitalized services and other asset purchases	(4,170)
Change in encumbrances and appropriation carryforwards	(8,075)
Other expenses - Non-Operating Funds	(2,119)
Expenses which do not require budgetary funding but are GAAP basis expenses:	
Depreciation expense	6,655
Other Net GAAP expenses	(2,062)
Net loss of SFGH requiring General Fund subsidy on a budget basis	<u>\$ (78,250)</u>

SFGH has agreements with third-party payors that provide for reimbursement to SFGH at amounts different from its established rates. Contractual adjustments under third-party reimbursement programs represent the difference between SFGH's established rates and amounts reimbursed by third-party payors. Major third-party payors with whom such agreements have been established are Medicare, Medi-Cal, the State of California through Senate Bills 855 and 1255 and the Short-Doyle mental health

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program, the federal Medi-Cal Medical Education Program and Administrative Claiming System, and a managed care agreement signed with a health maintenance organization (HMO).

During the year ended June 30, 2005, Medicare and Medi-Cal revenue accounted for \$73 million and \$77 million of net patient service revenue, respectively. As of June 30, 2005, SFGH had net patient receivables from Medicare of \$8.1 million and net patient receivables from Medi-Cal of \$14.2 million.

State of California Senate Bill 855 (SB-855) was passed by the state legislature in July 1991 to provide additional funding to hospitals which provide a significant portion of their services to Medi-Cal recipients. In order to receive additional funds, the City must transfer funds to the State Medi-Cal program so that the funds may be matched by federal funds. Gross patient revenue recorded by SFGH for SB-855 totaled \$113.1 million for the year ended June 30, 2005. This revenue was offset by a reduction in the General Fund operating subsidy of \$80.7 million for net SB-855 revenues of \$32.4 million for the year ended June 30, 2005.

In addition, SFGH receives funding from the State of California under Senate Bill 1255 (SB-1255) which establishes a funding pool through public and private sector contributions with matching federal participation. For the year ended June 30, 2005, SFGH recognized gross patient revenue in the amount of \$65.0 million offset by a reduction in the contribution provided by the City of \$30.5 million for net SB-1255 revenues of \$34.5 million.

Under the Medi-Cal Medical Education program, SFGH is reimbursed for medical education costs incurred for services rendered to Medi-Cal beneficiaries. For the year ended June 30, 2005, SFGH recognized net patient service revenue in the amount of \$2.3 million pertaining to this program.

As of June 30, 2005, SFGH had Medi-Cal supplemental reimbursement receivables for SB-855, SB-1255, and other federal and state settlement payments of approximately \$13.3 million.

The State of California provides support to SFGH through a realignment of funding provided from vehicle license fees and sales tax allocated to California's counties. SFGH recognized \$61.1 million as other operating revenue for the year ended June 30, 2005, from realignment funding.

In addition, SFGH was reimbursed by the State of California, under the Short-Doyle program, for mental health services provided to qualifying residents based on an established rate per unit of service not to exceed an annual negotiated contract amount. During the year ended June 30, 2005, reimbursement under the Short-Doyle program amounted to approximately \$5.8 million and is included in State and other nonoperating revenues.

State of California Proposition 99, the Tobacco Tax Initiative, allocates funds to counties for health care services to indigent persons and others who are unable to pay for health care services. Proposition 99 funds allocated to SFGH for the year ended June 30, 2005, amounted to \$1.2 million and are included in other operating revenue.

SFGH provides care without charge or at amounts less than its established rates to patients who meet certain criteria under its charity care policy. Charges foregone based on established rates were \$213 million and estimated costs and expenses to provide charity care were \$109 million in fiscal year 2004-2005.

The City contracts on a year-to-year basis on behalf of SFGH with the University of California (UC). Under the contract, SFGH serves as a teaching facility for UC professional staff, medical students, residents, and interns who, in return, provide medical and surgical specialty services to SFGH's patients. The total amount for services rendered under the contract for the year ended June 30, 2005, was approximately \$77.6 million.

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In 1996, California passed Senate Bill 1953, mandating that all California acute care hospitals meet new seismic safety standards by 2013. In January 2001, the San Francisco Health Commission approved a resolution to support a rebuild effort for the hospitals, and the Department of Public Health conducted a series of planning meetings to review its options. It became evident that rebuilding rather than retrofitting was required, and that rebuilding SFGH presented a unique opportunity for the Department to make system-wide as well as structural improvements in its delivery of care for patients in 2013 and beyond.

