Municipal Secondary Market Disclosure Information Cover Sheet

This cover sheet should be sent with all submissions made to the Municipal Securities Rulemaking Board, Nationally Recognized Municipal Securities Information Repositories, and any applicable State Information Depository, whether the filing is voluntary or made pursuant to Securities and Exchange Commission rule 15c2-12 or any analogous state statute.

See www.sec.gov/info/municipal/nrmsir.htm for list of current NRMSIRs and SIDs

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IF THIS FILING RELATES TO ALL SECURITIES ISSUED BY THE ISSUER OR ALL SECURITIES OF A SPECIFIC CREDIT or issued under a single indenture:

Issuer's Name (please include name of state where Issuer is located):

THE CITY OF SAN DIEGO, CALIFORNIA (STATE: CALIFORNIA)

1991 General Obligation Bonds (Public Safety Communications Project): CUSIP 797236

San Diego Open Space Park Facilities District No. 1 General Obligation Bonds Refunding Series 1994: CUSIP 797290

THE CITY OF SAN DIEGO, CALIFORNIA (OBLIGOR, PURSUANT TO CERTIFICATES OF PARTICIPATION); (STATE: CALIFORNIA)

2003 Certificates of Participation (1993 Balboa Park/Mission Bay Park Refunding) Evidencing Undivided Proportionate Interests in Lease Payments to be Made by the City of San Diego Pursuant to a Lease with the San Diego Facilities and Equipment Leasing Corporation: CUSIP 797260

SAN DIEGO FACILITIES AND EQUIPMENT LEASING CORPORATION OF THE CITY OF SAN DIEGO (STATE: CALIFORNIA)

Certificates of Undivided Interest in Installment Payments Payable from Net System Revenues of the Water Utility Fund of the City of San Diego, California, Series 1998: CUSIP 797263

CITY OF SAN DIEGO/MTDB AUTHORITY (STATE: CALIFORNIA)

2003 Lease Revenue Refunding Bonds (San Diego Old Town Light Rail Transit Extension Refunding): CUSIP 797448

CONVENTION CENTER EXPANSION AUTHORITY (STATE: CALIFORNIA)

Lease Revenue Bonds, Series 1998 (City of San Diego, California, as Lessee): CUSIP 79727L

PUBLIC FACILITIES FINANCING AUTHORITY OF THE CITY OF SAN DIEGO (STATE: CALIFORNIA);

Lease Revenue Bonds Series 2007A (Ballpark Refunding):   CUSIP 797299

Lease Revenue Bonds Series 2002B (Fire and Life Safety Facilities Project): CUSIP 797299

Subordinated Water Revenue Bonds, Series 2002 (Payable Solely from Subordinated Installment Payments Secured by Net System Revenues of the Water Utility Fund): CUSIP 79730C

Other Obligated Person's Name (if any):____

(Exactly as it appears on the Official Statement Cover)

Provide six-digit CUSIP* number(s), if available, of Issuer: See above section for all CUSIP numbers.

*(Contact CUSIP's Municipal Disclosure Assistance Line at 212.438.6518 for assistance with obtaining the proper CUSIP numbers.)

TYPE OF FILING:

[X] Electronic ______ pages

Paper (no. of pages attached) _______

If information is also available on the Internet, give URL: **NOT AVAILABLE**____

WHAT TYPE OF INFORMATION ARE YOU PROVIDING? (Check all that apply)

A. Annual Financial Information and Operating Data pursuant to Rule 15c2-12
(Financial information and operating data should not be filed with the MSRB.)

Fiscal Period Covered:

B. Audited Financial Statements or CAFR pursuant to Rule 15c2-12Fiscal Period Covered:

C. Notice of a Material Event pursuant to Rule 15c2-12 (Check as appropriate)

1. Principal and interest payment delinquencies _____
2. Non-payment related defaults _____
3. Unscheduled draws on debt service reserves reflecting financial difficulties _____
4. Unscheduled draws on credit enhancements reflecting financial difficulties _____
5. Substitution of credit or liquidity providers, or their failure to perform _____
6. Adverse tax opinions or events affecting the tax-exempt status of the security _____
7. Modifications to the rights of security holders _____
8. Bond calls _____
9. Defeasances _____
10. Release, substitution, or sale of property securing repayment of the securities _____
11. **Rating changes__X__**

D. Notice of Failure to Provide Annual Financial Information as Required

E. Other Secondary Market Information (Specify):____

I hereby represent that I am authorized by the issuer or obligor or its agent to distribute this information publicly:
Issuer Contact:

