NEW ISSUE – BOOK-ENTRY ONLY

RATINGS: Fitch: "AA"
Moody's: "Aa2"
S&P: "AA-"
(See "RATINGS.")

In the opinion of Goodwin Procter LLP, Los Angeles, California, Bond Counsel to the Authority, based upon an analysis of existing laws, regulations, rulings, and judicial decisions and assuming, among other matters, the accuracy of certain representations and compliance with certain covenants and requirements, interest on the 2010A Bonds is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986, as amended, and is exempt from State of California personal income taxes. In the further opinion of Bond Counsel, interest on the 2010A Bonds is not a specific preference item for purposes of federal individual or corporate alternative minimum taxes, although Bond Counsel observes that such interest is included in adjusted current earnings in calculating federal corporate alternative minimum taxable income. Bond Counsel expresses no opinion regarding other tax consequences relating to the ownership or disposition of, or the accrual or receipt of interest on, the 2010A Bonds. See "TAX MATTERS."

City of San Diego PUBLIC UTILITIES Water & Wastewater

$123,075,000
PUBLIC FACILITIES FINANCING AUTHORITY OF THE CITY OF SAN DIEGO
WATER REVENUE BONDS, REFUNDING SERIES 2010A
(Payable Solely From Installment Payments Secured by Net System Revenues of the Water Utility Fund)

Dated: Date of Delivery **Due: August 1, as shown on the inside cover**

The $123,075,000 Public Facilities Financing Authority of the City of San Diego Water Revenue Bonds, Refunding Series 2010A (Payable Solely From Installment Payments Secured by Net System Revenues of the Water Utility Fund) (the "2010A Bonds") are being issued by the Public Facilities Financing Authority of the City of San Diego (the "Authority") pursuant to Article 11 (commencing with Section 53580) of Chapter 3 of Part 1 of Division 2 of Title 5 of the California Government Code, and an Indenture, dated as of January 1, 2009, as amended and supplemented by a First Supplemental Indenture, dated as of June 1, 2009, and by a Second Supplemental Indenture, dated as of June 1, 2010 (collectively, the "Indenture"), each by and between the Authority and Wells Fargo Bank, National Association, as trustee (the "Trustee"). The proceeds of the 2010A Bonds, together with other available funds, will be used to (i) prepay all of the outstanding 1998 Certificates, (ii) fund a reserve account in the Reserve Fund to satisfy the 2010A Reserve Requirement, and (iii) pay costs of issuance with respect to the 2010A Bonds. Capitalized terms used on this cover page and not otherwise defined shall have the meanings ascribed to them elsewhere in this Official Statement. See in particular "APPENDIX B – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS – Indenture" and " – Installment Purchase Agreement."

The 2010A Bonds are limited obligations of the Authority secured by Revenues consisting primarily of 2010A Installment Payments to be made by the City to the San Diego Facilities and Equipment Leasing Corporation (the "Corporation") under the 2010A Supplement. The 2010A Installment Payments will be assigned by the Corporation to the Authority pursuant to the Assignment Agreement. See "SECURITY AND SOURCES OF PAYMENT FOR THE 2010A BONDS" and "APPENDIX B – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS – Installment Purchase Agreement."

The pledge of and lien on Net System Revenues securing the payment of the 2010A Installment Payments are, in all respects, on parity with the pledge of and lien on Net System Revenues securing the other Outstanding Parity Obligations. See "SECURITY AND SOURCES OF PAYMENT FOR THE 2010A BONDS – Parity Obligations."

THE 2010A BONDS ARE LIMITED OBLIGATIONS OF THE AUTHORITY PAYABLE SOLELY FROM AND SECURED SOLELY BY THE REVENUES PLEDGED THEREFOR AND AMOUNTS ON DEPOSIT IN CERTAIN FUNDS AND ACCOUNTS ESTABLISHED UNDER THE INDENTURE. THE OBLIGATION OF THE CITY TO MAKE 2010A INSTALLMENT PAYMENTS UNDER THE 2010A SUPPLEMENT DOES NOT CONSTITUTE AN OBLIGATION OF THE CITY FOR WHICH THE CITY IS OBLIGATED TO LEVY OR PLEDGE ANY FORM OF TAXATION OR FOR WHICH THE CITY HAS LEVIED OR PLEDGED ANY FORM OF TAXATION. NEITHER THE FULL FAITH AND CREDIT OF THE AUTHORITY, THE CITY, THE COUNTY OF SAN DIEGO (THE "COUNTY"), THE STATE OF CALIFORNIA (THE "STATE"), OR ANY POLITICAL SUBDIVISION OF THE STATE NOR THE TAXING POWER OF THE CITY, THE COUNTY, THE STATE, OR ANY POLITICAL SUBDIVISION OF THE STATE IS PLEDGED TO THE PAYMENT OF THE PRINCIPAL OF OR INTEREST ON THE 2010A BONDS. THE AUTHORITY HAS NO TAXING POWER. NEITHER THE 2010A BONDS NOR THE OBLIGATION OF THE CITY TO MAKE 2010A INSTALLMENT PAYMENTS CONSTITUTES AN INDEBTEDNESS OF THE AUTHORITY, THE CITY, THE COUNTY, THE STATE, OR ANY POLITICAL SUBDIVISION OF THE STATE WITHIN THE MEANING OF ANY CONSTITUTIONAL OR STATUTORY DEBT LIMITATION OR RESTRICTION.

The 2010A Bonds will accrue interest from their date of delivery and interest thereon will be payable on February 1 and August 1 of each year, commencing on August 1, 2010. The 2010A Bonds will bear interest at the respective rates set forth on the inside cover page hereof. See "DESCRIPTION OF THE 2010A BONDS – General" and "APPENDIX B – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS."

The 2010A Bonds will be issued only in fully-registered form in denominations of $5,000 and any integral multiple thereof and, when issued, will be registered in the name of Cede & Co., as the nominee of The Depository Trust Company, New York, New York ("DTC"). DTC will act as securities depository for the 2010A Bonds. Ownership interests in the 2010A Bonds may be purchased in book-entry form only. So long as DTC or its nominee is the Owner of the 2010A Bonds, the principal, the redemption premium, if any, and interest on the 2010A Bonds will be made as described in "APPENDIX E – INFORMATION REGARDING THE BOOK-ENTRY ONLY SYSTEM."

The 2010A Bonds are subject to optional redemption as described herein. See "DESCRIPTION OF THE 2010A BONDS – Redemption of 2010A Bonds."

This cover page contains information for general reference only. Potential purchasers are advised to read the entire Official Statement to obtain information essential to making an informed investment decision.

The 2010A Bonds are offered when, as, and if delivered to and received by the Underwriters, subject to the approval of legality by Goodwin Procter LLP, Los Angeles, California, Bond Counsel. Certain legal matters will be passed upon for the Authority and the San Diego Facilities and Equipment Leasing Corporation (the "Corporation") by Goodwin Procter LLP, for the City and the Authority by Jan I. Goldsmith, City Attorney, and for the Underwriters by their counsel, Nixon Peabody LLP, Los Angeles, California. It is anticipated that the 2010A Bonds will be available for delivery through the facilities of DTC in New York, New York on or about June 30, 2010.

Morgan Stanley **De La Rosa & Co.**

RBC Capital Markets

Dated: June 16, 2010

MATURITY SCHEDULE

Maturity Date (August 1)	Principal Amount	Interest Rate	Yield	Price	CUSIP [(1)]
2022	$12,510,000	5.000%	4.020%	108.056%[(2)]	79730C DX9
2023	13,150,000	5.000	4.100	107.370 [(2)]	79730C DY7
2024	15,910,000	5.000	4.190	106.603 [(2)]	79730C DZ4
2025	18,815,000	5.000	4.280	105.844 [(2)]	79730C EA8
2026	19,805,000	5.250	4.350	107.281 [(2)]	79730C EB6
2027	20,880,000	5.250	4.420	106.691 [(2)]	79730C EC4
2028	22,005,000	5.250	4.490	106.106 [(2)]	79730C ED2

(1) Copyright, American Bankers Association. CUSIP data are provided by Standard & Poor's CUSIP Service Bureau, a division of The McGraw-Hill Companies, Inc. ("CUSIP Service Bureau"). Such CUSIP data are provided only for the convenience of the reader and are not intended to create a database and do not serve in any way as a substitute for the services and information provided by the CUSIP Service Bureau. CUSIP is a registered trademark of the American Bankers Association. The City, the Authority, the Corporation, and the Underwriters do not assume any responsibility for the accuracy of any CUSIP data set forth herein or for any changes or errors in such data.

(2) Priced to optional redemption date of August 1, 2020; callable at par.

PUBLIC FACILITIES FINANCING AUTHORITY OF THE CITY OF SAN DIEGO

Joseph W. Craver, *Chair –Public Member*
John Chalker, *Vice Chair – Public Member*
There is one Public Member vacancy
Gail R. Granewich, *Secretary – City Treasurer*
William Anderson – *Assistant Executive Director of the Redevelopment Agency*

CITY OF SAN DIEGO

Mayor

Jerry Sanders

City Council

Sherri S. Lightner (District 1)
Kevin Faulconer (District 2)
Todd Gloria (District 3)
Tony Young (District 4)
Carl DeMaio (District 5)
Donna Frye (District 6)
Marti Emerald (District 7)
Ben Hueso, Council President (District 8)

City Attorney

Jan I. Goldsmith

City Officials

Jay M. Goldstone, *Chief Operating Officer*
Mary Lewis, *Chief Financial Officer*
Gail R. Granewich, *City Treasurer*
Eduardo Luna, *City Auditor*
Kenton C. Whitfield, *City Comptroller*
Andrea Tevlin, *Independent Budget Analyst*
Elizabeth Maland, *City Clerk*

Public Utilities Department

Alex Ruiz, Interim Director of Public Utilities
Marsi A. Steirer, Interim Assistant Director of Business Support Branch
Jim Fisher, Assistant Director of Water Branch
Ann Sasaki, Assistant Director of Wastewater Branch
Tom Crane, Assistant Director of Strategic Programs

Special Services

BOND AND DISCLOSURE COUNSEL
Goodwin Procter LLP
Los Angeles, California

TRUSTEE
Wells Fargo Bank, National Association
Los Angeles, California

FINANCIAL ADVISOR
Montague DeRose and Associates, LLC
Westlake Village, California

No dealer, broker, salesperson, or other person has been authorized by the City, the Authority, or the Corporation to give any information or to make any representations other than those contained herein and, if given or made, such other information or representations must not be relied upon as having been authorized by the City, the Authority, or the Corporation. This Official Statement does not constitute an offer to sell or the solicitation of an offer to buy, nor shall there be any sale of the 2010A Bonds by a person in any jurisdiction in which it is unlawful for such person to make an offer, solicitation, or sale.

This Official Statement is not a contract with the purchasers of the 2010A Bonds. Statements contained in this Official Statement that involve estimates, forecasts or matters of opinion, whether or not expressly so described herein, are intended solely as such and are not to be construed as a representation of facts.

The information set forth herein has been furnished by the City and by other sources that are believed to be reliable. The Underwriters have provided the following sentence for inclusion in this Official Statement: the Underwriters have reviewed the information in this Official Statement in accordance with, and as part of, their responsibility to investors under the federal securities law as applied to the facts and circumstances of this transaction, but the Underwriters do not guarantee the accuracy or completeness of such information.

The information and expressions of opinion herein are subject to change without notice and neither the delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the City, the Authority, the Corporation, or any other parties described herein since the date hereof. All summaries of the 2010A Bonds, the Indenture, the Master Installment Purchase Agreement, the 2010A Supplement, the Assignment Agreement, and other documents summarized herein are made subject to the provisions of such documents respectively and do not purport to be complete statements of any or all of such provisions.

This Official Statement is submitted in connection with the issuance of the 2010A Bonds referred to herein and may not be reproduced or used, in whole or in part, for any other purpose.

The City maintains a website that includes investor information at http://www.sandiego.gov/investorinformation. However, the information presented at such website is not part of this Official Statement, is not incorporated by reference herein, and should not be relied upon in making an investment decision with respect to the 2010A Bonds.

THE 2010A BONDS HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, IN RELIANCE UPON AN EXEMPTION CONTAINED IN SUCH ACT. THE 2010A BONDS HAVE NOT BEEN REGISTERED OR QUALIFIED UNDER THE SECURITIES LAWS OF ANY STATE.

IN CONNECTION WITH THIS OFFERING, THE UNDERWRITERS MAY OVERALLOT OR EFFECT TRANSACTIONS THAT STABILIZE OR MAINTAIN THE MARKET PRICE OF THE 2010A BONDS AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME. THE UNDERWRITERS MAY OFFER AND SELL THE 2010A BONDS TO CERTAIN DEALERS AND DEALER BANKS AND BANKS ACTING AS AGENT AT PRICES LOWER THAN THE PUBLIC OFFERING PRICE STATED ON THE COVER PAGE HEREOF AND SAID PUBLIC OFFERING PRICE MAY BE CHANGED FROM TIME TO TIME BY THE UNDERWRITERS.

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THE CITY OF SAN DIEGO

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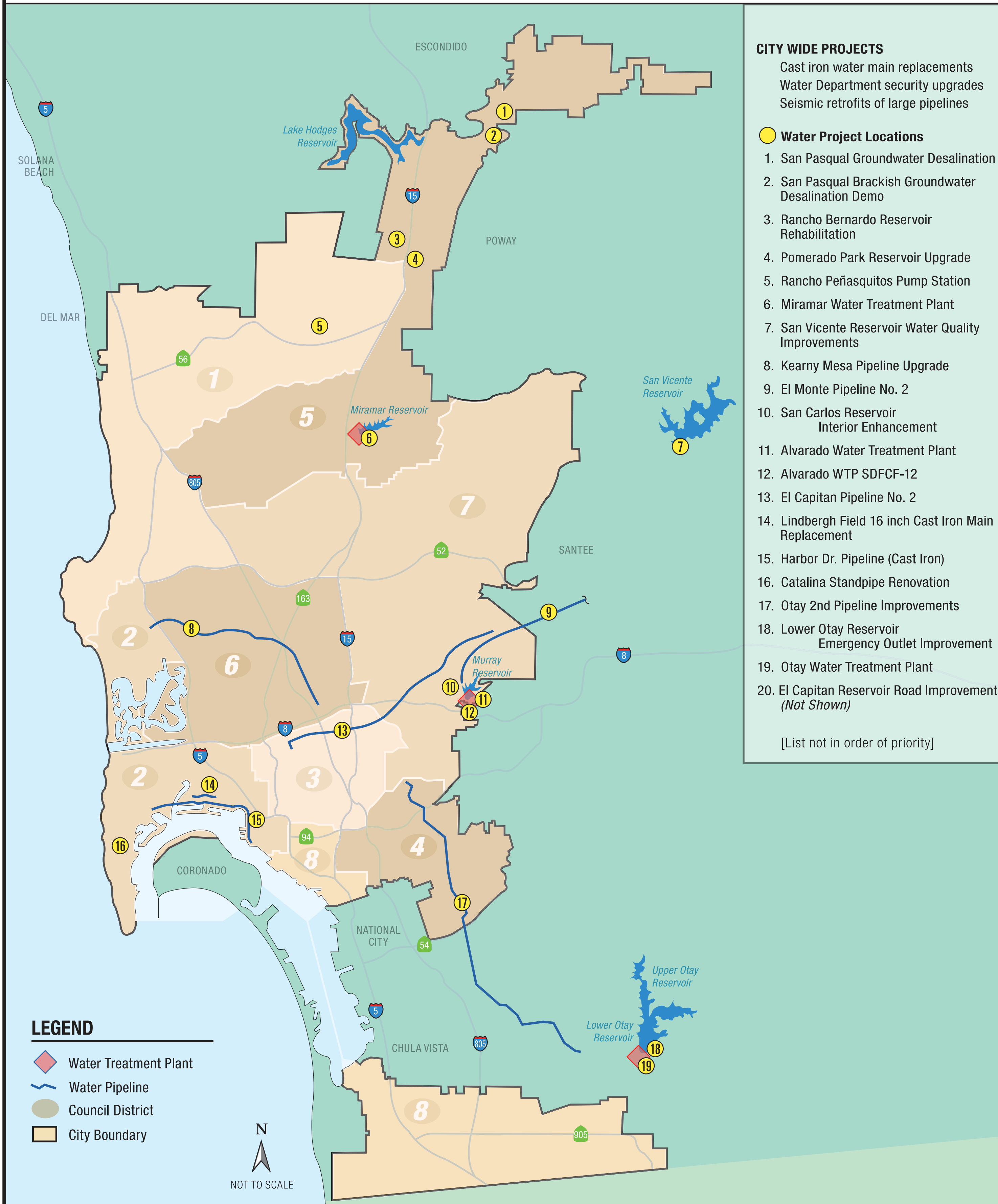

CITY WIDE PROJECTS

Cast iron water main replacements
Water Department security upgrades
Seismic retrofits of large pipelines

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2. San Pasqual Brackish Groundwater Desalination Demo
3. Rancho Bernardo Reservoir Rehabilitation
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15. Harbor Dr. Pipeline (Cast Iron)
16. Catalina Standpipe Renovation
17. Otay 2nd Pipeline Improvements
18. Lower Otay Reservoir Emergency Outlet Improvement
19. Otay Water Treatment Plant
20. El Capitan Reservoir Road Improvement *(Not Shown)*

[List not in order of priority]

OFFICIAL STATEMENT

$123,075,000
PUBLIC FACILITIES FINANCING AUTHORITY OF THE CITY OF SAN DIEGO
WATER REVENUE BONDS, REFUNDING SERIES 2010A
(Payable Solely From Installment Payments
Secured by Net System Revenues of the Water Utility Fund)

INTRODUCTION

This introduction is not a summary of this Official Statement. It is only a brief description of and guide to, and is qualified by, more complete and detailed information contained in the entire Official Statement, including the cover page and appendices hereto and the documents described herein. All statements contained in this introduction are qualified in their entirety by reference to the entire Official Statement. References to and summaries of the laws of the State of California and any documents, reports, and other instruments referred to herein do not purport to be complete and such references are qualified in their entirety by reference to each such law, document, report, or instrument. All capitalized terms used in this Official Statement and not otherwise defined herein have the meanings set forth in the Indenture or the Master Installment Purchase Agreement, each as defined herein. See "APPENDIX B – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS – Indenture" and " – Installment Purchase Agreement."

General

The $123,075,000 Public Facilities Financing Authority of the City of San Diego Water Revenue Bonds, Refunding Series 2010A (Payable Solely From Installment Payments Secured by Net System Revenues of the Water Utility Fund) (the "2010A Bonds") are being issued by the Public Facilities Financing Authority of the City of San Diego (the "Authority") pursuant to Article 11 (commencing with Section 53580) of Chapter 3 of Part 1 of Division 2 of Title 5 of the California Government Code, and an Indenture, dated as of January 1, 2009, as amended and supplemented by a First Supplemental Indenture, dated as of June 1, 2009, and by a Second Supplemental Indenture, dated as of June 1, 2010 (collectively, the "Indenture"), each by and between the Authority and Wells Fargo Bank, National Association, as trustee (the "Trustee"). The proceeds of the 2010A Bonds, together with other available funds, will be used to (i) prepay all of the 1998 Certificates (as defined herein), (ii) fund a reserve account in the Reserve Fund to satisfy the 2010A Reserve Requirement, and (iii) pay costs of issuance with respect to the 2010A Bonds. See "DESCRIPTION OF THE 2010A BONDS," "SECURITY AND SOURCES OF PAYMENT FOR THE 2010A BONDS," and "APPENDIX B – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS."

Changes to Preliminary Official Statement

Certain information in the Official Statement has been updated since the Preliminary Official Statement, dated June 9, 2010. The changes, in addition to those resulting from the pricing of the 2010A Bonds, are the result of a report released on June 8, 2010, by a San Diego County civil grand jury containing recommendations pertaining to the City's financial condition. See "ADDITIONAL INFORMATION."

The 2010A Bonds

The 2010A Bonds will accrue interest from their date of delivery and interest thereon will be payable on February 1 and August 1 of each year, commencing on August 1, 2010 (each, an "Interest Payment Date"). The 2010A Bonds will bear interest at the rates set forth on the inside cover page hereof. See "DESCRIPTION OF THE 2010A BONDS – General" and "APPENDIX B – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS."

The 2010A Bonds are being issued only in fully-registered form in denominations of $5,000 and any integral multiple thereof and, when issued, will be registered in the name of Cede & Co., as the nominee of The Depository Trust Company, New York, New York ("DTC"). DTC will act as securities depository for the 2010A Bonds. Ownership interests in the 2010A Bonds may be purchased in book-entry form only. So long as DTC or its nominee is the Owner of the 2010A Bonds, the principal, the redemption premium, if any, and interest on the 2010A Bonds will be made as described in "APPENDIX E – INFORMATION REGARDING THE BOOK-ENTRY ONLY SYSTEM."

Security and Sources of Payment for the 2010A Bonds

The 2010A Bonds are limited obligations of the Authority secured by Revenues (as defined herein) of the Authority consisting primarily of 2010A Installment Payments (as defined herein) to be made by the City of San Diego (the "City") to the San Diego Facilities and Equipment Leasing Corporation (the "Corporation") under the 2010A Supplement to Amended and Restated Master Installment Purchase Agreement, dated as of June 1, 2010 (the "2010A Supplement"), to the Amended and Restated Master Installment Purchase Agreement, dated as of January 1, 2009 (the "Master Installment Purchase Agreement"), as previously supplemented and as supplemented by the 2010A Supplement (the Master Installment Purchase Agreement, together with the 2010A Supplement and all other supplements thereto, the "Installment Purchase Agreement"), each by and between the City and the Corporation. The 2010A Installment Payments will be assigned by the Corporation to the Authority pursuant to the Assignment Agreement, dated as of June 1, 2010 (the "Assignment Agreement"), by and between the Corporation and the Authority. See "SECURITY AND SOURCES OF PAYMENT FOR THE 2010A BONDS."

