

MANAGEMENT'S DISCUSSION AND ANALYSIS

This section of the City and County of San Francisco's (the City) Comprehensive Annual Financial Report (CAFR) presents a narrative overview and analysis of the financial activities of the City for the fiscal year ended June 30, 2009. We encourage readers to consider the information presented here in conjunction with additional information in our transmittal letter. Certain amounts presented as 2007-2008 summarized comparative financial information in the basic financial statements have been reclassified to conform to the presentation in the 2008-2009 basic financial statements.

FINANCIAL HIGHLIGHTS

The assets of the City exceeded its liabilities at the end of the fiscal year by approximately \$6.07 billion (net assets). Of this amount, the City's unrestricted net assets, decreased from \$229.5 million to a deficit of \$165.2 million.

The government's total net assets decreased by \$368.1 million or 5.7 percent over the previous fiscal year. Within the \$368.1 million, the government's total capital assets net of related debt and restricted assets increased by \$71.6 million, which includes a \$15.5 million decrease related to an adjustment to beginning net assets of the business-type activities, and were offset by a \$394.7 million decrease in unrestricted net assets. A significant portion of the decrease in unrestricted net assets is due to recognition of \$301.3 million other postemployment benefit expense and \$33.5 million pollution remediation liabilities in the current fiscal year, of which \$27.5 million was reported as an adjustment to beginning net assets as a result of the implementation of the new pollution remediation accounting standard.

The City's governmental funds reported total revenues of \$3.68 billion; an \$8.2 million or 0.2 percent slight increase over the prior year. The growth in property tax revenues of \$92.7 million and the growth in federal and state grant revenues of approximately \$49.2 million were largely offset by declines in other local taxes and other revenues. Governmental funds expenditures totaled \$3.65 billion for this period, a \$109.4 million or 3.1 percent increase, reflecting increases in cost of living and growth in demand for government services.

At the end of the fiscal year, the City's General Fund had an unreserved fund balance of \$28.2 million, representing 1.2 percent of total General Fund expenditures of \$2.41 billion. The General Fund's unreserved fund balance decreased by 63.4 percent from the prior year amount of \$77.1 million. Factors contributing to this decline include a moderate decrease in total revenue, increase in demand for services and the City's related use of fund balances.

The City's total long-term debt, including all bonds, loans, commercial paper and capital leases increased by \$454.9 million during this fiscal year. The City issued a total of \$963.9 million in debt. Of this amount, \$175.5 million was for general obligation bonds for improvement works for the San Francisco General Hospital, clean and safe neighborhood parks as well as Seismic Safety Loan Program. A total of \$163.3 million in certificates of participation for the Laguna Honda Hospital were issued for the construction and improvement of the Laguna Honda Hospital. The City also issued a total of \$118.1 million General Obligation Bonds to refund the variable rate General Obligation Bonds (Laguna Honda Hospital) and a total of \$145.3 million in Lease Revenue Refunding bonds to refund the variable rates Lease Revenue Bonds (Moscone Center Expansion Project). In addition, the San Francisco International Airport issued a total of \$314.9 million Revenue Refunding Notes to refund various variable rate demand bonds.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis are intended to serve as an introduction to the City's basic financial statements. The City's basic financial statements comprise three components: (1) **Government-wide** financial statements, (2) **Fund** financial statements, and (3) **Notes** to the financial statements. This report also contains other **supplementary information** in addition to the basic financial statements themselves. These various elements of the Comprehensive Annual Financial Report are related as shown in the graphic below.

Organization of City and County of San Francisco Comprehensive Annual Financial Report

CAFR	Introductory Section	INTRODUCTORY SECTION			
	+				
	Financial Section	Management's Discussion and Analysis			
		Government-wide Financial Statements	Fund Financial Statements		
		Statement of net assets	Governmental Funds	Proprietary Funds	Fiduciary Funds
			Balance Sheet	Statement of net assets	Statement of fiduciary net assets
		Statement of activities	Statement of revenues, expenditures, and changes in fund balances	Statement of revenues, expenses, and changes in fund net assets	Statement of changes in fiduciary net assets
			Budgetary comparison statement	Statement of cash flows	
		Notes to the Financial Statements			
		Required Supplementary Information Other Than MD&A			
Information on individual non-major funds and other supplementary information that is not required					
+					
Statistical Section	STATISTICAL SECTION				

The following figure summarizes the major features of the financial statements. The overview section below also describes the structure and contents of each of the statements in more detail.

	Government-wide Statements	Fund Financial Statements		
		Governmental	Proprietary	Fiduciary
Scope	Entire entity (except fiduciary funds)	The day-to-day operating activities of the City for basic governmental services	The day-to-day operating activities of the City for business-type enterprises	Instances in which the City administers resources on behalf of others, such as employee benefits
Accounting basis and measurement focus	Accrual accounting and economic resources focus	Modified accrual accounting and current financial resources focus	Accrual accounting and economic resources focus	Accrual accounting and economic resources focus; except agency funds do not have measurement focus
Type of asset and liability information	All assets and liabilities, both financial and capital, short-term and long-term	Current assets and liabilities that come due during the year or soon thereafter	All assets and liabilities, both financial and capital, short-term and long-term	All assets held in a trustee or agency capacity for others
Type of inflow and outflow information	All revenues and expenses during year, regardless of when cash is received or paid	Revenues for which cash is received during the year or soon thereafter; expenditures when goods or services have been received and the related liability is due and payable	All revenues and expenses during year, regardless of when cash is received or paid	All additions and deductions during the year, regardless of when cash is received or paid

Government-wide Financial Statements

The government-wide financial statements are designed to provide readers with a broad overview of the City's finances, in a manner similar to a private-sector business.

The **statement of net assets** presents information on all of the City's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether or not the financial position of the City is improving or deteriorating.

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

Both of the government-wide financial statements distinguish functions of the City that are principally supported by taxes and intergovernmental revenues (governmental activities) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (business-type activities). The governmental activities of the City include public protection, public works, transportation and commerce, human welfare and neighborhood development, community health, culture and recreation, general administration and finance, and general City responsibilities. The business-type activities of the City include an airport, port, public transportation systems (including parking), water and power operations, an acute care hospital, a long-term care hospital, sewer operations, and a produce market.

The government-wide financial statements include not only the City itself (known as the primary government), but also a legally separate redevelopment agency, the San Francisco Redevelopment Agency, and a legally separate development authority, the Treasure Island Development Authority (TIDA), for which the City is financially accountable. Financial information for these component units is reported separately from the financial information presented for the primary government. Included within the governmental activities of the government-wide financial statements are the San Francisco County Transportation Authority and San Francisco Finance Corporation. Included within the business-type activities of the government-wide financial statements is the operation of the San Francisco Parking Authority. Although legally separate from the City, these component units are blended with the primary government because of their governance or financial relationships to the City.

Fund Financial Statements

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

Governmental funds. Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements - i.e. most of the City's basic services are reported in governmental funds. These statements, however, focus on (1) how cash and other financial assets can readily be converted to available resources and (2) the balances left at year-end that are available for spending. Such information may be useful in determining what financial resources are available in the near future to finance the City's programs.

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

The City maintains several individual governmental funds organized according to their type (special revenue, debt service, capital projects and permanent funds). Information is presented separately in the governmental funds balance sheet and in the governmental funds statement of revenues, expenditures, and changes in fund balances for the General Fund, which is considered to be a major fund. Data from the remaining governmental funds are combined into a single, aggregated presentation. Individual fund data for each of the non-major governmental funds is provided in the form of combining statements elsewhere in this report.

