

CITY AND COUNTY OF SAN FRANCISCO
Management's Discussion and Analysis (Continued)
Year ended June 30, 2010

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, 2010. We encourage readers to consider the information presented here in conjunction with additional information in our transmittal letter. Certain amounts presented as 2008-2009 summarized comparative financial information in the basic financial statements have been reclassified to conform to the presentation in the 2009-2010 basic financial statements.

FINANCIAL HIGHLIGHTS

The assets of the City exceeded its liabilities at the end of the fiscal year by approximately \$5.97 billion (net assets). Of this balance, \$5.70 billion represents the City's investment in capital assets net of related debt and \$647.5 million represents restricted net assets. This is offset by a deficit in unrestricted net assets of \$377.6 million. The City's total net assets decreased by \$96.5 million or 1.6 percent over the previous fiscal year. Of this amount, total capital assets net of related debt and restricted assets increased by \$113.0 million and were offset by a \$209.5 million decrease in unrestricted net assets. The decrease in unrestricted net assets is primarily due to recognition of \$239.5 million other postemployment benefit expense in the fiscal year.

The City's governmental funds reported total revenues of \$3.79 billion, a \$109.9 million or 3.0 percent increase over the prior year. Within this, revenues from property taxes, other local taxes, and intergovernmental grants grew by approximately \$59.6 million, \$68.1 million and \$55.4 million respectively. At the same time, there was a decline in revenues from charges for services, business taxes and hotel room taxes. Governmental funds expenditures totaled \$3.77 billion for this period, a \$121.4 million or 3.3 percent increase, reflecting increases in demand for governmental services of \$51.0 million, debt service payments of \$40.4 million and capital outlay of \$30.0 million.

At the end of the fiscal year, the City's General Fund unreserved fund balance decreased from the prior year's \$28.2 million by \$30.2 million to a deficit of \$2.0 million. The primary cause of this decrease was the increasing unavailable amounts from delays in cash receipts of state intergovernmental reimbursements.

The City's total long-term debt, including all bonds, loans, commercial paper and capital leases increased by \$2.06 billion during this fiscal year. The City issued a total of \$3.90 billion in debt this year. Of this amount, a total of \$355.1 million in general obligation bonds were issued for improvements for the San Francisco General Hospital and neighborhood parks. In addition, \$37.9 million in certificates of participation were issued for multiple street improvement projects. The San Francisco International Airport issued a total of \$1.72 billion Revenue Bonds. Of this, \$485.8 million was for renovation and other capital plans and \$1.23 billion was for bond refunding and restructuring of long-term debt to take advantage of lower interest rates. The San Francisco Water Enterprise issued \$1.31 billion in revenue bonds to retire commercial paper notes and certain outstanding revenue bonds, and to provide new money for capital projects of the massive Water System Improvement Program. The San Francisco Wastewater Enterprise issued \$239.6 million in revenue bonds to retire commercial paper notes and provide funding for Wastewater Enterprise capital improvement projects. The City issued \$167.7 million in Certificates of Participation to fund the construction of the future headquarters of the San Francisco Public Utilities Commission at 525 Golden Gate Avenue.

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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 revenues, expenditures, and changes in fund balances	Statement of revenues, expenses, and changes in fund net assets	Statement of changes in fiduciary net assets
		Statement of activities	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				

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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

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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.

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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.

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GOVERNMENT-WIDE FINANCIAL ANALYSIS

Net Assets
June 30, 2010
(in thousands)

	Governmental activities		Business-type activities		Total	
	2010	2009	2010	2009	2010	2009
Assets and deferred outflows:						
Current and other assets.....	\$ 2,165,396	\$ 1,982,121	\$ 3,638,011	\$ 2,106,943	\$ 5,803,407	\$ 4,089,064
Capital assets.....	3,177,822	3,028,915	10,056,170	9,460,894	13,233,992	12,489,809
Deferred outflows.....	-	-	89,505	57,157	89,505	57,157
Total assets and deferred outflows....	<u>5,343,218</u>	<u>5,011,036</u>	<u>13,783,686</u>	<u>11,624,994</u>	<u>19,126,904</u>	<u>16,636,030</u>
Liabilities:						
Current liabilities.....	1,087,991	955,509	1,139,045	1,248,969	2,227,036	2,204,478
Noncurrent liabilities	3,102,242	2,750,324	7,828,747	5,615,879	10,930,989	8,366,203
Total liabilities.....	<u>4,190,233</u>	<u>3,705,833</u>	<u>8,967,792</u>	<u>6,864,848</u>	<u>13,158,025</u>	<u>10,570,681</u>
Net assets:						
Invested in capital assets, net of related debt *.....	1,833,733	1,725,203	4,240,971	4,204,644	5,699,016	5,630,550
Restricted *.....	382,070	371,831	278,084	231,107	647,460	602,938
Unrestricted (deficit) *.....	(1,062,818)	(791,831)	296,839	324,395	(377,597)	(168,139)
Total net assets.....	<u>\$ 1,152,985</u>	<u>\$ 1,305,203</u>	<u>\$ 4,815,894</u>	<u>\$ 4,760,146</u>	<u>\$ 5,968,879</u>	<u>\$ 6,065,349</u>

* See note 2(k)

Analysis of Net Assets

Net assets may serve as a useful indicator of the government's financial position. As noted earlier, at the end of fiscal year 2009-2010, the City's total net assets exceeded liabilities by \$5.97 billion.

The largest portion of the net assets reflects the City's \$5.70 billion investment in capital assets (e.g. land, buildings, and equipment) less any outstanding debt related to the acquisition of these assets. This is 95.5 percent of the City's total net assets, a 1.2 percent increase over the prior year, and is largely due to growth in net capital assets in the governmental activities as well as at Laguna Honda Hospital, MTA and Port 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, \$647.5 million (10.9 percent) represents restricted resources that are subject to external limitations regarding their use. The governmental activities have a \$1.06 billion deficit in the unrestricted net assets component, due largely to an increase in transfers to business-type activities and the continual recognition of other postemployment benefit expense, in conformance with GASB Statement No. 45 requirements. Another contribution to the governmental activities deficit unrestricted net assets is a total of \$388.4 million of long-term bonds used for the rebuilding and improving Laguna Honda Hospital and to fund certain park facilities projects at the Port (see Note 2(k)). The business-type activities reported positive balances in all categories of net assets at the end of this fiscal year.