Name_____**MARY LEWIS** ______________________________Title_____**CHIEF FINANCIAL OFFICER** _____________
Employer_____**CITY OF SAN DIEGO**____
Address_____**202 C STREET, MAIL STATION 9A**__________City ___**SAN DIEGO**__State__**CA**__Zip Code__**92101**

Dissemination Agent Contact:

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Address_____**202 C STREET, MAIL STATION 9A**__________City ___**SAN DIEGO**__State__**CA**__Zip Code__**92101**
Relationship to Issuer: __**DISCLOSURE REPRESENTATIVE**

Press Contact:
Name_____ ________________ ___________________________Title___ ____
Employer_____ ____
Address____ ____City ____ __State______Zip Code__ ____________________

Dated December 12, 2008

NOTICE IS HEREBY GIVEN that on December 11, 2008, Fitch Ratings (Fitch) upgraded its ratings on the City of San Diego, California's general obligation bonds, lease revenue bonds, certificates of participation and water system obligations identified on the cover hereof. Specifically, Fitch upgraded to "A+" from "BBB+" its underlying rating with a stable outlook on the City's general obligation bonds, and upgraded to "A" from "BBB-" its underlying rating with a stable outlook on the City's lease revenue bonds and certificates of participation. Fitch also upgraded its underlying ratings to "AA-" from "BBB+" on the City's water utility senior-lien revenue bonds and to "A+" from "BBB" on the City's subordinate water utility revenue bonds. A new rating of "A" was issued on the City of San Diego Lease Revenue Refunding Bonds, Series 2007 (Ballpark Refunding), also with a stable outlook.

On December 11, 2008, Moody's Rating Services (Moody's) upgraded its underlying ratings to "A1" from "A2" on the City's water utility senior-lien revenue bonds and to "A2" from "A3" its underlying rating on the City's water utility subordinate water utility revenue bonds, both with a stable outlook.

On December 12, 2008, Standard & Poor's Rating Service (S&P) affirmed its underlying ratings of "AA-" on the City's water utility senior-lien revenue bonds and "A+" on the City's subordinate water utility revenue bonds, both with a stable outlook.

The ratings reflect the view of the rating agencies and any desired explanation of the significance of a rating should be obtained from the respective rating agency. Such ratings are not a recommendation to buy, sell or hold any City indebtedness. Generally, a rating agency bases its ratings on the information and materials furnished to it and on investigations, studies and assumptions of its own. There is no assurance that such ratings will continue for any given period or that such ratings will not be revised downward or withdrawn entirely provided, if in the view of such rating agency, circumstances warrant. Any such downward revision or withdrawal of such ratings may have an adverse effect on the market price or marketability of the City's obligations identified on the cover page hereof.

DATED Dec. 18, 2008

CITY OF SAN DIEGO

By: Mary Lewis

Mary Lewis
Chief Financial Officer

Distribution: Nationally Recognized Municipal Securities Information Repositories

EXHIBIT A

Nationally Recognized Municipal Securities Information Repositories approved by the Securities and Exchange Commission:

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Tagging Info

Fitch Upgrades San Diego, California GOs to 'A+'; Lease Revs to 'A' & Water Revs to 'AA-'

Ratings
11 Dec 2008 8:04 PM (EST)

Fitch Ratings-San Francisco-12 December 2008: Fitch Ratings has upgraded and removed from Rating Watch Positive the following ratings for the City of San Diego, California (the city) as outlined below:

*San Diego
--General obligation (GO) bonds to 'A+' from 'BBB+';
--Certificates of participation (1993 Balboa Park/Mission Bay Park) series 2003 to 'A' from 'BBB-'.

Fitch has also upgraded and removed from Rating Watch Positive several other tax-supported and water revenue bonds issued by the city and related entities.

San Diego Public Facilities Financing Authority
--Lease revenue bonds series 2002B to 'A' from 'BBB-';
--Subordinated water revenue bonds, series 2002 to 'A+' from 'BBB'.

San Diego Facilities and Equipment Leasing Corporation
--Certificates of undivided interest, series 1998 (secured by a senior lien on water revenues) to 'AA-' from 'BBB+'.

San Diego Metropolitan Transit Development Board
--Lease revenue refunding bonds series 2003 to 'A' from 'BBB-'.

Convention Center Expansion Financing Authority
--Lease revenue bonds series 1998A to 'A' from 'BBB-'.

Fitch's rating actions affect a total of $760 million in par.