In May 2005, the Mayor created the Blue Ribbon Committee (the Committee) on SFGH's future location. The Committee's charge was to make a recommendation on where SFGH should be built: (1) on the existing Potrero Hill campus or (2) at Mission Bay, collocating with the University of California at San Francisco (UCSF).

In October 2005, the Health Commission accepted the Committee's recommendation to rebuild at its current Potrero Avenue campus.

In addition to the Potrero location recommendation, the Committee recommended that the City begin the process of ascertaining whether a General Obligation bond for a SFGH rebuild can be approved by voters as well as what dollar amount voters are likely to approve. The City should identify additional mechanisms for financing the hospital replacement.

**(h) Clean Water Program**

The Clean Water Program (CWP) was established in 1977 pursuant to bond resolutions to account for the City's municipal sewage treatment and disposal system.

CWP's revenue, which consists mainly of sewer service charges, is pledged for the payment of principal and interest on various outstanding Sewer Revenue Bonds.

As of June 30, 2005, the CWP had outstanding commitments with third parties for capital projects and for materials and services totaling \$40.1 million.

**(i) San Francisco Market Corporation**

The San Francisco Market Corporation is a non-profit corporation organized to acquire, construct, finance, and operate a produce market. The information about this non-profit corporation is presented in the financial statements of the proprietary funds as a non-major fund.

**(12) SAN FRANCISCO REDEVELOPMENT AGENCY**

The Redevelopment Agency of the City and County of San Francisco (the Agency) is a public body, corporate and politic, organized and existing under the Community Redevelopment Law of the State of California. Since the organization of the Agency in 1948, the Agency has completed four redevelopment project areas and twelve redevelopment project areas are now underway. In addition, the Agency is undertaking feasibility studies for two potential redevelopment areas, designated by the Board of Supervisors of the City, and proposed expansion to two existing project areas.

The Agency acts as the lead Agency in administering the Housing Opportunities for Persons with AIDS (HOPWA) program, which is funded by a grant from the U.S. Department of Housing and Urban Development. The Agency applied for and was awarded a "Special Projects of National Significance" grant under the HOPWA program to provide partial rent subsidies and back to work job training.

In 1998, the Board of Supervisors approved ordinances and resolutions adopting the Mission Bay North and South Redevelopment Plans, Interagency Cooperation Agreements, Tax Allocation Agreements, and related ordinances and resolutions. The two project areas total 303 acres. The Agency has entered into an Owner Participation Agreement with the owner/developer to provide for development of the project

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areas. The proposed development in the north includes 3,000 housing units, 20% of which will be affordable units, urban entertainment retail space, City-serving retail space, neighborhood-serving retail space and public open space. The proposed development in the south will include 3,090 housing units, 20% of which will be affordable units, a UCSF research campus, a hotel, City-serving and neighborhood-serving retail space, commercial industrial space, a new fire and police station, and a 500-student public school on land to be donated by UCSF.

As of June 30, 2005, 1,079 residential units, including 148 affordable units, 24,000 square feet of office space, and 72,650 square feet of neighborhood retail space have been completed in Mission Bay North. Another 552 residential units are under construction, of which 159 units are affordable. A commercial office building totaling 285,000 square feet and two UCSF research building of 550,000 square feet have been completed in Mission Bay South. Mission Bay is expected to create over 31,000 new permanent jobs. The Mission Bay development will take place over 20 to 30 years, and will require investment of over \$145 million in new public infrastructure. Total development costs for the two project areas are expected to exceed \$4 billion.

The construction of the Jessie Square Garage (the Garage), which contains 450 parking spaces, was completed and started operations in February 2005. During the year ended June 30, 2003, the Garage construction was financed by tax allocation bonds issued. The City has advanced tax increment revenue for debt service payments, which will be repaid from net operating revenues from the Garage.

The Agency has no direct taxing power and does not have the power to pledge the general credit or taxing power of the City, the State of California or any political subdivision thereof. However, California's Health and Safety Code allows redevelopment agencies with appropriate approvals of the local legislative bodies to recover costs of financing public improvements from increased tax revenues (tax increment) associated with increased property values of individual project areas. During the year, the Agency's revenue from property tax increment was \$53.3 million.

