

## COUNTY OF SANTA CRUZ, CALIFORNIA

### Management's Discussion & Analysis For the Year Ended June 30, 2005

This section the County of Santa Cruz (the "County") comprehensive annual financial report presents a discussion and analysis of the County's financial performance during the fiscal year ended June 30, 2005. Please read it in conjunction with the transmittal letter at the front of this report and the County's basic financial statements following this section.

#### FINANCIAL HIGHLIGHTS

- The assets of the County exceeded liabilities at the close of the 2004 – 2005 fiscal year by \$397,010,514 (*net assets*). Of this amount, \$26,058,395 (*unrestricted net assets*) may be used to meet ongoing obligations to citizens and creditors, 103,696,877 is restricted for specific purpose (*restricted net assets*), and 267,255,242 is invested in capital assets, net of related debt.
- The government's total net assets increased by \$10,314,439 (exclusive of prior period adjustments). This increase is mostly attributable to a \$7.2 million judgment in favor of the County.
- As of June 30, 2005, the County's governmental funds reported combined ending fund balances of \$142,716,838, a decrease of \$9,444,021 (exclusive of prior period adjustments and change in reserve for inventories) in comparison with the prior year. Approximately 78% of the combined fund balances, \$100,351,231, is available to meet the County's current and future needs (*unreserved fund balance*).
- At the end of the fiscal year, unreserved fund balance for the general fund was \$26,807,546, or 9% of total general fund expenditures. This amount is budgeted to be spent in the next fiscal year, except for \$7 million designated for various purposes, including those shown on page 29.
- The County's total long-term liabilities decreased by \$9,761,598 in comparison with the prior year (excluding compensated absences, estimated claims, and post-closure liability). The decrease resulted primarily from the scheduled principal payments, and the refunding of the 1995 A Lease Revenue Refunding Bonds.

#### OVERVIEW OF THE FINANCIAL STATEMENTS

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

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## Management's Discussion & Analysis For the Year Ended June 30, 2005

### **Government-wide Financial Statements**

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

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

The *statement of activities* presents information showing how the County's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the 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 these government-wide financial statements distinguish functions of the County that are principally supported by taxes and intergovernmental revenues (*governmental activities*) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (*business-type activities*). The governmental activities of the County include general government, public protection, health and sanitation, public assistance, education, recreation and culture, and public ways and facilities. The business-type activities of the County include the County Disposal Sites CSA 9, and the following Board of Supervisor Governed Districts – Boulder Creek CSA 7, Rolling Woods CSA 10, Septic Tank Maintenance CSA 12, Freedom County Sanitation District, Davenport Sanitation District, Place de Mer CSA 2, Sand Dollar Beach CSA 5, Trestle Beach CSA 20, Summit West CSA 54, and Graham Hill CSA 57 operations.

Component units are included in our basic financial statements and consist of legally separate entities for which the County is financially accountable and that have substantially the same board as the County or provide services entirely to the County. The Santa Cruz County Sanitation District is reported as a discretely presented component unit of the County. The District is managed by the County Department of Public Works and provides sanitation services to the unincorporated areas of the County.

### **Fund Financial Statements**

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

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### Management's Discussion & Analysis For the Year Ended June 30, 2005

**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 County's basic services are reported in the 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 County'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 the governmental funds and governmental activities.

The County maintains several individual governmental funds organized according to their type (general, special revenue, debt service, and capital projects). Information is presented separately in the governmental funds balance sheet and in the governmental funds statement of revenues, expenditures, and changes in fund balances for the general fund and the Redevelopment Agency, which are considered to be major funds. 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 County adopts an annual appropriated budget. The budget is a compilation of operating budgets from individual functional units within the General Fund, Special Revenue Funds, Capital Projects Funds, and Proprietary Funds (operating plans). Budgets are adopted for all funds except for Debt Service Funds and certain special revenue funds, namely, Public Finance Authority, General Assessments, and Health Realignment Funds. A budgetary comparison schedule has been provided for the General Fund and Special Revenue-Redevelopment Agency to demonstrate compliance with these budgets.