Fitch has also assigned the following new ratings:

San Diego Public Facilities Financing Authority
--$152.8 million ballpark lease revenue refunding bonds, series 2007A 'A';
--$63 million water revenue bonds, refunding series 2009A 'AA-' (for a bond sale to take place via negotiation on or about Jan. 12, 2009).

The Rating Outlook is Stable.

Fitch has also assigned ratings to a new water revenue bond series and a lease-secured issue not previously rated by Fitch, also with a Stable Rating Outlook.

Fitch will release rating action commentaries with details on key rating factors for these actions tomorrow.

Fitch will review its 'BBB+' rating, on San Diego Public Facilities Financing Authority's $893.7 million in outstanding sewer revenue bonds within the next several months as the city gets closer to a parity bond issuance. This rating currently is on Rating Watch Positive.

Contact: Amy S. Doppelt +1-415-732-5612 San Francisco or Douglas Scott +1-512-215-3725, Austin.

Fitch issued an exposure draft on July 31, 2008 proposing a recalibration of tax-supported and water/sewer revenue bond ratings, which, if adopted, may result in an upward revision of these ratings (see Fitch Research on 'Exposure Draft: Reassessment of Municipal Ratings Framework"). Fitch has deferred its final determination on municipal recalibration due to market conditions and plans to revisit the recalibration in the first quarter of 2009 (see press release 'Fitch Defers Final Determination on U.S. Municipal Ratings Recalibration,' dated Oct. 7, 2008).

Media Relations: Cindy Stoller, New York, Tel: +1 212 908 0526, Email: cindy.stoller@fitchratings.com.

Fitch's rating definitions and the terms of use of such ratings are available on the agency's public site, 'www.fitchratings.com'. Published ratings, criteria and methodologies are available from this site, at all times. Fitch's code of conduct, confidentiality, conflicts of interest, affiliate firewall, compliance and other relevant policies and procedures are also available from the 'Code of Conduct' section of this site.

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New Issue: **San Diego (City of) CA Water Enterprise**

MOODY'S UPGRADES TO A1 FROM A2 THE RATING ON CITY OF SAN DIEGO'S SENIOR LIEN WATER REVENUE BONDS

SUBORDINATE LIEN RATING UPGRADED TO A2 FROM A3

San Diego (City of) CA Water Enterprise
Water/Sewer
CA

Moody's Rating

ISSUE	RATING
Water Revenue Bonds, Refunding Series 2009A	A1

Sale Amount	$65,000,000
Expected Sale Date	01/16/09
Rating Description	Water Revenue

Opinion

NEW YORK, Dec 16, 2008 -- Moody's has assigned an A1 rating to the Water Revenue Bonds, Refunding Series 2009A, of the City of San Diego's Water Enterprise. We have also upgraded to A1 from A2 the rating on the utility's parity senior lien water revenue bonds and upgraded to A2 from A3 the rating on the system's subordinate bonds. In addition, we have changed the outlook on these ratings to stable from negative. The rating upgrade is based on the system's significantly improved financial performance since 2005, which is confirmed by the city's release over the past two years of five Comprehensive Annual Financial Reports (CAFRs), for the fiscal years ending 2003 through 2007. The fundamental strength of the enterprise remains a key credit factor, including its essentiality and its large, strong, and diverse service area, which provides a relatively high degree of revenue stability. The ratings also reflect the utility's favorable debt position, which is likely to remain manageable despite the expected addition of a significant amount of new debt during the next five years necessitated by the current Capital Improvement Program. The stable outlook reflects our expectation that, despite the anticipated increase in debt, rate increases already in place through 2011 will continue to provide strong debt service coverage, and with the planned capital improvements, the system will have met most of its long term capital needs for the foreseeable future. The proceeds of the current issue will be used to refund $57 million in privately placed short term debt maturing on January 30, 2009.

Following the current sale, the ratings will apply to approximately $310 million in senior lien debt and approximately $272 million in subordinated debt. The system also has approximately $150 million in additional subordinated debt which was also privately placed and will mature in August 2009.

FINANCIAL RESULTS HAVE IMPROVED SIGNIFICANTLY

Since their low point in 2003, the water system's financial operations have improved steadily. Increased water sales, largely through growth, combined with very tight controls on Operating and Maintenance (O&M) expenditures, which increased by an average annual rate of 4.1% between 2004 and 2007, enabled the utility to increase total debt service coverage from 1.02 times in 2004 to 1.99 times in 2007. These coverage levels, which include capacity charge revenues, improved despite a notable decrease in such charges. Largely as a result of the weak housing market, which affected San Diego earlier than other parts of the state, capacity charge revenues decreased from $17.7 million in 2004 to $13.7 million in 2007. This downward trend is continuing, despite a 19.5% increase in the capacity charge rate in 2008. Nonetheless, the system was able to continue to improve its financial position. The utility's strong financial performance in recent years enabled it to increase unrestricted cash from $141 million in 2004 to $197 million in 2007, which affords the system a very strong liquidity position, thereby enhancing operating flexibility.