The Public Initiatives Development Corporation (PIDC) was formed in May of 2002 to develop affordable housing on the Agency's behalf. On November 12, 2004, PIDC and Wincopin Circle, LLLP formed a limited partnership, Plaza Apartments Associates, L.P. (the Partnership). PIDC is the managing general partner and owns a 0.01% interest in the partnership. Wincopin Circle, LLLP is a limited partner and owns a 99.99% interest. The Partnership is currently constructing a 106-unit affordable housing project in the South of Market project area. The project, which is scheduled for completion in December 2005, was originally undertaken by PIDC. Additionally, PIDC transferred all related assets (including the rights to a ground lease) and liabilities to the Partnership.

In order to facilitate construction and rehabilitation within the project areas, various construction loan notes, promissory notes, community district facility bonds, and mortgage revenue bonds with an aggregate outstanding balance of approximately \$662 million as of June 30, 2005, have been issued. When these obligations are issued, they are secured by the related mortgage indebtedness and special assessment taxes, and, in the opinion of management, are not considered obligations of the Agency or the City and therefore not included in the basic financial statements. Debt service payments will be made by developers or property owners.

California Health and Safety Code Section 33334.3 requires the Agency to set aside 20% of the proceeds from its incremental property tax revenues for expenditures for low and moderate income housing. Related interest earned must also be set aside for such purposes. The Agency established a Low and Moderate Income Housing Fund to account for this commitment and has budgeted \$362 million for such expenditures since its inception. The Agency has expended \$249 million for low- and moderate-income housing since its inception.

The Agency had commitments under contracts for capital improvements of approximately \$23.3 million as of June 30, 2005.

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**(13) TREASURE ISLAND DEVELOPMENT AUTHORITY**

The TIDA is a nonprofit public benefit corporation. The TIDA was authorized in accordance with the Treasure Island Conversion Act of 1997 and designated as a redevelopment agency pursuant to Community Redevelopment Law of the State of California. The TIDA is governed by seven commissioners who are appointed by the Mayor, subject to confirmation by the City's Board of Supervisors. The specific purpose of the TIDA is to promote the planning, redevelopment, reconstruction, rehabilitation, reuse and conversion of the property known as Naval Station Treasure Island for the public interest, convenience, welfare and common benefit of the inhabitants of the City.

The mission of TIDA is to redevelop the former Naval Station Treasure Island and to manage its integration with the City in compliance with federal, state and City guidelines (including the California Tidelands Trust) to maximize revenues to the City's General Fund; to create new job opportunities for San Francisco residents, including assuring job opportunities for homeless and economically disadvantaged residents; to increase recreational and bay access venues for San Francisco and Bay Area residents; and to promote the welfare and well being of the citizens of San Francisco.

The services provided by TIDA include negotiating the acquisition of former Naval Station Treasure Island with the U.S. Navy and establishing the Treasure Island Redevelopment Project; renting Treasure Island facilities leased from the U.S. Navy to generate revenues sufficient to cover operating costs; maintaining Treasure Island facilities owned by the U.S. Navy which are not leased to the TIDA or the City; providing facilities for special events, film production and other commercial business uses; providing 1,000 housing units; and overseeing the U.S. Navy's toxic remediation activities on the former naval base.

During fiscal year 2004-2005, TIDA's primary source of revenues included facility and housing rents. During fiscal year 2002-2003, TIDA received Navy agreement to initiate the process of early transfer, including competitive selection of a contractor to complete the Navy's Treasure Island Remediation Program with Navy funding but under TIDA direction and supervision; entered an exclusive negotiating agreement with a private developer for the redevelopment of the former naval base; and completed a draft Environmental Impact Report (EIR) for the transfer.

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**(14) INTERFUND RECEIVABLES, PAYABLES, AND TRANSFERS**

“Due to” and “due from” balances have primarily been recorded when funds overdraw their share of pooled cash or when there are transactions between entities where one or both entities do not participate in the City’s pooled cash. The composition of interfund balances as of June 30, 2005, is as follows (in thousands):