THE BONDS ARE LIMITED OBLIGATIONS OF THE AUTHORITY PAYABLE SOLELY FROM AND SECURED SOLELY BY THE REVENUES PLEDGED THEREFOR AND AMOUNTS ON DEPOSIT IN CERTAIN FUNDS AND ACCOUNTS ESTABLISHED UNDER THE INDENTURE. THE OBLIGATION OF THE CITY TO MAKE 2010A INSTALLMENT PAYMENTS UNDER THE 2010A SUPPLEMENT DOES NOT CONSTITUTE AN OBLIGATION OF THE CITY FOR WHICH THE CITY IS OBLIGATED TO LEVY OR PLEDGE ANY FORM OF TAXATION OR FOR WHICH THE CITY HAS LEVIED OR PLEDGED ANY FORM OF TAXATION. NEITHER THE FULL FAITH AND CREDIT OF THE AUTHORITY, THE CITY, THE COUNTY OF SAN DIEGO (THE "COUNTY"), THE STATE OF CALIFORNIA (THE "STATE"), OR ANY POLITICAL SUBDIVISION OF THE STATE NOR THE TAXING POWER OF THE CITY, THE COUNTY, THE STATE, OR ANY POLITICAL SUBDIVISION OF THE STATE IS PLEDGED TO THE PAYMENT OF THE PRINCIPAL OF OR INTEREST ON THE BONDS. THE AUTHORITY HAS NO TAXING POWER. NEITHER THE BONDS NOR THE OBLIGATION OF THE CITY TO MAKE 2010A INSTALLMENT PAYMENTS CONSTITUTES AN INDEBTEDNESS OF THE AUTHORITY, THE CITY, THE COUNTY, THE STATE, OR ANY POLITICAL SUBDIVISION OF THE STATE WITHIN THE MEANING OF ANY CONSTITUTIONAL OR STATUTORY DEBT LIMITATION OR RESTRICTION.

Redemption of the 2010A Bonds

The 2010A Bonds are subject to optional redemption prior to maturity as described herein. See "DESCRIPTION OF THE 2010A BONDS – Redemption of 2010A Bonds."

Rate Covenant

The City has covenanted in the Master Installment Purchase Agreement to fix, prescribe, and collect rates and charges for the City's water service, as described below (the "Water Service"), which will be at least sufficient to yield the greater of (i) Net System Revenues (as defined herein) sufficient to pay during each Fiscal Year (as defined herein) all Obligations (as defined herein) payable in such Fiscal Year, or (ii) Adjusted Net System Revenues (as defined herein) during each Fiscal Year equal to 120% of the Adjusted Debt Service (as defined herein) for such Fiscal Year. The City's fiscal year, which begins on July 1 of each year and ends on June 30 of the following year, is referred to herein as the "Fiscal Year." The Water Service rendered by the City includes the collection, conservation, production, storage, treatment, transmission, furnishing, and distribution services made available or provided by the City's water system (the "Water System"). See "SECURITY AND SOURCES OF PAYMENT FOR THE 2010A BONDS – Rate Covenant" and "WATER SYSTEM FINANCIAL OPERATIONS – Rate Stabilization Fund; Other Funds and Accounts." In addition, for information on the possible limitation on the City's ability to comply with the rate covenant as a consequence of Proposition 218 (as defined herein), see "RISK FACTORS – Rate-Setting Process Under Proposition 218" and "CONSTITUTIONAL LIMITATIONS ON TAXES AND WATER RATES AND CHARGES – Article XIIIC" and " – Article XIIID."

Reserve Fund

In connection with the issuance of the 2010A Bonds, a portion of the amounts in the reserve fund established for the 1998 Certificates, in an amount equal to the 2010A Reserve Requirement, will be transferred to the Trustee and deposited into a separate account in the Reserve Fund to fully fund the Reserve Requirement (as defined herein). See "SECURITY AND SOURCES OF PAYMENT FOR THE 2010A BONDS – Reserve Fund."

Obligations to be Prepaid or Refunded

A portion of the proceeds from the sale of the 2010A Bonds, along with other available moneys held under the 1998 Trust Agreement (as hereinafter defined), will be used to prepay all of the San Diego Facilities and Equipment Leasing Corporation Certificates of Undivided Interest (In Installment Payments Payable from Net System Revenues of the Water Utility Fund of the City of San Diego), Series 1998 (the "1998 Certificates"), currently outstanding in the aggregate principal amount of $141,320,000. The $141,320,000 in principal amount of 1998 Certificates that will be prepaid with a portion of the proceeds of the 2010A Bonds and such other moneys are herein defined as the "Refunded 1998 Certificates." See "THE REFUNDING PLAN."

Outstanding Parity and Subordinated Obligations

The 2010A Installment Payments securing payment of the 2010A Bonds are payable from Net System Revenues on a basis that is equal in right of payment by the City of its other Outstanding Parity Obligations (as defined herein) under the Installment Purchase Agreement and that is senior in right of payment by the City of its other Outstanding Subordinated Obligations (as defined herein) under the Installment Purchase Agreement. As of June 1, 2010, the City had $625,535,000 aggregate principal amount of Outstanding Parity Obligations. After the issuance of the 2010A Bonds and the prepayment of the Refunded 1998 Certificates, the City will have $607,290,000 aggregate principal amount of Outstanding Parity Obligations. As of June 1, 2010, the City had $276,033,478 aggregate principal amount of Outstanding Subordinated Obligations. See "THE REFUNDING PLAN," "SECURITY AND SOURCES OF PAYMENT FOR THE 2010A BONDS – Parity Obligations" and " – Subordinated Obligations," and "WATER SYSTEM FINANCIAL OPERATIONS – Outstanding Indebtedness."

Issuance of Additional Obligations

Pursuant to the Master Installment Purchase Agreement, the City may not create any Obligations, the payments of which are senior or prior in right to the payment by the City of Parity Obligations. The City may at any time enter into or create an obligation or commitment to pay amounts advanced under any Reserve Fund Credit Facility (as defined herein), which obligation constitutes a Parity Obligation or a Subordinated Obligation, as designated by the City (each, a "Reserve Fund Obligation"), provided that the Obligation to which the Reserve Fund Obligation relates is permitted to be entered into under the terms of the Master Installment Purchase Agreement. The City may incur additional Obligations, payments with respect to which will be on parity with or subordinated in priority to the City's obligation to make 2010A Installment Payments, subject to satisfaction of the conditions specified in the Master Installment Purchase Agreement. See "SECURITY AND SOURCES OF PAYMENT FOR THE 2010A BONDS – Issuance of Additional Obligations" and WATER SYSTEM CAPITAL IMPROVEMENT PROGRAM – Financing Plans for the CIP."

The Water System

The City owns the Water System and operates the Water System through its Public Utilities Department (the "Public Utilities Department"). The City has expanded the Water System from time to time to satisfy its mission statement, which is to provide safe, reliable water in an efficient, cost-effective, and environmentally responsible manner. See "WATER SYSTEM ORGANIZATION AND MANAGEMENT," "WATER SYSTEM SERVICE AREA AND FACILITIES," "WATER SUPPLY," "WATER SYSTEM REGULATORY REQUIREMENTS," "WATER SYSTEM CAPITAL IMPROVEMENT PROGRAM," and "WATER SYSTEM FINANCIAL OPERATIONS."

Continuing Disclosure

The City has agreed to provide, or cause to be provided to the Municipal Securities Rulemaking Board, in accordance with Rule 15c2-12(b)(5), as amended (the "Rule"), promulgated by the United States Securities and Exchange Commission (the "SEC") under the Securities Exchange Act of 1934, as amended, certain annual financial information and operating data and, in a timely manner, notice of certain material events. These covenants have been made in order to assist the Underwriters in complying with the Rule. Beginning in March 2004 and continuing through 2008, the City failed to comply with various filing deadlines for a number of undertakings due to the unavailability of audited financial statements for the City. Each required annual report and audited financial statement was subsequently filed. The City is current with its filings and is in compliance with its continuing disclosure obligations. See "CONTINUING DISCLOSURE."

2006 SEC Order and Related Matters

SEC Order. On November 14, 2006, the City entered into a cease-and-desist order (the "Order") with the SEC relating to violations of the antifraud provisions of the federal securities laws in connection with the offer and sale of municipal securities in calendar years 2002 and 2003 and other related public financial disclosures concerning its pension and retiree health care liabilities. The SEC concluded that the "City, through its officials, acted with scienter," because "City officials acted recklessly in failing to disclose material information regarding [pension and retiree health care] liabilities." The Order imposed certain remedial sanctions, including the retention of an independent consultant to review and assess the City's policies, procedures, and internal controls with respect to bond offerings, including disclosures made in its financial statements. On January 16, 2007, the City retained Stanley Keller of the law firm of Edwards Angell Palmer & Dodge, LLP to serve as Independent Consultant. The Independent Consultant is required to conduct annual reviews of the City's policies, procedures, and internal controls for a three year period and to provide copies of such reports to the SEC. The Independent Consultant's final report was presented to the City Council of the City (the “City Council”) on March 8, 2010. The Order settled all claims between the City and the SEC with respect to the alleged violations of the federal securities laws in 2002 and 2003.

Audited Financial Reports. As a result of various investigations into the City regarding, principally, the events that were the subject of the SEC Order, the completion and release of the City’s audited financial statements were substantially delayed. The City issued its Comprehensive Annual Financial Reports (each, a “CAFR”) with unqualified opinions for Fiscal Years 2003 through 2008 during the period from June 2007 through March 2009. The City received an unqualified opinion from its outside auditor on December 21, 2009, with respect to the Fiscal Year 2009 CAFR, which was received and filed with the City Council of the City (the “City Council”) on February 1, 2010. The City is now current with respect to all financial reporting.

City Ratings. Beginning in 2004, as a further result of the investigations into the City and the related delays in the completion and release of the City’s CAFRs, Moody’s Investors Service, Inc. (“Moody’s”), and Fitch Ratings (“Fitch”) began to downgrade the credit ratings on the City’s obligations and changed the outlook on those ratings to negative. Standard & Poor’s Ratings Services, a division of The McGraw-Hill Companies, Inc. (“S&P”), placed the City’s credit rating on negative outlook and subsequently suspended its credit ratings on all City obligations. The City’s credit ratings were reinstated in May 2008 by S&P in connection with the release of its CAFRs for Fiscal Years 2003 through 2006. The City currently maintains ratings on its bonds and other City debt obligations from all three rating agencies to the extent that such bonds and debt obligations were rated at issuance or were subsequently rated. See “RATINGS” for a description of the ratings assigned to the Series 2010A Bonds.

The Authority and the Corporation

The Authority is a California joint exercise of powers authority established pursuant to a joint exercise of powers agreement by and between the City and the Redevelopment Agency of the City of San Diego. The Authority was organized, in part, to finance, acquire, construct, maintain, repair, operate, and control certain capital facilities improvements for the City.

The Corporation is a nonprofit charitable corporation duly organized and existing under and by virtue of the laws of the State. The Corporation was organized to acquire, lease, and/or sell to the City real and personal property to be used in the municipal operations of the City.

Forward-Looking Statements

Certain statements included or incorporated by reference in this Official Statement constitute “forward-looking statements” within the meaning of the United States Private Securities Litigation Reform Act of 1995, Section 21E of the United States Securities Exchange Act of 1934, as amended, and Section 27A of the United States Securities Act of 1933, as amended. Such statements are generally identifiable by the terminology used such as “plan,” “intend,” “expect,” “propose,” “estimate,” “project,” “budget,” “anticipate,” or other similar words. The achievement of certain results or other expectations contained in such forward-looking statements involves known and unknown risks, uncertainties, and other factors that may cause the actual results, performance, or achievements described to be materially different from any future results, performance, or achievements expressed or implied by such forward-looking statements. No updates or revisions to these forward-looking statements are expected to be issued if or when the expectations, events, conditions, or circumstances on which such statements are based change. The forward-looking statements in this Official Statement are subject to risks and uncertainties that could cause actual results to differ materially from those expressed in or implied by such forward-looking statements. **READERS ARE CAUTIONED NOT TO PLACE UNDUE**

RELIANCE ON SUCH FORWARD-LOOKING STATEMENTS, WHICH SPEAK ONLY AS OF THE DATE HEREOF.

Miscellaneous

Copies of the Indenture, the Installment Purchase Agreement, the Assignment Agreement, and other financing documents may be obtained upon request from the Trustee at Wells Fargo Bank, National Association, 707 Wilshire Boulevard, 17th Floor, Los Angeles, CA 90017.

THE REFUNDING PLAN

A portion of the proceeds of the 2010A Bonds, along with other available moneys held under the 1998 Trust Agreement, will be used to prepay the Refunded 1998 Certificates, as more particularly described in the following table:

Maturity Date	Principal Amount	Prepayment/ Redemption Price	Prepayment/ Redemption Date	CUSIP [1]
August 1, 2024	$ 38,405,000	100.50%	June 30, 2010	797263 BB5
August 1, 2028	102,915,000	100.00	June 30, 2010	797263 BC3

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The Refunded 1998 Certificates will be prepaid in accordance with the terms of that certain Trust Agreement, dated as of August 1, 1998, as supplemented and amended by that certain First Amendment to Trust Agreement, dated as of August 1, 2009 (collectively, the "1998 Trust Agreement"), each by and among the City, the Corporation, and Wells Fargo Bank, National Association, as successor trustee for the 1998 Certificates (the "1998 Trustee"). On the date of delivery of the 2010A Bonds, a portion of the proceeds from the sale of the 2010 Bonds will be transferred to the 1998 Trustee, which proceeds, together with certain moneys currently on deposit in the funds and accounts established under the 1998 Trust Agreement and currently being held by the 1998 Trustee, will be used to call and prepay the Refunded 1998 Certificates on or about June 30, 2010.

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ESTIMATED SOURCES AND USES OF BOND PROCEEDS AND OTHER AVAILABLE AMOUNTS

The following table details the estimated sources and uses of the proceeds from the sale of the 2010A Bonds and the moneys transferred from certain funds and accounts established under the 1998 Trust Agreement.

Estimated Sources:	
Principal Amount of the 2010A Bonds	$123,075,000.00
Amounts Released under 1998 Trust Agreement	24,003,444.27
Plus: Original Issue Premium	8,309,754.65
Total Sources	$155,388,198.92
Estimated Uses:	
2010A Bond Proceeds Used to Prepay Refunded 1998 Certificates	$130,392,437.45
Transfers to Prepay Refunded 1998 Certificates	13,969,438.81
Transfer to Reserve Fund	10,034,005.46
Payment of Costs of Issuance (1)	992,317.20
Total Uses	$155,388,198.92

(1) Costs of Issuance for the 2010A Bonds are expected to include, but are not limited to, Underwriters' discount, the fees and expenses of the City, the Authority, the Corporation, and the Trustee, and their respective counsel, as well as Bond Counsel and Disclosure Counsel.

DESCRIPTION OF THE 2010A BONDS

General

The 2010A Bonds will be issued as fully-registered bonds in denominations of $5,000 and any integral multiple thereof and, when issued, will be registered in the name of Cede & Co., as the nominee of The Depository Trust Company, New York, New York ("DTC"). DTC will act as securities depository for the 2010A Bonds. Ownership interests in the 2010A Bonds may be purchased in book-entry form only. So long as DTC or its nominee is the Owner of the 2010A Bonds, principal of, redemption premium, if any, and interest on the 2010A Bonds will be made as described in "APPENDIX E – INFORMATION REGARDING THE BOOK-ENTRY ONLY SYSTEM."

The 2010A Bonds will accrue interest from their date of delivery and interest thereon will be payable on February 1 and August 1 of each year, commencing on August 1, 2010. The 2010A Bonds will bear interest at the respective rates set forth on the inside cover page hereof. Interest on the 2010A Bonds shall be calculated on the basis of a 360-day year, comprised of twelve 30-day months. Interest coming due on a date that is not a Business Day shall be payable on the immediately following Business Day. Each 2010A Bond shall bear interest from the Interest Payment Date next preceding the date of authentication thereof, unless such date of authentication is during the period commencing after a Record Date (as defined herein) through and including the next succeeding Interest Payment Date, in which event such 2010A Bond shall bear interest from such Interest Payment Date, or unless such date of authentication is on or before the first Record Date, in which event such 2010A Bond shall bear interest from its dated date; provided, however, that if, on the date of authentication of any 2010A Bonds, interest is then in default on the Outstanding 2010A Bonds, such 2010A Bonds shall bear interest from the Interest Payment Date to which interest has previously been paid or made available for payment on the Outstanding 2010A Bonds.

Payment of interest on the 2010A Bonds due on or before the maturity or prior redemption thereof shall be made to the Owner or Owners of record as of the fifteenth day of the calendar month preceding the applicable Interest Payment Date, whether or not such day is a Business Day (each, a "Record Date"), on the registration books kept by the Trustee pursuant to the Indenture, such interest to be paid by check mailed by first class mail on such Interest Payment Date to such Owner at his address as it appears on such books; provided, that in the event the ownership of such 2010A Bonds is no longer maintained in book-entry form by DTC or any other securities depository for the 2010A Bonds, such payment shall be made by wire transfer to any Owner of at least $1,000,000 in aggregate principal amount of 2010A Bonds, in immediately available funds to an account in the continental United States designated in writing by such Owner to the Trustee prior to the applicable Record Date.

Redemption of 2010A Bonds

Optional Redemption. The 2010A Bonds shall be subject to redemption, in whole or in part, at the option of the Authority (upon the direction of the City), on or after August 1, 2020, at any time, from and to the extent of prepaid 2010A Installment Payments paid pursuant to the 2010A Supplement, at a redemption price equal to the principal amount of 2010A Bonds called for redemption, together with interest accrued thereon to the date fixed for redemption, without premium.

Notice of Redemption. Pursuant to the Indenture, each notice of redemption shall be mailed to the Owners not more than 60 days nor less than 30 days prior to the redemption date and shall state the date of such notice, the redemption price (including the name and appropriate address of the Trustee), and, in the case of 2010A Bonds to be redeemed in part only, the respective portions of the principal amount thereof to be redeemed. Each such notice shall also state that on said date there will become due and payable on each of said 2010A Bonds the principal amount thereof and, in the case of a 2010A Bond to be redeemed in part only, the specified portion of the principal amount thereof to be redeemed, together with interest accrued thereon to the redemption date, and that from and after such redemption date, interest thereon shall cease to accrue, and shall require that such 2010A Bonds be then surrendered at the address of the Trustee specified in the redemption notice. Notice of redemption may be conditioned upon the occurrence of future events, including but not limited to the issuance of refunding bonds, and may be given and rescinded by the Trustee prior to the redemption date, upon written instruction of the Authority.

Effect of Redemption. If notice of redemption has been duly given as provided in the Indenture and money for the payment of the redemption price of the 2010A Bonds called for redemption is held by the Trustee, then on the redemption date designated in such notice, the 2010A Bonds shall become due and payable, and from and after the date so designated, interest on the 2010A Bonds so called for redemption shall cease to accrue, and the Owners of such 2010A Bonds shall have no rights in respect thereof except to receive payment of the redemption price thereof. The insufficiency of any such notice shall not affect the sufficiency of the proceedings for redemption.

SECURITY AND SOURCES OF PAYMENT FOR THE 2010A BONDS

Pledge of Revenues; Installment Payments

Pursuant to the Indenture, the 2010A Bonds are limited obligations of the Authority payable solely from the Revenues and amounts on deposit in the funds and accounts established under the Indenture (other than amounts on deposit in the Rebate Fund). The term "Revenues," as applied to the 2010A Bonds, means all 2010A Installment Payments received by or due to be paid to the Corporation pursuant to the 2010A Supplement and the interest or profits from the investment of money in any account or fund (other than the Rebate Fund) pursuant to the Indenture. The 2010A Installment Payments will be assigned by the Corporation to the Authority pursuant to the Assignment Agreement. To secure the pledge of the Revenues, the Authority will transfer, convey, and assign to the Trustee, for the benefit of the Owners, all of the Authority's right to receive 2010A Installment Payments from the City. See "APPENDIX B – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS – Indenture."

Pledge of Net System Revenues

Pursuant to the Installment Purchase Agreement, the City agrees to make Installment Payments (including the 2010A Installment Payments) solely from Net System Revenues until such time as the Purchase Price for any Components has been paid in full (or provision for the payment thereof has been made pursuant to the Installment Purchase Agreement), and the City grants a first priority lien on and pledge of Net System Revenues to secure the payment of such Installment Payments (including the 2010A Installment Payments). The City will not discontinue or suspend any Installment Payments (including the 2010A Installment Payments) required to be made by the City under the Installment Purchase Agreement, whether or not the Project or any part thereof is operating or operable or has been completed, or its use is suspended, interfered with, reduced, curtailed, or terminated, in whole or in part, and such Installment Payments (including the 2010A Installment Payments) shall not be subject to reduction, whether by offset or otherwise, and will not be conditioned upon the performance or nonperformance by any party of any agreement for any cause whatsoever.

The term "Net System Revenues" is defined in the Master Installment Purchase Agreement as, for any Fiscal Year, the System Revenues for such Fiscal Year, less the Maintenance and Operation Costs of the Water System for such Fiscal Year.

The term "System Revenues" is defined in the Master Installment Purchase Agreement as all income, rents, rates, fees, charges, and other moneys derived from the ownership or operation of the Water System, including, without limiting the generality of the foregoing: (a) all income, rents, rates, fees, charges, or other moneys derived by the City from the water services or facilities, and commodities or byproducts, including hydroelectric power, sold, furnished or supplied through the facilities of or in the conduct or operation of the business of the Water System, and including, without limitation, investment earnings on the operating reserves to the extent that the use of such earnings is limited to the Water System by or pursuant to law, and earnings on any Reserve Fund for Obligations, but only to the extent that such earnings may be utilized under the indenture, trust agreement, loan agreement, lease, or installment purchase agreement under which the applicable Obligations are issued (each, an "Issuing Instrument') for the payment of debt service for such Obligations; (b) standby charges and Capacity Charges derived from the services and facilities sold or supplied through the Water System; (c) the proceeds derived by the City directly or indirectly from the lease of a part of the Water System; (d) any amount received from the levy or collection of taxes that are solely available and are earmarked for the support of the operation of the Water System; (e) amounts received under contracts or agreements with governmental or private entities and designated for capital costs for the Water System; and (f) grants for maintenance and operations received from the United States of America or from the State; provided, however, that System Revenues shall not include: (1) in all cases, customers' deposits or any other deposits or advances subject to refund until such deposits or advances have become the property of the City; and (2) the proceeds of borrowings. Notwithstanding the foregoing, there shall be deducted from System Revenues any amounts transferred into a Rate Stabilization Fund as contemplated by the Master Installment Purchase Agreement and any amounts transferred from current System Revenues to the Secondary Purchase Fund as permitted by the Master Installment Purchase Agreement. There shall be added to System Revenues any amounts transferred out of such Rate Stabilization Fund or the Secondary Purchase Fund to pay Maintenance and Operation Costs of the Water System. See "WATER SYSTEM FINANCIAL OPERATIONS – Rate Stabilization Fund; Other Funds and Accounts."