Bolstered by 6.5% annual rate increases, which came into effect in 2008 and are approved through 2011, the utility's favorable trend in financial operations is likely to continue for the near term. Despite the current tightness in water supply throughout the state, and a significant amount of additional planned debt, the city's reasonable projections indicate combined debt service coverage levels at or above 1.6 times through 2013. In addition to the rate increases, the projections include usage decreases due to conservation of 7.5% in 2009 and 15% in 2010, and only a modest increase in connections. Managing O&M expenses, which increase at an annual rate of 3.2% through 2013, is also key to these projections.

The city's formal reserve policies call for the maintenance of a 45-day operating reserve, funded at $19.9 million in fiscal 2008. The city also maintains an emergency capital reserve of $5 million. A separate $7.1 million "Secondary Purchase Reserve" is available to fund emergency water purchases. The city also established a rate stabilization fund, totaling $20.5 million in fiscal 2008. While these funds are part of its formal reserves, they are quite modest given the size of the system's operations. However, our favorable view of the system's liquidity position is based on its unrestricted cash, which is very strong as mentioned above. Given the utility's reasonable operating projections, we expect the system's overall cash position to remain strong.

LARGE, STRONG AND DIVERSE SERVICE AREA

The ratings on the city's water revenue bonds are in large part based upon the size, diversity and economic strength of the system's 330 square mile service area, which encompasses the city of San Diego as well as a few small areas outside the city limits. The enterprise provides primarily retail water service to the entire service area, which has a population of about 1.3 million. The city's economy and tax base exhibited strong and steady growth since the late-1990's until the onset of the recent statewide real estate downturn. The city is affected by the deterioration of the residential real estate market, with home prices falling about 30% year-over-year as of October 2008. However, given the disparity between market and assessed values, the decline in market value has not translated into a decrease in AV. The city's AV grew in fiscal 2009 by 5.7%, an annual rate substantially slower than any since 1998, but nonetheless positive. By comparison, San Diego County's total AV rose by only 2.7%.

Historical retail service connections had grown steadily at approximately 1% annually since 2000 to reach nearly 270,000 in 2004. However, since then annual increases have averaged a much lower 0.33% reaching just 274,398 in 2008. Single family domestic customers account for 42.5% and other domestic customers add 18.7% of water revenues (unaudited), while commercial/industrial customers represent 20.5%. There are no dominant commercial or industrial customers; the largest wholesale customer, California-American Water Company, accounted for 3.4% of fiscal 2008 revenues (unaudited). The only retail customers responsible for more than 1% of total water fund revenues were the City of San Diego which accounted for 4.0% at fiscal year end 2008, and the U.S. Navy which accounted for 2.76% (again, both figures unaudited).

FAVORABLE DEBT POSITION WILL LIKELY BE RESTORED AFTER AMBITIOUS CAPITAL PLAN FUNDED LARGELY WITH NEW DEBT

At the end of 2007, the city's water system debt, including approximately $20 million SRF debt, stood at approximately $640 million which resulted in a debt ratio of 30.5%, consistent with the nationwide A1 median of 30.1%. This total amount includes $57 million in short term debt, privately placed in 2007, which will be refunded with the current offering. In 2008, the city borrowed another $150 million through private placement, as market access limitations persisted. The utility's capital needs are significant and it expects to spend $724 million on projects between 2009 and 2013, 80% of the cost of which is expected to be financed with debt. The largest components of the plan are improvement and expansion of its treatment plants ($207 million) and pipe replacement ($279 million). In 2009 the city expects to borrow approximately $400 million, including the current issue. Less than $200 million will be new money as the 2008 borrowing will also be refunded this year. Through 2013 another $330 million of new money borrowing is expected, increasing the utility's debt ratio to approximately 50%, which remains manageable. And notably, at the end of the current capital improvement program, the utility will be compliant with all regulations and have sufficient capacity for the foreseeable future.

The current bonds are expected to be secured by a senior lien on the net revenues of the system. The security provisions are typical with a rate covenant and additional bonds test of 1.2 times. The debt service reserve requirement is subject to a typical three tier test and will be met with bond proceeds. The additional bonds test for all debt is 1.0 times although we expect actual coverage levels to be much higher.