The City adopts an annually appropriated budget for its General Fund. A budgetary comparison statement has been provided for the General Fund to demonstrate compliance with this budget.

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

- **Enterprise funds** are used to report the same functions presented as business-type activities in the government-wide financial statements. The City uses enterprise funds to account for the operations of the San Francisco International Airport (SFO or Airport), Port of San Francisco (Port), San Francisco Water Enterprise (Water), Hetch Hetchy Water and Power (Hetch Hetchy), Municipal Transportation Agency (MTA), Laguna Honda Hospital, San Francisco General Hospital Medical Center, and the San Francisco Wastewater Enterprise (Wastewater), all of which are considered to be major funds of the City.
- **Internal Service funds** are used to report activities that provide supplies and services for certain City programs and activities. The City uses internal service funds to account for its fleet of vehicles, management information services, printing and mail services, and for lease-purchases of equipment by the San Francisco Finance Corporation. Because these services predominantly benefit governmental rather than business-type functions, they have been included within governmental activities in the government-wide financial statements. The internal service funds are combined into a single, aggregated presentation in the proprietary fund financial statements. Individual fund data for the internal service funds is provided in the form of combining statements elsewhere in this report.

Fiduciary funds. Fiduciary funds are used to account for resources held for the benefit of parties outside the City. The City employees' pension and health plans, the external portion of the Treasurer's Office investment pool, and the agency funds are reported under the fiduciary funds. Since the resources of these funds are not available to support the City's own programs, they are not reflected in the government-wide financial statements. The accounting used for fiduciary funds is much like that used for proprietary funds.

Notes to the Basic Financial Statements

The notes to the basic financial statements provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements.

Required Supplementary Information

In addition to the basic financial statements and accompanying notes, this report presents certain required supplementary information concerning the City's progress in funding its obligation to provide pension and other postemployment benefits to its employees.

Combining Statements and Schedules

The combining statements and schedules referred to earlier in connection with non-major governmental funds, internal service funds, and fiduciary funds are presented immediately following the required supplementary information on pensions and other postemployment benefits.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

Net Assets June 30, 2009 (In thousands)

	Governmental activities		Business-type activities		Total	
	2009	2008	2009	2008 *	2009	2008 *
Assets:						
Current and other assets.....	\$ 1,982,121	\$ 1,905,426	\$ 2,106,943	\$ 2,109,649	\$ 4,089,064	\$ 4,015,075
Capital assets.....	3,028,915	2,931,077	9,460,894	9,148,394	12,489,809	12,079,471
Total assets.....	<u>5,011,036</u>	<u>4,836,503</u>	<u>11,567,837</u>	<u>11,258,043</u>	<u>16,578,873</u>	<u>16,094,546</u>
Liabilities:						
Noncurrent liabilities outstanding...	2,750,324	2,324,641	5,558,722	5,558,339	8,309,046	7,882,980
Other liabilities.....	955,509	926,806	1,248,969	851,355	2,204,478	1,778,161
Total liabilities.....	<u>3,705,833</u>	<u>3,251,447</u>	<u>6,807,691</u>	<u>6,409,694</u>	<u>10,513,524</u>	<u>9,661,141</u>
Net assets:						
Invested in capital assets, net of related debt **.....	1,725,203	1,436,842	4,017,577	3,935,008	5,443,483	5,371,850
Restricted.....	371,831	410,111	415,237	421,904	787,068	832,015
Unrestricted (deficit) **.....	<u>(791,831)</u>	<u>(261,897)</u>	<u>327,332</u>	<u>491,437</u>	<u>(165,202)</u>	<u>229,540</u>
Total net assets.....	<u>\$ 1,305,203</u>	<u>\$ 1,585,056</u>	<u>\$ 4,760,146</u>	<u>\$ 4,848,349</u>	<u>\$ 6,065,349</u>	<u>\$ 6,433,405</u>

* The 2008 ending balances in the table above have not been restated as discussed in Note 2(t) to the basic financial statements.

** In accordance with GASB implementation guidance, the City reclassified \$299.3 million of total net assets from invested in capital assets, net of related debt to unrestricted to reflect the primary government as a whole perspective.

Analysis of Net Assets

Net assets may serve as a useful indicator of the government's financial position. At the end of fiscal year 2008-2009, the City's total net assets exceeded liabilities by \$6.07 billion.

The largest portion of the net assets reflects the City's \$5.4 billion investment in capital assets (e.g. land, buildings, and equipment) less any outstanding debt related to the acquisition of these assets. This is 89.8 percent of the City's total net assets, a 1.3 percent increase over the prior year, and is largely due to growth in net capital assets with the governmental activities as well as at the Laguna Honda Hospital, Hetch Hetchy, and Water, which are business-type activities of the City. Since the government uses capital assets to provide services, these assets are not available for future spending. Further, the resources required to pay the debt related to these assets must come from other sources since the capital assets themselves cannot be liquidated to pay that liability.

Another portion of the City's net assets, \$787.1 million (13.0 percent) represents restricted resources that are subject to external limitations regarding their use. The governmental activities have a \$791.8 million deficit in the unrestricted net asset component, due to an overall increase in expenses over revenues as well as the continual recognition of other postemployment benefit expense, in conformance and compliance with GASB Statement No. 45 requirements. Also contributing to the governmental activities deficit unrestricted net assets is \$299.3 million of long-term bonds used for the purpose of rebuilding and improving Laguna Honda Hospital (see Note 2 (k)). The business-type activities reported positive balances in all categories of net assets at the end of this fiscal year.

Changes in Net Assets
Year Ended June 30, 2009
(In thousands)

	Governmental activities		Business-type activities		Total	
	2009	2008	2009	2008	2009	2008
Revenues						
Program revenues:						
Charges for services.....	\$ 392,411	\$ 461,625	\$ 2,034,298	\$ 1,973,961	\$ 2,426,709	\$ 2,435,586
Operating grants and contributions.....	909,695	926,089	186,776	181,725	1,096,471	1,107,814
Capital grants and contributions.....	44,048	36,079	87,253	152,511	131,301	188,590
General revenues:						
Property taxes.....	1,302,071	1,189,511	-	-	1,302,071	1,189,511
Business taxes.....	388,653	396,025	-	-	388,653	396,025
Sales and use tax.....	172,794	190,967	-	-	172,794	190,967
Hotel room tax.....	214,460	219,089	-	-	214,460	219,089
Utility users tax.....	89,801	86,964	-	-	89,801	86,964
Other local taxes.....	126,017	155,951	-	-	126,017	155,951
Interest and investment income.....	35,434	57,929	49,691	67,217	85,125	125,146
Other.....	44,086	25,939	201,624	233,244	245,710	259,183
Total revenues.....	<u>3,719,470</u>	<u>3,746,168</u>	<u>2,559,642</u>	<u>2,608,658</u>	<u>6,279,112</u>	<u>6,354,826</u>
Expenses						
Public protection.....	1,109,311	1,020,457	-	-	1,109,311	1,020,457
Public works, transportation and commerce.....	254,955	342,411	-	-	254,955	342,411
Human welfare and neighborhood development.....	908,449	848,195	-	-	908,449	848,195
Community health.....	608,733	567,410	-	-	608,733	567,410
Culture and recreation.....	319,994	347,433	-	-	319,994	347,433
General administration and finance.....	238,601	250,295	-	-	238,601	250,295
General City responsibilities.....	72,634	80,887	-	-	72,634	80,887
Unallocated Interest on long-term debt.....	93,387	97,694	-	-	93,387	97,694
Airport.....	-	-	683,335	651,581	683,335	651,581
Transportation.....	-	-	863,218	830,411	863,218	830,411
Port.....	-	-	71,778	67,495	71,778	67,495
Water.....	-	-	277,162	252,802	277,162	252,802
Power.....	-	-	96,228	109,436	96,228	109,436
Hospitals.....	-	-	820,236	812,399	820,236	812,399
Sewer.....	-	-	184,977	182,712	184,977	182,712
Market.....	-	-	1,144	1,052	1,144	1,052
Total expenses.....	<u>3,606,064</u>	<u>3,554,782</u>	<u>2,998,078</u>	<u>2,907,888</u>	<u>6,604,142</u>	<u>6,462,670</u>
Increase/(decrease) in net assets before special items and transfers....	<u>113,406</u>	<u>191,386</u>	<u>(438,436)</u>	<u>(299,230)</u>	<u>(325,030)</u>	<u>(107,844)</u>
Special items.....	-	-	-	(41,026)	-	(41,026)
Transfers.....	<u>(393,259)</u>	<u>(477,341)</u>	<u>393,259</u>	<u>477,341</u>	-	-
Change in net assets.....	<u>(279,853)</u>	<u>(285,955)</u>	<u>(45,177)</u>	<u>137,085</u>	<u>(325,030)</u>	<u>(148,870)</u>
Net assets at beginning of year, as restated..	<u>1,585,056</u>	<u>1,871,011</u>	<u>4,805,323</u>	<u>4,711,264</u>	<u>6,390,379</u>	<u>6,582,275</u>
Net assets at end of year.....	<u>\$ 1,305,203</u>	<u>\$ 1,585,056</u>	<u>\$ 4,760,146</u>	<u>\$ 4,848,349</u>	<u>\$ 6,065,349</u>	<u>\$ 6,433,405</u>