The term "Maintenance and Operation Costs of the Water System" is defined in the Master Installment Purchase Agreement as (a) any Qualified Take or Pay Obligation (as defined herein), and (b) the reasonable and necessary costs spent or incurred by the City for maintaining and operating the

Water System, calculated in accordance with generally accepted accounting principles, including (among other things) the reasonable expenses of maintenance and repair and other expenses necessary to maintain and preserve the Water System in good repair and working order, and including administrative costs of the City attributable to the Water System, including the Project and the Installment Purchase Agreement, salaries and wages of employees of the Water System, payments to such employees' retirement systems (to the extent paid from System Revenues), overhead, taxes (if any), fees of auditors, accountants, attorneys or engineers, and insurance premiums, and including all other reasonable and necessary costs of the City or charges required to be paid by it to comply with the terms of the Obligations, including the Installment Purchase Agreement, including any amounts required to be deposited in the Rebate Fund pursuant to a Tax Certificate, and fees and expenses payable to any "Credit Provider" (which term is defined in the Master Installment Purchase Agreement to mean any municipal bond insurance company, bank, or other financial institution or organization that is performing in all material respects its obligations under any policy of insurance, letter of credit, standby purchase agreement, revolving credit agreement, or other credit arrangement providing credit support or liquidity with respect to Parity Obligations (each, a "Credit Support Instrument")) (other than in repayment of a "Credit Provider Reimbursement Obligation" (which term is defined in the Master Installment Purchase Agreement to mean any obligation of the City to repay, from Net System Revenues, amounts advanced by a Credit Provider as credit support or liquidity for Parity Obligations, which obligation shall constitute a Parity Obligation or a Subordinated Obligation, as designated by the City)), but excluding in all cases (1) depreciation, replacement, and obsolescence charges or reserves therefor, (2) amortization of intangibles or other bookkeeping entries of a similar nature, (3) costs of capital additions, replacements, betterments, extensions, or improvements to the Water System, which under generally accepted accounting principles are chargeable to a capital account or to a reserve for depreciation, (4) charges for the payment of principal of and interest on any general obligation bond heretofore or hereafter issued for Water System purposes, and (5) charges for the payment of principal of and interest on any debt service on account of any Obligation on a parity with or subordinate to the Installment Payments.

The term "Qualified Take or Pay Obligation" is defined in the Master Installment Purchase Agreement as the obligation of the City to make use of any facility, property, or services, or some portion of the capacity thereof, or to pay therefor from System Revenues, or both, whether or not such facilities, properties, or services are ever made available to the City for use, and there is provided to the City a certificate of the City or of an Independent Engineer to the effect that the incurrence of such obligation will not adversely affect the ability of the City to comply with the rate covenant contained in the Installment Purchase Agreement. As of the date of issuance of the 2010A Bonds, there will be no outstanding Qualified Take or Pay Obligations.

Parity Obligations

The 2010A Installment Payments shall be Parity Obligations under the Installment Purchase Agreement and, as of the date of delivery of the 2010A Bonds, the payment of the 2010A Installment Payments will be on parity with the right of payment of other Outstanding Parity Obligations under the Installment Purchase Agreement. The term "Parity Obligations" is defined in the Master Installment Purchase Agreement as (i) Parity Installment Obligations (as defined herein), (ii) Obligations, the principal of and interest on which are payable on a parity with Parity Installment Obligations, and (iii) Reserve Fund Obligations. The term "Parity Installment Obligations" is defined in the Master Installment Purchase Agreement as Obligations consisting of or payable from Installment Payments, which are not subordinated in right of payment to other Installment Payments.

The term "Obligations" is defined in the Master Installment Purchase Agreement as (i) obligations of the City for money borrowed (such as bonds, notes, or other evidences of indebtedness) or as installment purchase payments under any contract (including Installment Payments), or as lease payments under any financing lease (determined to be such in accordance with generally accepted accounting principles), the principal of and interest on which are payable from Net System Revenues; (ii) obligations to replenish any debt service reserve funds with respect to such obligations of the City; (iii) obligations secured by or payable from any of such obligations of the City; and (iv) obligations of the City payable from Net System Revenues under (a) any contract providing for payments based on levels of, or changes in, interest rates, currency exchange rates, stock or other indices, (b) any contract to exchange cash flows or a series of payments, or (c) any contract to hedge payment, currency, rate spread, or similar exposure, including but not limited to interest rate cap agreements.

All Parity Obligations are secured by a first priority lien on and pledge of Net System Revenues. All Parity Obligations are of equal rank with each other without preference, priority, or distinction of any Parity Obligations over any other Parity Obligations. As of the date of delivery of the 2010A Bonds, the pledge and right of payment from Net System Revenues securing the 2010A Installment Payments (which, in turn, secure the payment of the 2010A Bonds) will be on a parity with the pledge and right of payment from Net System Revenues securing Installment Payments that, in turn, secure the payment of (i) the 2010A Bonds, (ii) the Public Facilities Financing Authority of the City of San Diego Water Revenue Bonds, Refunding Series 2009A (Payable Solely From Installment Payments Secured by Net System Revenues of the Water Utility Fund) (the "2009A Bonds"), which were issued on January 29, 2009, and which are currently outstanding in the aggregate principal amount of $156,155,000, and (iii) the Public Facilities Financing Authority of the City of San Diego Water Revenue Bonds, Series 2009B (Payable Solely From Installment Payments Secured by Net System Revenues of the Water Utility Fund) (the "2009B Bonds"), which were issued on June 26, 2009, and which are currently outstanding in the aggregate principal amount of $328,060,000. See "THE REFUNDING PLAN" and "WATER SYSTEM FINANCIAL OPERATIONS – Outstanding Indebtedness."

Subordinated Obligations

The Master Installment Purchase Agreement permits the issuance of Obligations secured by a lien on and pledge of Net System Revenues, which lien and pledge is subordinate to the lien on and pledge of Net System Revenues securing Parity Obligations (each, a "Subordinated Obligation"). In addition, nothing contained in the Master Installment Purchase Agreement limits the ability of the City to grant a lien on and pledge of the Net System Revenues that is subordinate to any liens on and pledges of Net System Revenues for the benefit of Parity Obligations and Subordinated Obligations contained therein. See "APPENDIX B – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS."

The City has previously borrowed the Existing SRF Loan (as defined below) for its Water System from the State Revolving Fund in the original aggregate principal amount of $21,525,249, which Existing SRF Loan constitutes a Subordinated Obligation. The Existing SRF Loan is currently outstanding in the aggregate principal amount of $17,573,478, is payable on a semi-annual basis, and matures in 2025. The City has applied for additional loans under the State Revolving Fund in the amount of $50 million (the "Additional SRF Loans"). The California Department of Public Health ("DPH") is currently reviewing the City's applications for such Additional SRF Loans. DPH is expected to fund certain selected applications by summer 2010. Future Additional SRF Loans will be Parity Obligations. See "WATER SYSTEM CAPITAL IMPROVEMENT PROGRAM – Financing Plans for the CIP."

As of the date of delivery of the 2010A Bonds, the pledge and right of payment from Net System Revenues on a basis that is junior and subordinate to the lien and pledge of Net System Revenues securing Parity Obligations secure the payment of Subordinated Obligations that, in turn, secure the payment of (i) the outstanding Public Facilities Financing Authority of the City of San Diego Subordinated Water Revenue Bonds, Series 2002 (Payable Solely From Subordinated Installment Payments Secured By Net System Revenues of the Water Utility Fund) (the "2002 Subordinated Bonds"), currently outstanding in the aggregate principal amount of $258,460,000, and (ii) a loan from the State of California Department of Health Services Safe Drinking Water State Revolving Fund (the "State

Revolving Fund"), which is currently outstanding in the aggregate principal amount of $17,573,478 and is payable on a semi-annual basis and matures in 2025 (the "Existing SRF Loan") (together with the outstanding 2002 Subordinated Bonds, the "Outstanding Subordinated Obligations"). See "THE REFUNDING PLAN" and "WATER SYSTEM FINANCIAL OPERATIONS – Outstanding Indebtedness."

The Water Utility Fund

The City accounts for its water operations through an enterprise fund known as the "Water Utility Fund." The Water Utility Fund was established pursuant to an amendment to the City Charter effective February 11, 1963, and is accounted for separately from other funds of the City. The City has agreed and covenanted in the Master Installment Purchase Agreement that all System Revenues shall be received by the City in trust and shall be deposited when and as received in the Water Utility Fund, which fund the City agrees and covenants to maintain so long as any Obligations remain unpaid, and all moneys in the Water Utility Fund shall be so held in trust and applied and used solely as provided in the Master Installment Purchase Agreement. The City further has agreed to pay from the Water Utility Fund: (1) directly or as otherwise required all Maintenance and Operation Costs of the Water System; and (2) to the Trustee, for deposit in the Payment Fund for Parity Obligations, including Reserve Fund Obligations that are Parity Obligations, the amounts specified in any Issuing Instrument, as payments due on account of Parity Obligations (including any Credit Provider Reimbursement Obligations that are Parity Obligations). In the event there are insufficient Net System Revenues to make all of the payments contemplated by clause (2) of the immediately preceding sentence, then said payments shall be made as nearly as practicable, pro rata, based upon the respective unpaid principal amounts of said Parity Obligations.

After the payments described in the preceding paragraph have been made, and in any event not less frequently than January 15 and July 15 of each year, any remaining Net System Revenues shall be used to make up any deficiency in the Reserve Funds for Parity Obligations. Notwithstanding the use of a Reserve Fund Credit Facility in lieu of depositing funds in the related Reserve Fund for Parity Obligations, in the event of any draw on the related Reserve Fund Credit Facility, there shall be deemed a deficiency in such Reserve Fund for Parity Obligations until the amount of the Reserve Fund Credit Facility is restored to its pre-draw amount. In the event there are insufficient Net System Revenues to make up all deficiencies in all Reserve Funds for Parity Obligations, such payments into the Reserve Funds shall be made as nearly as practicable pro rata based on the respective unpaid principal amount of all Parity Obligations. Any amounts thereafter remaining in the Water Utility Fund may from time to time be used to pay the amounts specified in any Issuing Instrument as payments due on account of Subordinated Obligations (including any Reserve Fund Obligations for Subordinated Obligations, any Credit Provider Reimbursement Obligations that are Subordinated Obligations, and any Subordinated Credit Provider Reimbursement Obligations), provided the following conditions are met: (1) all Maintenance and Operation Costs of the Water System are being and have been paid and are then current; and (2) all deposits and payments contemplated by clause (2) of the preceding paragraph shall have been made in full and no deficiency in any Reserve Fund for Parity Obligations shall exist, and there shall have been paid, or segregated within the Water Utility Fund, the amounts payable during the current month pursuant to clause (2) of the preceding paragraph.

After deposits described in the preceding paragraphs have been made, any amounts thereafter remaining in the Water Utility Fund may be used for any lawful purpose of the Water System. See "APPENDIX B – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS."

Rate Covenant

The City has covenanted in the Master Installment Purchase Agreement to fix, prescribe, and collect rates and charges for the Water Service that will be at least sufficient to yield the greater of (i) Net System Revenues sufficient to pay during each Fiscal Year all Obligations payable in such Fiscal Year or (ii) Adjusted Net System Revenues during each Fiscal Year equal to 120% of the Adjusted Debt Service for such Fiscal Year. The City may make adjustments from time to time in such rates and charges and may make such classification thereof as it deems necessary, but the City will not reduce the rates and charges then in effect unless the Net System Revenues from such reduced rates and charges will at all times be sufficient to meet the requirements of the Installment Purchase Agreement. The term "Adjusted Net System Revenues" is defined in the Master Installment Purchase Agreement as, for any Fiscal Year, the Net System Revenues for such Fiscal Year, minus an amount equal to earnings from investments in any Reserve Fund securing Parity Obligations for such Fiscal Year. The term "Adjusted Debt Service" is defined in the Master Installment Purchase Agreement as, for any Fiscal Year, Debt Service on Parity Obligations for such Fiscal Year, minus an amount equal to earnings from investments in any Reserve Fund for Parity Obligations for such Fiscal Year. Net System Revenues (and, therefore, Adjusted Net System Revenues) may be increased or reduced by transfers in to or out of the Rate Stabilization Fund or the Secondary Purchase Fund. See " – Pledge of Net System Revenues" above. For information on the possible limitation on the City's ability to comply with the rate covenant described above as a consequence of Proposition 218, see "RISK FACTORS – Rate-Setting Process Under Proposition 218" and "CONSTITUTIONAL LIMITATIONS ON TAXES AND WATER RATES AND CHARGES – Article XIIIC" and "– Article XIIID." For a description of the reserve funds established by the City within the Water Utility Fund, see "WATER SYSTEM FINANCIAL OPERATIONS – Rate Stabilization Fund; Other Funds and Accounts."

Reserve Fund

In connection with the issuance of the 2010A Bonds, a portion of the amounts in the reserve fund established for the 1998 Certificates, in the amount of $10,034,005.46 (which amount is equal to the 2010A Reserve Requirement), will be transferred to the Trustee and deposited into a separate account in the Reserve Fund. Such deposit, along with amounts previously deposited into the Reserve Fund in connection with the issuance of the 2009A Bonds and the 2009B Bonds, will fully fund the Reserve Requirement in the amount of $48,433,934.87. The 2009A Bonds, the 2009B Bonds, and the 2010A Bonds are secured by the Reserve Fund.

The term "Reserve Requirement" is defined in the Indenture as, as of any date of calculation, an amount equal to the least of (i) 10% of the proceeds (within the meaning of Section 148 of the Internal Revenue Code of 1986, as amended (the "Code") of any bonds authorized and issued under the Indenture, including the 2009A Bonds, the 2009B Bonds, the 2010A Bonds and any other bonds issued thereunder on a parity with the 2010A Bonds (collectively, the "Bonds"); (ii) 125% of average annual debt service on the then-Outstanding Bonds; or (iii) Maximum Annual Debt Service for that and any subsequent year. Upon early redemption of any of the Bonds, the Authority, at the request of the City, may request the Trustee to recalculate and reduce any Reserve Requirement, whereupon any excess in the Reserve Fund over and above such Reserve Requirement shall be transferred to the Payment Fund.

The Authority may replace all or a portion of the Reserve Requirement with a reserve surety bond, insurance policy, letter of credit, or other similar instrument (each, a "Reserve Fund Credit Facility"), providing, by its terms, a stated amount as a credit towards or in satisfaction of all or part of the Reserve Requirement. Under the Indenture, such Reserve Fund Credit Facility must be rated "Aa3" or "AA-" or better by at least two Rating Agencies at the time of purchase or issuance. In addition, within 12 months after the date that the Authority obtains actual knowledge that any such Reserve Fund Credit Facility is no longer rated at least "Aa3" or "AA-" by any Rating Agency, the Authority shall either

(i) deposit into the Reserve Fund money in an amount equal to the stated or principal amount of such Reserve Fund Credit Facility or (ii) obtain a substitute Reserve Fund Credit Facility that satisfies the provisions of the Indenture.

Issuance of Additional Obligations

Pursuant to the Master Installment Purchase Agreement, the City may incur additional Obligations, payments with respect to which will be on parity with or subordinated in priority to the City's obligation to make 2010A Installment Payments, subject to satisfaction of the conditions specified in the Master Installment Purchase Agreement, as described below.

Issuance of Parity Obligations. The City may not create any Obligations, the payments of which are senior or prior in right to the payment by the City of Parity Obligations. The City may issue or create any other Parity Obligations, provided that (i) there shall not have occurred and be continuing an Event of Default under the terms of the Installment Purchase Agreement, any Issuing Instrument, or any Credit Support Instrument and (ii) the City obtains or provides a certificate or certificates, prepared by the City or at the City's option by a Consultant, showing that:

(1) the Net System Revenues as shown by the books of the City for any 12 consecutive month period within the 18 consecutive months ending immediately prior to the incurring of such additional Parity Obligations shall have amounted to or exceeded the greater of (i) at least 1.20 times the Maximum Annual Debt Service on all Parity Obligations to be Outstanding immediately after the issuance of the proposed Parity Obligations or (ii) at least 1.00 times the Maximum Annual Debt Service on all Obligations to be Outstanding immediately after the issuance of the proposed Parity Obligations; or

(2) the estimated Net System Revenues for the five Fiscal Years following the earlier of (a) the end of the period during which interest on those Parity Obligations is to be capitalized or, if no interest is to be capitalized, the Fiscal Year in which the Parity Obligations are issued, or (b) the date on which substantially all new Components to be financed with such Parity Obligations are expected to commence operations, will be at least equal to 1.20 times the Maximum Annual Debt Service for all Parity Obligations that will be Outstanding immediately after the issuance of the proposed Parity Obligations.

The certificate or certificates described in clause (2) above will not be required if the Parity Obligations being issued are for the purpose of refunding (A) then Outstanding Parity Obligations if at the time of the issuance of such Parity Obligations a certificate of an Authorized City Representative is delivered showing that the sum of Adjusted Debt Service on all Parity Obligations Outstanding for all remaining Fiscal Years after the issuance of the refunding Parity Obligations will not exceed the sum of Adjusted Debt Service on all Parity Obligations Outstanding for all remaining Fiscal Years prior to the issuance of such refunding Parity Obligations; or (B) then Outstanding Balloon Indebtedness, Tender Indebtedness, or Variable Rate Indebtedness, but only to the extent that the principal amount of such indebtedness has been put, tendered to, or otherwise purchased pursuant to a standby purchase or other liquidity facility relating to such indebtedness. For additional information relating to the terms and conditions for the issuance of the Parity Obligations under the Master Installment Purchase Agreement, see "APPENDIX B – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS."

Issuance of Subordinated Obligations. Pursuant to the Master Installment Purchase Agreement, if (i) no Event of Default has occurred and is continuing, and (ii) no event of default or termination event attributable to an act of or failure to act by the City under any Credit Support Instrument has occurred and is continuing, the City may issue or incur additional Subordinated Obligations, and such Subordinated Obligations shall be paid in accordance with the provisions of the Master Installment Purchase

Agreement, provided that the City obtains or provides a certificate or certificates, prepared by the City or at the City's option by a Consultant, showing that:

(1) the Net System Revenues as shown by the books of the City for any 12 consecutive month period within the 18 consecutive months ending immediately prior to the incurring of such additional Subordinated Obligations shall have amounted to at least 1.00 times the Maximum Annual Debt Service on all Obligations that will be Outstanding immediately after the issuance of the proposed Subordinated Obligations; or

(2) the estimated Net System Revenues for the five Fiscal Years following the earlier of (a) the end of the period during which interest on those Subordinated Obligations is to be capitalized or, if no interest is to be capitalized, the Fiscal Year in which the Subordinated Obligations are issued; or (b) the date on which substantially all new facilities financed with such Subordinated Obligations are expected to commence operations, will be at least equal to 1.00 times the Maximum Annual Debt Service on all Obligations that will be Outstanding immediately after the issuance of the proposed Subordinated Obligations.

The certificate or certificates described in clauses (1) and (2) above will not be required if the Subordinated Obligations being issued are for the purpose of refunding (i) then-Outstanding Parity Obligations or Subordinated Obligations if at the time of the issuance of such Subordinated Obligations a certificate of an Authorized City Representative is delivered showing that the sum of Debt Service for all remaining Fiscal Years on all Parity Obligations and Subordinated Obligations Outstanding after the issuance of the refunding Subordinated Obligations will not exceed the sum of Debt Service for all remaining Fiscal Years on all Parity Obligations and Subordinated Obligations Outstanding prior to the issuance of such refunding Subordinated Obligations; or (ii) then-Outstanding Balloon Indebtedness, Tender Indebtedness, or Variable Rate Indebtedness, but only to the extent that the principal amount of such indebtedness has been put, tendered to, or otherwise purchased by a standby purchase agreement or other liquidity facility relating to such indebtedness. For additional information relating to the terms and conditions for the issuance of the Subordinated Obligations under the Master Installment Purchase Agreement, see "APPENDIX B – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS."