**Proprietary funds** are generally used to account for services for which the County charges customers—either outside customers, or internal units or departments of the County. Proprietary funds provide the same type of information as shown in the government-wide financial statements, only in more detail. The County 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 County enterprise funds used to account for the operations of the County include the County Disposal Sites CSA 9, and the following Board of Supervisor Governed Districts—Boulder Creek CSA 7, Rolling Woods CSA 10, Septic Tank Maintenance CSA 12, Freedom County Sanitation District, Davenport Sanitation District, Place de Mer CSA 2, Sand Dollar Beach CSA 5, Trestle Beach CSA 20, Summit West CSA 54, and Graham Hill CSA 57 operations.

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### Management's Discussion & Analysis For the Year Ended June 30, 2005

- **Internal Service funds** are an accounting device used to accumulate and allocate costs internally among the County's various functions. The County uses internal service funds to account for its central duplicating, information services, public works, service center, and self-insurance (risk management, dental and health, liability and property, workers' compensation, employee benefit staffing, and state unemployment insurance) functions. 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** are used to account for resources held for the benefit of parties outside the County. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are not available to support the County's own programs. The fiduciary funds the County maintains are agency funds. Since agency funds are custodial in nature (i.e., assets equal liabilities), they do not involve the measurement of results of operations.

#### **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 (other than MD&A)**

In additions to the basic financial statements and accompanying notes, this report presents certain required supplementary information concerning the County's general fund budgetary comparison schedule and progress in funding its obligation to provide pension benefits to its employees.

#### **Combining Statements and Schedules**

The combining and individual fund statements and schedules referred to earlier in connections with non-major governmental funds, enterprise and internal service funds, and fiduciary funds are presented immediately following the required supplementary information.

# COUNTY OF SANTA CRUZ, CALIFORNIA

## Management's Discussion & Analysis For the Year Ended June 30, 2005

### GOVERNMENT-WIDE FINANCIAL ANALYSIS

#### Net Assets

	Governmental Activities		Business-Type Activities		Total		Variance %
	2005	2004	2005	2004	2005	2004	
<b>Assets:</b>							
Current and other assets	\$ 268,381,847	\$ 256,681,497	\$ 18,370,921	\$ 19,033,914	\$ 286,752,768	\$ 275,715,411	4.00
Capital assets	430,405,298	131,336,916	24,686,395	23,798,416	455,091,693	155,135,332	193.35
Total assets	<u>698,787,145</u>	<u>388,018,413</u>	<u>43,057,316</u>	<u>42,832,330</u>	<u>741,844,461</u>	<u>430,850,743</u>	72.18
<b>Liabilities:</b>							
Current and other liabilities	112,149,434	125,623,053	1,091,664	1,756,605	113,241,098	127,379,658	(11.10)
Long-term liabilities	225,792,369	196,716,222	5,800,480	5,329,930	231,592,849	202,046,152	14.62
Total liabilities	<u>337,941,803</u>	<u>322,339,275</u>	<u>6,892,144</u>	<u>7,086,535</u>	<u>344,833,947</u>	<u>329,425,810</u>	4.68
<b>Net Assets:</b>							
Invested in capital assets, net of related debt	244,385,838	46,942,253	22,869,404	21,424,864	267,255,242	68,367,117	290.91
Restricted	103,442,277	16,191,546	254,600	308,058	103,696,877	16,499,604	528.48
Unrestricted	13,017,227	2,545,339	13,041,168	14,012,873	26,058,395	16,558,212	57.37
Total net assets	<u>\$ 360,845,342</u>	<u>\$ 65,679,138</u>	<u>\$ 36,165,172</u>	<u>\$ 35,745,795</u>	<u>\$ 397,010,514</u>	<u>\$ 101,424,933</u>	291.43

#### Analysis of Net Assets

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. For the County, assets exceed liabilities by \$397,010,514 at the close of the current fiscal year.

The portion of the County's net assets invested in capital assets, net of related debt, \$267,255,242 (67%), reflects its investment in capital assets (e.g. land, building and structures, and equipment), less any related debt used to acquire those assets that are still outstanding. The County uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending. Although the County's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

An additional portion of the County's net assets, \$103,696,877 (26%), represents resources that are subject to external restrictions on how they may be used.