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Changes in Net Assets
Year Ended June 30, 2010
(in thousands)

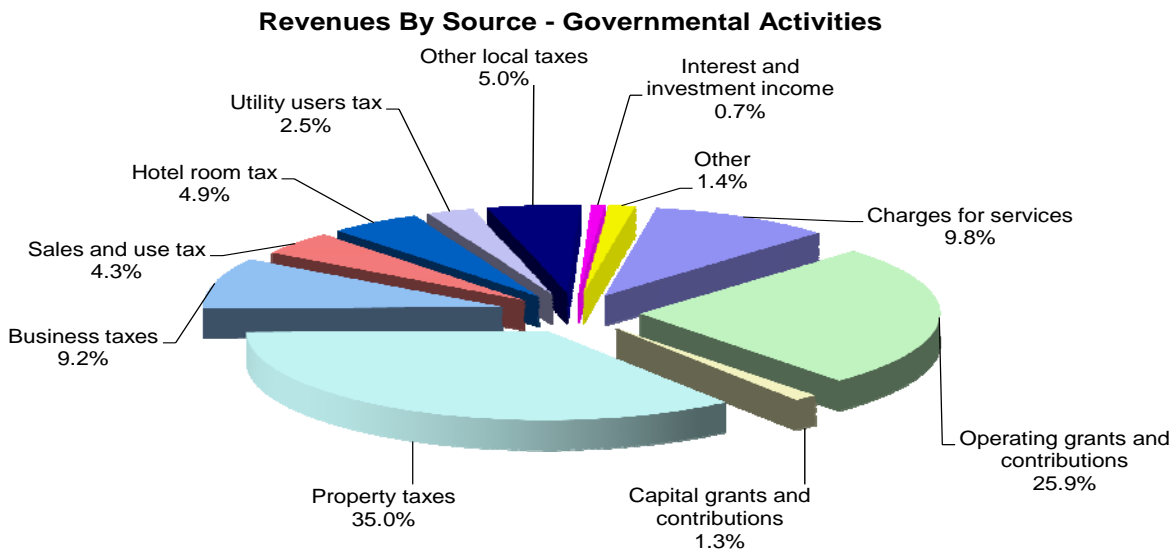
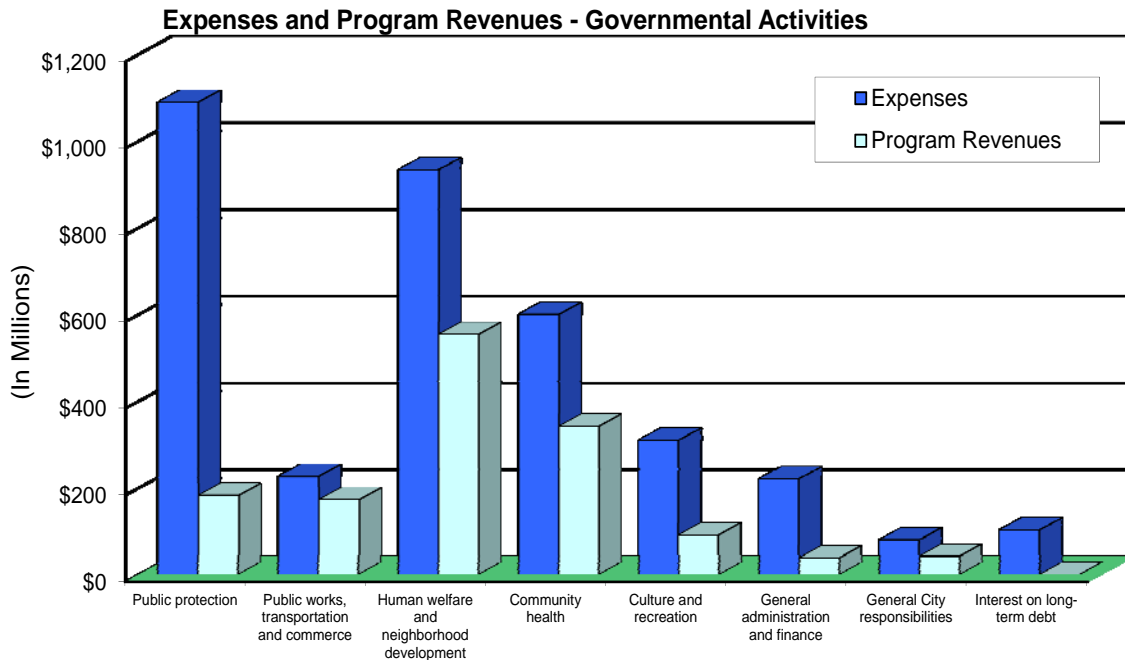
	Governmental activities		Business-type activities		Total	
	2010	2009	2010	2009	2010	2009
Revenues						
Program revenues:						
Charges for services.....	\$ 376,688	\$ 392,411	\$ 2,158,042	\$ 2,034,269	\$ 2,534,730	\$ 2,426,680
Operating grants and contributions.....	997,091	909,695	182,572	186,805	1,179,663	1,096,500
Capital grants and contributions.....	50,349	44,048	180,253	107,118	230,602	151,166
General revenues:						
Property taxes.....	1,345,040	1,302,071	-	-	1,345,040	1,302,071
Business taxes.....	354,019	388,653	-	-	354,019	388,653
Sales and use tax.....	164,769	172,794	-	-	164,769	172,794
Hotel room tax.....	186,849	214,460	-	-	186,849	214,460
Utility users tax.....	94,537	89,801	-	-	94,537	89,801
Other local taxes.....	194,070	126,017	-	-	194,070	126,017
Interest and investment income.....	27,877	35,434	44,471	49,691	72,348	85,125
Other.....	54,410	44,086	176,064	181,759	230,474	225,845
Total revenues.....	<u>3,845,699</u>	<u>3,719,470</u>	<u>2,741,402</u>	<u>2,559,642</u>	<u>6,587,101</u>	<u>6,279,112</u>
Expenses						
Public protection.....	1,089,309	1,109,311	-	-	1,089,309	1,109,311
Public works, transportation and commerce.....	225,589	254,955	-	-	225,589	254,955
Human welfare and neighborhood development.....	933,039	908,449	-	-	933,039	908,449
Community health.....	599,741	608,733	-	-	599,741	608,733
Culture and recreation.....	310,063	319,994	-	-	310,063	319,994
General administration and finance.....	221,471	238,601	-	-	221,471	238,601
General City responsibilities.....	80,246	72,634	-	-	80,246	72,634
Unallocated Interest on long-term debt.....	102,635	93,387	-	-	102,635	93,387
Airport.....	-	-	661,044	683,335	661,044	683,335
Transportation.....	-	-	897,500	863,218	897,500	863,218
Port.....	-	-	73,573	71,778	73,573	71,778
Water.....	-	-	325,242	277,162	325,242	277,162
Power.....	-	-	119,109	96,228	119,109	96,228
Hospitals.....	-	-	842,488	820,236	842,488	820,236
Sewer.....	-	-	201,403	184,977	201,403	184,977
Market.....	-	-	1,119	1,144	1,119	1,144
Total expenses.....	<u>3,562,093</u>	<u>3,606,064</u>	<u>3,121,478</u>	<u>2,998,078</u>	<u>6,683,571</u>	<u>6,604,142</u>
Increase/(decrease) in net assets before transfers.....	283,606	113,406	(380,076)	(438,436)	(96,470)	(325,030)
Transfers.....	(435,824)	(393,259)	435,824	393,259	-	-
Change in net assets.....	<u>(152,218)</u>	<u>(279,853)</u>	<u>55,748</u>	<u>(45,177)</u>	<u>(96,470)</u>	<u>(325,030)</u>
Net assets at beginning of year.....	<u>1,305,203</u>	<u>1,585,056</u>	<u>4,760,146</u>	<u>4,805,323</u>	<u>6,065,349</u>	<u>6,390,379</u>
Net assets at end of year.....	<u>\$ 1,152,985</u>	<u>\$ 1,305,203</u>	<u>\$ 4,815,894</u>	<u>\$ 4,760,146</u>	<u>\$ 5,968,879</u>	<u>\$ 6,065,349</u>