POSSIBLE SUPPLY REDUCTION IN THE NEAR TERM

The city relies on San Diego County Water Authority for more than 80% of its supply. Like most of Southern California, the Authority is dependant upon the Metropolitan Water District of Southern California (MWD) for most of its supply. MWD's supply, in turn, has been affected by drought conditions as well as various legal/environmental challenges affecting the state's ability to export water from the Bay-Delta. The Authority delivered an average of approximately 688,000 acre-feet of water per year over the past five years, supplying about 89% of its members' needs. Approximately three-quarters of the water that the Authority provides its members it purchases from MWD; the Authority is the largest single purchaser of MWD water, representing 26% of MWD deliveries. For 2008 the Authority assumed 81.7% of water sold would come from MWD, 8.6% from the Imperial Irrigation District, 6.2% from the All-American and Coachella Canals and 3.5% from spot water transfers. The Authority's storage capabilities are increasing. Within the service area storage is somewhat limited by comparison with annual deliveries: the Authority has 24,000 acre-feet of emergency storage in the Olivenhain Reservoir, and agreements to store approximately 60,000 acre-feet in member agency reservoirs. The Authority currently has a pilot groundwater storage project in the Central Valley which can store up to 30,000 acre-feet. The Authority's large capital improvement plan is focused largely on diversifying its sources of supply and increasing its storage capacity. With the current drought, the city has implemented voluntary conservation measures which will reduce usage.

Outlook

The stable outlook for debt obligations of the water enterprise reflects the stable financial operations of the utility and our expectation that the city will be able to implement its capital plan while preserving its financial strength. The current economic recession and water supply questions pose some potential difficulties for the utility. The utility's successful navigation through the recession, the drought and its sizable capital plan could improve bondholder security.

KEY STATISTICS

2008 estimated population served: 1.3 million

Senior debt service coverage, fiscal 2007: 3.9x

Total debt service coverage, fiscal 2007: 1.99x

Rate Covenant: 1.20x

Additional Bonds Test: 1.20x

Operating Ratio, Fiscal 2007: 81.8%

Net Working Capital, fiscal 2007: $244 million (96.1% of operations and maintenance expense)

The last rating action was on February, 15 2006 when the ratings on the utility's ratings were affirmed.

The principal methodology used in rating the utility's bonds was Analytical Framework For Water And Sewer System Ratings which can be found at www.moodys.com in the Credit Policy & Methodologies directory, in the Ratings Methodologies subdirectory. Other methodologies and factors that may have been considered in the process of rating this issuer can also be found in the Credit Policy & Methodologies directory.

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Ratings

Back

San Diego Water Revenue Bond Ratings Affirmed

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Publication date: 12-Dec-08, 12:53:16 EST
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- Current Ratings

NEW YORK (Standard & Poor's) Dec. 12, 2008--Standard & Poor's Ratings Services affirmed its 'AA-' underlying rating (SPUR), and stable outlook, on San Diego, Calif.'s senior-lien water revenue bonds, and its 'A+' SPUR, and stable outlook, on the city's subordinate-lien water revenue bonds. We also assigned a 'AA-' SPUR and stable outlook to the $62.985 million series 2009A water revenue refunding bonds.

The ratings reflect our view of the city's following credit strengths:

-- Good historical and projected debt service coverage, even after excluding one-time capacity charge revenue;

-- Strong cash reserves bolstered by targeted cash reserve policies;

-- Council-approved system rate increases through fiscal 2011; and

-- A diverse service area economy and customer base.

We believe offsetting credit concerns include the system's:

-- Significant capital improvement plan (CIP) driven by regulatory concerns in the next five years and additional long-term capital and rate pressures related to water supply needs;

-- Required annual approvals by city council for customer water charge increases related to passed-through water purchase costs, which are also subject to Proposition 218 requirements; and

-- Legal provisions that allow net system revenue calculations to include transfers from the rate stabilization fund and secondary purchase funds.

A senior-lien pledge of installment payments payable from the net revenues of the city's water system secures the series 2009A water revenue refunding bonds and series 1998 certificates of undivided interest. A subordinate-lien pledge secures the series 2002 bonds. Series 2009A bond proceeds will be used to pay off $57 million in note principal at the end of January 2009; the city council has authorized the issuance of the long-term series 2009A bonds at a market interest rate of up to 10%.