The remaining (7%) represents the unrestricted net assets, \$26,058,395 which may be used to meet the government's ongoing obligations to citizens and creditors.

At the end of the current fiscal year, the County reported positive balances in all three categories of net assets, both for the County as a whole, as well as for its separate governmental activities.

# COUNTY OF SANTA CRUZ, CALIFORNIA

## Management's Discussion & Analysis For the Year Ended June 30, 2005

### Change in Net Assets

	Governmental Activities		Business-Type Activities		Total		Variance %
	2005	2004	2005	2004	2005	2004	
<b>Revenues</b>							
<b>Program Revenues:</b>							
Charges for services	\$ 70,988,310	\$ 63,997,734	\$ 12,723,001	\$ 12,184,964	\$ 83,711,311	\$ 76,182,698	9.88
Operating grants and contr.	175,186,665	184,463,919	258,215	320,418	175,444,880	184,784,337	(5.05)
Capital grants and contr.	6,828,522	-	20,192	1,619	6,848,714	1,619	422921.25
<b>General revenues:</b>							
Property taxes	82,709,543	64,880,739	-	-	82,709,543	64,880,739	27.48
Other taxes	14,796,284	14,211,827	-	-	14,796,284	14,211,827	4.11
Investment earnings	6,039,649	3,672,892	511,375	293,205	6,551,024	3,966,097	65.18
Miscellaneous\	8,387,836	10,953,731	1,178,991	642,167	9,566,827	11,595,898	(17.50)
Total revenues	<u>364,936,809</u>	<u>342,180,842</u>	<u>14,691,774</u>	<u>13,442,373</u>	<u>379,628,583</u>	<u>355,623,215</u>	6.75
<b>Expenses:</b>							
General government	27,947,824	25,065,854	-	-	27,947,824	25,065,854	11.50
Public protection	104,329,495	115,996,350	-	-	104,329,495	115,996,350	(10.06)
Public ways and facilities	33,102,514	41,229,761	-	-	33,102,514	41,229,761	(19.71)
Health and sanitation	84,028,324	81,903,397	-	-	84,028,324	81,903,397	2.59
Public assistance	85,081,345	83,909,463	-	-	85,081,345	83,909,463	1.40
Education	3,977,056	3,926,053	-	-	3,977,056	3,926,053	1.30
Recreation and culture	7,588,935	7,948,990	-	-	7,588,935	7,948,990	(4.53)
Interest on long-term debt	8,986,254	8,453,032	-	-	8,986,254	8,453,032	6.31
County Disposal Sites CSA	-	-	11,831,440	12,381,318	11,831,440	12,381,318	(4.44)
Boulder Creek CSA	-	-	317,212	326,541	317,212	326,541	(2.86)
Rolling Woods CSA	-	-	57,258	46,093	57,258	46,093	24.22
Septic Tank Maintenance CSA	-	-	996,508	793,196	996,508	793,196	25.63
Freedom County Sanitation District	-	-	280,406	551,016	280,406	551,016	(49.11)
Davenport Sanitation District	-	-	501,029	401,144	501,029	401,144	24.90
Place Del Mer CSA	-	-	67,778	35,668	67,778	35,668	90.02
Sand Dollar Beach CSA	-	-	180,705	148,206	180,705	148,206	21.93
Trestle Beach CSA	-	-	29,721	25,734	29,721	25,734	15.49
Summit West CSA	-	-	4,239	3,937	4,239	3,937	7.67
Graham Hill CSA	-	-	6,101	7,142	6,101	7,142	(14.58)
Total expenses	<u>355,041,747</u>	<u>368,432,900</u>	<u>14,272,397</u>	<u>14,719,995</u>	<u>369,314,144</u>	<u>383,152,895</u>	(3.61)
Change in net assets	9,895,062	(26,252,058)	419,377	(1,277,622)	10,314,439	(27,529,680)	(137.47)
Net assets, beginning of year	65,679,138	63,694,546	35,745,795	39,610,159	101,424,933	103,304,705	(1.82)
Prior period adjustments	285,271,142	28,236,650	-	(2,586,742)	285,271,142	25,649,908	1012.17
Net assets, end of year	<u>\$ 360,845,342</u>	<u>\$ 65,679,138</u>	<u>\$ 36,165,172</u>	<u>\$ 35,745,795</u>	<u>\$ 397,010,514</u>	<u>\$ 101,424,933</u>	291.43