Analysis of Changes in Net Assets

The City's total net assets decreased by \$96.5 million during fiscal year 2009-2010. The governmental activities had a net assets decrease of \$152.2 million whereas the business-type activities realized an increase of \$55.7 million. With the exception of San Francisco Water Enterprise and General Hospital, all of the City's business type activities contributed to this growth. The former enterprises had decreases in net assets totaling \$72.4 million while the others, including Airport, Hetch Hetchy, Laguna Honda, MTA, Wastewater Enterprise and Port reported a total growth of \$128.1 million in net assets. Laguna Honda, with a \$66.5 million increase in net assets accounted for 51.9% of this improvement.

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The City's governmental activities experienced a \$126.2 million or 3.4 percent growth in total revenues. This included a \$87.4 million growth in operating grants and contributions, a \$68.1 million rise in other local tax and a \$43.0 million increase in property tax with a slight growth in capital grants, utility user taxes, and other revenues. These improvements were partly offset by a decline in other revenue sources including a \$34.6 million decrease in business taxes, a \$27.6 million drop in hotel room tax and a \$15.7 million reduction in charges for services. The City's governmental activities expenses reported a moderate reduction of \$44.0 million or 1.2 percent this fiscal year. The combined net revenue growth and expenditure reduction were largely offset by the increase of \$42.6 million in net transfer to business-type activities. A discussion of these and other changes is presented in the governmental activities and business-type activities sections that follow.



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Governmental activities. Governmental activities decreased the City's total net assets by approximately \$152.2 million. Key factors contributing to this year's change are discussed below.

Overall, total revenues from governmental activities were \$3.85 billion, a \$126.2 million or 3.4 percent increase over the prior year. For the same period, expenses totaled \$3.56 billion before transfers of \$435.8 million, resulting in a total net assets decrease of \$152.2 million by June 30, 2010.

Property taxes revenue grew moderately, by \$43.0 million or 3.3 percent. Other local taxes revenue grew by \$68.1 million, of which \$34.7 million were from Property Transfer Tax due to the passage of Proposition N in November 2008. Proposition N increased the transfer tax rate from 0.75% to 1.5% for all transactions valued over \$5 million. That, coupled with an increase in very large commercial transactions during the fiscal year, significantly contributed to the revenue growth. There was also a \$31.1 million revenue increase from the Access Line Tax, due, in part, to fiscal 2009-2010 being the first full year for this revenue source. Proposition O was passed by voters in November 2008 with an effective date of April 2009. This Proposition eliminated the 911 Emergency Response Fee and replaced it with a per-line Access Line Tax of the same amount.

The operating and capital grants and contributions reported a growth of \$93.7 million. This was largely due to the increases from federal sources, including \$66.9 million for human welfare programs, \$23.1 million for public protection and \$25.3 million for public works. These were partly reduced by a combined decrease of \$21.6 million in other governmental activities.

Revenues from business, hotel, and sale taxes totaled approximately \$705.6 million, which represents a \$70.3 million decrease over the prior year. This was due primarily to the decrease in business taxes by \$34.6 million, 8.9 percent, and the decrease in sales and use taxes by \$8.0 million, 4.6 percent. The continued recession was a significant factor in both cases. In addition, hotel room taxes decreased by \$27.6 million, 12.9 percent, reflecting a drop in hotel room charges per night from \$172 per room-night to \$155 per room-night.

Total charges for services revenues dropped this year by \$15.7 million, or 4.0 percent. Within this, there was an increase of \$11.6 million in litigation settlements and about \$7.8 million in rents and concessions and parking revenues. These increases were partially offset by a drop of \$37.0 million from 911 fees because that revenue source was replaced by the Access Line Tax in this fiscal year.