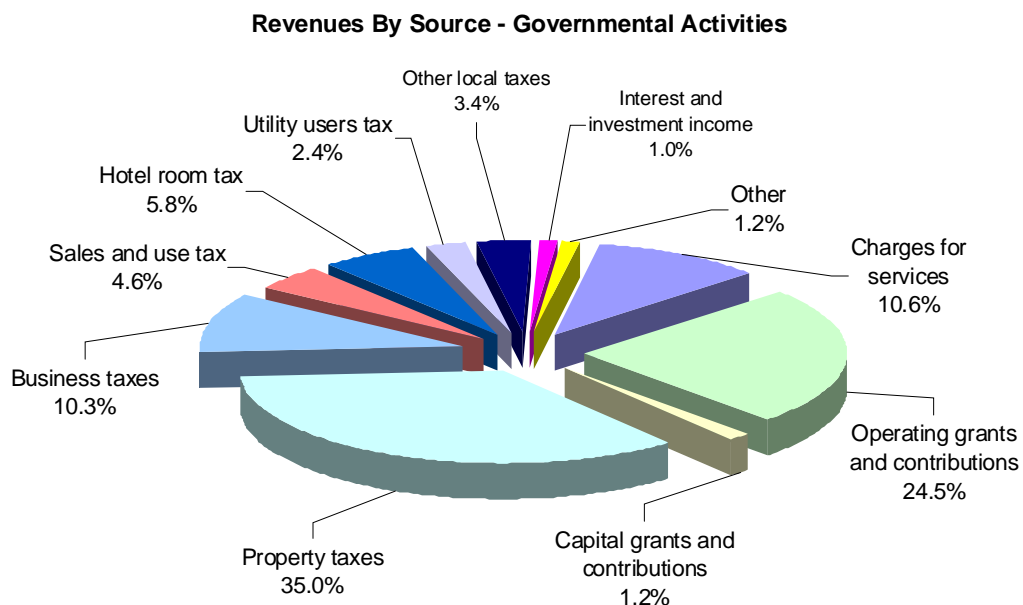
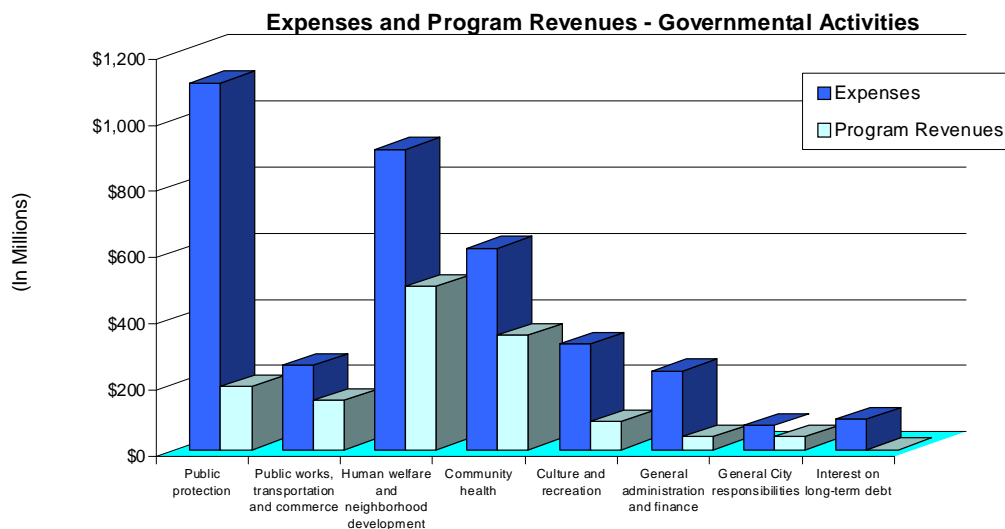
* The 2008 ending balances in the table above have not been restated as discussed in Note 2 to the basic financial statements.

Analysis of Changes in Net Assets

The City's total net assets decreased by \$325.0 million during fiscal year 2008-2009. Both the governmental and business-type activities realized net asset decreases of \$279.9 million and \$45.2 million, respectively. Within the business-type activities, Laguna Honda reported a major growth in net assets of \$77.0 million mainly due to the capital asset transfers funded with governmental resources.

In addition, Water, Wastewater, Hetch Hetchy and Market Corporation also reported a combined growth of \$51.4 million increase in net assets due to these funds managing their decreasing revenues against their expenses. These increases are offset by the combined decrease of net assets of \$173.5 million from the remaining enterprises, including MTA, Airport, Port and General Hospital.

The City's governmental-type activities experienced a \$26.7 million or 0.7 percent decline in total revenues. Despite the \$112.6 million growth in property tax and \$8.0 million in capital grants and contributions and a combined growth of \$21.0 million in utility user taxes and other revenues, there was a general decline in remaining revenue sources that range from \$7.4 million in business taxes to \$69.2 million in charges for services. The City's governmental activities expenses also increased moderately by \$51.3 million or 1.4 percent this fiscal year, which contributed to the gap between public expenses and revenues. A discussion of these and other changes is presented in the governmental activities and business-type activities sections that follow.



Governmental activities. Governmental activities decreased the City's total net assets by approximately \$279.9 million. Key factors contributing to this year's change are discussed below.

Overall, total revenues from governmental activities were \$3.72 billion, a \$26.7 million or 0.7 percent decrease over the prior year. For the same period, expenses totaled \$3.61 billion before transfers of \$393.3 million, resulting in a total net asset decrease of \$279.9 million by June 30, 2009.