### Analysis of Change in Net Assets

The County's net assets increased by \$10,314,439 (exclusive of prior period adjustments) during the current fiscal year. These increases are explained in the government and business-type activity discussion below.

**Governmental activities** increased the County's net assets by \$9,895,062, thereby accounting for 96% of the total increase in net assets of the County. Key elements of this increase are as follows:

- \$7.2 million judgment settlement
- \$2.4 million increased interest savings
- \$7 million increase in property tax growth
- \$1.3 million increase from transient occupancy taxes and deed transfer taxes

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The decrease in expenditures is largely due to the completion of major public works projects, and the elimination of operating transfers in and operating transfers out in the public protection category.

### FINANCIAL ANALYSIS OF THE COUNTY'S FUNDS

As noted earlier, the County uses fund accounting to ensure and demonstrate compliance with financial related legal requirements.

#### Governmental Funds

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

At June 30, 2005, the County's governmental funds reported combined ending fund balances of \$142,716,838, a decrease of \$9,444,021 (exclusive of prior period adjustments) in comparison with the prior year. Approximately 70% or \$100,351,231 of the combined ending fund balances constitutes unreserved fund balance, which is available to meet the County's current and future needs, of which, \$28,958,359 is available for the County's General Fund. The remainder of fund balance is reserved to indicate that it is not available for new spending because it has been committed: (1) \$13,193,183 to pay debt service, (2) \$6,765,585 to fund asset acquisitions, (3) \$13,540,983 to liquidate contractual commitments of the period, and (4) \$8,865,856 for a variety of other purposes.

Revenues for governmental functions totaled \$364,256,179 in fiscal year 2004-2005, which represents an increase of \$21,440,111, or 6.25% from fiscal year 2003-2004. Expenditures for governmental functions, totaling \$372,622,951, increased by \$15,614,419, or 4.37% from fiscal year 2003-2004. In the fiscal year 2004-2005, expenditures for governmental functions exceeded revenues by \$8,366,772.

The general fund is the primary operating fund of the County. At June 30, 2005, unreserved fund balance of the general fund was \$26,807,546 while its total fund balance was \$28,958,359. The undesignated portion plus encumbrances totaled \$21,634,900 and were used to finance the 2005-2006 budget. As a measure of the general fund's liquidity, it may be useful to compare both unreserved fund balance and total fund balance to total fund expenditures. Unreserved general fund balance represents 9% of the total general fund expenditures of \$291,617,807, while its total fund balance represents 10% of that same amount. The unreserved portion of the general fund balance reflects budget savings, without which would necessitate further budgetary reductions.

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### Management's Discussion & Analysis For the Year Ended June 30, 2005

The Redevelopment Agency is a major special revenue fund of the County. At June 30, 2005, unreserved/designated fund balance was \$53,279,577 while its total fund balance was \$67,269,463. Designations include \$26,207,264 for Redevelopment Agency projects and \$27,072,313 for Redevelopment Agency debt service.

The following table presents the amount of revenues from various sources as well as increases or decreases from the prior year:

#### Revenues Classified by Source Governmental Funds

	2005	% of Total	2004	% of Total	Change	% of Change
Taxes and assessments	\$ 97,505,827	26.77	\$ 79,092,566	23.07	\$ 18,413,261	23.28
License and permits	10,071,972	2.77	9,013,130	2.63	1,058,842	11.75
Fines and forfeitures	12,783,894	3.51	5,198,755	1.52	7,585,139	145.90
Use of Money and Property	5,802,129	1.59	3,672,892	1.07	2,129,237	57.97
Intergovernmental	182,007,281	49.97	184,744,588	53.89	(2,737,307)	(1.48)
Charges for Services	47,737,922	13.11	49,785,849	14.52	(2,047,927)	(4.11)
Other Revenues	8,347,154	2.29	11,308,288	3.30	(2,961,134)	(26.19)
Total	<u>\$ 364,256,179</u>	<u>100%</u>	<u>\$ 342,816,068</u>	<u>100%</u>	<u>\$ 21,440,111</u>	<u>6.25</u>