Interest and investment income revenue decreased by \$7.6 million, or 21.3 percent, primarily due to declining interest rates on the City's pooled investments. Those dropped from an estimated 2.56 percent to 1.38 percent over the 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 City added investments with longer maturities that had higher interest yields. As of June 30, 2010, 80.5% of the pooled investments will mature within 1 to 5 years compared to 54.4% last fiscal year. At the end of this fiscal year, deposits and investments with the City Treasury grew by \$1.25 billion, or 41.8%, of which \$203.0 million was for unspent general obligation bond proceeds issued in the fiscal year to fund the General Hospital rebuild project and \$1.05 billion represented the unspent proceeds from revenue bonds issued by business-type activities in the fiscal year to fund various major capital improvement projects.

Net transfers to business-type activities were \$435.8 million, a 10.8 percent or \$42.6 million increase over the prior fiscal year. The net increase was mainly due to a decrease of transfers to the General Fund by the City's hospitals. In this fiscal year, Laguna Honda Hospital reimbursed the General Fund for \$2.1 million capital expenditures compared to its \$50.9 million expenditure reimbursement in the prior year. The General Fund's operating subsidies to MTA, General Hospital and Laguna Honda Hospital were about \$402.9 million this fiscal year, substantially the same as last year's total of \$401.2 million.

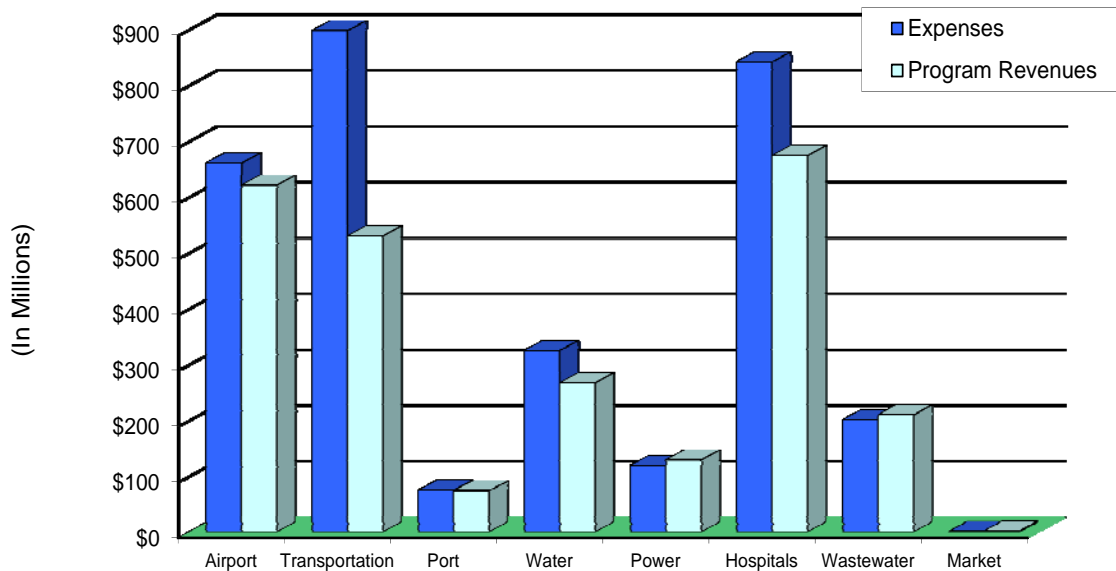
The decrease in total governmental expenses of \$44.0 million or 1.2 percent was primarily due to a reduction in net other postemployment benefits (OPEB) costs as discussed in Note 9(d).

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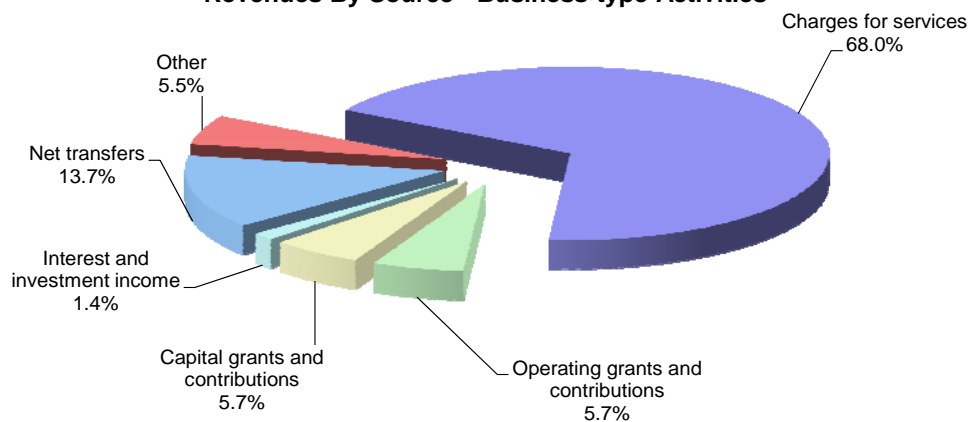
There was a total decrease of \$85.4 million in expenses for public protection, public works, community health, culture and recreation and general administration and finance reflecting a reduction in personnel costs. These decreases were partly offset by an increase of \$24.6 million in the human welfare and neighborhood services functions due to growth in social services and community-based programs. In addition, interest expense increased \$9.2 million correlating with increases in debt obligations.

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 (30.6 percent), followed by human welfare and neighborhood development (26.2 percent) and community health (16.8 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 (25.9 percent), charges for services (9.8 percent), and business taxes (9.2 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 - Business-type Activities



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Business-type activities increased the City's net assets by \$55.7 million. Key factors contributing to this increase are:

- The Municipal Transportation Agency (MTA) had net assets of \$1.83 billion at the end of this fiscal year, essentially unchanged from the prior year, reflecting only a modest increase in assets of \$4.1 million. The increase is attributable to growth in operating revenues, capital contributions and net transfers, offset by a rise in operating expenses and a decrease in nonoperating revenues. The largest portion of the MTA's net assets reflects its investment in capital assets, which totaled \$3.12 billion, offset by accumulated depreciation of \$1.16 billion and related debt of \$50.1 million which nets to \$1.92 billion reported as net assets invested in capital assets, net of related debt. The remainder of the MTA's net assets is composed of restricted net assets including deposits and investments with the City and receivables. Finally, the MTA has an unrestricted deficit net asset balance of \$105.6 million, which is slightly improved over the prior year's deficit balance of \$106.5 million.
- Laguna Honda Hospital, the City's skilled nursing care hospital, increased net assets by \$66.5 million or 14.4 percent this year, reflecting continued progress on construction of the new hospital complex. This increase is primarily related to \$68.7 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 \$2.1 million from Laguna Honda Hospital to the General Fund to reimburse the General Fund for certain hospital capital outlay. Laguna Honda Hospital also received \$16.4 million of capital contributions from Tobacco Settlement Funds to fund construction, and a \$37.1 million subsidy transfer from the General Fund offset by \$61.4 million in losses this year as compared to \$47.9 million in losses in the prior year. The other transfers that it received came from San Francisco General Hospital for \$6.1 million to fund its budgetary cost overruns and from Hetch Hetchy Water and Power for \$1.7 million for energy savings reimbursements.
- General Hospital, the City's acute care hospital, ended the fiscal year with a net asset deficit of \$41.9 million. Contributing to the General Hospital's change in net assets is the following: (1) An overall increase in operating revenues of approximately 8 percent primarily attributable to a 10 percent increase in Medicare billing rate in FY2010; (2) offset by rising operating expenses due primarily to escalating personnel retirement and benefit costs; and (3) increases in net transfers. Transfers in and out will vary from year to year based upon the City's budget.
- Hetch Hetchy Water and Power is composed of two segments: 1) Hetch Hetchy Water upcountry operations and water system and 2) Hetch Hetchy Power, also referred to as the Power Enterprise. A number of the facilities are joint assets and are used for both water and power operations. Hetch Hetchy Water's net assets decreased by \$0.1 million from the prior year, while Hetch Hetchy Power's net assets increased by \$12.1 million or 3.7 percent during the year. Contributing to this combined net increase of \$12.0 million was an increase in Hetch Hetchy Power's total revenue by \$9.2 million or 9.6 percent over the prior year primarily due to increased electricity sales of \$5.2 million and third party sales to other municipalities and governmental agencies under Western System Power Pool agreements. Additionally, other nonoperating revenues increased by \$3.8 million or 140.1 percent, which is mostly due to a \$2.9 million settlement with the State Department of Water Resources (DWR) related to the Combustion Turbine project. The increased revenues were offset by increases in expenses due to increases in general liability expenses of \$1.8 million and write-off of development costs of \$10.2 million related to the DWR settlement mentioned above. Also, there was \$11.7 million of non-capitalizable construction related activities and \$2.9 million of solar incentive program expenses.
- The City's Water Enterprise is the third largest municipal water agency in California. For the fiscal year 2009-2010, it reported net assets of \$415.7 million, a decrease of \$46.6 million or 10.1 percent from the prior year. The primary reason for the decrease was an increase in expenses of \$49.1 million or 17.7 percent, offset by an increase in revenue of \$3.4 million or 3.2 percent. The latter was due to an average 15 percent increase in retail rates partially offset by a reduction in consumption. Operating expenses increased by \$29.7 million due to a combination of increases in judgments and claims for \$23.0 million, increased services provided by other departments for \$7.5 million, and depreciation of \$3.5 million. These were offset by a reduction in other operating expenses of

CITY AND COUNTY OF SAN FRANCISCO
Management's Discussion and Analysis (Continued)
Year ended June 30, 2010

\$5.0 million for non-capitalized project expenses and capital project write-offs. In addition, interest expense increased by \$18.4 million attributable to an increase of \$1.31 billion of revenue bonds.

- The City's Wastewater Enterprise had total net assets of \$1.03 billion at the end of fiscal year 2009-2010. This total increased from the prior year by \$14.7 million or 1.5 percent. This was primarily due to an increase in revenues of \$4.5 million or 2.1 percent, \$3.0 million of which was due to a rate increase offset by a reduction of other operating revenues of \$1.8 and a \$0.1 million reduction in interest and investment earnings due to falling interest rates and reduced cash balances. Total expenses also increased by \$16.4 million or 8.9 percent due to an increase in operating expenses of \$9.8 million of non-capitalized project expenses and capital project write-offs, \$4.1 million of materials and supplies, \$1.9 million of additional depreciation, \$1.9 million increase in personal services, mainly related to retirement costs, and \$0.7 million in services provided by other departments. These increased operating costs were partially offset by decreases in other operating costs of \$1.8 million of contractual services for engineering and inspection services. During fiscal year 2009-2010, revenues exceeded expenses by \$14.7 million. While net assets did increase, this change in net assets was less than the previous year's increase in net assets by \$12.0 million or 44.8 percent.
- The Port is responsible for a seven and one-half mile stretch of waterfront land and its revenue is derived primarily from property rentals to commercial and industrial enterprises and a diverse mix of maritime operations. The Port's net assets increased by \$11.1 million in the 2009-2010 fiscal year. This was mainly due to \$10.6 million in capital contributions from the City's general obligation bond proceeds for park and open space improvements.
- The Airport's net assets increased by \$19.1 million or 7.1 percent during the current year. This is an increase of \$63.1 million over the prior year's loss of \$44.0 million. The increase is primarily the result of \$25.5 million or 4.6 percent of additional aviation revenues, concession revenues, parking revenues, and net sales and service revenues due to increased passenger traffic. The Airport also realized decreases in the operating expenses of \$4.4 million, 0.9 percent, and decreases in nonoperating expenses of \$19.3 million mostly due to a decrease of \$17.9 million in interest expense because the Airport refunded and restructured a large portion of its long-term debt. Also, as of June 30, 2010, the Airport's net assets invested in capital assets, net of related debt were a negative \$71.2 million because of the residual effect of the Airport depreciating its assets faster than the repayment of its bonded debt.

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 \$999.1 million, an increase of \$14.1 million or 1.4 percent over the prior year. The City realized a growth in total governmental funds revenues, including growth in property tax revenues, other local taxes and the combined federal and state revenues for a total of \$190.8 million. These increases were partly offset by a decline in other taxes, including business, hotel room tax, sale and use taxes, as well as interest and investment income as discussed earlier, leaving a net increase of \$109.9 million in revenues at the end of the fiscal year. In addition, charges for services decreased by \$37.3 million primarily due to Proposition O replacing the 911 Emergency Response Fee, a charge for services, with a new Access Line local tax.