Property tax revenue grew significantly by \$112.6 million or 9.5 percent primarily due to a growth in assessed valuation in the current fiscal year over prior fiscal year. Business taxes decreased by \$7.4 million or 1.9 percent. Revenues from hotel, sales, utility users and other local taxes totaled approximately \$603.1 million, a \$49.9 million decrease over the prior year. Of this, property transfer tax (part of other local taxes) decreased by \$37.3 million or 43.2% that reflected the depressed number and value of transactions for the City for the fiscal year. Sales and use tax decreased by \$18.2 million or 9.5%, hotel room tax by \$4.6 million or 2.1% and parking tax (part of other local taxes) by \$2.7 million or 4.1%. The Access Line Tax of \$10 million approved by voters in November 2008 that replaced the Emergency Response Fee helped to improve the revenue shortfall in the other local taxes. In general, the decreases in other local taxes correlated with declined business and tourist activities as well as the increased unemployment rate caused by the global credit crunch and weak economy.

Total charges for services revenues dropped this year by \$69.2 million, or 15.0 percent. Of this amount, \$50.1 million was the decline of development impact fees due to a downturn in the economy that negatively affected development and construction activities and sale of housing units. The remaining decreases reflected a general decline in governmental fee-based services including building safety charges, building permits, ambulance billings and others.

Interest and investment income revenue was down by \$22.5 million, 38.8 percent, due to declining interest rates on the City's pooled investments from the gross annual 4.3 percent to 2.6 percent and lower daily cash balances caused by delays in state grant and subvention payments during the fiscal year. In general, these returns reflect the City's concentration of investments in Treasury Bills and Notes and other government agencies short-term investments. As interest rates fell and stayed low for short term investments, the Portfolio included investments with longer maturities that had higher interest yields. As of June 30, 2009, 45.7% of the pooled investment will mature within 1 year compared to the 71.1% last fiscal year. Also, the portfolio now holds Temporary Liquidity Guarantee Program bonds, which are corporate bonds backed by the Federal Deposit Insurance Corporation and the U.S. government. At the end of the fiscal year, deposits and investments for governmental activities with the City Treasury were \$984.3 million, a 15.3 percent decrease over the prior year.

Revenues from capital grants and contributions totaled \$44.0 million this year compared to \$36.1 million last year. This \$7.9 million, or 22.1 percent increase was mainly for streets, roads and library improvement projects.

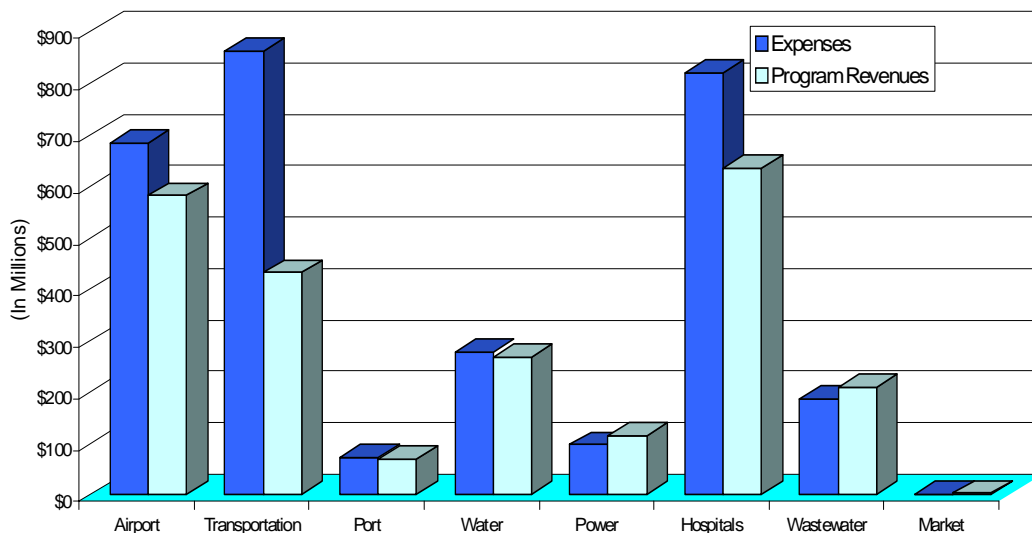
Net transfers to business-type activities were \$393.3 million, a 17.6 percent or \$84.1 million decrease over the prior fiscal year. The total General Fund transfers to MTA, General Hospital and Laguna Honda remains at about the same level of \$402 million this fiscal year. Yet, both General Hospital and Laguna Honda reimbursed the General Fund for a total of approximately \$50.9 million of capital expenditures related to the hospital rebuild projects paid in prior years. In addition, the transfers from the San Francisco County Transportation Authority to MTA were reduced by \$24.8 million and the City Facilities Improvement Funds to Laguna Honda for the hospital rebuild were reduced by approximately \$8.7 million.

The increase in total governmental expenses of \$51.3 million or 1.4% was primarily due to increases in demand for the government's services, salaries related expenses, including other postemployment benefits, and claims against the City. Major components of the increase include approximately \$60.3 million increases in the human welfare and neighborhood services functions due to growth in increased aid programs, social services contracts and various community based organization services. Community health expenses also grew by \$41.3 million due to higher levels of health services that were provided. The majority of the growth in public protection services is offset by a similar amount in the

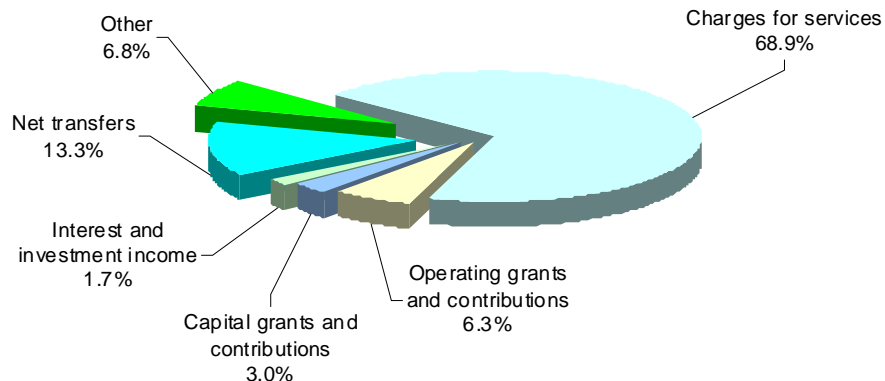
decline in public works, transportation and commerce since the Emergency Communications Department has been reclassified to the public protection function from the public works, transportation and commerce function in the last fiscal year. This reclassification is to better reflect the nature of services provided by the department. These overall increases in expenses are partially offset by decreases of \$27.4 million, \$11.7 million, and \$8.3 million in the functions of culture and recreation, general administration and general city responsibilities expenses, respectively, due to a combination of decreases in administrative costs and decreased elections and related expenses as compared to last year.

The charts on the previous page illustrate expenses and program revenues by functional area, and all revenues by source. As shown, public protection is the largest function (30.8 percent), followed by human welfare and neighborhood development (25.2 percent) and community health (16.9 percent). General revenues are not shown by program or function because they are used to support activities citywide. The distribution of these revenues shows property tax (35.0 percent) as the single largest funding source, followed by operating grants and contributions (24.5 percent), charges for services (10.6 percent), and business taxes (10.4 percent). This relative ranking is equivalent to the prior fiscal year and the actual percentage distributions showed only small differences.