After issuing the 2009A refunding bonds, the water system will have about $750 million of revenue bonds, state revolving fund loans, and private placement notes outstanding secured by senior and subordinate liens of the system's net revenue. The system has no variable rate debt outstanding. Coverage of senior debt service on the senior-lien debt by net system revenue in fiscal 2007 was a strong 3.6x, in our opinion. Total combined senior and subordinate debt service, was also what we consider strong at 1.8x. Based on fiscal 2008 unaudited results, system officials estimate net system income--including operating receipts, capacity charges, and interest earning revenue--provided what we consider strong senior and combined debt service coverage of approximately 3.0x and 1.5x, respectively. Fiscal 2008 unaudited results reflect a 38% decline in one-time capacity charges due to slowing residential construction. Excluding all capacity charges, estimated senior and combined debt service coverage in fiscal 2008 drops to 2.6x and what we view as a good 1.3x, respectively. Coverage of fixed water purchase charges and combined debt service, excluding capacity charges, totaled an adequate 1.15x in fiscal 2008, in our opinion, based on unaudited results.

Fiscal 2009 projections include a 6.5% rate increase approved by council and an 8.4% rate increase, effective Jan. 1, 2009, to offset rising water purchase costs and a one-year pilot project to study the viability of increasing potable water sources through reuse and reservoir augmentation. Together with the sewer rates, overall residential rates are somewhat above-average for a regional system, at about $96 per 7,500 gallons per month, but what we believe is a still-manageable 2.5% of the city's 2007 median household effective buying income.

"The stable outlook reflects our expectation that pre-approved rate increases should help to maintain good debt service ratios in the next several years, despite the city's implementation of a large capital improvement program associated with regulatory requirements," said credit analyst Sussan Corson.

Complete ratings information is available to subscribers of RatingsDirect, the real-time Web-based source for Standard & Poor's credit ratings, research, and risk analysis, at www.ratingsdirect.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com; select your preferred country or region, then Ratings in the left navigation bar, followed by Credit Ratings Search.

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San Diego Public Facilities Financing Authority, CA

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Credit Profile		
US$62.985 mil wtr rev rfdg bnds ser 2009A due 08/01/2039		
Long Term Rating	AA-/Stable	New
San Diego certs of undivided int (payable from net sys revs of wtr util fd)		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
San Diego Pub Facs Fincg Auth, California		
San Diego, California		
San Diego Pub Facs Fincg Auth (San Diego) sub wtr (MBIA)		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

Rationale

Standard & Poor's Ratings Services affirmed its 'AA-' underlying rating (SPUR), and stable outlook, on San Diego, Calif.'s senior-lien water revenue bonds and its 'A+' SPUR, and stable outlook, on the city's subordinate-lien water revenue bonds.

The ratings reflect our view of the city's following credit strengths:

- Good historical and projected debt service coverage, even after excluding one-time capacity charge revenue;
- Strong cash reserves bolstered by targeted cash reserve policies;
- Council-approved system rate increases through fiscal 2011; and
- A diverse service area economy and customer base.

We believe offsetting credit concerns include the system's:

- Significant capital improvement plan (CIP) driven by regulatory concerns in the next five years and additional long-term capital and rate pressures related to water supply needs;

- Required annual approvals by city council for customer water charge increases related to passed-through water purchase costs, which are also subject to Proposition 218 requirements; and
- Legal provisions that allow net system revenue calculations to include transfers from the rate stabilization fund and secondary purchase funds.

A senior-lien pledge of installment payments payable from the net revenues of the city's water system secures the series 2009A water revenue refunding bonds and series 1998 certificates of undivided interest. A subordinate-lien pledge secures the series 2002 bonds. Series 2009A bond proceeds will be used to pay off $57 million in note principal at the end of January 2009; the city council has authorized the issuance of the long-term series 2009A bonds at a market interest rate of up to 10%.

Covering 400 square miles with a population of 1.3 million, San Diego's water system provides retail water services to a stable customer base consisting of 273,398 primarily residential (91%) and commercial or industrial (6%) retail accounts. The city also serves five wholesale customers, which account for 4% of total water sales revenue. As of fiscal year-end June 30, 2008, the water system's 10 leading retail customers accounted for a very diverse 11% of total water utility fund revenues, in our opinion. The city of San Diego (4% of water sales revenue) and the U.S. Navy (3%) remain the two leading customers. The water system is supplied primarily by raw water imported by the San Diego County Water Authority (CWA; 'AA+' SPUR), which accounts for more than 90% of the system's water supply. CWA, in turn, received 76% of its water from the Metropolitan Water District of Southern California (MWD; 'AAA' SPUR) in 2007.