**Due to/from other funds (in thousands):**

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
General	Nonmajor Governmental Funds	\$ 18,117
	Internal Service Funds	1,374
	San Francisco International Airport	1,052
	Municipal Transportation Agency	762
	Laguna Honda Hospital	8,438
		<u>29,743</u>
Nonmajor Governmental Funds	Nonmajor Governmental Funds	12,303
		<u>12,303</u>
Internal Service	General Fund	796
	Nonmajor Governmental Funds	861
	General Hospital Medical Center	545
	Laguna Honda Hospital	99
		<u>2,301</u>
Water Department	Municipal Transportation Agency	2,593
		<u>2,593</u>
Hetch Hetchy Water and Power	General Fund	1,061
	Nonmajor Governmental Funds	12,496
	Municipal Transportation Agency	102
	General Hospital Medical Center	595
	Water Department	81
		<u>14,335</u>
Municipal Transportation Agency	Nonmajor Governmental Funds	33,837
	Water Department Fund	2,574
		<u>36,411</u>
Total		<u>\$ 97,686</u>

**Due to/from primary government and component units:**

<u>Receivable Entity</u>	<u>Payable Entity</u>	<u>Amount</u>
Primary government - governmental	Component unit - Redevelopment Agency	<u>\$ 3,375</u>

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Transfers (in thousands):

Transfers:  Funds	Funds									Total Transfers Out
	General Fund	Nonmajor Governmental	Internal Service Funds	San Francisco International Airport	Hetch Hetchy	Municipal Transportation Agency	San Francisco General Hospital	Clean Water	Laguna Honda Hospital	
General fund.....	\$ -	\$ 71,432	\$ 270	\$ 4,611	\$ -	\$ 137,770	\$ 78,940	\$ -	\$ 37,207	\$ 330,230
Nonmajor governmental funds.....	51,228	35,137	-	-	-	94,906	-	1,922	-	183,193
San Francisco International Airport.....	19,677	-	-	-	-	-	-	-	-	19,677
Municipal Transportation Agency.....	-	12,298	-	-	-	-	-	-	-	12,298
San Francisco General Hospital.....	81,304	350	-	-	-	-	-	-	2,032	83,686
Clean Water.....	-	48	-	-	1,628	-	-	-	-	1,676
Laguna Honda Hospital.....	79	-	-	-	-	-	-	-	-	79
Total transfers in.....	<u>\$ 152,288</u>	<u>\$ 119,265</u>	<u>\$ 270</u>	<u>\$ 4,611</u>	<u>\$ 1,628</u>	<u>\$ 232,676</u>	<u>\$ 78,940</u>	<u>\$ 1,922</u>	<u>\$ 39,239</u>	<u>\$ 630,839</u>

The \$330.2 million General Fund transfer out includes a total of \$253.9 million in operating subsidies to Municipal Transportation Agency, General Hospital Medical Center, and Laguna Honda Hospital (note 11). The transfers of \$71.4 million from the General Fund to the nonmajor governmental funds is to provide support to various City programs such as the public library and the Children and Families Fund, as well as to provide resources for the payment of debt service. The transfers between the nonmajor governmental funds are to provide support for various City programs and to provide resources for the payment of debt service.

The General Fund received transfers in of \$81.3 million from General Hospital Medical Center, of which \$80.7 million was reimbursement for the SB 855 matching program (note 11(g)), and \$19.7 million from the San Francisco International Airport, representing a portion of concession revenue (note 11 (a)). The \$95 million transfer from nonmajor governmental funds is for capital and operating transfers from the San Francisco County Transportation Authority to the Municipal Transportation Agency.

**(15) COMMITMENTS AND CONTINGENT LIABILITIES**

**(a) Grants and Subventions**

Receipts from federal and state grants and other similar programs are subject to audit to determine if the monies were expended in accordance with appropriate statutes, grant terms and regulations. The City believes that no significant liabilities will result.

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**(b) Operating Leases**

The City has noncancellable operating leases for certain buildings and data processing equipment, which require the following minimum annual payments (in thousands):

**Primary Government**

**Governmental Activities**

<u>Fiscal Years</u>	
2006.....	\$ 27,319
2007.....	24,008
2008.....	20,940
2009.....	11,535
2010.....	9,951
2011-2015.....	18,206
2016-2020.....	3,600
Total.....	<u>\$ 115,559</u>

Operating lease expense incurred for fiscal year 2004-2005 was approximately \$28.9 million.