Expenses and Program Revenues - Business-type Activities



Revenues By Source and Net Transfers - Business-type Activities



Business-type activities. Business-type activities decreased the City's net assets by \$45.2 million. Key factors contributing to this decline are:

- The Municipal Transportation Agency (MTA) had net assets of \$1.83 billion at the end of this fiscal year, a \$73.7 million decrease for the period. The City's municipal railway, MUNI, accounts for 97.6 percent or \$1.79 billion of these net assets. The remainder represents the combined net assets of the Department of Parking and Traffic and the Parking Authority. MUNI's net assets decreased by \$70.9 million this fiscal year compared to an increase of \$14.3 million the prior fiscal year. This year's change was based on \$668.0 million in total revenues and net transfers versus \$738.7 million in total expenses. Net transfers increased by \$23.2 million and operating and non-operating revenues grew by about \$1.7 million. The latter reflects modest increases in passenger fare, advertising rental and other revenues. At the same time, the railway saw a \$74.8 million decrease in federal and state capital contributions and a \$35.2 million increase in total expenses. Within this, salary and fringe benefit expense, including the cost of other post-employment benefits, increased by \$21.3 million and the cost of service from other City departments rose by \$13.6 million. The remaining expense increase is due to a small net increase in depreciation, contractual services, and administrative expenses. This year, the City's General Fund total subsidy to MTA was \$229.7 million. Of this, \$180.8 million went to MUNI and \$48.9 million went to the Department of Parking and Traffic. This was a \$26.2 million increase and a \$0.7 million decrease, respectively, for each entity over the prior year.
- Laguna Honda Hospital, the City's skilled nursing care hospital, increased net assets by \$77.0 million or 20.1 percent this year, reflecting continued progress on construction of the new hospital complex. This increase is primarily related to \$97.6 million of transfers from the non-major governmental funds for the hospital's capital activities, which are supported by general obligation bonds and certificates of participation. The increase is partially offset by a transfer of \$25.9 from Laguna Honda Hospital to the General Fund to reimburse the General Fund for certain hospital capital asset expenditures. Laguna Honda Hospital also received a \$55.5 million subsidy from the General Fund offset by \$47.9 million in losses this year as compared to a \$49.8 million in losses in the prior year.
- General Hospital, the City's acute care hospital had a decrease in net assets of \$58.0 million, which resulted in a net deficit of \$16.1 million at June 30, 2009. The decrease was partially the result of a smaller operating subsidy from the General Fund that was \$19.1 million less than the prior year. General Hospital also transferred \$25.0 million to the General Fund to reimburse capital activities related to the General Hospital rebuild project that were previously paid by the General Fund.
- Hetch Hetchy operates San Francisco's water storage and power generating facilities in the Sierra Nevada Mountains. Its total net assets were \$444.4 million at the end of fiscal year 2009, a \$23.2 million increase over the prior year when a \$14.7 million decrease was reported. That decrease consisted of a \$26.5 increase in net assets from operating and non-operating revenue and expenses offset by a \$41.2 million one-time write-off of a turbine project. This year, Hetch Hetchy's operating expenses fell by \$13.2 million due to a \$10.1 million decrease in the cost of purchased power from the Western System Power Pool and a \$13.7 million decrease in claims liability expenses. These were offset by increases of \$4.3 million in personnel costs, \$4.1 million in contractual service costs, \$2.2 million for San Francisco's new Go-Solar incentive program as well as increases in depreciation and other expenses equaling about \$2.1 million. Total revenues for this year were \$122.1 million, a decrease of \$14.4 million since last year. This includes a \$6.6 million decrease in revenues from electricity sales to Modesto and Turlock Irrigation Districts and other municipalities; a \$2.6 million decrease in revenue from TIDA, a \$2.6 million increase in sales to City departments, and a \$2.1 million increase in water assessment fees to the San Francisco Water Enterprise and others. This year's total revenue decrease also included an approximately \$12.1 million decline in non-operating revenue primarily due to \$7.6 million one-time refunds and reimbursements in the prior year, and about a \$2.3 million fall in investment and interest income in fiscal year 2009 due to lower interest rates.

- The City's Water Enterprise reported net assets of \$462.3 million, a \$1.0 million or 0.2 percent increase over the prior year. The enterprise is engaged in a massive, multi-billion dollar, ten-year project to rebuild the City's water system know as the Water System Improvement Program (WSIP). Directly related to this effort, the enterprise's total assets and total liabilities increased by \$243.8 million and \$242.8 million, respectively. Within this, net capital assets rose by \$233.3 million and current assets increased by \$11.1 million, including a \$13.7 million total increase in receivables from suburban customers and approximately \$4.7 million increase in receivables from mainly other City retail ratepayers, offset by a \$7.8 million decrease in cash balances due to a decline in interest earnings and increases in operating expenses. Liabilities show an increase of \$229.6 million in commercial paper associated with WSIP, a reduction of \$25.3 million in bond principal repayment, approximately \$20.0 million increase in accounts payable for capital projects, and the WSIP program; \$15.9 increase in the liability for other postemployment benefit expenses, and \$4.3 million in arbitrage payable expense, and a net reduction of about \$1.3 million in claims and other current liabilities.
- The City's Wastewater Enterprise had net assets of \$1.01 billion at the end of this fiscal year, a \$26.7 million or 2.7 percent increase for the fiscal year. The enterprise reported total revenues of \$211.7 million, a \$4.2 million increase over the prior year. This included an \$11.5 million increase in charges for service due to a 9.0% rate increase on July 1, 2008. That was partially offset by a decline of \$5.4 million in capacity fee revenues related to a drop in building permits, and a decrease of \$1.9 million in interest and other income, reflecting the drop in interest rates during the period. Total expenses were about \$185.0 million, a \$2.3 million increase over the prior year. This included an increase of \$5.6 million for services of other departments, particularly the City's Department of Public Works for sewer repair, street cleaning and engineering work. Concurrently, contractual service expense increased \$1.9 million, material and supplies declined by \$3.8 million, interest and other expenses fell by a net of \$1.7 million.
- The Port had an increase in net assets of \$2.5 million from its current year activities, however the ending net assets decreased by a total of \$40.6 million due to prior year restatements, which resulted from a prior year adjustment for fixed assets of \$15.5 million and a restatement due to recognizing a pollution remediation cost of \$27.5 million in accordance with GASB Statement No. 49.
- The Airport's net assets decreased by \$44.0 million or 14.0 percent from the prior year. The decrease is primarily the result of increased operating expenses over last year of \$27.3 million and a decrease in nonoperating revenues of \$12.2 million and an increase in nonoperating expenses of \$4.4 million and a decreased federal capital contribution of \$11.3 million. The main reasons for the increase in operating expenses was higher personnel costs of \$14.3 million due to base wage increases and other postemployment benefits, and increased depreciation expense of \$7.1 million due to additional capital assets placed in service and additional contractual services of \$3.3 million for marketing and other services. In addition, repairs and maintenance increased by \$1.7 million. Although operating revenues grew by \$15.5 million or 2.9% driven largely by increased aviation revenues, concession and parking and transportation revenue, it was not enough to offset the combined effect of the aforementioned increases in operating expenses and the decreases in nonoperating revenues mostly due to lower interest and other earnings, and the increase in interest expense. Finally, the transfer from the Airport to the City's General Fund was \$26.8 million this year, a 3.5 percent growth over fiscal year 2007-2008.

FINANCIAL ANALYSIS OF THE CITY'S FUNDS

As noted earlier, the City uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental Funds

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

At the end of the current fiscal year, the City reported combined ending governmental fund balances of \$985.0 million, an increase of \$13.3 million over the prior year. The City realized growth in total governmental funds revenues, including growth in property tax revenues, federal and state revenues for a total of \$141.9 million. These increases were offset by a decline in the rest of other taxes, such as business, hotel room tax, other local taxes, as well as interest and investment income as discussed earlier, leaving a net increase of \$8.2 million in revenues for the fiscal year.