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Year ended June 30, 2010

Within the governmental funds, the Special Revenue and Capital Projects funds had unreserved deficits of \$134.2 million and \$43.8 million, respectively, while the General Fund had a slight deficit of \$2.0 million, offset by the Permanent Funds positive balance of \$2.0 million. Combined the governmental funds total unreserved fund balance had a deficit of \$178.0 million. 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 (\$39.6 million), (2) encumbrances for existing contracts and purchase orders (\$279.6 million), (3) funds continued for programs or projects in future fiscal years (\$745.5 million), (4) debt service (\$68.5 million) and (5) assets not available for appropriation (\$43.9 million).

The General Fund is the chief operating fund of the City and had a total fund balance of \$191.8 million at the end of the fiscal year. This included a reserved fund balance of \$193.8 million and an unreserved deficit of \$2.0 million, which reflects, in part, the delays in cash receipts for intergovernmental revenue sources. For the year, the General Fund's total revenues exceeded expenditures by \$351.5 million, before transfers and other items of \$461.4 million. In the aggregate, the resulting total fund balance decreased by \$109.9 million for the fiscal year ended June 30, 2010. Overall, the slightly better than projected revenues, particularly in real estate property transfer taxes and hotel room taxes were offset by an increased rate of expenditure growth due to growing demand for services and personnel costs across City functions and a reduction of reimbursement of prior year capital project costs paid for the two hospital rebuild projects. The decline in total fund balance includes the effects of drawing upon the City's Rainy Day Reserves consistent with Charter provisions, with \$34.2 million provided to the General Fund and \$24.5 million provided to the San Francisco Unified School District.

Proprietary Funds

The City's proprietary fund statements provide the same type of information found in the business-type 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 \$224.1 million, the Water Enterprise \$80.2 million, the Hetch Hetchy Water and Power were \$173.7 million, the Wastewater Enterprise Program were \$30.5 million, the Port were \$32.0 million and the Market Corporation were \$4.8 million. In addition, the MTA, the San Francisco General Hospital and Laguna Honda Hospital had deficits in unrestricted net assets of \$105.6 million, \$92.0 million and \$50.8 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 increased by approximately \$55.7 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, Net	Change In Net Assets
Airport.....	\$ 576,738	\$ 474,206	\$ 102,532	\$ (99,490)	\$ 44,204	\$ (28,100)	19,146
Water.....	265,218	277,970	(12,752)	(33,371)	-	(493)	(46,616)
Hetch Hetchy.....	128,590	118,387	10,203	3,190	-	(1,400)	11,993
Municipal Transportation Agency.....	303,117	894,931	(591,814)	219,120	114,133	262,704	4,143
General Hospital.....	482,448	653,864	(171,416)	64,622	-	80,993	(25,801)
Wastewater Enterprise.....	209,843	185,512	24,331	(9,599)	-	-	14,732
Port.....	66,579	72,517	(5,938)	876	5,518	10,616	11,072
Laguna Honda Hospital.....	123,828	188,181	(64,353)	2,957	16,398	111,504	66,506
Market Corporation.....	1,681	1,119	562	11	-	-	573
Total.....	\$ 2,158,042	\$ 2,866,687	\$ (708,645)	\$ 148,316	\$ 180,253	\$ 435,824	\$ 55,748

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Year ended June 30, 2010

Fiduciary Funds

The City maintains fiduciary funds for the assets of the San Francisco Employees' 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 \$13.2 billion, representing a \$1.25 billion increase over the prior year, a 10.5 percent change. This increase is primarily a result of market increases and the net difference between contributions received by the funds and benefit payments made from the funds. The Investment Trust Fund's net assets were \$582.6 million at year's end, compared to \$565.4 million at the end of the previous fiscal year. This 3.0 percent increase represents the increase in additions over withdrawals or distributions to external participants of the funds 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.

During the year, actual revenues and other resources were \$55.3 million more than budgeted. The City realized \$39.3 million, \$37.3 million, \$19.0 million, \$7.6 million and \$5.6 million more revenue than budgeted in property taxes, real property transfer tax, hotel room tax, utility users tax and fines, forfeitures, and penalties, respectively. These increases were partly offset by \$53.5 million shortfall of actual revenue compared to budgeted revenue in other categories, namely, business taxes, federal grants and subventions, charges for services and other resources.

Differences between the final budget and the actual (budgetary basis) expenditures resulted in \$83.5 million in expenditure savings. Major factors include:

- \$24.2 million savings in the Human Services Agency, due largely to lower than budgeted client assistance and aid as well as other operating costs.
- \$13.4 million in savings on general administration and finance and other general city responsibilities from salary-related expenditures and non-personnel service.
- \$16.7 million in savings due to close-out of unspent General Reserve not used for supplemental appropriation or other contingencies during fiscal year 2009-2010.
- \$7.8 million savings mainly in Police, Emergency Communication and Fire departments from salary and benefit related expenditures.
- \$8.5 million in savings due to non-personnel services 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 \$4.2 million primarily from capital projects.

The net effect of moderate revenue increases, savings in expenditures and reduction in reserve balances was a positive unreserved budgetary fund balance available for subsequent year appropriation of \$105.3 million at the end of fiscal year 2009-2010. The City's fiscal year 2010-2011 Adopted Original Budget assumed an available balance of \$79.9 million, so an additional \$25.4 million remains available. (See also Note 4 to the Basic Financial Statements for additional fund balance details).

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Year ended June 30, 2010

Capital Assets and Debt Administration

Capital Assets

The City's capital assets for its governmental and business-type activities as of June 30, 2010, increased by \$744.2 million, 6.0 percent, to \$13.23 billion (net of accumulated depreciation). Capital assets include land, buildings and improvements, machinery and equipment, park facilities, roads, streets, bridges and intangible assets. Governmental activities contributed \$148.9 million or 1.2 percent to this total while \$595.3 million or 4.8 percent was from business-type activities. Details are shown in the table below.