After issuing the 2009A refunding bonds, the water system will have about $750 million of revenue bonds, state revolving fund (SRF) loans, and private placement notes outstanding secured by senior and subordinate liens of the system's net revenue. The system has no variable rate debt outstanding. Coverage of senior debt service on the senior-lien debt by net system revenue in fiscal 2007 was a strong 3.6x, in our opinion. Total combined senior and subordinate debt service—including the 2002 bonds, debt service on SRF loans, and interest on short-term notes outstanding—was also what we consider strong at 1.8x. Based on fiscal 2008 unaudited results, system officials estimate net system income—including operating receipts, capacity charges, and interest earning revenue—provided what we consider strong senior and combined debt service coverage of approximately 3.0x and 1.5x, respectively. Fiscal 2008 unaudited results reflect a 38% decline in one-time capacity charges due to slowing residential construction. Excluding all capacity charges, estimated senior and combined debt service coverage (DSC) in fiscal 2008 drops to 2.6x and what we view as a good 1.3x, respectively. Coverage of fixed water purchase charges and combined debt service, excluding capacity charges, totaled an adequate 1.15x in fiscal 2008, in our opinion, based on unaudited results.

Fiscal 2009 projections include a 6.5% rate increase approved by council and an 8.4% rate increase, effective Jan. 1, 2009, to offset rising water purchase costs and a one-year pilot project to study the viability of increasing potable water sources through reuse and reservoir augmentation. Together with the sewer rates, overall residential rates are somewhat above average for a regional system, at about $96 per 7,500 gallons per month, but what we believe is a still-manageable 2.5% of the city's 2007 median household effective buying income.

Officials have identified reserve policies to maintain cash within the system, including a targeted 70-day operating reserve to be used for unplanned operating expenditures, a secondary purchase reserve funded at 6% of annual water purchase costs to offset potential disruptions in the water supply, a $5.0 million emergency reserve for capital expenditures, and a $20.5 million rate stabilization fund. The system also maintains restricted cash reserves for debt service requirements. System officials estimate that combined cash in the operation reserve, secondary fund, rate stabilization fund, and emergency reserve in fiscals 2007 and 2008 totaled $50.6 million and $52.6 million, respectively, or what we consider to be a good 73 days' cash. Total audited cash in the system at fiscal year-end 2007 was $196 million, equivalent to 283 days of operating expenses.

The system's CIP for 2009 through 2013 totals $724 million, with 71% of the capital project expenditures related to a California Department of Health compliance order to fund pipe replacement, improve treated water storage, and treatment facility upgrades. The system has previously issued a total of $200 million in private placement notes in 2007 and 2008 and intends to use series 2009A bond proceeds to pay off $57 million of the 2007 note. We understand that in early 2009 system officials plan to issue $326 million of series 2009B long-term bonds to take out the 2008 notes and fund new capital projects. System officials intend to issue long-term debt to cover 80%, or $580 million, of the five-year CIP. We believe the CIP is likely to increase as the city continues to identify needs associated with long-term water resource planning.

In fiscals 2008 and 2009, water rates increased by 6.5% in each year and the city council has already approved a 6.5% annual increase for fiscal 2010, effective July 1, 2009. The city council also approved rate increases, effective Jan. 1, in fiscal 2008 (3%) and fiscal 2009 (8.4%) to cover pass-through charges to cover increased purchased water costs. A 3.1% portion of the 8.4% rate increase in fiscal 2009 includes a temporary rate increase to cover the costs of the one-year water reuse pilot project and sunsets in June 30, 2010. The council will annually determine pass-through charges to cover likely future increases in purchased water costs. Pass-through water charges are also subject to Proposition 218 hearings; the city has complied with notice and protest procedures and has not had any rate increase legally challenged pursuant to Proposition 218.

In our view, the senior-lien provisions in the master installment purchase agreement are somewhat permissive. Net system revenue calculations include transfers from the rate stabilization fund and secondary reserve, as well as capacity charges. The senior-lien 1.2x annual debt service (ADS) rate covenant allows debt service and revenue to be reduced to account for interest earnings on the debt service reserve of the certificates. The senior-lien provisions also require 1.2x maximum annual debt service (MADS) coverage using either historical revenues in 12 out of the past 18 months or future estimated revenues adjusted for rate increases and estimated revenue from expected water system additions, improvements, and extensions.