The governmental funds have a combined deficit of \$63.5 million in the unrestricted fund balance component. Of the \$63.5 million deficit, \$95.6 million was from Special Revenue and Capital Projects funds. The remainder of the fund balances in governmental funds is reserved, a measure of the fund resources already committed and not available for new spending. These commitments include support for (1) a General Fund "rainy day" reserve (\$98.3 million), (2) encumbrances for existing contracts and purchase orders (\$233.1 million), (3) funds continued for programs or projects in future fiscal years (\$610.2 million), (4) funds reserved for future debt service payments (\$75.9 million), and (5) assets not available for appropriation (\$31.1 million).

The General Fund is the chief operating fund of the City and had an unreserved fund balance of \$28.2 million and a total fund balance of \$301.7 million at the end of the fiscal year. For the year, the General Fund's total revenues exceeded expenditures by \$306.6 million, before transfers and other items of \$410.6 million. In the aggregate, the resulting total fund balance decreased by \$104.0 million for the fiscal year ended June 30, 2009. Overall, this was due to smaller than expected increase in revenues, particularly in real estate property transfer tax, grants and subventions, and an increased rate of expenditure growth due to growth in demand for services and personnel costs across City functions. These factors were partly offset by management controls on the General Fund expenditures put in place during the middle of this fiscal year.

As a measure of the General Fund's liquidity, it may be useful to compare both unreserved fund balance and total fund balance to total fund expenditures. For this fiscal year, the unreserved fund balance of \$28.2 million represents 1.17 percent of total General Fund expenditures of \$2.4 billion, and the total fund balance of \$301.7 million represents essentially 12.5 percent of that amount. At the end of the prior fiscal year, the General Fund's unreserved fund balance of \$77.1 million was 3.2 percent of total expenditures of \$2.39 billion, and the total fund balance represented approximately 17.0 percent of expenditure. This change also reflects the City's relatively higher use of budgetary use of balances and reserves in fiscal 2008-2009 due to the weak economy of the City.

Proprietary Funds

The City's proprietary fund statements provide the same type of information found in the business-activities section of the government-wide financial statements, but in more details.

At the end of the current fiscal year, the unrestricted net assets for the Airport were \$226.3 million, the Water Enterprise \$83.9 million, the Hetch Hetchy Water and Power were \$170.7 million, the Wastewater Enterprise Program were \$26.3 million, and the Port were \$31.7 million. In addition, the MTA, the San Francisco General Hospital and Laguna Honda Hospital had deficits in unrestricted net assets of \$106.5 million, \$67.5 million and \$42.2 million, respectively.

The following table shows actual revenues, expenses and results of operations for the current fiscal year in the City's proprietary funds (in thousands). As seen here, the total net assets for these funds decreased by approximately \$45.2 million due to current year operations. Reasons for this change are discussed in the previous section on the City's business-type activities.

	Operating Revenues	Operating Expenses	Operating Income (Loss)	Non-Operating Revenues (Expense)	Capital Contributions and Others	Interfund Transfers	Change In Net Assets
Airport.....	\$ 551,283	\$ 478,589	\$ 72,694	\$ (119,634)	\$ 29,780	\$ (26,849)	\$ (44,009)
Water.....	265,781	248,315	17,466	(15,356)	-	(1,143)	967
Hetch Hetchy.....	115,274	96,228	19,046	4,477	-	(302)	23,221
Municipal Transportation Agency.....	257,083	860,471	(603,388)	235,572	55,915	237,882	(74,019)
General Hospital.....	448,881	628,387	(179,506)	66,365	-	55,155	(57,986)
Wastewater Enterprise.....	208,654	169,300	39,354	(12,663)	-	-	26,691
Port.....	66,467	71,234	(4,767)	2,037	1,558	3,644	2,472
Laguna Honda Hospital.....	119,329	191,266	(71,937)	24,034	-	124,872	76,969
Market Corporation.....	1,546	1,144	402	115	-	-	517
Total.....	<u>\$ 2,034,298</u>	<u>\$ 2,744,934</u>	<u>\$ (710,636)</u>	<u>\$ 184,947</u>	<u>\$ 87,253</u>	<u>\$ 393,259</u>	<u>\$ (45,177)</u>

Fiduciary Funds

The City maintains fiduciary funds for the assets of the San Francisco Employee's Retirement System and Health Service System, and manages the investment of monies held in trust to benefit public service employees. At the end of the current fiscal year, the net assets of the Retirement System and Health Services System combined totaled \$11.9 billion, representing a \$3.96 billion decrease over the prior year, a 24.9 percent change. This decrease is essentially due to a decrease in the fair value of the Retirement System's investments resulting from a decline in financial and real estate market conditions. The Investment Trust Fund's net assets were \$565.4 million at year's end, compared to \$538.4 million at the end of the previous fiscal year. This 5.0 percent increase represents the increase in additions over withdrawals or distributions to external participants in the current year.

General Fund Budgetary Highlights

The City's final budget differs from the original budget in that it contains carry-forward appropriations for various programs and projects, and supplemental appropriations approved during the fiscal year. In fiscal year 2008-2009, the City approved approximately \$3.3 million in General Fund supplemental appropriations with additional state revenues associated with the November 2008 and May 2009 elections.

During the year, actual revenues and other resources were \$162.2 million less than budgeted. The City realized \$9.5 million more revenue than budgeted in property taxes and utility users taxes. There was a total of \$171.7 million shortfall of actual revenue compared to budgeted revenue in other categories, namely, business taxes, other local taxes, licenses permits and franchises, fines forfeitures and penalties, rents and concessions, federal, state and other grants and subventions, charges for services, and other resources.

Differences between the final budget and the actual (budgetary basis) expenditures resulted in \$128.9 million in expenditure savings. Major factors include:

- \$31.4 million savings in the Human Services Agency, due largely to lower than budgeted client assistance and aid as well as other operating costs. These savings are partially offset by reductions in Human Service federal and state subvention revenues.
- \$22.2 million savings in Fire, Police, Juvenile Probation and Sheriff departments achieved through delayed or freezing certain civilian and uniform positions.
- \$28.0 million in savings due to close-out of unspent General Reserve not used for supplemental appropriation or other contingencies during fiscal year 2008-2009.
- \$20.3 million in savings on general administration and finance and other general city responsibilities.
- \$14.1 million in savings in salary and fringe benefit costs in the Department of Public Health. In addition, the General Services Agency – Department of Public Works and Business and Economic Development had a combined savings of \$7.5 million primarily from capital projects and some City grant programs.

The net effect of revenue shortfall, savings in expenditures and reduction in appropriations and reserve balances was a positive unreserved budgetary fund balance available for subsequent year appropriation of \$95.4 million at the end of fiscal year 2008-2009. The City's fiscal year 2009-2010 Adopted Original Budget assumed an available balance of \$94.5 million, so an additional \$0.9 million remains available. (See also Note 4 to the Basic Financial Statements for additional fund balance details.)

Capital Assets and Debt Administration

Capital Assets

The City's capital assets for its governmental and business-type activities as of June 30, 2009, increased by \$410.3 million, 3.4 percent, to \$12.49 billion (net of accumulated depreciation). Capital assets include land, buildings and improvements, machinery and equipment, park facilities, roads, streets, and bridges. Governmental activities contributed \$97.8 million or 0.8 percent to this total while \$312.5 million or 2.5 percent was from business-type activities. Details are shown in the table below.