**Business-type Activities**

<u>Fiscal Years</u>	<u>San Francisco International Airport</u>	<u>Port of San Francisco</u>	<u>Municipal Transportation Agency</u>	<u>General Hospital Medical Center</u>	<u>Total Business-type Activities</u>
2006.....	\$ 5,320	\$ 2,739	\$ 4,682	\$ 5,457	\$ 18,198
2007.....	5,727	2,936	4,101	2,766	15,530
2008.....	5,741	2,936	3,874	1,910	14,461
2009.....	4,631	2,936	3,874	1,457	12,898
2010.....	-	2,936	3,314	1,277	7,527
2011-2015...	-	14,684	167	-	14,851
2016-2020...	-	13,888	179	-	14,067
2021-2025...	-	13,888	135	-	14,023
2026-2030...	-	13,888	121	-	14,009
2031-2035...	-	13,888	-	-	13,888
2036-2040...	-	13,888	-	-	13,888
2041-2045...	-	13,888	-	-	13,888
2046-2050...	-	11,341	-	-	11,341
Total.....	<u>\$ 21,419</u>	<u>\$ 123,836</u>	<u>\$ 20,447</u>	<u>\$ 12,867</u>	<u>\$ 178,569</u>

Operating lease expense incurred for the Airport, Port, MTA, and SFGH for fiscal year 2004-2005 was \$5.9 million, \$2.6 million, \$6.2 million, and \$4.8 million, respectively.

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**Component Unit - Redevelopment Agency**

The Redevelopment Agency (Agency) has noncancellable operating leases for its office sites, which require the following minimum annual payments (in thousands):

Fiscal Years		
2006.....	\$	1,930
2007.....		867
2008.....		846
2009.....		853
2010.....		862
2011-2015.....		4,351
2016-2020.....		4,351
2021-2025.....		4,351
2026-2030.....		4,351
2031-2035.....		4,351
2036-2040.....		4,350
2041-2045.....		4,350
2046-2050.....		4,350
Total.....	\$	40,163

Rent payments totaling \$2.1 million are included in the Agency's financial statements for the year ended June 30, 2005.

Several City departments lease land and various facilities to tenants and concessionaires who will provide the following minimum annual payments (in thousands):

**Primary Government**

**Governmental Activities**

Fiscal Years		
2006.....	\$	1,191
2007.....		861
2008.....		626
2009.....		567
2010.....		598
2011-2015.....		2,466
2016-2020.....		1,815
2021-2025.....		340
2026-2030.....		70
2031-2035.....		17
Total.....	\$	8,551

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**Business-type Activities**

Fiscal Years	San Francisco International Airport	Port of San Francisco	General Hospital Medical Center	Municipal Transportation Agency	Market Corp	Total Business-type Activities
2006.....	\$ 56,954	\$ 25,379	\$ 1,950	\$ 3,143	\$ 912	\$ 88,338
2007.....	47,487	22,951	1,991	2,958	782	76,169
2008.....	45,818	21,311	2,033	2,634	476	72,272
2009.....	38,694	19,593	2,077	2,168	380	62,912
2010.....	29,946	17,161	2,123	1,303	405	50,938
2011-2015.....	20,406	76,230	2,168	2,965	1,305	103,074
2016-2020.....	-	63,890	-	-	-	63,890
2021-2025.....	-	54,080	-	-	-	54,080
2026-2030.....	-	45,230	-	-	-	45,230
2031-2035.....	-	42,800	-	-	-	42,800
2036-2040.....	-	33,473	-	-	-	33,473
2041-2045.....	-	21,142	-	-	-	21,142
2046-2050.....	-	16,678	-	-	-	16,678
2051-2055.....	-	7,197	-	-	-	7,197
2056-2060.....	-	7,000	-	-	-	7,000
2061-2065.....	-	7,000	-	-	-	7,000
2066-2070.....	-	2,485	-	-	-	2,485
Total.....	<u>\$ 239,305</u>	<u>\$ 483,600</u>	<u>\$ 12,342</u>	<u>\$ 15,171</u>	<u>\$ 4,260</u>	<u>\$ 754,678</u>

**Component Unit - Redevelopment Agency**

The Agency leases various facilities within the Yerba Buena Center, Western Addition, and Hunters Point areas. The minimum annual payments are as follows (in thousands):