The following provides an explanation of revenues by source that changed significantly from the prior year:

The changes are primarily due to the State buyout of Motor Vehicle in Lieu taxes in exchange for property tax revenues, and the loss of the ¼ cent sales tax revenues previously accounted for as intergovernmental revenues.

The other significant increase was derived from the \$7.2 million favorable judgment from the new Emeline Avenue Health Facilities building.

The following table presents expenditures by function compared to prior year amounts:

#### Expenditures Classified by Function Governmental Funds

	2005	% of Total	2004	% of Total	Change	% of Change
General government	\$ 25,717,788	6.90	\$ 23,638,513	6.62	\$ 2,079,275	8.80
Public protection	104,108,066	27.94	105,349,946	29.51	(1,241,880)	(1.18)
Public ways and facilities	42,176,057	11.32	26,519,216	7.43	15,656,841	59.04
Health and sanitation	83,982,180	22.54	83,237,724	23.32	744,456	0.89
Public assistance	84,639,192	22.71	85,584,648	23.97	(945,456)	(1.10)
Education	3,971,263	1.07	4,016,639	1.13	(45,376)	(1.13)
Recreation and culture	7,439,779	2.00	7,917,550	2.22	(477,771)	(6.03)
Capital outlay	3,825,553	1.03	5,417,219	1.52	(1,591,666)	(29.38)
Debt service - bond redemption	7,136,022	1.92	4,512,403	1.26	2,623,619	58.14
Debt service - issue cost	334,720	0.09	2,117,335	0.59	(1,782,615)	(84.19)
Debt service - interest and fiscal charges	9,292,331	2.49	8,697,339	2.44	594,992	6.84
Total	<u>\$ 372,622,951</u>	<u>100%</u>	<u>\$ 357,008,532</u>	<u>100%</u>	<u>\$ 15,614,419</u>	<u>4.37</u>



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The County Disposal Sites CSA had total net assets of \$27,933,454 at June 30, 2005, of which \$10,467,818 is unrestricted.

The following table shows the Enterprise Funds' actual revenues, expenses and results of operations for the current fiscal year:

	Major Fund		Total
	County Disposal Sites CSA	Nonmajor Funds	
Operating revenues	\$ 11,342,862	\$ 2,476,501	\$ 13,819,363
Operating expenses	(11,658,666)	(2,420,863)	(14,079,529)
Operating loss	(315,804)	55,638	(260,166)
Net non-operating revenues/(expenses)	597,352	187,551	784,903
Net income/(loss) before contributions	281,548	243,189	524,737
Capital contributions	-	20,192	20,192
Chang in net assets	\$ 281,548	\$ 263,381	\$ 544,929

The net income before contributions of the enterprise funds was \$524,737.

The internal service funds' activities attributable to the enterprise funds amounts to a decrease in net assets of \$2,798,434.

**GENERAL FUND BUDGETARY HIGHLIGHTS**

After the adoption of the budget, the final budget was increased due to additional financial resources made available from the State and Federal Agencies. Actual expenditures were \$8 million less than the original budget, excluding appropriations for general contingencies. The 2004-05 total expenditures were \$.6 million less than the prior fiscal year or .19%. This is due to salary savings, and the deferral of capital projects and other spending.

The original budget estimates for revenues were \$.6 million under budget. The designations decreased by \$464,850 for the Health Services facility. The undesignated fund balance increased by \$8,134,772 from 2003-04. This was mostly due to the favorable judgment of \$7.2 million for the Emeline Avenue Health Services building. Designations and Undesignated fund balance reflect a total increase of \$7,669,922 from 2003-04.

For additional information, readers should refer to the letter of transmittal.