**Capital Assets, Net of Accumulated Depreciation
(in thousands)**

	Governmental Activities		Business-type Activities		Total	
	2009	2008	2009	2008 *	2009	2008 *
Land.....	\$ 155,512	\$ 151,917	\$ 180,919	\$ 196,264	\$ 336,431	\$ 348,181
Facilities and Improvement..	2,337,478	2,188,543	6,306,617	6,114,993	8,644,095	8,303,536
Machinery and equipment....	58,648	60,701	785,888	780,793	844,536	841,494
Infrastructure.....	290,144	281,329	793,866	794,180	1,084,010	1,075,509
Property held under lease....	-	-	2,218	2,464	2,218	2,464
Easements.....	-	-	62,694	65,448	62,694	65,448
Construction in progress.....	187,133	248,587	1,328,692	1,194,252	1,515,825	1,442,839
Total.....	\$ 3,028,915	\$ 2,931,077	\$ 9,460,894	\$ 9,148,394	\$ 12,489,809	\$ 12,079,471

* The 2008 ending balances in the table above have not been restated as discussed in Note 2 to the basic financial statements.

Major capital asset events during the current fiscal year included the following:

- Under governmental activities, net capital assets increased by \$97.8 million mainly due to the increase in construction in progress and completed assets at various park and recreational sites, branch libraries, various street improvement and traffic signal upgrades. About \$226.0 million worth of construction-in-progress work was substantially completed and capitalized as facilities and improvement and infrastructure. Of the completed projects, \$119.9 million is for the California Academy of Science and approximately \$56.8 million for various Recreation Centers such as Duboce Park, Larsen Sava Pool and J.P. Murphy Clubhouse and \$46.6 million in various street and public work projects. Apart from the increase in various city-wide parks, libraries, public works and traffic signal projects, the City also funded the General Hospital Rebuild Project with general obligation bonds proceeds issued in the fiscal year. The rebuild project for the fiscal year totaled \$39.6 million and was recorded under the governmental activities.
- The Water Enterprise's net capital assets increased by \$233.3 million or 18.4 percent. Close to 53.3 percent, or \$124.2 million, of the change reflects the net increase in construction-in-progress on the enterprise's ten-year capital plan, including the Water System Improvement Program. This change includes a \$282.7 million increase in construction projects offset by \$138.8 million in transfers to facilities and improvements, \$14.5 million transfers to equipment, and \$5.2 million expensed for projects not continued. Major additions to construction work included Tesla Treatment Facility, McLaren Park Pump Station Upgrade, New Crystal Springs Bypass Tunnel, Local Water Main Replacement Program and other Water System Improvement Program. The remaining net increase of \$48.8 million reflects the increase to facilities, improvements and equipment less increase to depreciation. The Water Enterprise had \$12.7 million in development costs and \$9.9 million in site acquisition as of June 30, 2009 for an office building located at 525 Golden Gate Avenue. Demolition of existing site was completed in June 2009. Construction is expected to start in January 2010 with an expected completion date of February 2012, with an expected occupancy date of April 2012.
- MTA's net capital assets decreased by \$36.3 million or 1.8 percent, compared to the previous year, which was attributed to a decline in construction work for new and existing projects and more depreciation expense for existing assets. Construction completion of the Muni Metro East Maintenance Facility occurred in the summer of 2008. The facility is a new, state-of-the-art storage yard, maintenance shop and operations/dispatch facility for a fleet of 80 light rail vehicles. The advanced preliminary engineering for Phase II of the Third Street Light Rail Project is near completion and is pending approval to enter into final design in fiscal year 2010.
- Laguna Honda Hospital's net capital assets increased by \$112.8 million or 35.4 percent due almost entirely to construction-in-progress on the capital project to rebuild the hospital. This work is principally funded by the Laguna Honda General Obligation Bonds and the Certificates of Participation issued by the City.
- General Hospital's net capital assets decreased by \$13.5 million or 20.0 percent, primarily due to handing over the hospital rebuild project to the governmental activities for managing and financing with the first series of \$131.7 million general obligation bonds issued in the current fiscal year. The total amount approved by the voters for the rebuild project is \$887.4 million.
- The Wastewater Enterprise reported a net increase of \$34.1 million or 2.5 percent due to completion of the Southeast Water Pollution Control Program Digester Cover and Mixing Improvements, Oceanside Heating, Ventilation, Air conditioning assessment, North Point Facilities Wet Weather Improvements-Pumps, and other capital projects throughout the system.
- Hetch Hetchy net capital assets increased by \$14.3 million or 5.5 percent during the year. Contributing to this net increase was the addition in construction work in progress and in land and rights-of-way over depreciation and deletion of assets.

- The Airport's net capital assets decreased \$16.2 million or 0.5 percent largely due to depreciation and deletions of certain capital projects. Major capital additions this fiscal year included Terminal 2 Renovation, Secure Connector Terminal 3 to Boarding Area G, and Runway 28R-10L Overlay and Reconstruction.
- The Port's net capital assets decreased by \$16.3 million or 5.9 percent from its previously reported capital asset balance of \$275.1 million primarily due to a restatement of \$15.5 million on certain land improvements that had not been depreciated but determined to be exhaustible assets and should have been depreciated in prior periods and \$2.5 million of reclassification of other assets to capital assets.

At the end of the year, the City's business-type activities had approximately \$520.0 million in commitments for various capital projects. Of this, Water Enterprise had an estimated \$303.4 million, MTA had \$68.4 million, Wastewater had \$23.8 million, Airport had \$39.0 million, Hetch Hetchy had \$22.3 million, Port had \$7.2 million, Laguna Honda had \$53.7 million and the General Hospital had \$2.2 million. In addition, there was approximately \$58.2 million reserved for encumbrances in capital project funds for the general government.

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

For governmental activities, no net infrastructure assets were recorded in fiscal year 2000-2001 (the first year of presentation in the GASB 34 format), because the historical costs did not meet the threshold established by GASB. Beginning in fiscal year 2001-2002, newly completed projects are capitalized and ongoing infrastructure projects are accounted for in construction in progress.

Additional information about the City's capital assets can be found in Note 7 to the Basic Financial Statements.

Debt Administration

At the end of the current fiscal year, the City had total long-term and commercial paper debt outstanding of \$8.04 billion. Of this amount, \$1.17 billion is general obligation bonds backed by the full faith and credit of the City and \$6.87 billion is revenue bonds, loans, certificates of participation, capital leases, and other debt of the City secured solely by specified revenue sources.

As noted previously, the City's total long-term debt including all bonds, loans, commercial paper and capital leases increased by \$454.9 million during fiscal year 2008-2009, due to the issuance of new debt in the governmental and business-type activities. The net increase in obligations was \$221.6 million in governmental activities and was primarily due to issuance of new debt. For the business-type activities, the net increase in obligations was \$233.3 million primarily due to the issuance of commercial paper by the Airport, San Francisco Water Enterprise and San Francisco Wastewater Enterprise.

The City issued \$578.4 million in refunding bonds, with \$118.1 million in general obligation refunding bonds to take advantage of lower interest rates to reduce debt payments; \$145.3 million in lease revenue refunding bonds and \$314.9 million by the Airport in revenue refunding notes to stabilize variable interest expense set to reset to higher rates due to the downgrade of the bonds insurers caused by the turmoil in the financial markets. The Airport likewise converted the tax status of \$266.7 million of variable rate refunding bonds, from Alternative Minimum Tax (AMT) to Non-AMT to lower interest payments. In addition, the City issued \$131.7 million in general obligation bonds to finance the rebuilding and improve the earthquake safety of the San Francisco General Hospital and \$42.5 million to finance the construction and improvement of parks and recreational facilities in the City and made the fourth borrowing in the amount of \$1.3 million on the Seismic Safety Loan Program general obligation bonds under the Board of Supervisors Resolution No. 65-07 for loans to finance the seismic retrofitting of masonry buildings within the City. Lease revenue bonds for \$34.3 million were issued, through the San Francisco Finance

Corporation to finance the construction and renovation of public libraries and certificates of participation were issued for \$163.3 million for the construction and equipping of Laguna Honda Hospital. The San Francisco International Airport, San Francisco Water Enterprise and San Francisco Wastewater Enterprise issued commercial paper in the total amount of \$1.2 billion of which \$845.3 million was repaid. The Hetch Hetchy Water and Power Enterprise issued \$6.3 million in clean renewable energy bonds to finance the installation of solar energy equipment on selected City-owned facilities.