Fiscal Years	
2006.....	\$ 3,019
2007.....	2,899
2008.....	2,839
2009.....	2,843
2010.....	2,948
2011-2015.....	14,880
2016-2020.....	15,401
2021-2025.....	14,323
2026-2030.....	15,190
2031-2035.....	16,250
2036-2040.....	17,405
2041-2045.....	18,692
2046-2050.....	5,430
2051-2055.....	440
2056-2060.....	350
2061-2065.....	325
2066-2070.....	287
2071-2075.....	250
2076-2080.....	158
2081-2085.....	150
2086-2090.....	150
2091-2095.....	150
2096-2099.....	68
Total.....	<u>\$ 134,447</u>

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**(c) Other Lease Commitments**

The City is making lease payments to the Agency for the Moscone Convention Center in the amount of approximately \$18 million per year through July 1, 2025. The lease payments are intended to approximate the debt service requirements of the corresponding lease revenue bonds that were issued by the Agency to finance the construction and expansion of the Moscone Convention Center which are recorded as a long term obligation of the Agency. The City is also making lease payments to outside lessors for various telecommunication and information equipment through an internal service fund.

Amounts to be provided for capital leases are as follows (in thousands):

Fiscal Years	Moscone Convention Center	Other	Total
2006.....	\$ 17,871	\$ 424	\$ 18,295
2007.....	17,874	65	17,939
2008.....	18,571	-	18,571
2009.....	18,640	-	18,640
2010.....	18,717	-	18,717
2011-2015.....	94,631	-	94,631
2016-2020.....	79,211	-	79,211
2021-2025.....	16,433	-	16,433
Total minimum lease payments.....	281,948	489	282,437
Less amounts representing interest.....	(83,721)	(13)	(83,734)
Present value of maximum lease payments.....	<u>\$ 198,227</u>	<u>\$ 476</u>	<u>\$ 198,703</u>

**(d) Other Commitments**

The Retirement System has commitments to contribute capital for real estate and alternative investments in the aggregate amount of approximately \$718 million at June 30, 2005.

The City is a participant in the Peninsula Corridor Joint Powers Board (PCJPB), which was formed in 1991 to plan, administer, and operate the Peninsula CalTrain rail service. The City, on behalf of MUNI, is responsible for 11.6% of the net operating costs and administrative expenses of the PCJPB for operating and capital needs. During the fiscal year ended June 30, 2005, the City contributed \$6.4 million to the PCJPB for its operating needs. This is paid by MTA from the subsidy transfer it receives from the City.

**(16) RISK MANAGEMENT**

**Risk Retention Program Description**

The City is exposed to various risks of losses related to torts, theft of, damage to, and destruction of assets; business interruption; errors and omissions; automobile liability and accident claims (primarily for Muni Railway); medical malpractice; natural disasters; employee health benefit claim payments for direct provider care (collectively referred to herein as estimated claims payable); and injuries to employees (workers' compensation). With certain exceptions, it is the policy of the City not to purchase commercial insurance for the risks of losses to which it is exposed. Instead, the City believes it is more economical to manage its risks internally and set aside funds as needed for estimated current claim settlements and unfavorable judgments through annual appropriations and supplemental appropriations.

The City maintains limited excess coverage for certain facilities. The SFO carries liability insurance coverage of \$750 million and commercial property insurance coverage for full replacement value on all facilities owned by the SFO. The SFO does not carry insurance for losses due to seismic activity. The SFO is self-insured for general liability up to the first \$10,000 and the SFO carries liability insurance for

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any amounts in excess of \$10,000. The Port carries commercial insurance for all general liability, property and casualty risks of loss. Additionally, limited insurance coverage is maintained by the City for the Moscone Convention Center property, personal liability, and for art at City-owned museums.

The San Francisco Redevelopment Agency is a member of the Bay Cities Joint Powers Authority which provides coverage for its general liability, automobile liability, and public officials errors and omissions risks with combined single limits of \$15 million per occurrence and a deductible of \$50,000 self-insurance retention per occurrence.

Any claims relating to the construction of the Moscone Convention Center are indemnified by the City under an agreement between the Agency and the City.

Settled claims have not exceeded commercial insurance coverage in any of the past three fiscal years.

Expenditures and liabilities for all workers' compensation claims and other estimated claims payable are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported. Because actual claim liabilities depend on such complex factors as inflation, changes in legal doctrines, and damage awards, the process used in computing claim liabilities does not necessarily result in an exact amount. Claim liabilities are re-evaluated periodically to take into consideration recently settled claims, the frequency of claims, and other legal and economic factors. The recorded liabilities have not been discounted.