	Governmental Activities		Business-type Activities		Total	
	2010	2009	2010	2009	2010	2009
Land.....	\$ 155,512	\$ 155,512	\$ 179,652	\$ 180,919	\$ 335,164	\$ 336,431
Construction in progress.....	313,127	187,133	1,953,226	1,328,692	2,266,353	1,515,825
Facilities and Improvement.....	2,324,634	2,337,478	6,249,690	6,306,617	8,574,324	8,644,095
Machinery and equipment.....	52,504	58,648	809,949	785,888	862,453	844,536
Infrastructure.....	315,906	290,144	770,195	793,866	1,086,101	1,084,010
Property held under lease.....	-	-	24	2,218	24	2,218
Intangible assets.....	16,139	-	93,434	62,694	109,573	62,694
Total.....	<u>\$ 3,177,822</u>	<u>\$ 3,028,915</u>	<u>\$ 10,056,170</u>	<u>\$ 9,460,894</u>	<u>\$ 13,233,992</u>	<u>\$ 12,489,809</u>

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

- Under governmental activities, net capital assets increased by \$148.9 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. Among the various city-wide parks, libraries, public works and traffic signal projects and building improvement projects, the General Hospital Rebuild Project which is funded with General Obligations Bonds proceeds and recorded in governmental activities grew by \$86.1 million during the fiscal year. About \$83.9 million worth of construction-in-progress work was substantially completed and capitalized as facilities and improvement and infrastructure. Of the completed projects, about \$10.5 million in public library improvements and approximately \$36.7 million is for various parks and recreation centers such as Hamilton Pool, Sunnyside Clubhouse, and various park improvement projects including the Golden Gate Park. The remaining completed projects include public works and traffic signal projects.
- The Water Enterprise's net capital assets increased by \$363.1 million or 24.2 percent. Close to \$240.1 million, or 66.1 percent, 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. Major additions to construction work included Tesla Treatment Facility, New Crystal Springs Bypass Tunnel, Bay Division Pipeline Reliability Upgrade, Irvington Tunnel alternatives, and other Water System Improvement Program (WSIP). The total estimated cost for the WSIP is \$4.6 billion, including \$4.1 billion for capital projects and \$0.5 billion for net financing costs. The program is on target to meet an overall completion date of December 2015. During the fiscal year, there is an increase of \$123.7 million or 8.7 percent in structures, buildings, equipment and intangible assets, and a decrease of \$0.7 million in land and rights-of-way due to reclassification to intangible assets. The Water Enterprise has incurred 73 percent share or \$28.2 million in development costs for an office building located at 525 Golden Gate Avenue. Construction started in January 2010 with an expected completion date of February 2012, with an expected occupancy date of April 2012.
- MTA's net capital assets increased by \$11.3 million or 0.6 percent, compared to the previous year, which was attributed to an increase in construction work for new and existing projects with a corresponding increase in depreciation expense for existing assets. Phase II of the Third Street Light Rail Project, the "Central Subway" Project proceeded with detail design. This project will link the

CITY AND COUNTY OF SAN FRANCISCO
Management's Discussion and Analysis (Continued)
Year ended June 30, 2010

existing 5.2 mile Phase I T-Line, beginning at Caltrain and 4th Street and King Streets, to BART, Union Square and Chinatown to the north. The rail replacement project and reconstruction work on overhead replacement programs are part of the ongoing program to keep the system in good repair and to replace aging parts of the track network. MTA also incurred acquisition and design costs to refurbish and modernize the farebox collection system in the subway stations, to replace the radio communication system on the fleets, light rail wheel truing machines, an on-board camera project and the renovation and rehabilitation of streetcars. Construction costs of \$17.5 million was also incurred for maintenance facility projects.

- Laguna Honda Hospital's net capital assets increased by \$77.6 million or 18.0 percent due primarily 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 \$1.5 million or 2.9 percent, primarily because the rate of depreciation expense is higher than the increase in minor improvement projects. The hospital rebuild project was managed and financed by governmental activities with the second and third series of general obligation bonds totaling \$294.7 million issued in the current fiscal year. The total amount approved by the voters for the rebuilt project is \$887.4 million and total issued amount as of June 30, 2010 was \$426.3 million.
- The Wastewater Enterprise's net capital assets reported a slight increase of \$2.7 million or 0.2 percent mainly in construction activities. These include the Channel Pump Station Improvements Phase 2, Southeast Water Pollution and Odor Control Improvements, Sewer Spot Replacements and other capital projects throughout the system. The Wastewater Enterprise has incurred 15 percent share or \$5.8 million in development costs for the office building at 525 Golden Gate Avenue.
- Hetch Hetchy net capital assets increased by \$12.1 million or 4.4 percent during the year. Contributing to this net increase was acquisition of machinery and equipment and facilities improvements. The enterprise has a reclassification of \$30 million in intangible assets of water rights and emission reduction credits from facilities and improvements asset class during the year.
- The Airport's net capital assets increased \$127.4 million or 3.6 percent largely due to major capital additions including Terminal 2 Boarding Area D Renovations, Building 575 Improvements, and various other capital improvements.
- The Port's net capital assets increased by \$2.3 million or 0.9 percent mainly in construction activities that include the Pier 27 shoreside electrical power, Pier 80 security improvements and other improvement projects.

At the end of the year, the City's business-type activities had approximately \$1.33 billion in commitments for various capital projects. Of this, Water Enterprise had an estimated \$913.6 million, MTA had \$175.8 million, Wastewater had \$27.1 million, Airport had \$109.5 million, Hetch Hetchy had \$29.7 million, Port had \$7.1 million, Laguna Honda Hospital had \$61.3 million and the General Hospital had \$1.9 million. In addition, there was approximately \$80.3 million reserved for encumbrances in capital project funds for the general government projects.

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

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

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Debt Administration

At the end of the current fiscal year, the City had total long-term and commercial paper debt outstanding of \$10.10 billion. Of this amount, \$1.39 billion is general obligation bonds backed by the full faith and credit of the City and \$8.71 billion is revenue bonds, loans, certificates of participation, capital leases, and other debts 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 notes and capital leases increased by \$2.06 billion during fiscal year 2009-2010, due to the issuance of new debt in the governmental and business-type activities. The net increase in obligations due to issuance of new debt in governmental activities was \$117.5 million. For the business-type activities, the net increase in obligations was \$1.94 billion primarily due to the issuance of revenue bonds by almost all enterprises, except MTA, Laguna Honda, and Market Corporation, to fund various capital projects and acquisition of equipment.