Issuance of Additional Bonds Under the Indenture

Pursuant to the Indenture, the Trustee may, upon Written Request of the Authority, by a supplement to the Indenture, establish one or more other series of Bonds (the "Additional Bonds") secured by the pledge made under the Indenture equally and ratably with any Bonds previously issued and delivered, including the 2010A Bonds, in such principal amount as shall be determined by the Authority, but only upon compliance with the following requirements and any additional requirements set forth in the applicable Supplemental Indenture, which are conditions precedent to the execution and delivery of Additional Bonds:

(a) No Event of Default shall have occurred and be then continuing;

(b) The Supplemental Indenture providing for the execution and delivery of such Additional Bonds shall specify the purposes for which such Additional Bonds are then proposed to be delivered, which shall be one or more of the following: (i) to provide moneys needed to provide for Project Costs by depositing into the Acquisition Fund the proceeds of such Additional Bonds to be so applied; (ii) to provide for the payment or redemption of Bonds then Outstanding under the Indenture, by depositing with the Trustee moneys or investments required for such purpose under the defeasance provisions set forth in the Indenture; or (iii) to provide moneys needed to refund or refinance all or part of any other current or future obligations of the City with respect to the funding of the Water System. Such Supplemental Indenture may, but shall not be required to, provide for the payment of expenses incidental to such purposes, including the Costs of Issuance of such Additional Bonds, capitalized interest with respect thereto for any period authorized under the Code (in the case of Tax-Exempt Bonds), and, in the case of any Additional Bonds intended to provide for the payment or redemption of existing Bonds or other Obligations of the City, expenses incident to calling, redeeming, paying, or otherwise discharging the Obligations to be paid with the proceeds of the Additional Bonds;

(c) The Authority shall deliver or cause to be delivered to the Trustee, from the proceeds of such Additional Bonds or from any other lawfully available source of moneys, an amount (or a Reserve Fund Credit Facility in an amount) sufficient to increase the balance in the Reserve Fund to the Reserve Requirement for all Bonds, including the Additional Bonds, to be then Outstanding;

(d) The Additional Bonds shall be payable as to principal on August 1 and as to interest on February 1 and August 1 of each year during their term, except that the first interest payment due with respect thereto may be for a period of not longer than 12 months;

(e) Fixed serial maturities or mandatory sinking account payments, or any combination thereof, shall be established in amounts sufficient to provide for the retirement of all of the Additional Bonds of such series on or before their respective maturity dates;

(f) The aggregate principal amount of Bonds and Additional Bonds executed and delivered shall not exceed any limitation imposed by law or by any Supplemental Indenture; and

(g) The Trustee shall be the Trustee for the Additional Bonds.

Nothing in the Indenture limits in any way the power and authority of the Authority to incur other obligations payable from other lawful sources. See "APPENDIX B – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS."

WATER SYSTEM ORGANIZATION AND MANAGEMENT

History of Water System

The City has managed and operated the Water System since 1901, when it purchased the privately-owned San Diego Water and Telephone Company, and has expanded the Water System from time to time to satisfy its mission statement, which is to provide safe, reliable water in an efficient, cost-effective, and environmentally responsible manner. In furtherance of its mission, the City and other local retail water distributors formed the San Diego County Water Authority ("CWA") in 1944 for the purpose of purchasing Colorado River water from the Metropolitan Water District of Southern California ("MWD") and conveying such water to local distributors within the County.

The 1.3 million people living in the City used an average of approximately 202 million gallons per day ("MGD") of potable water in Fiscal Year 2009. One MGD for one year is equal to approximately 1,120 acre feet per year ("AFY"). The City's population is projected to increase approximately 21% in the next 20 years and the City expects that this projected growth will increase demand for potable water by approximately 13%. The City currently provides water to its customers primarily from two water sources: (1) by collecting approximately 10 - 15% of its water needs through local supplies, and (2) by purchasing approximately 85 - 90% of its water from CWA, a wholesale water agency that provided approximately 557,762 acre-feet ("AF") of imported water to its member agencies in the County in Fiscal Year 2009. CWA currently purchases the majority of its imported water from MWD, which is comprised of 26 public water agencies. MWD obtains its water from the Colorado River through the Federal Bureau of Reclamation and from northern California, via the State Water Project, through the California Department of Water Resources. In Fiscal Year 2009, MWD sold approximately 2.0 million AF of imported water to customers. Both CWA and MWD are developing storage and additional supplies, such as water transfers, to augment their imported water. Since 2008, the drought conditions in the State have triggered the need for both voluntary and mandatory reductions in water use. See "WATER SUPPLY."

Governance and Management of Water System

General. The Water System is owned by the City and operated by the City through the Public Utilities Department. The Public Utilities Department is comprised of four branches that are funded by both the Water Utility Fund and the Sewer Utility Fund, depending upon which system benefits from the tasks completed. Though the different branches cover all tasks required by the Public Utilities Department, separate accounting is kept for each fund. The Public Utilities Department ultimately reports to the Mayor, who has operational authority over the Public Utilities Department and appoints managers and directors who are charged with the operations of the Public Utilities Department. The Director of Public Utilities, who reports to the Chief Operating Officer, oversees the Public Utilities Department. The day-to-day operational responsibility for the Public Utilities Department rests with the Business Support Branch Assistant Director, the Water Branch Assistant Director, and the Wastewater Branch Assistant Director, each of whom reports to the Director of Public Utilities. The Assistant Director for Strategic Programs completes the Utilities Senior Executive Team and leads organizational efficiency and strategic planning efforts, as well as asset management functions. The Public Utilities management team is further comprised of Deputy Directors who head each of the ten major divisions, plus two Program Managers who report to the Water and Wastewater Assistant Directors.

Prior to the completion of the reorganization of the Water and Wastewater Utilities into a joint Public Utilities Department on July 1, 2009, the Water Department and the Metropolitan Wastewater Department had been separately managed since July 1, 1996. Prior to 1996, both enterprise funds were managed as a joint operation as the City's Water Utilities Department. The Water Utility Fund portion of the Public Utilities Department had approximately 786 budgeted full-time equivalent employees as of July 1, 2009, and anticipates having approximately 729 budgeted full-time equivalent employees for Fiscal Year 2011. The City Council retains the authority to approve the Public Utilities Department's budget, to set rates and charges of the Water System, and to approve execution of certain contracts. For information on how the City sets the rates and charges of the Water System see "WATER SYSTEM FINANCIAL OPERATIONS – Establishment of Water Service Charges." In accordance with the provisions of the City Municipal Code, the Water Utility Fund and the Sewer Utility Fund are administered in an enterprise account separate from the City's General Fund.

The Public Utilities Department consolidation of certain administrative and financial functions common to the Water Utility Fund and the Sewer Utility Fund created opportunities for greater efficiency, reduced personnel costs, and enhanced services to both internal personnel and external customers. Based on consolidation efforts, a total of 31 positions from the Water Utility Fund and the Sewer Utility Fund were eliminated in the consolidation. The Water Utility Fund added ten water conservation positions in Fiscal Year 2010 to enhance services related to conservation efforts during the drought cycle.

Officers. The current Senior Executive officers of the Public Utilities Department managing the Water Utility and Sewer Utility Funds and their respective biographies are as follows:

Alex Ruiz. Mr. Alex Ruiz currently serves as the City's Interim Director of Public Utilities. He was previously the City's Utilities Business Support Branch Assistant Director. In his capacity as Assistant Director, Mr. Ruiz oversaw the day-to-day operations of all Business Support activities. Mr. Ruiz has been with the City for 21 years. During the past 12 years, he has served in various management capacities within the City's Public Utilities Department, including Deputy Director of both the Customer Support Division and the Water Operations Division. Previous responsibilities have included assignments to the office of the City Manager for special project activities, including an assignment as the City's Labor Relations Manager. Mr. Ruiz received his Bachelor's Degree from the University of California at San Diego.

Marsi Steirer. Ms. Marsi A. Steirer currently serves as the City's Interim Assistant Director for the Business Support Branch. A City employee for 24 years, Ms. Steirer has worked for the Water Branch for 21 years. Ms. Steirer was responsible for formulating several of the Water Branch's strategic initiatives, including the conservation program, a 30-year water resources plan, strategic business plan, and water reuse initiatives. Her previous duties included serving as the Deputy Director of Long-Range Planning and Water Resources and Water Policy, CIP Finance and Planning Divisions. She is a graduate of the University of California, Riverside, and American University, Washington, D.C. Ms. Steirer is a member of the American Water Works Association, and she currently serves on the Research Advisory Committee of the Water Research Foundation.

Jim Fisher. Mr. Jim Fisher currently serves as the City's Utilities Water Branch Assistant Director and oversees the day-to-day operation and maintenance of the water system. Mr. Fisher holds a Bachelor of Science degree in Civil Engineering from San Diego State University and is a licensed Professional Civil Engineer in the State of California. Mr. Fisher has been with the City of San Diego for 19 years and has experience in the design, construction, operation, and maintenance of water systems. Mr. Fisher holds a Grade 5 Water Treatment Plant Operator and Grade 4 Distribution Operator certification with the State of California.

Ann Sasaki. Ms. Ann Sasaki is the Assistant Director for the Wastewater Branch. In this capacity, Ms. Sasaki is responsible for all operational divisions in the Sewer Utility Fund. This includes the Environmental Monitoring and Technical Services Division which provides lab support to the Water Utility Fund and Sewer Utility Fund and the Engineering and Program Management Division, which provides Capital Project Development and Management to the Water Utility Fund and Sewer Utility Fund. Ms. Sasaki was appointed to the position of Assistant Director in July 2009. Ms. Sasaki began her career with the City in 1986 as a Junior Engineer in the Water Utilities Department and later served as a Senior Civil Engineer. Ms. Sasaki earned a Bachelor of Science degree in Civil Engineering from California State University, Long Beach, and a Masters in Business Administration from the University of San Diego. She is a licensed Professional Civil Engineer in the State of California.

Thomas Crane. Mr. Thomas Crane serves as the Assistant Director, Strategic Programs for the Public Utilities Department. Mr. Crane holds a Bachelor of Science degree in Civil Engineering from the University of Maryland and a Master of Engineering in Nuclear Engineering from Pennsylvania State University. Mr. Crane has been in this position for one year. He operated his own consulting business for 15 years after retiring from the United States Navy after more than thirty one years of service. He has extensive experience in infrastructure, contract, and utilities management. He is a licensed Professional Engineer in the Commonwealth of Pennsylvania.

Branches. The Business Support Branch is comprised of the following Divisions:

Long Range Planning and Water Resources Division. This division provides long-range facilities planning, water and wastewater legislation and policy analysis, water resources development, watershed and resources protection, and management of the City's recycled water and water conservation programs.

Financial and Information Technology Division. This division provides administrative support for the Water Utility Fund and the Sewer Utility Fund, including: information systems, budget development and monitoring, rate setting and finance, and contract and grant administration.

Customer Support Division. This division provides high quality customer focused care and service to Public Utility Department patrons. The division handles and responds to more than 529,000 customer phone calls and emails annually, including account/billing inquiries, water conservation information, water waste complaints, and general water/sewer utility information. In addition, this division is responsible for customer billing and payment processing, meter reading and code enforcement, ensuring customer compliance with state backflow device requirements, and public information.

Employee Services and Internal Controls Division. This division provides employee, management, and strategic support services, as well as safety, security, training, and internal controls. The Employee Services and Internal Controls Division is also involved in a number of internal business support services, including services relating to contract formulation and administration, human resources, organizational development, and audit support.

The Water Branch is comprised of the following Divisions:

Water Construction and Maintenance Division. This division provides construction, maintenance and emergency response for the Water System. The division maintains approximately 274,000 metered service connections, approximately 24,000 fire hydrants, and more than 46,000 isolation valves. In addition, this division provides 24- hour emergency response, new service installation, water main repair, capital improvement program support, and maintenance, installation, and replacement of meters throughout the City.

System Operations Division. This division provides operations and maintenance of the City's potable and recycled water systems. This division operates and maintains three water treatment plants, 49 water pump stations, 31 treated water reservoirs, and more than 950 water regulators. In addition, this division provides operational engineering support for the Water Branch and water supply management for the Public Utilities Department.

The Wastewater Branch is comprised of the following Divisions:

Engineering and Program Management Division. This division provides engineering services for the Water, Wastewater, and Reclaimed Water System to ensure new facilities, repairs, and upgrades are planned and implemented in a fiscally-sound manner to meet regulatory and environmental standards. This division also provides long-range master planning, development review, condition assessment, water and sewer modeling, planning and pre-design for infrastructure, energy management, environmental support, facility information management, and oversight of the implementation of the Water, Wastewater, and Reclaimed Water Systems' capital improvement programs.

Environmental Monitoring and Technical Services Division. This division provides laboratory services for the Water and Wastewater Systems to ensure water quality standards are maintained to meet regulatory and environmental standards.

Wastewater Collection Division. This division provides efficient operations and maintenance of the wastewater collection system.

Wastewater Treatment and Disposal Division. This division operates and maintains a wastewater treatment plant, two water reclamation plants, a bio-solids processing facility, and eight large wastewater pump stations. With these facilities, the division provides regional wastewater treatment and disposal services to the City and 15 surrounding cities and special districts.

Oversight. The Independent Rates Oversight Committee ("IROC") was established by City ordinance in 2007 to assume and expand upon the oversight previously undertaken by the Public Utilities Advisory Commission, which no longer exists. There are 11 members on IROC, all of whom are appointed by the Mayor and confirmed by the City Council. The membership of IROC consists of representatives of each ratepayer class and professional experts in such fields as finance, engineering, construction, and the environment. IROC serves as an official advisory body to the Mayor and the City

Council on policy issues relating to the oversight of Public Utilities Department operations including, but not limited to, resource management, planned expenditures, service delivery methods, public awareness and outreach efforts, efforts to achieve high quality, and affordable utility services provided by the Public Utilities Department. IROC's duties and functions include reviewing reports from staff and performing an independent performance review on rate and bond proceeds expenditures, advising on the efficiency and performance of the Water System and the Wastewater System, advising on future cost allocation models, and the preparation of an annual public report on such issues to the Mayor and City Council. IROC meets at least every other month to review activities and issues for the Public Utilities Department.

On March 22, 2010, IROC issued its "Annual Report on the San Diego Public Utilities Department for the Fiscal Year 2009" (the "2009 IROC Report"). The 2009 IROC Report included a series of recommendations related to the planning for safe, reliable, and cost-effective alternatives to imported water, water conservation, and wastewater reuse, including recommendations that the Public Utilities Department continue to devote resources to developing the upgrade of certain water treatment processes to fully implement indirect potable reuse strategies, and encouraged the Public Utilities Department to move forward with the Automatic Meter Reading program in order to reduce meter reading costs and maximize potential conservation benefits. The 2009 IROC Report also recommended adopting an ordinance to support the required installation of sub-meters in new multi-family developments as well as requiring retrofitting existing buildings upon major property renovation. With respect to capital improvements, the 2009 IROC Report recommended that the Public Utilities Department and the Engineering and Capital Projects Department, which is responsible for the execution of the approved capital improvement projects, work to procure comprehensive and quarterly schedule and budget reports to ensure adequate oversight and management of the Water System's capital improvement program ("CIP"). The 2009 IROC Report also recommended that, in regards to the cost of purchased water from CWA and MWD, additional oversight and due diligence be undertaken over both the CWA and MWD budgets, internal cost structures, and their related pass-through rate increases and that City staff represent the interests of the City's ratepayers before the Boards of Directors and staff of CWA and MWD. On April 19, 2010, IROC was presented with information regarding, and IROC unanimously supported, the proposed issuance of the 2010A Bonds.

WATER SYSTEM SERVICE AREA AND FACILITIES

Water System Service Area

The Water System serves the City and certain surrounding areas, including retail, wholesale, and reclaimed water customers. The Water System's service area covers 403 square miles, including 342 square miles in the City, and approximately 1.3 million retail customers. The map that follows the Table of Contents of this Official Statement shows the boundaries of the service area of the Water System.

Retail Customer Base. The City has six types of retail customer groups, consisting of Single Family Residential ("SFR"), Multi-Family, Commercial, Industrial, Temporary Construction, and Irrigation. For information relating to reclaimed water customers, see " – Reclaimed Water Customer Base" below. For Fiscal Year 2009 retail customers accounted for approximately 92% of total water deliveries and such sales represented approximately 94% of the revenues from total sales of water. Of the Water System's more than 270,000 retail service connections, approximately 91% are SFR and Multi-Family residential accounts, with the balance for Commercial, Industrial, and other users. For Fiscal Year 2009, SFR and Multi-Family residential accounts comprised approximately 60% of total water sales revenue, with the balance for Commercial, Industrial and other users. Some of the SFR, Multi-Family, Commercial, and Industrial accounts have been classified as Irrigation, as described below.

The City's residential users are classified into SFR and Multi-Family classes. As described in the December 14, 2006, Cost of Service Rate Study (as adopted by the City Council in 2007, the "2007 Rate

Case"), these residential classes are assumed to be homogenous in water usage and therefore are assigned the same peaking factors. It is noted however that usage and peaking will vary among the individual customers.

Single Family Residential. SFR refers to individual dwelling units served by a separate meter, and accounted for approximately 41% of total water sales revenues in Fiscal Year 2009.

Multi-Family. Multi-Family encompasses multi-family dwellings such as apartment or condominium complexes, in which two or more dwelling units share the same meter, and accounted for approximately 18% of total water sales revenues in Fiscal Year 2009.

Commercial and Industrial. Commercial and Industrial user classes are comprised of a diverse group of customers and accounted for 22% of total water sales revenues in Fiscal Year 2009. These customers are treated equivalently in cost calculations and are assigned the same peaking factors. These customers also typically have lower peaking factors than residential customers due to their relatively consistent usage trend.

Irrigation. Prior to July 2007, the City did not recognize "Irrigation" as a separate customer class. As there is sufficient data to separate these users into such a class, such a class was created by separating the SFR, Multi-Family, Commercial, and Industrial accounts that are used solely for irrigation into a new class. These customers use water primarily to irrigate personal or business landscaping. This diverse group of customers accounted for 12% of total water sales revenue for Fiscal Year 2009.

Temporary Construction. Temporary construction refers to meters that are placed on fire hydrants during construction in order to provide water to the construction site until the installation of a permanent meter. Costs for these customers are usually higher than the average customer because of additional administrative costs associated with transient meters. This group of customers generated less than 0.5% of total water sales revenue for Fiscal Year 2009.

Irrigation and Temporary Construction customers typically have high peak demands characterized by relatively large amounts of water used in short periods of time when compared to average usage. As described in the 2007 Rate Case, peak usage is more costly to deliver than constant usage.

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The following table sets forth the historical number of retail connections to the Water System for each year from Fiscal Year 2005 through 2009.

TABLE 1

HISTORICAL NUMBER OF RETAIL CONNECTIONS TO WATER SYSTEM
Fiscal Year 2005 through Fiscal Year 2009
(Unaudited)

Customer Type	2005	2006	2007	2008	2009
Single Family Residential	217,933	219,079	219,984	220,519	220,854
Multi-Family	29,234	29,276	29,239	29,208	29,193
Commercial	15,542	15,558	15,604	15,603	15,598
Industrial	269	253	231	215	205
Outside City (1)	50	48	45	46	45
Irrigation(2)	7,467	7,431	7,463	7,462	7,465
Temporary Construction	422	391	374	345	296
TOTAL	270,917	272,036	272,940	273,398	273,656
Percent Growth	0.42%	0.41%	0.33%	0.17%	0.09%

Source: Public Utilities Department, City of San Diego.
(1) Represents retail customers located beyond the City limits that the City has agreed to service. The City's billing system identifies each such account as a separate customer type; due to the small number of such customers, the group is not classified as individual customer class.
(2) Established as a separate customer classification in Fiscal Year 2008; amounts for Fiscal Years 2005 through 2007 were derived from historical reports.

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The following table sets forth the 10 largest non-governmental retail customers and the 10 largest governmental customers of the Water System for Fiscal Year 2009, which customers provided approximately 1.55% and 10.29%, respectively, of the total sales revenues for such Fiscal Year.

TABLE 2

MAJOR NON-GOVERNMENTAL RETAIL CUSTOMERS
AND MAJOR GOVERNMENTAL CUSTOMERS
Fiscal Year 2009
(Unaudited)

Customers	Millions of Cubic Feet	Billings	% of Total Sales Revenues
MAJOR NON-GOVERNMENTAL RETAIL CUSTOMERS			
CP Kelco	40.73	$1,145,195	0.35%
Marine Park Corp	28.60	789,425	0.24%
San Diego Zoo	24.21	672,528	0.21%
Marriott Full Service	14.06	402,701	0.12%
Coca Cola Bottling Co	13.51	370,818	0.11%
Costa Verde Dev LLC	11.44	359,257	0.11%
Qualcomm Inc	12.30	354,049	0.11%
Garden Communities	11.47	350,722	0.11%
The Irvine Holding Co	9.28	295,309	0.09%
Scripps Clinic	10.53	295,295	0.09%
TOTAL TOP 10 NON-GOVERNMENTAL RETAIL CUSTOMERS	176.13	$5,035,299	1.55%
MAJOR GOVERNMENTAL CUSTOMERS			
City of San Diego	411.33	$12,671,101	3.90%
United States Navy	275.95	8,608,031	2.65%
University of California at San Diego	103.37	2,974,429	0.92%
California Department of Transportation	72.82	2,315,796	0.71%
San Diego Unified School District	55.63	2,071,321	0.64%
Other Federal Agencies (1)	64.19	1,864,405	0.57%
San Diego State University	32.72	951,056	0.29%
San Diego Port District	28.82	928,662	0.29%
County of San Diego	19.33	615,359	0.19%
Poway Unified School District	13.39	420,867	0.13%
TOTAL TOP 10 GOVERNMENTAL CUSTOMERS	1,077.55	$33,421,027	10.29%

Source: Public Utilities Department, City of San Diego.
(1) Includes several Federal agencies, including, but not limited to, the United States Post Office, the Federal Bureau of Investigation, and the United States Coast Guard.

Wholesale Customer Base. For Fiscal Year 2009, wholesale customers accounted for approximately 6% of total water deliveries and such sales represented approximately 4% of the revenues from total sales and/or treatment of water. The City currently sells and delivers or treats and delivers water on a wholesale basis to five wholesale customers: (1) the California-American Water Company ("Cal-American"), (2) the City of Del Mar ("Del Mar"), (3) the Santa Fe Irrigation District, (4) the San Dieguito Water District (together with the Santa Fe Irrigation District, the "Water Districts"), and (5) the Otay Water District ("OWD").

Cal-American. Since 1912, the City has been selling and delivering treated water to Cal-American, which in turn provides water to the cities of Coronado and Imperial Beach, as well as a portion of the City. The City's obligation to sell and deliver water to Cal-American and its customers was assumed by the City upon its original acquisition of the Water System. The City's agreement with Cal-American has been subsequently amended to establish minimum and maximum amounts of treated water that may be purchased by Cal-American from the City, an average system delivery and a supply price methodology, which incorporates all of the City's integrated system-wide costs (i.e., the costs associated with treatment, storage and pumping of the treated water supplied to Cal-American), including 60% of the water purchase replacement costs, 17% of the transmission and distribution costs associated with usage of mains that are 16 inches and larger, and a proportionate share of debt service for capital costs of the Water System. For Fiscal Year 2009, the City made approximately 6% of its total water deliveries to Cal-American and such sales represented approximately 3% of the revenues from total sales of water. The rates established within the City's agreement with Cal-American are renewed on an annual basis and permit mid-year rate adjustments to account for any purchased water cost increases from CWA.