***Estimated Claims Payable***

Numerous lawsuits related to the governmental fund types are pending or threatened against the City. The City's liability as of June 30, 2005 has been actuarially determined and includes an estimate of incurred but not reported losses.

Changes in the reported estimated claims payable since June 30, 2003, resulted from the following activity (in thousands):

	Beginning Fiscal Year Liability	Current Year Claims and Changes in Estimates	Claim Payments	Ending Fiscal Year Liability
2003-2004	\$ 93,304	\$ 71,967	\$ (37,835)	\$ 127,436
2004-2005	127,436	63,684	(38,865)	152,255

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Breakdown of the estimated claims payable at June 30, 2005 is as follows (in thousands):

<u>Governmental activities:</u>	
Current portion of estimated claims payables.....	\$ 37,487
Long-term portion of estimated claims payable.....	46,050
<u>Business-type activities:</u>	
Current portion of estimated claims payables.....	22,503
Long-term portion of estimated claims payable.....	46,215
 Total.....	 <u>\$ 152,255</u>

The Retirement System is involved in two class action type lawsuits which are collectively referred to as "Final Compensation" cases. These lawsuits allege that the Retirement System should include additional "pay types" in pension calculations. The most significant pay types common to all members of the Retirement System are lump sum payments after termination of employment for sick leave and vacation. The police, fire, and transit employees have additional claims for special pay types specific to those employee groups. There is also a lawsuit against the Retirement System by the Veteran Police Officers Association (VPOA) that alleges that the Retirement System should include Police Officers' Standards Training (POST) pay in pension calculations for those police officers who retired prior to the creation of the POST ranks. The Retirement System was successful in defending both of these class action lawsuits in the trial court. An appeal remains a possibility for either or both of these lawsuits. Should there be a successful appeal, the potential loss to the Retirement System is estimated to be less than \$100 million as of June 30, 2005.

**Workers' Compensation**

The City self-insures for workers' compensation coverage. The City's liability as of June 30, 2005 has been actuarially determined and includes an estimate of incurred but not reported losses. The total amount estimated to be payable for claims incurred as of June 30, 2005 was \$391.4 million which is reported in the appropriate individual funds in accordance with the City's accounting policies (note 2).

Changes in the reported accrued workers' compensation since June 30, 2003, resulted from the following activity (in thousands):

	Beginning Fiscal Year Liability	Current Year Claims and Changes in Estimates	Claim Payments	Ending Fiscal Year Liability
2003-2004	\$ 364,256	\$ 108,177	\$ (75,307)	\$ 397,126
2004-2005	397,126	87,372	(93,070)	391,428

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Breakdown of the accrued workers' compensation liability at June 30, 2005 is as follows (in thousands):

<u>Governmental activities:</u>	
Current portion of accrued workers' compensation liability.....	\$ 44,624
Long-term portion of accrued worker's compensation liability.....	170,181
<u>Business-type activities:</u>	
Current portion of accrued workers' compensation liability.....	38,005
Long-term portion of accrued worker's compensation liability.....	<u>138,618</u>
 Total.....	 <u>\$ 391,428</u>

**(17) SUBSEQUENT EVENTS (UNAUDITED)**

**Long-term Debt**

In July 2005, the City issued a total of \$150.1 million in General Obligation Bonds. They consist of the following four bonds: \$79.4 million California Academy of Sciences Improvement Bonds, Series 2005E, \$29.2 million Steinhart Aquarium Improvement Bonds Series 2005F, \$34 million Branch Library Facilities Improvement Bonds Series 2005G and \$7.5 million Zoo Facilities Bonds Series 2005H. The 2005E and 2005F Bonds will finance the acquisition, construction, and reconstruction of certain improvements to the Academy of Sciences and Steinhart Aquarium respectively. The 2005G Bonds were issued to provide funds to finance the acquisition, renovation and construction of branch libraries and other library facilities, other than the Main Library. The 2005H Bonds will finance the acquisition, construction and/or reconstruction of San Francisco Zoo facilities. The 2005E, 2005F, 2005G and 2005H Bonds have interest rates ranging from 3.0% to 5.0% and mature from June 2006 through June 2025.