The business-type activities issued a combined total of \$3.31 billion revenue bonds, of which \$1.23 billion was for refunding and restructuring Airport's long term debt for debt service and cash flow saving through five refunding bond transactions during the fiscal year. A number of which were made possible by the tax provisions of the American Recovery and Reinvestment Act of 2009, the economic stimulus package enacted by Congress. Several series of Airport's revenue bonds that were traded at distressed levels due to the credit rating downgrade of the liquidity facility provided by the financial institution because of the global financial crisis and those that were subject to the AMT tender were refunded during these transactions. The Airport also issued \$485.8 million of revenue bonds to fund new capital projects for the first time in about a decade. The San Francisco Water enterprise also issued a total of \$1.31 billion of revenue bonds, to refund \$229.6 million commercial paper notes and \$14.4 million outstanding revenue bonds as well as to provide new money for the WSIP capital projects and the Advanced Meter Infrastructure project. The San Francisco Wastewater enterprise issued a total of \$239.6 million revenue bonds to redeem approximately \$103.5 million commercial paper notes and to fund the Sewer System Improvement Program capital projects. In addition, the City's Public Utilities Commission issued \$167.7 million certificates of participation to fund construction of the future headquarters building of the San Francisco Public Utilities Commission (PUC) at 525 Golden Gate Avenue. Each of the three enterprises has an ownership interest in the building equal to their projected usage of space and each is responsible for a portion of the annual debt service payments based on their ownership percentages less contributed equity which is as follows: Water Enterprise (71.4%), Wastewater Enterprise (18.9%), and Hetch Hetchy Water and Power Enterprise (9.7%). The Port Commission issued \$36.5 million in revenue bonds to provide funds for the design, construction, reconstruction and improvements to various Port facilities during the fiscal year. The City also issued \$22.5 million in certificates of participation to finance the replacement of the back-up generator for the San Francisco General Hospital.

The City issued a total of \$355.1 million in general obligation bonds, of which \$294.7 million and \$60.4 million are to fund the General Hospital rebuild project and for various park and neighborhood facilities improvement projects, respectively. Lease revenue bonds for \$10.3 million were issued through the City and County of San Francisco Finance Corporation to finance equipment purchase. The City issued an additional \$37.9 million in certificates of participation for the acquisition and construction of improvements to various City streets.

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 \$161.79 billion in value as of the close of the fiscal year. As of June 30, 2010, the City had \$1.39 billion in authorized, outstanding property tax-supported general obligation bonds at par, which is equal to approximately 0.82 percent of gross (0.86 percent of net) taxable assessed value of property. As of June 30, 2010, there were an additional \$847.1 million 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 1.33 percent of gross (1.38 percent of net) taxable assessed value of property.

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Year ended June 30, 2010

The City's underlying ratings on general obligation bonds as of June 30, 2010 were:

Moody's Investors Service, Inc.	Aa1
Standard & Poor's	AA
Fitch Ratings	AA

During the fiscal year, Moody's Investors Service (Moody's) and Fitch Ratings recalibrated the City's ratings to Aa1 and AA from Aa2 and AA-, respectively. Fitch Ratings assigned their negative rating outlook on all the City's outstanding bonds in February 2010. Moody's revised the rating outlook from stable to negative in June 30, 2010. Standard & Poor's affirmed their ratings with a stable outlook.

In November 2010, Moody's downgraded to Aa2 from Aa1 the rating on the City's general obligation bonds. Moody's also downgraded by one notch their ratings on the City's various general fund obligations, including its abatement leases and settlement obligation bonds. The outlook on the City's ratings has been revised to stable.

The City's enterprise activities maintained their underlying debt ratings this fiscal year. Fitch upgraded the Airport's long-term credit rating from "A" with a Positive Rating Outlook to "A+" with a Stable Rating Outlook. Moody's Investors Services and Standard & Poor's maintained their long-term rating of "A1" and "A" respectively. The San Francisco Water Enterprise carried underlying ratings of "Aa2" and "AA-" from Moody's and Standard & Poor's, respectively. The San Francisco Waste Water Enterprise carried underlying ratings of "Aa3" and "AA-" 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 expected to continue to face economic challenges over the next few years. The following economic factors were considered in the City's fiscal year 2010-2011 budget.

- San Francisco's economy has not yet recovered from the effects of the recession throughout fiscal year 2009-2010, and continues to experience high unemployment rates. In addition, housing prices, residential and commercial rent, hotel revenues, industry employment, and retail sales all remained significantly below their pre-recession peaks.
- Unemployment in San Francisco began the fiscal year in July 2009 at 9.6% and closed the fiscal year at the same rate.
- The wage and salary employment base of San Francisco fell by 2,800 jobs between June 2009 and June 2010, a decline of 0.5%. This decline compares with a 4.9% drop in employment during FY 2008-2009, and suggests that San Francisco's employment picture has stabilized, but not recovered, in the past year.
- Although there was a 1.8% increase in jobs in the leisure and hospitality sector in San Francisco and California in fiscal year 2009-2010, it did not translate into growth for the hotel sector, which is a key barometer of San Francisco tourism. Hotel room occupancy did rise, but revenue per available hotel room declined significantly.
- Tax revenue declines resulted in the need for mid-year budget corrections to maintain a Charter-required balanced budget. These pressures on the City's General Fund budget are expected to continue into FY 2010-2011.
- In June 2010, the Controller's Office estimated that the FY 2011-2012 budget year would face a shortfall approaching or exceeding \$400 million to fund current service and staffing levels, due to the anticipated loss of one-time revenues included in the FY 2010-2011 budget coupled with likely increases in employee benefit and other costs.

CITY AND COUNTY OF SAN FRANCISCO

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

Public Information Officer
Pier 1, The Embarcadero
San Francisco, CA 94111

San Francisco Water Enterprise

Hetch Hetchy Water and Power
San Francisco Wastewater Enterprise
Chief Financial Officer
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

SFMTA Finance and Information Technology Services
1 South Van Ness Avenue, 8th Floor
San Francisco, CA 94103

Health Service System

Executive Director
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

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

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