Del Mar. Pursuant to an existing contract between the City and Del Mar, the City treats raw water that Del Mar purchases from CWA. The treatment price paid by Del Mar is primarily based on the Del Mar's pro-rata share of the Operation and Maintenance expenditures (herein described) attendant to the City's provision and treatment services. For Fiscal Year 2009, deliveries from the treatment of Del Mar water represented less than 0.1% of total deliveries and less than 0.5% of revenues from total sales of water. The rates established within the City's agreement with Del Mar are renewed on an annual basis.

Water Districts. Pursuant to an existing contract between the City and the Water Districts, which runs in perpetuity, the City delivers raw water from the Lake Hodges Reservoir. The contract sets the terms and rates pursuant to which the applicable Water Districts may purchase water from the City and provides each Water District with the right to purchase a specified amount of water. The purchase price charged to each Water District is based on a portion of Operation and Maintenance expenditures and capital improvement costs related to the City's provision of water to such Water Districts. For Fiscal Year 2009, these water sales represented less than 0.1% of total deliveries and such sales represented less than 0.5% of the revenues from total sales of water. The rates established within the City's contract with the Water Districts are renewed every two years.

OWD. The City's Otay Water Treatment Plant (the "OWTP") is capable of producing treated water in excess of the amounts needed by the Water System customer base traditionally serviced by the OWTP. In 1999, the City entered into an agreement with OWD to deliver up to 10 MGD of surplus treated water, which deliveries began in November 2005. The amounts paid by OWD for such treated water are determined in part by allocating to the City and OWD, based on the amount of treated water produced for each, the projected cost and expenses of all operations, maintenance and overhead, capital improvements, repairs and replacements under $100,000 to be incurred for or at the OWTP. This cost per AF, as determined pursuant to the preceding sentence, is added to the raw water rate, to determine the projected actual cost to OWD for the next succeeding Fiscal Year. Pursuant to the agreement, OWD may elect to pay its proportional share of costs to expand the OWTP to meet its future treated water demands, estimated to be from 10 to 20 MGD. Any expansion would be subject to the City's discretion and the execution of a separate agreement.

Reclaimed Water Customer Base. Reclaimed water (also referred to as recycled water) is produced from wastewater processed at water reclamation plants owned and operated by the City as part of the City's Wastewater System. Since 1997, the reclaimed water produced by the City has been carefully monitored by City and State health officials and water quality-control agencies to ensure that it meets all federal, State, and local water quality standards, including the safety standards applicable to water coming into human contact set forth under Title 22 of the California Code of Regulations, and is suitable for irrigation, industrial, and other non-potable uses. The City began billing OWD and the Olivenhain Municipal Water District for reclaimed water in Fiscal Year 2007. The City also provides reclaimed water to the City of Poway under the terms of an agreement entered into in 1998. Pursuant to the Public Utilities Department's calculations, approximately $1 million is due each year from the City of Poway. However, the City of Poway and the City disagree about the cost per AF of water delivered pursuant to this agreement, though the resolution of this disagreement is not expected to have a material adverse impact on the Net System Revenues available to pay debt service on the 2010A Bonds. In addition, certain wholesale customers of the Wastewater System have asserted a claim to a percentage of the capacity fees and revenues from the sale of reclaimed water from the South Bay Water Reclamation Plant. The current amount in dispute is approximately $2 million. The capacity fees and revenues from the sale of reclaimed water are being held by the City pending resolution of this matter. From Fiscal Year 2005 to Fiscal Year 2008, the number of Reclaimed Water System customers ranged from 356 to 450. In Fiscal Year 2009, the Reclaimed Water System had 470 customers. In calendar year 2009, reclaimed water represented 3% of the City's water supply portfolio. For Fiscal Year 2009, reclaimed water customers and processing accounted for approximately 2% of total water deliveries and accounted for approximately 2% the revenues from total sales of water.

Existing Water System Facilities

The Water System consists of nine raw water storage reservoirs, three water treatment plants, 31 treated water storage facilities, and over 3,222 miles of water transmission and distribution lines. Water is transported through 49 water-pumping stations and approximately 274,000 metered service connections.

Raw Water Reservoirs. The City has nine reservoirs with a total capacity of 408,593 AF, of which 227,463 AF was in storage as of March 29, 2010. Eight of the raw water storage facilities are directly connected to water treatment plants. One of the nine raw water storage facilities, Lake Hodges Reservoir (30,251 AF total capacity), is currently being connected to the Olivenhain Reservoir (completion projected for 2010) and will be available for City use via CWA aqueducts and pursuant to an agreement between the City and CWA as part of the Emergency Storage Project (the "Emergency Storage Project"). The project was developed through CWA to provide approximately 90,100 AF of reservoir storage and supporting distribution facilities to supplement existing emergency water supplies in the County in case of a prolonged interruption of imported water supplies. The City has agreements with the Water Districts to sell local runoff collected at the Lake Hodges Reservoir. The amount of water sold varies from year to year but has historically averaged approximately 6,000 AF on an annual basis. The Lower Otay Reservoir, Barrett Reservoir and Morena Reservoir (135,348 AF total capacity) service the OWTP in south San Diego; the El Capitan Reservoir, San Vicente Reservoir, Sutherland Reservoir and Lake Murray Reservoir (236,311 AF total capacity) service the Alvarado Water Treatment Plant (the "AWTP") in central San Diego; and the Miramar Reservoir (6,682 AF total capacity) services the Miramar Water Treatment Plant (the "MWTP") in north San Diego. According to City Council policy, the City shall have approximately 7.2 months of the annual (rolling 12 months) requirement of the City's demand available in primary water storage facilities. This water is to be used during emergencies, in the event of substantial disruption or interruption of imported water service. This required amount is currently maintained by the City's Water System. As of March 29, 2010, the City held approximately 7.5 months of storage within the City's reservoirs.

In 2006, a number of the City's raw water storage reservoirs were listed as "impaired" water bodies pursuant to Section 303(d) of the Federal Clean Water Act as a result of an initiative to apply federal wastewater standards to drinking water reservoirs. The City currently has a proactive watershed protection and improvement plan for its reservoirs.

The following table sets forth the City's raw water reservoirs and their respective storage capacities and storage levels.

TABLE 3

RAW WATER RESERVOIRS
(As of March 29, 2010)

Reservoir	Storage Capacity (AF)	Storage (AF)	Percent Full
Lake Hodges	30,251	20,590	68%
Lower Otay	49,849	35,938	72
Barrett	34,806	32,115	92
Morena	50,694	8,107	16
El Capitan	112,807	75,300	67
San Vicente	89,312	37,952 (1)	43
Sutherland	29,508	7,945	27
Lake Murray	4,684	4,160	89
Miramar	6,682	5,356	80
TOTAL	408,593	227,463 (2)	56 (3)

Source: Public Utilities Department, City of San Diego.
(1) Approximately 55% of the raw water stored at the San Vicente Reservoir was drawn down by the end of Fiscal Year 2009 in connection with improvements thereto.
(2) Figure includes small amount of water that is not accessible due to reservoir outlets being abandoned, blind flagged, or silted. Amount not available for usage is approximately 2% - 3% of total Storage amount.
(3) Figure represents percentage of Storage Capacity held in storage.

Water Treatment Plants. The Public Utilities Department maintains and operates three water treatment plants with a combined rated capacity of 294.2 MGD through which potable water is supplied. Supplemental treated supplies from CWA are used to help operate the distribution system reliably and efficiently. Ongoing upgrades to all three plants are expected to increase future rated capacity to 455 MGD and improve the City's ability to treat raw water, thereby further reducing the need to purchase treated water and providing capacity for customer growth. Of the total of 202,225 AF of water purchased from CWA during Fiscal Year 2009, approximately 23,892 AF was treated water. This represents a reduction in treated water purchases of approximately 9,098 AF compared to the projected purchase amount of 32,990 AF.

Alvarado Water Treatment Plant. The AWTP was originally constructed in 1951 and has a current rated capacity of 120 MGD. Several hydraulic improvements constructed in the mid-1970s and additional upgrades completed recently will, upon approval by DPH, increase the plant from its current rated capacity of 120 MGD to a rated capacity of 150 MGD. The AWTP is located next to Murray Reservoir near Interstate 8 and serves the general area from National City to the San Diego River. The CIP includes further upgrades that are designed to increase the AWTP's rated capacity to 200 MGD by Fiscal Year 2011.

Miramar Water Treatment Plant. The MWTP was originally constructed in 1962 and has a current rated capacity of 140 MGD. The MWTP is located next to Miramar Reservoir off Interstate 15. The MWTP provides drinking water to an estimated 500,000 customers in the general area north of the San Diego River. The CIP includes various upgrades to the plant, which are expected to increase the MWTP's rated capacity to 215 MGD by Fiscal Year 2011. This will further reduce the need to purchase treated water. Expansion of the raw water aqueducts by CWA will provide the MWTP access to water from San Vincente and Hodges Reservoirs.

Otay Water Treatment Plant. The current OWTP was constructed in 1989 and has a current rated capacity of 34.2 MGD. The OWTP serves the general area along the Mexico border and the southeastern portions of central San Diego. The CIP includes an upgrade to the plant that is designed to increase its rated capacity to 40 MGD by Fiscal Year 2011.

The following table summarizes the capacity and demands of the three Water Treatment Plants.

TABLE 4

CAPACITY AND DEMAND OF WATER SYSTEM WATER TREATMENT PLANTS
(In MGD)
As of December 31, 2009

Water Treatment Plant	Original Design Capacity	Current Rated Capacity	Future Rated Capacity(1)	Current Average Demand	Current Peak/Max Demand
Alvarado	66	120.0	200	84.3	108.7
Miramar	100	140.0	215	74.2	117.6
Otay	40	34.2	40	13.0	27.8
Total	206	294.2	455	171.5	254.1(2)

Source: Public Utilities Department, City of San Diego.

(1) Future Rated Capacity is based upon the completion of projects described above relative to the AWTP, MWTP and OWTP in the CIP by Fiscal Year 2011.

(2) Total is not intended to reflect the aggregate peak/maximum demand supported by all water treatment plants because such plants do not all reach the peak/maximum demand simultaneously.

Treated Water Storage Facilities. The Public Utilities Department maintains and operates 31 treated water storage facilities, including steel tanks, standpipes, concrete tanks, and rectangular concrete reservoirs. These facilities have capacities varying from less than 1 million gallons to 35 million gallons and in the aggregate hold a daily total of approximately 250 million gallons.

Delivery System. The Water System consists of approximately 3,222 miles of transmission and distribution pipelines, including transmission lines up to 84 inches in diameter and distribution lines as small as four inches in diameter. Transmission lines are pipelines with larger diameters that convey raw water to the water treatment plants and convey treated water from the water treatment plants to the treated water storage facilities. Distribution lines are pipelines with smaller diameters that directly service the retail users connected to a meter. The Public Utilities Department also maintains and operates 49 water pump stations that deliver treated water from the water treatment plants to approximately 274,000 metered service connections in over 128 different pressure zones. In addition, the Public Utilities Department maintains several emergency connections to and from neighboring water agencies, including the Santa Fe Irrigation District, the Poway Municipal Water District, Cal-American, the Sweetwater Authority and the Otay Water District.

For Fiscal Year 2009, the City's average daily water use, including Del Mar and Cal-American deliveries, was approximately 202 MGD, with peak day demands as high as 282.5 MGD. The City's three Water Treatment Plants provided 181.6 MGD, or 89.4%, of average demand and 235.5 MGD, or 83.4%, of peak demand. Due to current operational limitations with respect to the distribution system, City average and peak daily water demands are met with a combination of City-treated water and treated water supplied by CWA primarily through four metered treated water connections.

Insurance for the Water System

The City, through the statewide joint power authority risk pool, the California State Association of Counties-Excess Insurance Authority ("CSAC-EIA"), maintains an "All Risk" policy that includes Flood and Earthquake coverage for scheduled locations for amounts up to $25,000,000 per occurrence with a $25,000 deductible. The City also maintains an excess liability insurance policy in collaboration with a statewide joint powers authority risk pool, the CSAC-EIA for amounts up to $50,000,000; the City's self-insured retention is $5,000,000.

Utility Costs

The Water System is supplied with electricity and gas by an investor owned utility. The energy and utility services account for approximately 2% of the Water System's annual operating budget. To date, the Water System has not experienced any significant power shortages and there has not been any disruption in service to the Water System. Further, the Water System has sufficient self-generating resources to provide water services to domestic customers in the event of the occurrence of more significant power shortages. The Public Utilities Department recently completed installation of a 1 megawatt photovoltaic solar panel "farm" at the AWTP, which supplies approximately 40% of the local electrical demand.

WATER SUPPLY

Current Water Supply

The Water System currently receives its water supply from two sources: (1) local runoff and (2) water imported by CWA. Historically, approximately 10% to 15% of the water supply for the Water System comes from local rain runoff. This runoff is seasonal and variable in nature. The balance of the Water System water supply is imported from Northern California and the Colorado River and is supplied to the City by CWA, of which the City is a member agency.

The City is the largest purchaser of water from CWA, purchasing approximately 36% of the total imported water provided by CWA to its member agencies for Fiscal Year 2009. During Fiscal Year 2009, the Public Utilities Department purchased approximately 202,225 AF of water from CWA at a cost of $118.2 million. Currently, the City pays CWA $599 per AF for untreated water and $814 per AF for treated water. Approximately 9% of the City's water purchases are for treated water.

CWA Water Supply Rates (1)
Fiscal Years 2005 through 2010
(Per AF)

Fiscal Year	Municipal & Industrial (M&I) Rates (2) Untreated	Treated	Transportation Rate
2005	$349	$461	$55
2006	$360	$485	$60
2007	$365	$512	$60
2008	$390	$554	$60
2009	$463	$631	$64
2010	$532	$747	$67

Source: Public Utilities Department, City of San Diego.
(1) Rates for volumetric charges. Rates do not include additional charges such as Infrastructure Access Charge, Customer Service Charge, Storage Charge, Capacity Charge, or In-Lieu Charge.
(2) Rates as of June 30 for each fiscal year.

The following table sets forth the City's local water production and CWA supplied water for Fiscal Years 2005 through 2009.

TABLE 5

WATER SUPPLIES FOR THE CITY OF SAN DIEGO
Fiscal Years 2005 through 2009
(In AF)

Fiscal Year	Local Supplies	CWA Water Supplies	Total
2005	28,477	202,251	230,728
2006	40,844	197,361	238,205
2007	18,709	229,682	248,391
2008	25,911	219,323	245,234
2009	24,460	202,225	226,685

Source: Public Utilities Department, City of San Diego.

San Diego County Water Authority

The San Diego County Water Authority was organized on June 9, 1944, under the County Water Authority Act (the "CWA Act"). The primary mission of CWA is to provide its member agencies with a safe and reliable water supply. Pursuant to the CWA Act, CWA is authorized to acquire water and water rights within or outside the State of California and to develop, store, and transport such water. The CWA Act also authorizes CWA to exercise the power of eminent domain; to levy and collect taxes; to fix, prescribe, and collect rates or other charges for the delivery of water, use of facilities or property or provisions for service; and to fix in each fiscal year a water standby availability charge on land within the boundaries of CWA to which water is made available by CWA.

CWA consists of 24 member public agencies and creates a service area that encompasses approximately 952,200 acres (1,488 square miles), covering the foothills and coastal areas of the westerly third of San Diego County. The City of San Diego represents the largest land area (approximately 22%), the largest population (approximately 43%), and the highest assessed property value (approximately 47%) within CWA's service area. When CWA was established in 1944, its service area consisted of 94,707 acres. Growth has primarily resulted from the addition and annexation of additional service areas by member agencies.

The decision-making body of CWA is its 37-member Board of Directors. Each of the member agencies of CWA has at least one representative on the CWA Board of Directors. Any member agency may appoint one additional representative for each full 5% of total assessed value of property taxable for CWA purposes that is within the public agency's boundaries. As a result, the City is entitled to representation by 10 directors. Under the CWA Act, a member agency's vote is based on its "total financial contribution" to CWA since CWA's organization in 1944. Total financial contribution includes all amounts paid in taxes, assessments, fees, and charges to or on behalf of CWA or MWD. The CWA Act authorizes each CWA Board of Directors member to cast one vote for each $5,000,000, or major fractional part thereof, of the total financial contribution paid by the member agency. Based on this formula, the City is entitled to approximately 40% of all the votes. For comparison, the Helix Water District has the second highest voting entitlement, with approximately 7% of all the votes.

Since 1990, CWA has provided an average of 85% of the water supply within its service area. In Fiscal Year 2009, 202,225 acre-feet of water, or approximately 89% of the water supplies for the City, was delivered from CWA. The City projects that, with increases in the sale of reclaimed water and consistent use of local water sources, City purchases of water from CWA could drop to approximately 83% by Fiscal Year 2015.

As a wholesaling entity, CWA has no retail customers, but serves only its member agencies. Water supplies utilized within the CWA service area originate from two sources: (1) water imported by CWA from MWD and (2) local supplies (such as local runoff, groundwater, reclamation, conservation, and, prospectively, seawater desalination), with the water imported from MWD being the principal source of water supply. MWD obtains its water supply from two primary sources: the Colorado River, via the MWD's Colorado River Aqueduct, and the State of California Department of Water Resources' State Water Project, via the Edmund G. Brown California Aqueduct.

Drought conditions, population growth, and legal challenges have highlighted the need for diversification of the CWA water supply. As such, CWA has actively pursued a strategy of supply diversification that includes the acquisition and importation of additional water supplies, the development of additional local water supply projects, and augmentation of its water supply via local and regional water storage capacity.

CWA has made significant strides in diversifying water supplies for the San Diego region since 1991 when CWA imported water supplies only from MWD and had no rights to independent water supplies. Foremost among its efforts, CWA successfully negotiated and secured independent water rights associated with the Quantification Settlement Agreement (the "QSA") in 2003.

The QSA was enacted in October 2003 to provide the State of California the means to implement water transfers and supply programs that will allow the State to live within the State's 4.4 million acre-foot basic annual apportionment of Colorado River water. The QSA and its related water transfers and other agreements were signed by the United States Secretary of the Interior and representatives of various Indian tribes, the United States Bureau of Reclamation, the Coachella Valley Water District, the Imperial Irrigation District (the "IID"), MWD, and CWA. The QSA outlines how the State will reduce its overuse of Colorado River water over a fifteen year period. CWA's Colorado River Program manages the implementation of CWA's agreements under the QSA, including the water transfer agreement with the IID and the concrete lining of portions of the All-American and Coachella Canals. Under the QSA, CWA projects to receive 30% of its water supply from the water transfer and canal lining projects by 2020. The

QSA also commits to a restoration path for the environmentally sensitive Salton Sea and provides full mitigation for these water supply programs. The QSA was to provide the State up to 75 years of stability in its Colorado River water supplies.

Pursuant to the QSA and its related agreements, CWA is able to purchase up to 200,000 AF per year of conserved water from the IID. The agreement provides that water saved through conservation measures in Imperial Valley will be transferred to CWA. This water is highly reliable because it comes from the IID's Colorado River Water Priority 3 allocation. See the table entitled "Priorities under the 1931 California Seven-Party Agreement" under " – Metropolitan Water District of Southern California" below. These priorities are higher than MWD's fourth priority allocation of 550,000 AF. This means that water will likely remain available for transfer even during drought periods. Implementation of the water transfer began in calendar year 2003 with a transfer of 10,000 AF of water. The quantities of water transferred will increase according to an agreed-upon delivery schedule, ultimately providing up to 200,000 AF of water in calendar year 2021. This amount will continue to be transferred between 2021 and as late as 2077. In calendar year 2010, CWA is projected to purchase 80,000 AF from the IID as part of the ramped-up schedule of deliveries.

Also pursuant to the QSA, CWA receives approximately 78,000 AF per year of water conserved as a result of recently completed construction projects lining portions of the previously earthen All-American and Coachella Canals. The All-American Canal Lining Project will yield approximately 56,200 acre-feet of Colorado River water transfers per year to CWA and the Coachella Canal Lining Project will yield approximately 21,500 acre-feet per year to CWA. The canal lining projects will reduce the loss of water that occurred through seepage and that conserved water will be delivered to CWA. The Coachella Canal Lining Project was completed in December 2006. The All-American Canal Lining Project began construction in June 2007. This project is being built in three phases. The final phase is expected to be completed in 2010. The IID has certain limited call rights to a portion of the conserved water, but exercise of call rights would extend the term of the deliveries to CWA. The cost of the canal lining projects was in large part paid by State funds.

QSA related litigation. In November 2003, the IID brought litigation to "validate" 13 of the QSA related contracts as complying with California and federal law. The litigation also involves a review of the IID environmental impact report for the water transfers and the IID, CWA, MWD, and Coachella Valley Water District (the "CVWD") program environmental impact report for the QSA. All QSA related litigation has been coordinated in Sacramento County Superior Court.

One of the key issues of the pending QSA litigation is the constitutionality of the Quantification Settlement Agreement Joint Powers Authority Creation and Funding Agreement (the "QSA Funding Agreement"), pursuant to which the IID, the CVWD and CWA agreed to commit $133 million toward certain mitigation costs associated with implementation of the water transfer agreements, and $30 million toward the cost of restoration of and mitigation for the Salton Sea, with the State agreeing to be responsible for any costs exceeding those amounts.

In February 2010, Sacramento County Superior Court Judge Roland Candee invalidated the QSA on grounds that a provision in the contract failed to cap the State's Salton Sea environmental mitigation fees. The tentative ruling holds that the State's commitment was unconditional in nature and, as such, violated the State's debt limitation under the California Constitution. This judgment is being appealed. The QSA water transfers will continue through the appeal process.