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## Management's Discussion & Analysis For the Year Ended June 30, 2005

### CAPITAL ASSET AND DEBT ADMINISTRATION

#### Capital Assets

The County's capital assets for its governmental and business-type activities as of June 30, 2005 totaled \$455,091,693 (net of accumulated depreciation). This investment in capital assets includes land, construction in progress, infrastructure, buildings and structures, and equipment. The increase in the County's restated investments in capital assets for the current period was \$299,956,361 or 193.35%.

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

The County implemented the GASB 34 infrastructure requirements. Capital assets acquired after June 1980 are now being reported for the first time.

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.

Capital assets for the governmental and business-type activities are presented below to illustrate changes from the prior year:

	Governmental Activities		Business-Type Activities		Total		Variance %
	2005	Restated 2004	2005	2004	2005	2004	
	Land	\$ 48,867,561	\$ 43,352,752	\$ 1,858,849	\$ 1,858,849	\$ 50,726,410	
Construction in progress	4,236,840	870,501	-	-	4,236,840	870,501	386.71
Infrastructure	455,170,542	440,106,814	-	-	455,170,542	440,106,814	3.42
Buildings and structures	97,454,395	94,046,031	30,983,758	28,643,462	128,438,153	122,689,493	4.69
Equipment	41,851,178	46,709,528	8,934,197	8,646,820	50,785,375	55,356,348	(8.26)
Total	<u>\$ 647,580,516</u>	<u>\$ 625,085,626</u>	<u>\$ 41,776,804</u>	<u>\$ 39,149,131</u>	<u>\$ 689,357,320</u>	<u>\$ 664,234,757</u>	3.78

Additional information on the County's capital assets can be found in Note 5 on pages 64-66 of this report.

#### Long-term Debt

The County's long-term debt for governmental and business-type activities are presented below to illustrate changes from the prior year:

	Governmental Activities		Business-Type Activities		Total		Variance %
	2005	2004	2005	2004	2005	2004	
Tax allocation bonds	\$ 108,147,097	\$ 110,815,618	\$ -	\$ -	\$ 108,147,097	\$ 110,815,618	(2.41)
Refunding certificates of participation	36,540,565	27,177,022	-	-	36,540,565	27,177,022	34.45
Lease revenue bonds	-	10,595,000	-	-	-	10,595,000	(100.00)
Lease revenue refunding bonds	12,027,888	15,064,406	-	-	12,027,888	15,064,406	(20.16)
Certificates of participation	22,441,465	23,027,378	-	-	22,441,465	23,027,378	(2.54)
Revenue bonds	3,240,000	3,565,000	-	-	3,240,000	3,565,000	(9.12)
CA Health Facility	1,233,252	1,382,106	-	-	1,233,252	1,382,106	(10.77)
Loans payable	2,051,728	2,887,106	1,816,991	2,373,552	3,868,719	5,260,658	(26.46)
Capital leases	337,465	670,861	-	-	337,465	670,861	(49.70)
Local assessment bonds	-	40,000	-	-	-	40,000	(100.00)
Total	<u>\$ 186,019,460</u>	<u>\$ 195,224,497</u>	<u>\$ 1,816,991</u>	<u>\$ 2,373,552</u>	<u>\$ 187,836,451</u>	<u>\$ 197,598,049</u>	(4.94)

## COUNTY OF SANTA CRUZ, CALIFORNIA

### Management's Discussion & Analysis For the Year Ended June 30, 2005

For the governmental activities, the County had total long-term debt outstanding of \$186,019,460 as compared to \$195,224,497 in the prior year (excluding compensated absences and estimated claims). This amount was comprised of \$108,147,097 of Redevelopment Tax Allocation Bonds, \$36,540,565 of refunding certificates of participation, \$12,027,888 of lease revenue refunding bonds, \$22,441,465 of certificates of participation, \$3,240,000 of revenue bonds, \$1,233,252 of California Health facilities financing authority debt, \$2,051,728 of loans payable, and \$337,465 of capital leases. During the year, retirement of debt amounted to \$19,059,451, and new debt issuance amounted to \$10,512,751.