The City's Charter imposes a limit on the amount of general obligation bonds the City can have outstanding at any given time. That limit is three percent of the taxable assessed value of property in the City - approximately \$150 billion in value as of the close of the fiscal year. As of June 30, 2009, the City had \$1.17 billion in authorized, outstanding property tax-supported general obligation bonds, which is equal to approximately 0.75 percent of gross (0.78 percent of net) taxable assessed value of property. As of June 30, 2009, there were an additional \$1.2 billion in bonds that were authorized but unissued. If all of these general obligation bonds were issued and outstanding in full, the total debt burden would be approximately 1.52 percent of gross (1.58 percent of net) taxable assessed value of property.

The City's underlying ratings on general obligation bonds as of June 30, 2009 were:

Moody's Investors Service, Inc.	Aa2
Standard and Poor's	AA
Fitch Ratings	AA-

During the fiscal year, Moody's Investors Service upgraded the City's rating to Aa2 from Aa3 and revised the City's rating outlook from positive to stable, and Standard and Poor's affirmed rating with a stable outlook. Fitch Ratings affirmed ratings with their stable rating outlook on all the City's outstanding bonds.

The City's enterprise activities maintained their underlying debt ratings this fiscal year. The Airport's underlying bond ratings were affirmed by all rating agencies in conjunction with the issuance of their revenue refunding notes and the conversion of their variable rate refunding bonds to non-AMT. Moody's Investors Services, Standard & Poor's, and Fitch Ratings maintained their long-term rating of "A1", "A", and "A", respectively. The San Francisco Water Enterprise carried underlying ratings of "A1" and "AA-" from Moody's and Standard and Poor's, respectively. The San Francisco Waste Water Enterprise carried underlying ratings of "A2" and "A+" from Moody's and Standard & Poor's respectively.

Additional information in the City's long-term debt can be found in Note 8 to the Basic Financial Statements.

Economic factors and next year's budget and rates

The City, like the State, is faced with a set of financial challenges over the next few years. The following economic factors were considered in the City's fiscal year 2009-2010 budget.

- By the end of fiscal year 2008-2009, San Francisco's economy was weathering the State's recession relatively well compared to other Bay Area cities and regions throughout the State. The fundamental cause of the recession in California, as well as several other states in the United States, has been the downturn in the housing market. Housing prices across California have rapidly declined after more than a decade of double-digit annual appreciation.
- San Francisco's housing prices have fallen, although the rate of decline has been much lower than the state average. Between the second quarter of 2008 and the second quarter of 2009, housing prices in California have fallen by an average of 15.5 percent, whereas in the San Francisco metropolitan division they only fell by 8.1 percent during the same period¹.

¹ Source: Office of Federal Housing Enterprise Oversight Housing Price Index. The San Francisco Metropolitan Division includes San Francisco, San Mateo and Marin Counties.

- There is a fundamental difference in the City's housing market and those in the fast-growing suburban areas of the state. Consequently, San Francisco's economy has proven far more resilient than other parts of the state. While low mortgage rates certainly contributed to rising housing prices in San Francisco during the early years of the decade, the City has relatively few sub-prime mortgages, and its default rate on those mortgages has been far below the state average. During fiscal year 2008-2009, San Francisco recorded 1,424 Notices of Default, which was only 0.4 percent of the state total of 389,138². By contrast, San Francisco has approximately 2.2 percent of the state's population, suggesting a per capita default rate that was only one-sixth of the state average.
- The wage and salary employment base of San Francisco lost 16,999 jobs between March 2008 and March 2009, the latest data available³.
- Unemployment in San Francisco rose during fiscal year 2008-2009 to an annual average of 7.4 percent, up from 4.6 percent in 2007-2008. Nevertheless, this rate is significantly below the state average of 9.6 percent and further confirms the essential strength of the City's economy in the face of the state and national recession. San Francisco's June 2009 unemployment rate of 9.9 percent was the 8th lowest among California's 58 counties⁴.
- The office market struggled in fiscal year 2008-2009, with the vacancy rate climbing from 10.5 percent in the third quarter of 2008 to 15.2 percent in the second quarter of 2009. During the same period, office rental rates fell 30.4 percent to \$32.67 per square foot as of the second quarter of 2009⁵. In addition, the market experienced almost 1,325,000 square feet of negative net absorption during this time period. Despite falling commercial space under construction, fiscal year 2008-2009 saw the completion of a 33-story office tower at 555 Mission Street, the first high-rise office completed in San Francisco in five years.
- San Francisco's long-term economic fundamentals – the quality of its workforce, environment, technological base, and cultural amenities – are among the strongest of any city in the United States. These competitive advantages are likely to secure the City's continued prosperity during and after the economic recovery.

² Source: DataQuick.

³ Source: U.S. Bureau of Labor Statistics, Quarterly Census of Employment and Wages.

⁴ Source: State of California Employment Development Department (EDD).

⁵ Source: Grubb & Ellis.

REQUESTS FOR INFORMATION

This financial report is designed to provide our citizens, taxpayers, customers, and investors and creditors with a general overview of the City's finances and to demonstrate the City's accountability for the money it receives. Below are the contacts for questions about this report or requests for additional financial information.

City and County of San Francisco

Office of the Controller
1 Dr. Carlton B. Goodlett Place, Room 316
San Francisco, CA 94102-4694

Individual Department Financial Statements

San Francisco International Airport

Office of the Airport Deputy Director
Business and Finance Division
PO Box 8097
San Francisco, CA 94128

Port of San Francisco

Fiscal Officer
Pier 1, The Embarcadero
San Francisco, CA 94111

San Francisco Water Enterprise

Hetch Hetchy Water and Power
San Francisco Wastewater Enterprise
Director of Accounting Financial Services
1155 Market Street, 4th Floor
San Francisco, CA 94103

Laguna Honda Hospital

Chief Financial Officer
375 Laguna Honda Blvd.
San Francisco, CA 94116

Municipal Transportation Agency

MTA Finance and Administration
1 South Van Ness Avenue, 8th Floor
San Francisco, CA 94103

Health Service System

1145 Market Street, Suite 200
San Francisco, CA 94103

San Francisco General Hospital Medical Center

Chief Financial Officer
1001 Potrero Avenue, Suite 2A7
San Francisco, CA 94110

San Francisco Employees' Retirement System

Executive Director
30 Van Ness Avenue, Suite 3000
San Francisco, CA 94102

Component Unit Financial Statement

San Francisco Redevelopment Agency

One South Van Ness Avenue, 5th Floor
San Francisco, CA 94103

Blended Component Units Financial Statements

San Francisco County Transportation Authority

Deputy Director for Administration and Finance
100 Van Ness Avenue, 26th Floor
San Francisco, CA 94102

San Francisco Finance Corporation

Mayor's Office of Public Finance
City Hall, Room 336
1 Dr. Carlton B. Goodlett Place
San Francisco, CA 94102

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