Local supply and storage programs. CWA has encouraged development of additional water supply projects such as water recycling and groundwater projects through the award of Local Water Supply Development ("LWSD") incentives of up to $200 per AF for recycled water and groundwater produced and beneficially reused within CWA's service area. The purpose of CWA's LWSD Program is to promote the development of cost-effective water recycling and groundwater projects that prevent or reduce the demand for imported water and improve regional water supply reliability. The LWSD Program reimburses member agencies for all or a portion of the difference between the actual per AF cost of producing recycled water, and the revenue generated by the LWSD participant through the sale of that AF of recycled water (not to exceed $200 per AF). In February 2008, the LWSD Program was expanded to include funding for local brackish groundwater and seawater desalination projects.

CWA's local surface water program is responsible for optimizing the storage of runoff that occurs in the watersheds within CWA's service area with the storage of imported water. On average, local surface water is projected to supply nearly 7% of the region's annual water demands. Expansion of CWA's carryover storage capacity is a key part of local surface supply development. By 2015, CWA expects the San Vicente Dam Raise to raise the San Vicente Dam's height by an additional 117 feet, which is projected to yield an additional 152,500 AFY in local surface storage for imported supplies.

In 2004, CWA adopted a Regional Water Facilities Master Plan, which calls for additional supply diversification, specifically calling for up to 80,000 MGD of desalinated seawater to meet projected 2030 regional demands. A proposed 50 MGD seawater desalination project in Carlsbad has successfully cleared all regulatory requirements and is expected to begin construction soon. Additionally, CWA is exploring potential additional seawater desalination projects in the region and Mexico.

Metropolitan Water District of Southern California

The Metropolitan Water District of Southern California was created in 1928 by a vote of the electorates of several southern California cities. MWD's primary purpose is to provide a supplemental supply of water for domestic and municipal uses and purposes at wholesale rates to its member public agencies. There are 26 member public agencies of MWD, consisting of 14 cities, 11 municipal water districts, and CWA. MWD's service area comprises approximately 5,200 square miles and includes all or portions of the counties of Los Angeles, Orange, Riverside, San Bernardino, San Diego, and Ventura. MWD is governed by a 27-member Board of Directors, with each member agency having at least one representative on the Board of Directors. Representation and voting rights are based upon the assessed valuation of real property within the jurisdictional boundary of each member agency. CWA has four members on the MWD Board of Directors. The total population of the MWD service area is currently estimated at more than 18 million. MWD serves its member agencies as a water wholesaler and does not have any retail customers.

MWD imports water from two principal sources, the State Water Project in Northern California, via the California Aqueduct, and the Colorado River, via the Colorado River Aqueduct. In Fiscal Year 2009, MWD supplied approximately 2.0 million AF of water to its member agencies. During years of normal precipitation, MWD's existing water supplies have been historically sufficient to meet demands within the service area of MWD. In the future, several factors could impact to some extent the availability of both existing and future supplies in normal years.

Colorado River. The Colorado River was MWD's original source of water after MWD's establishment in 1928. The Colorado River Aqueduct, which is owned and operated by MWD, is 242 miles long, starting at Lake Havasu and terminating at Lake Matthews in Riverside County.

Under applicable laws, agreements, and treaties governing the use of water from the Colorado River, the State is entitled to use 4.4 million AF of Colorado River water annually, plus one-half of any surplus that may be available for use collectively in Arizona, California, and Nevada as declared on an annual basis by the United States Secretary of the Interior. Under the priority system that governs the distribution of Colorado River water made available to California, MWD holds the fourth priority right of 550,000 AFY and a fifth priority right of 662,000 AFY. MWD's fourth priority right is within

California's basic annual apportionment of 4.4 million AF; however, the fifth priority right is outside of this entitlement and therefore is not considered a firm supply of water. See the table below, which outlines the water allocation priorities under the governing 1931 California Seven-Party Agreement.

PRIORITIES UNDER THE 1931 CALIFORNIA SEVEN-PARTY AGREEMENT(1)

Priority	Description	Acre-Feet Annually
1	Palo Verde Irrigation District gross area of 104,500 acres of land in the Palo Verde Valley	3,850,000
2	Yuma Project in California not exceeding a gross area of 25,000 acres in California	
3(a)	Imperial Irrigation District and other lands in Imperial and Coachella Valleys(2) to be served by All-American Canal	
3(b)	Palo Verde Irrigation District – 16,000 acres of land on the Lower Palo Verde Mesa	
4	Metropolitan Water District of Southern California for use on the coastal plain	550,000
	SUBTOTAL	**4,400,000**
5(a)	Metropolitan Water District of Southern California for use on the coastal plain	550,000
5(b)	Metropolitan Water District of Southern California for use on the coastal plain (3)	112,000
6(a)	Imperial Irrigation District and other lands in Imperial and Coachella Valleys to be served by the All-American Canal	300,000
6(b)	Palo Verde Irrigation District – 16,000 acres of land on the Lower Palo Verde Mesa	
	TOTAL	**5,362,000**
7	Agricultural use in the Colorado River Basin in California	Remaining surplus

Source: Metropolitan Water District.

(1) Agreement dated August 18, 1931, among Palo Verde Irrigation District, Imperial Irrigation District, Coachella Valley County Water District, Metropolitan, the City of Los Angeles, the City of San Diego and the County of San Diego. These priorities were memorialized in the agencies' respective water delivery contracts with the Secretary of the Interior.

(2) The Coachella Valley Water District serves Coachella Valley.

(3) In 1946, the City of San Diego, the Water Authority, MWD and the Secretary of the Interior entered into a contract that merged and added the City of San Diego and the County of San Diego's rights to storage and delivery of Colorado River water to the rights of MWD.

Until 2003, MWD had been able to take full advantage of its fifth priority right as a result of the availability of surplus water and apportioned but unused water. However, Arizona and Nevada have increased their use of water from the Colorado River, leaving no unused apportionment available for California. In addition, a severe drought in the Colorado River Basin reduced storage in system reservoirs, such that MWD stopped taking surplus deliveries in 2003 in an effort to mitigate the effects of the drought. Prior to 2003, MWD could divert over 1.2 million acre-feet in any year, but since that time, MWD's net diversions of Colorado River water have been limited to a low of approximately 633,000 acre-feet in 2006 and a high of approximately 905,000 acre-feet in 2008. Average annual net deliveries for 2003 through 2008 were approximately 762,000 acre-feet, with annual volumes dependent primarily on availability of unused higher priority agricultural water and increasing transfers of conserved water. In 2009, MWD's Colorado River Aqueduct deliveries exceeded 1 million AF for the first time since 2002.

State Water Project. MWD's other major source of water is the State Water Project (the "SWP"). The SWP is owned by the State and operated by the Department of Water Resources ("DWR").

The SWP transports Feather River water stored in and released from Oroville Dam and unregulated flows diverted directly from the Bay-Delta south via the California Aqueduct to four delivery points near the northern and eastern boundaries of MWD. The total length of the California Aqueduct is 444 miles.

MWD is one of 29 agencies that have long-term contracts for water service from DWR and it is the largest agency in terms of the number of people it serves (approximately 18 million), the share of the SWP water for which it is entitled, and the total amount of annual payments made to DWR. MWD's contract with DWR provides for the delivery of 1,911,400 AF (46% of the total SWP entitlement). MWD also retains a "call" on 100,000 AFY on water transferred to the Coachella Valley Water District and the Desert Water Agency, if needed, so long as it pays for the financial obligations associated with the water during the call period.

The SWP was originally intended to meet demands of 4.2 million acre-feet per year. Initial SWP facilities were completed in the early 1970's, and it was envisioned that additional facilities would be constructed as contractor demands increased. Several factors, including increased costs and increased non-SWP demands for limited water supplies, combined to delay the construction of additional facilities. Water received from the SWP by MWD from 2002 through 2008, including water from water transfers, groundwater banking, and exchange programs varied from a low of 1,040,000 AF in calendar year 2008 to a high of 1,794,000 AF in calendar year 2004. MWD's allocation from the SWP for calendar year 2008 was 35% of its contracted amount, or 669,000 AF. MWD received approximately 1,040,000 AF of water using the SWP's California Aqueduct in 2008, including the allocation from the SWP and deliveries from water transfers, groundwater banking and exchange programs.

For calendar year 2009, DWR's October 2008 initial allocation estimate, an early estimate provided by DWR for the projected total allocation of water from the SWP, was set at 15% of contracted amounts. This estimate was adjusted upwards to 20%, 30%, and 40% of contracted amounts as of March 18, 2009, April 15, 2009, and May 20, 2009, respectively. This reduced allocation from the SWP reflects that water storage in the State's major reservoirs and runoff projections remained below average and regulatory restrictions on water exports from the Bay-Delta to protect listed fish species. Under the 40% allocation of contracted amounts, MWD received approximately 765,000 AF from its basic allocation and approximately 923,000 AF of total water from the SWP.

For calendar year 2010, DWR's November 2009 initial allocation estimate was set at 5% of the contracted amounts. The allocation estimate was adjusted upwards to 15% on February 23, 2010, and adjusted to 20% on March 30, 2010. On May 3, 2010, upon the completion of its most recent snowpack survey, DWR announced that the water supply allocation would be adjusted upward to 40% of the contracted amounts, mirroring the final allocation for calendar year 2009. DWR will conduct its final snowpack survey at the end of May 2010 for the final allocation for calendar year 2010. The average of SWP deliveries over the past 10 years is 68% of the amount requested by the 29 public agencies with long-term contracts to buy SWP water.

Environmental Concerns. The listing of several fish species as threatened or endangered under the federal or California Endangered Species Acts (respectively, the "Federal ESA" and the "California ESA" and, collectively, the "ESAs") have adversely impacted SWP operations and limited the flexibility of the SWP. An annual environmental water account established under the CALFED Bay-Delta Program (a collaboration of 25 state and federal agencies) as a means of meeting environmental flow requirements and export limitations has helped to mitigate these impacts. Currently, five species (the winter-run and spring-run Chinook salmon, Delta smelt, North American green sturgeon, and Central Valley steelhead) are listed under the ESAs. In addition, on June 25, 2009, the California Fish and Game Commission declared the long fin smelt a threatened species under the California ESA. The Federal ESA requires that before any federal agency authorizes funds or carries out an action it must consult with the appropriate federal fishery agency to determine whether the action would jeopardize the continued existence of any threatened or endangered species, or adversely modify habitat critical to the species' needs. The result of the consultation is known as a "biological opinion." In the biological opinion, the federal fishery agency determines whether the action would cause jeopardy to a threatened or endangered species or adverse modification to critical habitat and recommends reasonable and prudent alternatives or measures that would allow the action to proceed without causing jeopardy or adverse modification. The biological opinion also includes an "incidental take statement." The incidental take statement allows the action to go forward even though it will result in some level of "take," including harming or killing some members of the species, incidental to the agency action, provided that the agency action does not jeopardize the continued existence of any threatened or endangered species and complies with reasonable mitigation and minimization measures recommended by the federal fishery agency.

The United States Fish and Wildlife Service released the new biological opinion on December 15, 2008 setting forth its determination that the coordinated operations of the Central Valley Project and the SWP, as proposed, are likely to jeopardize the continued existence of the Delta smelt and adversely modify Delta smelt critical habitat. The biological opinion includes various alternative actions to address protection of the adult Delta smelt life stage, protection of larval and juvenile Delta smelt, improvement of habitat for Delta smelt growth and rearing, habitat restoration and monitoring and reporting and specifies "take" thresholds to address jeopardy to the species or destruction or adverse modification of critical habitat when the alternative actions are implemented. Based on the Water Allocation Analysis released by DWR on December 19, 2008, which analyzed the biological opinion's effects on SWP operations, export restrictions of water from the SWP under median hydrologic conditions could impact deliveries to MWD in the range of 300,000 to 700,000 AF annually.

Several legal challenges of completed biological opinions regarding the Delta smelt have been filed and have been consolidated into the Delta Smelt Consolidated Cases. Several legal challenges relating to biological opinions regarding the salmonid species have been filed and have been consolidated into the Consolidated Salmon Cases. The City is monitoring these developments, as these legal challenges would be a factor that could affect the SWP allocation to MWD, the water deliveries to CWA, and that ultimately could have an adverse affect on the water delivers to the City.

While MWD plans and manages reserve supplies to account for normal occurrences of drought conditions, the current prolonged drought conditions and regulatory restrictions on SWP operations, including but not limited to restrictions under the Federal and California Endangered Species Acts, have placed limitations on MWD's ability to provide water to its member agencies.

Agency Actions

MWD's declared policy is to meet all the supplemental needs of each of its member agencies. However, in late 2007, MWD first notified its member agencies that it expected considerable supply challenges that would result in insufficient core supplies from the Colorado River and SWP to meet demand. MWD announced it would draw from its Water Surplus and Drought Management supplement storage supplies to meet demands. This action triggered the implementation of CWA's Drought Management Plan, which was developed with member agency input and adopted by CWA's Board of Directors in 2006. The CWA Drought Management Plan contains a list of water management actions available to CWA during drought conditions to avoid or reduce impacts due to supply shortages. These actions are organized into three progressive stages that include: voluntary supply management, supply enhancement, and mandatory cutbacks. The declaration by MWD allowed CWA to proceed with the prescribed actions of its Drought Management Plan as necessary.

In February 2008, MWD's Board of Directors adopted a shortage allocation method. The method allows MWD, in the event of shortages, to allocate water based on uniform reduction by class of water service, with adjustments made for growth, loss of local supply, demand hardening due to implementation of water conservation, and the amount a member agency's dependence on MWD for its total water supply, as well as other water supply related factors.

On February 27, 2009, Governor Arnold Schwarzenegger proclaimed a state of emergency related to the ongoing drought and ordered immediate action to manage the crisis. In the proclamation, the Governor used his authority to direct all State government agencies to utilize their resources, implement a State emergency plan, and provide assistance for people, communities, and businesses impacted by the drought.

In response to continuing drought conditions and regulatory restrictions on water supplies from Northern California, the MWD Board of Directors announced on April 14, 2009, that water supply deliveries from MWD to CWA would be reduced by 13%. This reduced supply allocation would be in effective from July 1, 2009, through June 30, 2010.

On April 23, 2009, the CWA Board of Directors took actions to ensure the San Diego region does not exceed its reduced water supply allocation from MWD, implementing water supply cutbacks to its 24 member retail water agencies by approximately 8% (on average), effective July 1, 2009. CWA was able to partially mitigate the cutbacks put forth from MWD. Additionally, the CWA Board of Directors declared a Level 2 Drought Alert (the "Level 2 Drought Alert"), the second level of CWA's four-level model drought ordinance. The Level 2 Drought Alert enables CWA's 24 member retail water agencies to adopt mandatory conservation measures for residents and businesses, including use restrictions and tiered water rates that charge more for excessive water use.

For Fiscal Year 2011, MWD and CWA have announced that, initially, allocation estimates are anticipated to be similar to the Fiscal Year 2010 allocations. Actual deliveries and revised allocations for Fiscal Year 2011 are expected to increase during the year once actual hydrologic and water supply conditions are known. California has experienced above normal precipitation through the end of April 2010 and the California reservoir levels have shown improvement over last year. As of May 3, 2010, Lake Oroville is currently 61% full, compared to 59% last year and Lake Shasta is 97% full, up from 67% last year. The snowpack in the Sierra Nevada mountains was recorded on May 3, 2010, at 149% of normal, up from 67% of normal a year ago. At the Colorado River, the snow water equivalent in the upper basin is at 77% of average, and storage at Lake Powell has increased to 57% of capacity.

Based upon the resulting 8% reduction in water supply from CWA in Fiscal Year 2009, for Fiscal Year 2010, the City targeted a conservation effort from its customers that would mirror the actual Fiscal Year 2009 reduction of 8% in water supply. Through continued conservation actions, as of the end of March 2010, the City has successfully achieved an 11.2% reduction in water usage for Fiscal Year 2010. As the City is currently exceeding the targeted conservation effort for Fiscal Year 2010 and actual water deliveries are anticipated to be similar to those in Fiscal Year 2009, the City is planning to continue current water use restrictions but does not plan any additional water use restrictions at this time.

City Actions

As the City purchases approximately 85-90% of its water supply from CWA, the City has been proactive in developing methods to mitigate the exposure the City has to water supply restrictions from MWD or CWA. As such, the City has developed and is consistently developing methods to address its need for water supplies.

Adjustment to projections. The City's financial projections for the Water System for Fiscal Years 2010 through 2014 reflect an estimated 15% reduction in water sales based on current estimates from MWD/CWA on water supplies restrictions, with the resulting reduction in Water System revenues being generally offset by reductions in the Water System's operating budget. See "RISK FACTORS – Risks Relating to the Water Supply."

Drought action responses. The City has been proactive in responding to anticipated water supply issues with the development of voluntary programs and the development of a formal drought response plan. The City's drought response plan includes four levels and culminates in the declaration of drought emergency conditions. Various water conservation practices are encouraged during Drought Response Level 1 and such practices become mandatory upon the declaration of Drought Response Level 2.

In June 2007, the Mayor endorsed the City's participation in CWA's "20 Gallon Challenge," pursuant to which City residents and businesses were asked to voluntarily reduce the region's water use on average by 20 gallons per person, per day. The 20 Gallon Challenge is monitored on an on-going basis and its results have varied over time. The program was not required by law and any failure to meet the challenge did not result in any penalty to the City.

In July 2008, in response to dry weather conditions and uncertainty about future water deliveries, the City declared a Stage 1 Voluntary Compliance Water Watch (the "Stage 1 Voluntary Compliance Water Watch"), which applies during periods when the possibility exists that the Public Utilities Department will not be able to meet all of the water demands of its customers, and called for voluntary conservation measures pursuant to Division 38 of Article 7 of Chapter 6 of the San Diego Municipal Code as then in effect. Subsequent to such declaration and in connection with a region-wide effort coordinated by CWA to achieve greater county-wide consistency in drought response planning, the City Council approved amendments to the drought response plan set forth in the City's Municipal Code. Pursuant to such amendments, the Stage 1 Voluntary Compliance Water Watch was replaced with Drought Response Level 1, which may be declared by the Mayor upon resolution of the City Council when there is a reasonable probability, due to drought, that there will be a water supply shortage and that a consumer demand reduction of up to 10% is required in order to ensure that sufficient supplies will be available to meet anticipated demands.

On May 5, 2009, the City Council, upon recommendation of the Mayor, declared a Drought Response Level 2 Condition, which is also referred to as a Drought Alert Condition (the "Level 2 Drought Alert Condition"). Pursuant to the revisions to the City's Municipal Code referred to above, a Level 2 Drought Alert Condition is triggered when, due to drought, a consumer demand reduction of up to 20% is necessary in order to ensure that sufficient supplies will be available to meet anticipated demands. Voluntary water use restrictions in effect since July 2008 under the Stage 1 Voluntary Compliance Water Watch became mandatory on June 1, 2009. In addition to specific requirements in the City's Emergency Water Regulations, Water System customers are limited to landscape irrigation between the hours of 6:00 p.m. and 10:00 a.m. on no more than three assigned days per week from June through October and between the hours of 4:00 p.m. and 10:00 a.m. during the months of November through May. Furthermore, customers using standard lawn sprinklers for lawn watering and landscape irrigation are limited to no more than ten minutes per water station on an assigned watering day from June through October and no more than seven minutes per water station on an assigned watering day from November through May. See "RISK FACTORS – Risks Relating to the Water Supply."

Conservation. The Water Conservation Program was established by the City Council in 1985 and promotes permanent water savings. The Water Conservation Program accounted for over 33,789 AFY of potable water savings in Fiscal Year 2009. These savings have been achieved by creating a water conservation ethic, adopting programs, policies, and ordinances designed to promote water conservation practices, and implementing comprehensive public information and education campaigns.

The City utilizes a broad range of conservation methods, including: incentive programs for low-flush toilets and water conserving washing machines, survey programs, regulations, efficient landscaping and irrigation management programs, park and recreation partnerships, and public education and outreach.

The Public Utilities Department works closely with the City's Planning and Development Services Departments to incorporate water conservation requirements into the City's planning and permitting processes to ensure new communities and properties will have water-efficient landscapes. Changes in water conservation technologies may require periodic reassessment of long-range plans and water conservation programs to ensure that savings are realized. The Public Utilities Department continues to work with its proven water conservation programs while implementing new irrigation management programs to maximize water savings.

The City has developed and continues to develop strategic plans for the Water System.

1997 Strategic Plan for Water Supply (the "Strategic Plan"). The City's projected water demands and recommended future supplies were developed through the Strategic Plan, which was completed in 1997. The Strategic Plan estimated water demand through 2015 and identified infrastructure requirements necessary to ensure that facilities were in place to store, treat, and distribute required supplies in an efficient and effective manner. In August 1997, the City Council approved a water rate increase to help fund the initial years of the CIP.

The Strategic Plan called for the doubling of water savings from conservation programs, from 13,000 AFY to 26,000 AFY by calendar year 2005. The City achieved its calendar year 2005 goal, with conservation of approximately 29,400 AFY in that year. The City's continued conservation efforts have resulted in approximately 30,350 AFY, 31,500 AFY, 32,250 AFY, and 33,789 AFY of water savings for Fiscal Years 2006, 2007, 2008, and 2009, respectively. These efforts, along with proposed projects for cutting edge technologies such as brackish water desalination, are intended to provide the City with a reliable water supply that is less dependent on imports.

2002 Long-Range Water Resources Plan. In 2001, the City, with the assistance of a 12-member citizen's advisory committee, initiated an update of the Strategic Plan, known as the City of San Diego Long-Range Water Resources Plan (the "Long-Range Water Resources Plan"), which was adopted by the City Council on December 9, 2002.

The objectives of the Long-Range Water Resources Plan were to extend water demand projections through 2030 and also develop a decision-making framework for evaluating water supply options. The Long-Range Water Resources Plan identified various options to meet this medium to long-term demand. These options include water conservation, water reclamation, groundwater desalination, groundwater storage, ocean desalination, marine transport, Central Valley water transfers, and imported supply from CWA and MWD. Various alternative portfolios of water supply options were evaluated against a set of planning objectives to determine the appropriate strategic direction for development of water resources.