A subordinate-lien pledge of the water system's net revenues secures the series 2002 bonds. The system also has an SRF loan outstanding and issued short-term notes in 2007 and 2008 secured by a subordinate lien on par with the series 2002 bonds. The system covenants to maintain rates sufficient to cover total ADS by at least 1x. The series 2002 bond provisions allow additional bonds if the system can demonstrate at least 1x senior and subordinate MADS coverage by historical or future estimated net system revenues adjusted for rate increases and improvements. Provisions for both the senior and subordinate bonds include a fully funded debt service reserve for each series funded at the least of MADS, 10% of par, or 1.25x aggregate average ADS; the debt service reserve funds are cash-funded; however, the permitted investments are, in our view, somewhat permissive as they allow for investments in repurchase agreements rated in the three highest short-term rating categories.

Outlook

The stable outlook reflects our expectation that pre-approved rate increases should help to maintain good debt service ratios in the next several years, despite the city's implementation of a large CIP associated with regulatory requirements. The outlook also reflects our expectation that pass-through charges for increased water purchase costs and future rate increases will be approved, as necessary, and the system will adhere to its cash reserve policies to maintain sufficient liquidity in the system. Should a failure to continue to meet the requirements of the compliance order result in significant deterioration of DSC or liquidity, we could lower the ratings.

Water Supply

California continues to face pressure to reduce its dependence on Colorado River water, which places additional strain on MWD, CWA, and the city system to maintain a sustainable water supply. The state of California, in total, is apportioned 4.4 million acre-feet per year of Colorado River water, plus one-half of the surplus Colorado River water available collectively for Arizona, Nevada, and California. These other states have increased their respective draws of water in recent years, reducing the amount of surplus water left for California. Historically, California as a whole drew 5.2 million acre-feet of water per year due to the use of surplus water. Apart from the increased draw by other states, the Colorado River system is also in the midst of a prolonged drought, which has further reduced its available water. Furthermore, we believe the water supply to the region from the State Water Project could significantly decrease due to a recent court decision regarding endangered fish species and from other pending endangered species litigation.

The CWA maintains a regional water facilities master plan, which presents and evaluates alternatives to protecting and improving water supply, delivery, and flexibility. We understand that the city is also working on a water facilities master plan that will identify its needs beyond 2013. System officials expect new long-term water resource solutions to consist of conservation, reclamation, groundwater and water transfers.

Service Area Economy

San Diego's population, estimated at 1.32 million in fiscal 2007, has grown an average of about 1% per year since the 2000 U.S. Census. The economy consists of a mix of various high-tech clusters, including biotech and telecommunications, combined with a reliance on tourism and the military and defense industries. The city's economic base is also anchored by higher education and major scientific research institutions, including the University of California, San Diego, San Diego State University, Scripps Research Institute, the Salk Institute for Biological Studies, and the San Diego Supercomputer Center. On a per capita basis, market values are extremely strong, in our opinion, at approximately $134,000. Median household effective buying income is also what we consider strong, at 111% of the national average in 2007. The city has seen an increase in foreclosure activity with 1.52% of the city's housing units in some stage of foreclosure; however, water bill collections remain, in our view, strong and in line with historical levels at 98.8%.

Coverage Projections

System officials project what we consider to be good-to-strong total debt service coverage; the officials' projections reflect that net system revenues will cover existing and future senior and subordinate debt service, excluding note principal, from 1.4x-2.4x through fiscal 2013. Fiscals 2009 and 2010 projections assume a 7.5% and 15% reduction in water sales and offsetting costs associated with proposed water conservation measures, respectively. The system projections also do not include any increases in imported water costs or pass-through rate increases beyond fiscal 2009. Officials estimate the water fund's proportionate share of contributions to the pension fund and the retiree health care obligations represent about 5% of budget. In fiscal 2009, system officials budgeted for $11.5 million in capacity charges but, due to ongoing weakness in the construction sector, only expect to receive $3.9 million of this amount by year-end. Excluding capacity charges, projected fiscal 2009 revenue covers senior and subordinate debt service by a still-strong 1.8x, in our opinion.

Audits And Internal Controls

After several restatements in the fiscal 2002 water utility fund, we believe the city has made progress toward improving internal controls and disclosure processes. However, the city acknowledges it still has to continue to bolster internal controls, particularly in the areas of financial reporting, information technology, and internal controls. City management expects the full implementation of new enterprise resource planning software in January 2010 to help resolve internal control weaknesses and aid in the timely release of future financial reports. The city released its fiscal 2007 audit in late 2008 and city officials expect the release of the fiscal 2008 audit by March 2009.