In July 2005, the San Francisco Redevelopment Agency issued Tax Allocation Refunding Revenue Bonds Series 2005A in the amount of \$20.4 million and Taxable Tax Allocation Refunding Revenue Bonds Series 2005B in the amount of \$8.1 million. Series 2005A Bonds were issued for the purpose of refunding the entire Series 1998A Tax Allocation Revenue Bonds and partially refunding the Series 1998C Tax Allocation Refunding Revenue Bonds. Series 2005B Bonds were issued to refund the entire Series 1998B Tax Allocation Revenue Bonds and the Series 2000B Tax Allocation Revenue Bonds. Together, the 2005 Series A and B Bonds produced net present value savings exceeding \$2 million or 7.2% of the par amount of bonds refunded. In July 2005, the Agency issued Taxable Tax Allocation Revenue Bonds, Series 2005C in the amount of \$43.9 million and Tax Allocation Revenue Bonds, Series 2005D in the amount of \$16.2 million. The proceeds from the Series 2005C Bonds will be used primarily to fund the construction of low-income housing, provide for economic development in the Western Addition project area, and fund a capital reserve for the Yerba Buena Gardens. Series 2005D Bonds were issued for the purpose of funding the construction of infrastructure in the Mission Bay North project area.

In September 2005, the City issued General Obligation Bonds, Laguna Honda Hospital, Series 2005I in the amount of \$69 million. The bonds mature from June 2008 through June 2030. The bonds were issued to provide funds for the acquisition, improvement, construction and/or reconstruction of a new health care, assisted living and/or other type of continuing care facility or facilities to replace the Laguna Honda Hospital. The 2005I Bonds have interest rates ranging from 4.0% to 5.0%.

In September 2005, the San Francisco Water Department issued an additional \$10 million commercial paper notes to fund capital projects associated with Proposition A authorization. As of that date, there was \$90 million in commercial paper outstanding.

In October 2005, the San Francisco Finance Corporation issued Lease Revenue Bonds Series 2005A in the amount of \$9.4 million. The bonds mature from April 2006 through October 2010 and have interest rates ranging from 3.25% to 5.0%. The bonds were issued to provide funds to finance the acquisition and

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installation of certain equipment to be leased to the City under an Equipment Lease between the City and San Francisco Finance Corporation.

**Elections**

On November 8, 2005, the San Francisco voters approved the following propositions that will have a fiscal impact on the City:

**Proposition A – Community College District General Obligation Bonds** This is an ordinance that allows the Community College District to borrow \$246.3 million by issuing general obligation bonds. The District will use the money to construct and equip new facilities or buildings for performing arts, bio/stem cell technology, for student services and programs offered jointly with San Francisco State University, as well as to complete various construction projects at City College campuses and improve existing facilities by expanding intercampus communication systems, improving energy conservation, and supporting various training and educational programs. The principal and interest on general obligation bonds are paid with property tax revenues. Proposition A will require an increase in property taxes to pay for the bonds. In fiscal year 2006-2007, following issuance of the first series of bonds, the estimated annual costs of debt service would be \$6.5 million and result in a property tax rate of 0.057¢ per \$100 of assessed valuation (or \$5.66 per \$100,000 of assessed valuation).

In fiscal year 2009-2010, following issuance of the last series of bonds, and the year with the highest tax rate, the estimated costs of debt service would be \$19.5 million and result in a property tax rate of .15¢ per \$100 of assessed valuation (or \$15.44 per \$100,000 of assessed valuation). The best estimate of the average tax rate from fiscal year 2006-2007 through 2032-2033 is .11¢ per \$100 of assessed valuation (or \$10.71 per \$100,000 of assessed valuation). Based on these estimates, the highest estimated increase in annual property taxes for the owner of a home with an assessed value of \$400,000 would be approximately \$60.68.

**Proposition F – Neighborhood Firehouses** This is an ordinance that requires the City to maintain and operate all 42 firehouses and specific emergency and rescue vehicles and equipment at the same levels that were used on January 1, 2004. The City will be required to operate the following 24 hours a day: Operate each firehouse, provide adequate staff, operate an arson and investigation unit, maintain no fewer than four ambulances based in the firehouses, and maintain no fewer than four medical supervisors based in the firehouses. The fiscal impact of Proposition F is a new added cost of approximately \$4.4 to \$6.6 million annually, and a requirement to operate facilities and vehicles that currently cost the City approximately \$158 million annually. The costs could increase or decrease depending on how the City implements the ordinance. Under the City Charter, the ultimate cost of this proposal depends on decisions made in the City's annual budget process.