The Long-Range Water Resources Plan concluded that no single supply source will be sufficient to meet the City's future water demand. The priority supply portfolio options identified for implementation by 2010 are conservation, reclamation, groundwater, and transfers of surplus water from the water agencies in the Central Valley under long-term contracts or as spot commodity purchases.

The Long-Range Water Resources Plan recommended, among other things, that the common resource elements from the three top-scoring portfolios be implemented by 2010 (Phase 1). Resource elements that are different among these portfolios should then be examined to determine under what conditions they would become most feasible for the City to implement. Based on such factors as the success or failure of the CALFED Bay-Delta Program, emergence of a strong water transfer market, technology improvements in membrane treatment, and the outcome of the City's field investigations of local groundwater, three distinct paths or strategies could be taken and possibly implemented by 2020 (Phase 2). Once a particular strategy is chosen by the City, then Phase 3 of the Long-Range Water

Resources Plan would implement a variety of resource options by 2030, depending on the continued success of prior resource implementation and/or achievement of planning objectives.

Although the Long-Range Water Resources Plan initially prescribed the implementation of the common resource elements by 2010, development of these options and implementation of the common resource elements (except for conservation) have been delayed until 2012 or later because of delays in related capital projects from 2005 through 2007, when there was limited access to bond financing. The Public Utilities Department has met the initial conservation goal set forth in the Long-Range Water Resources Plan.

2005 Urban Water Management Plan. The City completed its Urban Water Management Plan (the "UWMP"), which builds upon the previously approved Long-Range Water Resources Plan and the Strategic Plan. Together, the UWMP, the Long-Range Water Resources Plan and the Strategic Plan set conservation water savings goals of 32,000 AFY by 2010, 36,000 AFY by 2020, and 46,000 AFY by 2030. The UWMP reports the activities the City is embarking upon to secure a safe, reliable water supply for the City, including establishment of the City's Water Conservation Program (the "Water Conservation Program"), improvements to the City's water treatment plants, identification and securing of additional sources of water and improve most of water supply reliability in the region through groundwater investigation, alternative storage projects, and participation in emergency storage projects.

The City is currently in the early stages of preparing its next update to the UWMP (the "2010 UWMP"), which will relate to general long-range water resources and is scheduled to be completed in late 2010. The 2010 UWMP intends to focus on global warming, compliance with AB 32 (The Global Warming Solutions Act of 2006), energy efficiency, regional water supply issues, and recent legislation aimed at increasing water-use efficiency and improvements in water resources planning.

Groundwater. The City has several relatively small groundwater basins within its jurisdiction, from San Pasqual in the north, to the San Diego River in the center of the City, to the Tijuana River Valley in the south. The largest basin, the San Diego Formation, lies along the coast from the Mexican border to Point Loma.

The City is presently pursuing groundwater feasibility projects in San Pasqual, the San Diego River System, and the San Diego Formation and exploring new technologies such as desalinating brackish groundwater that are designed to provide affordable water supply sources. These projects include the San Pasqual Brackish Groundwater Desalination Demonstration Project and the Groundwater Pilot Production Wells in the San Diego Formation, Mission Valley, and San Pasqual basins. The desalination projects consist of extracting groundwater from the basin and desalinating the water, while the Groundwater Pilot Production Wells project consists of constructing pilot production wells at various sites to perform aquifer tests and hydrogeological analyses of the basins. Brackish groundwater is a possible alternative water supply source and is part of the City's planning efforts. Local water supply projects, particularly groundwater exploration, are locally controlled and can offer enhanced drought protection. Though the City is currently pursuing groundwater projects, groundwater does not currently make up a significant source of water for the City.

Indirect Potable Reuse Demonstration Project. In addition to previously described action to address water supply issues, the City plans to expand its development of groundwater assets including desalination of brackish groundwater and its utilization of reclaimed water. As part of this development, the City will consider, among other things, an independent energy and economic analysis of all water supply augmentation methods in the Long-Range Water Resources Plan and a pilot indirect potable reuse demonstration project (the "IPR Project"). The IPR Project objectives consist of the following: explore the feasibility of producing water that can be sent to a reservoir and later distributed as drinking water; design, procure, install, operate, and test a one million gallon per day advanced water purification facility at the North City Water Reclamation Plant; coordinate with State regulators on permit conditions; and conduct a public information and outreach program. If the IPR Project meets regulatory requirements and provides evidence of the viability of the indirect potable reuse through reservoir augmentation, the City may consider the feasibility of constructing a full-scale project estimated to be able to produce 16 million gallons a day. Such a future plant would be designed to send advanced treated water to the San Vicente Reservoir via a 23-mile pipeline where it would be redistributed as potable water after months of blending and additional treatment. See "WATER SYSTEM FINANCIAL OPERATIONS – Establishment of Water Service Charges" for a description of the commodity charge increase approved by the City Council and the Mayor to fund the IPR Project.

Reclaimed Water. The majority of expenses relating to the production of reclaimed water accrue to the City's Wastewater System, while revenues from the sale of reclaimed water accrue to the Water System primarily because of a $70 million investment that the Water System made in expanding the non-potable reclaimed water distribution system (purple pipe) in the late 1990s. The City has made significant capital investments in the reclaimed water program. To date, approximately $460 million has been spent on two water reclamation plants (consisting of the North City Water Reclamation Plant (the "NCWRP") and the South Bay Water Reclamation Plant (the "SBWRP"), distribution systems and related facilities. Approximately 25% of those costs were covered by State and federal grants.

Located in the Miramar area, the NCWRP has been operational since 1997 and has a permitted design capacity of 30 MGD. The plant operated at an average flow of 23 MGD during Fiscal Year 2009. NCWRP produced an average of 7 MGD of reclaimed water each day that is distributed to users through the Public Utilities Department's Northern Water Distribution System. NCWRP limits its production of reclaimed water (tertiary treatment) to the amount the Public Utilities Department expects to sell. Sewage that is treated at NCWRP for conversion to reclaimed water flows to the Public Utilities Department's Northern Water Distribution System. Sewage that is treated at NCWRP for discharge into the ocean flows to the Point Loma Wastewater Treatment Plant. Approximately 16 MGD of return flow to the Wastewater System results from excess secondary effluent from the NCWRP, which is returned to the collection system for disposal via the Point Loma Wastewater Treatment Plant. As of June 30, 2009, the plant currently serves nearly 450 retail customers, two wholesale customers, the City of Poway, and the Olivenhain Municipal Water District.

The SBWRP is located on Dairy Mart Road, near the international border with Mexico. The SBWRP, which commenced delivery of reclaimed water to customers in the summer of 2006, has a permitted design capacity of 15 MGD and operated at approximately 9 MGD during Fiscal Year 2009. The average influent flows treated during Fiscal Year 2009 were 8 MGD, with approximately 3 MGD discharged to the ocean outfall and approximately 5 MGD reclaimed water distributed. The majority of the reclaimed water is sold to the Otay Water District, a local water agency with more than 600 meter connections. The SBWRP also sells reclaimed water to three retail customers including the U.S. International Boundary & Water Commission Treatment Plant, located just to the east of the water reclamation facility.

Reclaimed water usage is seasonal and is primarily used for irrigation. Customers also use the water for dust suppression or soil compaction at construction sites, in cooling towers, ornamental fountains, and for office building toilet and urinal flushing (dual plumbing). During the summer of 2009, the two reclamation plants met a peak production of approximately 13 MGD at NCWRP and a peak production of approximately 8 MGD at SBWRP. Conversely, during cooler months, production ranges from two to eight MGD for both reclamation plants. Reclaimed water production continues to increase each year due to the City's marketing efforts to reach "in-fill" customers, who, as identified by the City's Recycled Water Master Plan 2005, are located near existing reclaimed water distribution lines.

Reclaimed water rates were lowered from $1.34 to $0.80 per hundred cubic feet ("HCF") on July 1, 2001. As of January 1, 2010, the reclaimed water rate was approximately 22% of the equivalent potable water rate charged to irrigation customers. The Public Utilities Department is currently completing an update to a reclaimed water pricing study. The scope of the study includes development of recommendations for reclaimed water commodity rates, base fees, capacity charges, alternative rate structures and a reclaimed water rate model. Factors included in the pricing study include cost of operation and maintenance for production and distribution facilities, capital costs for the most feasible expansion projects, and marketability of reclaimed water given current potable water use restrictions and potable water pricing. It is anticipated that the reclaimed water pricing study will be completed in calendar year 2010. See "WATER SYSTEM SERVICE AREA AND FACILITIES – Water System Service Area" for a description of reclaimed water produced by the City.

The following table sets forth the City's planned water supply sources from Fiscal Year 2010 to Fiscal Year 2030.

TABLE 6

PROJECTED WATER SUPPLY SOURCES
Fiscal Years 2010 to 2030
(AFY)

Water Supply Sources	2010	%	2015	%	2020	%	2025	%	2030	%
CWA	201,901	84%	205,178	83%	212,260	83%	222,238	83%	231,725	84%
Local Surface Water	29,000	12	29,000	12	29,000	11	29,000	11	29,000	11
Reclaimed Water	8,525	4	12,200	5	15,200	6	15,200	6	15,200	5
Total	239,426	100%	246,378	100%	256,460	100%	266,438	100%	275,925	100%

Source: 2005 Urban Water Management Plan, as supplemented.

WATER SYSTEM REGULATORY REQUIREMENTS

Federal Requirements

The City's Water System operations are subject to the provisions of the Federal Safe Drinking Water Act (as amended, the "Safe Drinking Water Act"), which sets forth requirements relating to the protection of drinking water and its sources, including rivers, lakes, reservoirs, springs, and ground water wells, against both naturally-occurring and man-made contaminants that may be found in drinking water. The Safe Drinking Water Act is administered by the United States Environmental Protection Agency (the "EPA"), with direct oversight by DPH and includes, among other things, primary standards for 104 chemical, microbiological, radiological, and physical contaminants in drinking water and requirements for the preparation of consumer confidence reports, water system operator certifications, water distributions system monitoring, treatment plan monitoring and drinking water source assessments. The Safe Drinking Water Act also requires that every five years the EPA establish a list of contaminants that are known or anticipated to occur in public water systems and may require future regulation under the Safe Drinking Water Act. From this contaminant candidate list, the EPA identifies contaminants that are priorities for additional research and data gathering, which information is then used to determine whether or not a regulation is appropriate. This process is repeated for each list every five years. The EPA recently completed its latest review and no additional primary standards were added to the regulations. The EPA is currently evaluating the risks from several additional compounds and organisms including: microbial contaminants; the byproducts of drinking water disinfection; fire retardants; radon; water systems that do not currently disinfect their water but get it from a potentially vulnerable ground water source; and issues related to water treatment and distribution system operational practices impacting distribution system water storage tanks' water quality. The Public Utilities Department currently complies with all applicable standards and regulations of the Safe Drinking Water Act.

The EPA also establishes Secondary Drinking Water Regulations, which are non-enforceable guidelines for contaminants that may cause negative aesthetic (such as taste or odor) or cosmetic effects (such as tooth discoloration). Water systems are not required to adopt these secondary standards, but states may choose to adopt and enforce them. The State has adopted the secondary standards and the City currently meets all such standards.

State Regulations

As an operator of a large municipal water system, the City is responsible for complying with various state requirements, including the California Environmental Quality Act, as amended (Division 13 of the California Public Resources Code) ("CEQA"), with respect to the operational requirements, design and construction standards for dams and reservoirs, distribution systems and pipelines, requirements for control of Cryptosporidium and other water safety issues and training, and other requirements for certification of water treatment and distribution operators. Failure to meet these standards may subject the City to civil or criminal sanctions. The Public Utilities Department is currently in compliance with all applicable State regulations. See " – Compliance Order by the California Department of Public Health" below.

Proposed Regulations

In December 2006, the EPA promulgated the Stage 2 Disinfectants and Disinfection Byproducts Rule ("Stage 2 DBPR") and the Long Term 2 Enhanced Surface Water Treatment Rule, which built upon prior rules to address protection of public water systems against microbial contaminants, especially Cryptosporidium, and at the same time, reduce potential health risks of disinfection byproducts. The Stage 2 DBPR requires operators of public water systems to determine if they exceed permitted disinfection byproduct concentration levels and, if so, identify actions that may be taken to mitigate future high disinfection byproduct levels. The City has complied with the initial phase of the Stage 2 DBPR and has completed its initial distribution system evaluation and complied with its reporting and monitoring requirements by the compliance deadlines set forth in the Stage 2 DBPR. The City expects to comply with all remaining requirements of the Stage 2 DBPR, a portion of which is expected to be financed with proceeds of additional water revenue bonds described under "WATER SYSTEM CAPITAL IMPROVEMENT PROGRAM – Financing Plans for the CIP."

Other new regulations, including regulations that are in effect but whose compliance are not yet mandated (such as the Ground Water Rule promulgated by the EPA pursuant to the National Primary Drinking Water Regulation) and regulations that are currently proposed, will continue to impact the operation of the Water System and its associated costs. Also, the costs of proposed new regulations, including rules and regulations regarding radon, groundwater and filter backwash, are currently unknown. See "RISK FACTORS – Statutory and Regulatory Compliance."

Compliance Order by the California Department of Public Health

DPH is the regulatory agency responsible for ensuring that water systems meet the federal regulations outlined above, as well as additional or stricter State regulations. In January 1994, DPH notified the City that certain deficiencies in the Water System were found during a routine sanitary survey of the Water System conducted by the DPH Drinking Water Field Operations Branch. The deficiencies primarily related to the future reliability of various components of the Water System. As a result, the City and DPH entered into a compliance agreement (the "1994 Compliance Agreement") pursuant to which the City agreed to correct operational deficiencies noted during the survey and undertake the required capital improvements to the Water System by the deadlines established in the 1994 Compliance Agreement. The City was notified in January of 1997 that it was not in compliance with the 1994 Compliance Agreement. At that time, the DPH issued a compliance order (the "1997 Compliance Order"), which has been amended from time to time, including most recently in May 2007 (as amended to date, the "DPH Compliance Order"), to include additional items that were not in the 1997 Compliance Order. The DPH Compliance Order will remain in effect until the projects required thereunder are completed.

The Public Utilities Department believes it has made substantial progress in completing the projects set forth in the DPH Compliance Order and is currently meeting the ongoing requirements thereof, including the obligation to provide DPH with quarterly progress reports and hold periodic status meetings. In addition, on February 26, 2007, the City authorized rate increases of 6.5% per year for Fiscal Years 2008 through 2011 to finance projects mandated in the DPH Compliance Order as well as other CIP projects.

DPH has the authority to impose civil penalties if the City fails to meet DPH Compliance Order deadlines, although DPH has not imposed such penalties to date. Violation of the DPH Compliance Order may be subject to judicial action, including civil penalties specified in California Health and Safety Code Section 116725 ("Section 116725"). Pursuant to Section 116725, a violation of a schedule of compliance for a primary drinking water standard may result in a maximum penalty of $25,000 per day for each violation; and a violation of other standards, such as turbidity, the penalties can reach $5,000 per day. There are a number of additional enforcement tools prescribed by law, including public notification, citations, citations with fines, public hearings, mandatory water conservation, litigation, and service connection moratoriums.

The costs for bidding, constructing and completing the required work will fluctuate depending on variables such as changes in the cost of materials and labor. The estimated DPH Compliance Order project costs and DPH-related project costs for Fiscal Year 2010 through Fiscal Year 2014 is approximately $419 million. The Public Utilities Department anticipates financing such costs with existing net assets, present and future revenues, and financing proceeds secured by system revenues provided, however, there can be no assurance that any or all of such financing sources will be available or secured.

Permits and Licenses

The Water System holds a Water Supply Permit from the DPH for operation of certain of its facilities (the "Water Supply Permit"). The City is required to apply for an amendment to its Water Supply Permit as changes occur within the Water System, including the capacity and process improvements at the water treatment plants. The City works closely with the DPH during the design, construction and subsequent operations of all improvements that result in amendments to the Water Supply Permit to ensure amendment approval. Various other permits and licenses are required to operate the water treatment plants, water impounding system, water quality lab and distribution system. The City does not anticipate any problems with continued Water System operation under existing and planned future permits and licenses.

WATER SYSTEM CAPITAL IMPROVEMENT PROGRAM

The Capital Improvement Program

The Water System's capital improvement program ("CIP"), which was originally prescribed in the Strategic Plan developed in 1997 and supplemented and updated in 2002 by the Long-Range Water Resources Plan, each with the assistance of a citizen task force, was developed to ensure that the City has a cost-effective, safe and reliable water supply. See "WATER SUPPLY – Future Water Supply for the Water System." The City reevaluates the projects contained in the CIP and the timing of improvements on an annual basis. Changes to the CIP are made to reflect changing priorities within the Water System and may occur as a result of project scope changes, date revisions, project sequencing and operational considerations. There are five fundamental driving forces behind the expansion and upgrades of the City's Water System: replacement of aging infrastructure to reduce pipeline breaks and emergency repairs, increasing treatment capacity and improving process technology, expansion of the Water System to accommodate retail growth, compliance with Federal Safe Drinking Water Act, and satisfaction of the DPH Compliance Order. Approximately 60% of the anticipated projects to be constructed from Fiscal Years 2010 to 2014 are either mandated by the DPH Compliance Order or are related to DPH projects.

In April 2002, the City Council adopted increases to the water base fee rates and commodity rates to increase revenues from retail sales in each of the following five Fiscal Years by 6% per year. The revenues generated by such rate increases were used to fund the continued upgrade and expansion of the Water System as prescribed by the CIP.

Despite not accessing the public bond market in Fiscal Years 2005 and 2006 and relying on short-term private financing in Fiscal Years 2007 and 2008, the Public Utilities Department completed 69 capital projects aggregating approximately $567.9 million between Fiscal Year 2005 and Fiscal Year 2009, including improvements to water treatment plants, water storage reservoirs, water pump stations, water pipelines, reclaimed water projects and cast iron pipeline projects. In February 2007, the City Council adopted rate increases of 6.5% per year for Fiscal Years 2008 through 2011 to help finance capital improvement projects, including projects related to water treatment plants, pipelines, reservoirs and pump stations, projects related to anticipated growth within the City's service area, annual allocation project groups and projects required by or related to applicable State and federal regulations and orders. The CIP remains subject to change and is expected to include additional projects for implementation subsequent to 2011, based on the program priorities explained previously.

Description of Major Projects

The Public Utilities Department has developed a comprehensive CIP to address current and future Water System needs. See " – Project Schedule and Cost" below.

The CIP projects can be classified into one of nine categories as they relate to the Water System. Some of these projects were included in the original CIP as set forth in the Strategic Plan, while others have been added to the CIP or had their schedules modified since the Strategic Plan was finalized. The map that follows the Table of Contents of this Official Statement shows the location of the major CIP projects. Brief descriptions of the projects in each of the categories are provided below.

Water Treatment Plants. The CIP includes projects that will rehabilitate and upgrade the AWTP, the MWTP and the OWTP. As part of the Alvarado Upgrade, the rated capacity of the AWTP will be expanded to 200 MGD by Fiscal Year 2011 to meet future water demands through 2030. The MWTP will be expanded to a capacity of 215 MGD by Fiscal Year 2010 to meet future water demands through 2030. The improvements to the OWTP, which will increase the OWTP's rated capacity from 34.2 MGD to 40 MGD, are expected to be completed by Fiscal Year 2011. Such improvements to the City's water treatment plants will also assist the City in complying with the requirements of the Federal Safe Drinking Water Act and the DPH Compliance Order. See "WATER SYSTEM REGULATORY REQUIREMENTS – Federal Requirements" and " – Compliance Order by the California Department of Public Health."

Pipelines. The CIP includes pipeline projects relating to the continued rehabilitation, replacement, and installation of distribution and transmission lines throughout the Water System.

Included in the anticipated pipeline projects is the replacement of approximately 20 miles per year of existing cast iron distribution mains that have passed their 50-year service life. Approximately 155 miles of such mains remain to be replaced.

Pump Stations. The CIP includes projects that will replace, rehabilitate and construct pump stations throughout the Water System.

Raw Water Storage Facilities. The CIP includes projects that will upgrade the raw water outlet structures on three reservoirs and make emergency outlet improvements at the Lower Otay Reservoir.

Treated Water Storage Facilities. The rehabilitation and construction projects included in the CIP through Fiscal Year 2011 will increase treated water storage capacity by 6% as compared to the amount available at July 1, 1998, when implementation of the CIP projects began.

Reclaimed Water Facilities. The North City Reclamation Distribution System Expansion is currently in the design phase and construction will begin in Fiscal Year 2010.

Groundwater Projects. See "WATER SUPPLY – Future Water Supply for the Water System – Groundwater" for a description of groundwater feasibility projects being explored by the City in San Pasqual, Mission Valley, and the San Diego Formation.

Security Projects. The water security projects include adding cameras, motion detectors, access control elements, and eight-foot high fences to water facilities. The facilities include nine lakes and dams, three treatment plants, an operations yard, 40 pump stations, 20 water tanks, five regulators and 50 pipeline locations. Communication elements will be installed so that all camera images can be monitored from a security operations center located in the City of Chollas.

Miscellaneous Projects. Miscellaneous CIP projects include air valve adjustments, corrosion control for existing facilities, installation of pressure reducing stations, installation of flow meters and security enhancements at various water facilities. Also included are pooled contingencies, which are contingency amounts identified for each project to protect against uncertainties in the construction of such projects. All of the project contingencies are aggregated into a single pool of contingencies rather than included in the budget for each project.

Project Schedule and Costs

The current cost estimate of CIP projects for the period from Fiscal Year 2010 through Fiscal Year 2014 is approximately $695 million, and the cost estimates are subject to change. The budget for each project and program is established and approved by the City Council and adjustments to such budget require approval of the City Council.

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The following table shows categories of projects with the estimated cost of expenditures contained in the CIP for the period of Fiscal Years 2010 to 2014. Final CIP project costs will be refined as the CIP progresses.