For the business-type activities, the County had total long-term debt outstanding of \$1,816,991 as compared to \$2,373,552 in the prior year (excluding post-closure liability). This amount was all loans payable. During the year, retirement of debt amounted to \$556,561. There were no additions to long-term debt for business-type activities.

The component unit, Santa Cruz Sanitation District, had total long-term debt outstanding of \$28,696,632 as compared to \$30,392,736 in the prior year. This amount was comprised of \$9,335,000 of Waste Water Revenue Refunding Bonds, \$950,000 of Limited Obligation Refunding Improvement Bonds, \$18,370,380 of Loans Payable, and \$41,252 of Unamortized Discount. During the year, retirement of debt amounted to \$12,022,356, and new debt issuance amounted to \$10,326,252.

The County's total debt decreased by \$11,457,802, or 5.0% during the current fiscal year (excluding compensated absences, estimated claims, and post-closure liability). The key factor in this increase/decrease resulted primarily from the scheduled principal payments and the refunding of the 1995A Lease Revenue Refunding Bonds.

Additional information on the County's long-term debt can be found in Note #9 on pages 68-78 of this report.

### **ECONOMIC FACTORS AND NEXT YEAR'S BUDGET RATES**

The County financial position is presently in line with the budgetary parameters set by the Board of Supervisors and as amended for the 2004-05 fiscal year. The General Fund's ending undesignated year end fund balance increased by \$8,134,772 from the prior year.

Real property assessment at January 1, 2005 showed an average increase of 9.6% over the prior year, and property tax growth is expected to continue in the next fiscal year.

Sales tax revenue is expected to increase as the economy continues to recover. Actual revenues for the 2004-05 fiscal year were slightly higher than our budget estimates.

## COUNTY OF SANTA CRUZ, CALIFORNIA

### Management's Discussion & Analysis For the Year Ended June 30, 2005

The financial deficits of the State of California have shifted financial responsibilities to local agencies. Counties must continue to give up monthly flows of revenue to improve the State's cash flows. Because of this cash flow shift, the County of Santa Cruz had to increase its working capital borrowing by \$8 million for 2004-05 and additional \$1 million in 2005-06.

Constitutional Amendment 1A, which was approved on the November 2004 ballot, redefines the State's fiscal policy toward local government. This Proposition, under specified conditions, limits the State's ability to extract more local property taxes and requires payment for future and past mandated costs of Counties, Cities, and Districts. It further provides for the return of a portion of local property tax revenues by the year 2006-07 and repayment of unpaid State mandated programs over three years commencing in the 2006-07 fiscal year.

To finance the additional ERAF property tax shift, the County borrowed \$2.4 million from the Santa Cruz County Redevelopment Agency as allowed by law, to be repaid with interest in 2006-07 and 2007-08. This repayment is less than the expected repayment from the loan made to the State last fiscal year of \$5.3 million for the VLF gap problem which was to be repaid by statute on August 15, 2006 but was actually repaid to the County on July 26, 2005, a year earlier. Because the County used \$4 million of its working capital reserve to fund the VLF Gap, that amount has been restored in the 2005-06 final budget.

The County received a favorable judgment of \$7.2 million for construction damage caused by mold damage on a newly constructed facility of which \$2.4 million was reserved to reimburse other agencies for costs incurred prior to the settlement.

During fiscal year 2004-05, unreserved fund balance in the general fund increased to \$26,807,546. The County has appropriated the full amount for spending in the 2005-06 fiscal year budget, except for \$7 million designated for specific purposes. The County is expected to end the fiscal year with a \$16 million balance remaining to avoid using designations and budget reductions without other unanticipated revenues.

In October, 2005, the County adopted the final budget for the 2005-06 fiscal year. Due to slow economic growth in revenues and increased labor costs, departments submitted budgets that reflect minor increases or no increases in the net cost to the county.

For further discussion, please see the accompanying transmittal letter.

### **REQUEST FOR INFORMATION**

This financial report is designed to provide a general overview of the County's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Auditor-Controller's Office, County of Santa Cruz, 701 Ocean Street, Room 100, Santa Cruz, CA 95060.