TABLE 7

SUMMARY OF PROJECTED CIP PROJECTS [(1)]
Fiscal Years 2010 through 2014

Description	2010	2011	2012	2013	2014	Total
Water Treatment Plants	$ 83,881,204	$ 31,310,409	$ 1,639,389	$ 3,905,061	$ 9,074,934	$129,810,997
Pipelines	48,074,621	53,410,139	61,430,309	59,022,991	78,307,599	300,245,659
Pump Stations	3,840,792	831,375	2,438,729	3,523,976	2,401,166	13,036,038
Raw Water Reservoirs	449,014	914,062	3,440,796	9,135,167	11,054,503	24,993,542
Treated Water Reservoirs	493,575	608,607	768,112	1,848,048	4,442,486	8,160,828
Reclaimed Water Facility	7,106,101	7,414,401	2,980,224	1,000,000	1,000,000	19,500,726
Groundwater	7,643,634	18,528,908	20,127,520	1,209,935	6,669,226	54,179,223
Security	10,109,000	7,592,776	326,295	0	0	18,028,071
Miscellaneous	7,800,000	21,178,596	29,023,958	33,762,636	34,817,241	126,582,431
Total	$169,397,941	$141,789,273	$122,175,332	$113,407,814	$147,767,155	$694,537,515

Source: Public Utilities Department, City of San Diego.

(1) Amounts reflect the aggregate costs of all CIP projects required to satisfy the DPH Compliance Order as well as projects related thereto or necessary for the operation thereof. For Fiscal Year 2010 through Fiscal Year 2014, approximately 60% of the capital program is either mandated by DPH or DPH-related projects.

Financing Plans for the CIP

The CIP is funded through a combination of System Revenues, bond proceeds, grants, and State Revolving Fund loans. The Public Utilities Department currently expects that approximately 80% of the costs of the CIP through Fiscal Year 2014 will be funded with a combination of bond proceeds, grants, and State Revolving Fund loans. The following table sets forth the anticipated CIP financing needs through Fiscal Year 2014:

Fiscal Year	Total
2010	$ 0
2011	124,000,000
2012	206,000,000
2013	0
2014	285,000,000
Total	**$615,000,000**

The remaining 20% of the costs of the CIP will be paid on a pay-as-you-go-basis, which are supported by currently approved water rates. See "WATER SYSTEM FINANCIAL OPERATIONS – Financial Projections and Modeling Assumptions." These projected costs include a 4% annual inflation factor due to anticipated increases in construction costs over time, which assumed inflation rate is intended to be a conservative estimate to ensure that the Public Utilities Department has adequate resources reserved to complete the necessary projects.

The Public Utilities Department has distinguished between repair and replacement and expansion CIP costs to properly apply revenue sources. New customers will benefit from capacity created by expansion projects. These projects will be funded by capacity charges and bond proceeds. Capacity charge revenues will range from $5.6 million to $5.7 million over the period from Fiscal Year 2010 through Fiscal Year 2014.

In addition, the Public Utilities Department has applied for the Additional SRF Loans in the aggregate principal amount of $50 million. Proceeds of the Additional SRF Loans, if received and approved by the City Council, will be used for the following projects: the OWTP Upgrade – Phase I in the amount of $7 million; the OWTP Upgrade – Phase II in the amount of $11 million; the AWTP Upgrade – Phase IV in the amount of $12 million; and the MWTP Upgrade and Expansion in the amount of $20 million. All future Additional SRF Loans will be Parity Obligations. The Public Utilities Department anticipates that the amount of bonded indebtedness to be issued in the future will be reduced by the amount of the Additional SRF Loans received from DPH, if any.

Environmental Compliance

The projects contained in the CIP are generally subject to CEQA. Under CEQA, a project that may have a significant effect on the environment and that is to be carried out or approved by a public agency must comply with a comprehensive environmental review process, including the preparation of an Environmental Impact Report ("EIR"). An EIR reflects not only an independent technical analysis of the project's potential impacts, but also the comments of other agencies with some form of jurisdiction over the project, and the comments of interested members of the public. Contents of an EIR include a detailed statement of the project's potentially significant environmental effects; any such effects that cannot be avoided if the project is implemented; mitigation measures proposed to eliminate or minimize such effects; alternatives to the proposed project; and any significant irreversible environmental changes that would result from the project. Approximately 4% of CIP projects reviewed between May 2002 and August 2008 have required an EIR. If an agency determines that the project itself will not have a significant effect on the environment, it may adopt a written statement (called a "Negative Declaration") to that effect and need not prepare an EIR. A Negative Declaration was prepared for approximately 2% of CIP projects reviewed between May 2002 and August 2008. A Mitigated Negative Declaration ("MND") is appropriate for projects that could potentially result in a significant environmental impact, but revisions or standard mitigation measures are incorporated into the project that clearly mitigate the impact. Approximately 7% of CIP projects reviewed between May 2002 and August 2008 resulted in the preparation of a MND. Statutory exemptions are activities that are not subject to CEQA. CIP projects can also be exempted if they fit a specific "category" of activities identified by the State Legislature. Between May 2002 and August 2008, approximately 87% of CIP projects have qualified for either a statutory or categorical exemption. Once an agency approves or determines to carry out a project, either following an EIR process or after adopting a Negative Declaration, it must file a notice of such determination. Any action or proceeding challenging the agency's determination must be brought within 30 days following the filing of such notice.

As part of its regular planning and budgetary process, the City prepares in accordance with local, State and federal law and regulations separate environmental documents for each of the CIP projects and evaluates the projects under the City's environmental impact review procedures, which were developed in compliance with State law and regulations. The City requires that all environmental documents and evaluations be completed prior to any authorization of funding for construction by the City Council and the Mayor.

The CIP involves replacement, upgrading and increasing capacity of existing facilities. Accordingly, the City does not believe that environmental considerations will adversely affect the completion of the CIP within the contemplated budget or the current timetable.

Project Management for the CIP

Prior to October 2007, the engineering design and construction of CIP projects, as well as their planning and attendant program controls, were all conducted by personnel within the Public Utilities Department. A reorganization of engineering functions for the City as a whole, including the Public Utilities Department's divisions and their respective responsibilities, resulted from recommendations of a steering committee assembled as part of the City's Business Process Reengineering program initiative to enhance the efficiencies and effectiveness of City government by, among other things, reviewing and improving City processes and procedures. The recommendations were presented to the Chief Operating Officer and Mayor and approved by the City Council. Project management, engineering design and construction of Water CIP projects are now managed by CIP project managers in the City's Engineering and Capital Projects Department ("E&CP"). Planning of and program controls for Water CIP projects are conducted and monitored by the Water Policy and Strategic Planning Division of the Public Utilities Department. See "WATER SYSTEM ORGANIZATION AND MANAGEMENT – Governance and Management of Water System."

E&CP provides a full range of engineering services for the City's capital investment in its various types of infrastructure and provides traffic engineering services to the community. E&CP is responsible for the planning, design, project management, and construction management of public improvement projects; quality control and inspection of private work permitted in the right-of-way; and surveying and materials testing. E&CP's activities include work on various public infrastructure assets to rehabilitate, restore, improve, and add to the City's capital facilities. E&CP's activities cover a wide range of City-wide projects including: libraries; fire, lifeguard and police stations; parks and recreation centers; lighting and signals, street improvements, bikeways and other transportation projects; drainage and flood control facilities; rebuilding and expanding water and wastewater pipelines, treatment plants, and pump stations; and dry utilities under-grounding projects. These functions are provided through four of the five divisions within the E&CP.

Architectural Engineering & Parks Division. This division manages the implementation of non right-of-way and vertical capital improvement projects. This responsibility includes the design and project management of water treatment plants, reservoirs and pump station projects.

Field Engineering Division. This division manages construction contracts, materials testing, land surveying services and geological assessment/support. This responsibility includes quality assurance/quality control inspection of CIP projects within the City's jurisdiction.

Project Implementation and Technical Services Division. This division provides centralized technical, operational and project support services to the other divisions within the Public Utilities Department, as well as other departments in the City. These services include preliminary engineering and asset management, project controls, CIP fund management, Americans with Disabilities Act compliance review for CIP projects, quality control and standards, and environmental and permitting assistance.

Right-of-Way Design Division. This division manages the implementation of right-of-way and related horizontal capital improvement projects, including the design and project management of water pipelines, flood plains and drainage infrastructure, and utilities under-grounding projects.

Contract Disputes

From time to time, the City is engaged in disputes with the contractors and subcontractors working on the CIP. As of June 1, 2010, there are no pending contract disputes with vendors or contractors working on the CIP in excess of $1 million.

Insurance

The City requires the consultant or contractor selected to design or construct a CIP project to provide minimum insurance therefor. Design consultants are required to provide at a minimum commercial general liability insurance of $1 million per occurrence ($2 million aggregate), commercial auto liability insurance of $1 million per occurrence, workers' compensation insurance of $1 million, architect and engineer's professional liability insurance of $1 million per occurrence ($2 million aggregate) and errors and omissions insurance for design-build projects. Construction contractors are required to provide at a minimum, among other things, commercial and general liability insurance aggregate limit of $2 million (other than products/completed operations) and $2 million (products/completed operations), personal injury insurance of $1 million each occurrence, commercial automobile liability insurance of $1 million combined single limit per accident and contractors builders risk property insurance in an amount equal to 115% of the contract value. Further, depending upon the size and scope of a project, the City's Risk Management Department may require increased insurance coverage at any time, and from time to time, based upon its assessment of the degree of risk for such project.

WATER SYSTEM FINANCIAL OPERATIONS

Establishment of Water Service Charges

The primary sources of moneys deposited in the Water Utility Fund are derived from revenues generated by Water Service charges to City residents and commercial enterprises, capacity charges on new, additional, or larger connections to the Water System within the City, and interest income on fund balances. Water Service charges to City utility customers are collected on a municipal water bill, which also includes sewer charges and storm drain fees. Bills are rendered on a bi-monthly basis for single family and most multi-family dwellings and on a monthly basis for industrial, commercial, and large multi-family dwellings. In accordance with the provisions of the City Municipal Code, these funds are administered in an enterprise account separate from the City's General Fund.

The City establishes fees based upon the costs incurred by the City to meet customer demand for water and pay for required capital improvements. Staff within the Water System and senior management within the City analyze rates and charges to determine the amounts necessary to support the Water System based upon revenue and expenditure data from the various divisions of the Public Utilities Department. Staff evaluates the adequacy of revenues and recommends rate adjustments to correspond with projected changes in maintenance and operations costs and the timing and magnitude of capital expenditures. This rate and charge analysis is conducted annually for management purposes and whenever it is required to assist planned financings and proposed rate adjustments.

Subsequent to consideration of the recommendations set forth in the 2007 Rate Case, in February 2007 the City Council adopted rate increases of 6.5% per year, effective every July 1, for Fiscal Years 2008 through 2011 in compliance with the requirements of Proposition 218. The rate increases were based on comprehensive forecasted annual Operation and Maintenance expenditures and additional capital costs for the Fiscal Years 2008 through 2011, which were based upon the City's budgeted Fiscal Year 2007 expenditures, adjusted for changes since the budget was developed and for anticipated changes in operations and the effect of inflation in future years. See "WATER SYSTEM FINANCIAL OPERATIONS – Operation and Maintenance Expenditures." Based on January 1, 2010, effective rates, the typical monthly water bill of $65.76 is approximately 1.25% of median household income in the County.

The water fees are composed of two components: a base fee and a commodity charge. The base fee is determined by the size of a customer's meter, and is charged to the customer regardless of whether the customer uses water. The base fee is based upon the assumption that the Public Utilities Department incurs certain costs in order to be in a position to serve the commodity to the water customer upon demand. Those costs are incurred by the Public Utilities Department regardless of whether the customer uses the commodity or not. They include such costs as the general administrative costs of the Public Utilities Department for billing, payment processing, and account management related to the Water System. The size of the customer's connection provides an approximation of the amount of water the customer conceivably could have delivered to his or her property.

The commodity charge is a charge for the amount of water consumed. The commodity charge is set at a rate based upon HCF of water consumed. Currently, the City has two types of commodity charges: a three-tiered rate for SFR, and a separate single rate for each of the other customer classes, including multi-family residential, commercial/industrial, and temporary construction/irrigation. The three-tiered rate structure for SFRs assesses a higher charge per unit of water as the level of consumption increases.

The City has historically increased water rates to reflect increases in the cost of water purchased from CWA, which is based on the costs for the infrastructure, operation and maintenance of CWA's water supply system and the cost CWA pays to purchase water from MWD. CWA generally increases the rates it charges on an annual basis with its Board of Directors approving the rates in June to be effective the following January. Following a CWA announcement of higher rates, the City calculates the impact to its cost of purchased water and the rate adjustment it must make to its customers to recover those increased costs. It then follows the procedures necessary to satisfy Proposition 218's public notice and hearing requirements and procedures established by the City for receiving and tabulating protests against increases to water rates. The City Council acts on the proposed rate adjustments for the recovery from Public Utilities Department customers of increased costs resulting from CWA's rate increases. The purchased water cost increase affects both the base fee and commodity charges within the City's water billing structure. In October 2007, the City Council approved a 2.9% CWA-related rate increase to recover revenue in the amount of the purchase water cost increase from CWA, which is anticipated to generate approximately $9.8 million annually. This CWA-related rate increase became effective on January 1, 2008. On November 18, 2008, the City Council and Mayor approved a $0.20 per equivalent dwelling unit ("EDU") increase to the base fee and an 8.5% increase to the commodity charge to generate sufficient revenue to offset the increased water wholesale purchase costs from CWA, which increase became effective on January 1, 2009, and is anticipated to generate approximately $19.5 million annually.

In addition, the City Council and Mayor also approved on November 18, 2008 a commodity charge increase of 3.08% to generate $10.8 million in revenue to be used in conjunction with a $1.0 million grant, to provide funding for the $11.8 million IPR Project, the goal of which is to determine the feasibility of indirect potable reuse, which consists of using highly treated reclaimed water to augment the City's drinking water supply. Subsequent to this specific rate increase taking effect on January 1, 2009, the City was awarded a grant from the Bureau of Reclamation in the amount of $2.9 million, which is expected to reduce the ultimate amount needed to fund the IPR Project. The approved commodity charge rate increase is scheduled to remain in effect through the end of Fiscal Year 2010 or until the required amount of revenue is collected, at which time such rate increase will sunset.

On November 17, 2009, the City Council and the Mayor approved a $0.12 per EDU increase to the base fee and an increase of 10.60% to the commodity charges to offset the increase in the wholesale purchase costs from CWA, which became effective on January 1, 2010, and which is anticipated to generate approximately $24.8 million annually.

On April 13, 2010, the MWD Board of Directors approved a 7.5% increase to the cost of purchased water to be effective January 1, 2011, and a 7.5% increase to the cost of purchased water to be effective either September 1, 2011 or January 1, 2012 for all of MWD's member agencies, including

CWA. CWA is in the process of determining the amount of the rate increase it will need to "pass-through" to CWA's member agencies, including the City. CWA's Board of Directors will hold a public hearing for discussion and a vote for approval for their proposed rate increases in June 2010. If CWA's Board of Directors does approve a rate increase for the cost of purchased water to their member agencies, the City will then calculate the effects of the CWA "pass-through" charges and present the necessary rate adjustments to the City Council for discussion and approval of the adjustments to the City water rates and charges to accommodate the increase in charges from CWA. This will require the City to satisfy Proposition 218 public hearing and notification requirements. The City has previously held the required public hearing in the November timeframe. To date, the City Council has approved all previously proposed rate adjustments presented by City staff to accommodate the increased costs of purchased water from CWA. The City has adjusted the water rates and charges to generate an amount equal to the increased charges from CWA for the cost of water. The City attempts to make these rate increases proportionate to the increased cost of purchased water from CWA.

Water rates have also been increased to help fund the Public Utilities Department's DPH Compliance Order project and DPH-related project costs and to permit the City to recover increased utility costs. Utility cost-related increases have not occurred since the 1980s. Any such increases will be subject to the procedures necessary to satisfy Proposition 218's public notice and hearing requirements and procedures established by the City. See "WATER SYSTEM REGULATORY REQUIREMENTS – Compliance Order by the California Department of Public Health."

The following table sets forth the five-year Water Service charge for each customer class from Fiscal Year 2005 through Fiscal Year 2009.

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TABLE 8

FIVE-YEAR WATER SERVICE CHARGE HISTORY FOR SINGLE FAMILY RESIDENTIAL, MULTI-FAMILY, COMMERCIAL, INDUSTRIAL, IRRIGATION, AND TEMPORARY CONSTRUCTION
Fiscal Years 2005 through 2009

Justification for Increase:		**Revenue Requirement**	**Increase in Water Costs from CWA**	**Revenue Requirement**	**Increase in Water Costs from CWA**	**Revenue Requirement**	**Revenue Requirement**	**Increase in Water Costs from CWA**	**Revenue Requirement**	**Increase in Water Costs from CWA and IPR Project**
Increase amount:		**Approx. 9.6%**	**$0.00**	**Approx. 9.4%**	**Approx. $0.25/EDU**	**Approx. 9.0%**	**6.5%**	**$0.14/EDU**	**6.5%**	**$0.20/EDU**
BASE FEES(1)		7/1/04	1/1/05	7/1/05	1/1/06	7/1/06	7/1/07(3)	1/1/08	7/1/08	1/1/09
Meter Size:	⅝ inch	$13.08	$13.08	$14.31	$14.56	$15.87	$15.18	$15.32	$16.32	$16.52
	¾ inch	13.08	13.08	14.31	14.56	15.87	15.18	15.32	16.32	16.52
	1 inch	13.97	13.97	15.29	15.69	17.11	22.17	22.41	23.86	24.20
	1 ½ inch	62.52	62.52	68.41	69.16	75.41	38.13	38.59	41.10	41.76
	2 inch	96.24	96.24	105.31	106.61	116.24	58.09	58.83	62.66	63.72
	3 inch	345.44	345.44	377.98	380.38	414.73	104.98	106.38	113.29	115.29
	4 inch	576.30	576.30	630.59	634.69	692.00	171.83	174.17	185.49	188.83
	6 inch	1,286.28	1,286.28	1,407.45	1,414.95	1,542.72	337.46	342.12	364.36	371.02
	8 inch	1,733.10	1,733.10	1,896.36	1,909.36	2,081.78	537.01	544.47	579.86	590.52
	10 inch	2,323.85	2,323.85	2,542.76	2,562.26	2,793.63	770.49	781.23	832.01	847.35
	12 inch	3,232.55	3,232.55	3,537.06	3,570.06	3,892.44	1,435.00	1,455.06	1,549.64	1,578.30
	16 inch	5,394.93	5,394.93	5,903.13	5,974.63	6,514.14	2,499.62	2,534.62	2,699.37	2,749.37

COMMODITY CHARGE										
Customer Type:	**Usage**(4)**:**	7/1/04	1/1/05	7/1/05	1/1/06	7/1/06	7/1/07	1/1/08	7/1/08	1/1/09
	Increase amount:	4.4%	$0.054/HCF	4.4%	$0.047/HCF	4.5%	6.5%	$0.09/HCF	6.5%	8.5% (CWA) and 3.08%(IPR)
Single Family Residential										
Tier 1	0-7 HCF	$1.487	$1.541	$1.609	$1.656	$1.731	$2.262	$2.352	$2.505	$2.795
Tier 2	8-14 HCF	1.884	1.938	2.023	2.070	2.163	2.461	2.551	2.717	3.032
Tier 3	15+ HCF	2.076	2.130	2.223	2.270	2.372	2.775	2.865	3.051	3.404
Multi-Family(2)	per HCF(5)	1.737	1.791	1.870	1.917	2.003	2.461	2.551	2.717	3.032
Commercial (2)	per HCF(5)	1.737	1.791	1.870	1.917	2.003	2.357	2.447	2.606	2.908
Industrial(2)	per HCF(5)	1.737	1.791	1.870	1.917	2.003	2.357	2.447	2.606	2.908
Irrigation(2)	per HCF(5)	–	–	–	–	–	2.524	2.614	2.784	3.107
Temporary Construction(2)	per HCF(5)	–	–	–	–	–	2.524	2.614	2.784	3.107

Source: Public Utilities Department, City of San Diego.
(1) The base fee is dependent on the meter size.
(2) On July 1, 2007, the City established separate categories for Multi-Family, Commercial/Industrial, and Irrigation/Temporary Construction.
(3) Decrease in base fees for 2-inch and smaller meters reflect the 2007 Rate Case and pricing methodologies revised to reflect American Water Work Association methodologies.
(4) HCF (Hundred Cubic Feet) = 748 gallons.
(5) One rate for all usage amounts.
Note: No rate increase in January 2007.

Water Service Charges. The Water System's water service charge for all retail user classes includes a fixed base fee and a commodity rate. While the service charge is charged to each water meter and varies with meter size, the commodity rate is applied to a customer's water usage. Table 8 above sets forth the base fees for the various water meter sizes in the Water System as of Fiscal Year 2009. The following table sets forth such base fees for Fiscal Year 2010 and 2011, which rates have been adopted by the City Council.

TABLE 9

BASE FEES
Fiscal Years 2010 and 2011

Meter Size (inch)	July 1, 2009	January 1, 2010	July 1, 2010
5/8	$ 17.59	$ 17.71	$ 18.86
3/4	17.59	17.71	18.86
1	25.77	25.97	27.66
1 1/2	44.47	44.87	47.79
2	67.86	68.50	72.95
3	122.78	123.98	132.04
4	201.10	203.10	216.30
6	395.14	399.14	425.08
8	628.90	635.30	676.60
10	902.43	911.63	970.89
12	1,680.89	1,698.09	1,808.47
16	2,928.08	2,958.08	3,150.36

Source: Public Utilities Department, City of San Diego.

The City has a tiered commodity rate structure for SFR customers that is broken down by water usage within each rate block. The remaining retail customers (Multi-Family, Commercial, Industrial, Temporary Construction, and Irrigation) are billed under the same uniform commodity rate for their respective customer classification. See Table 8 for a schedule of commodity rate(s) applicable to each customer class as of Fiscal Year 2009. The following table sets forth the commodity rates for the Water System for Fiscal Years 2010 and 2011, which have been adopted by the City Council.

TABLE 10

COMMODITY RATES
Fiscal Years 2010 through 2011

Customer Class	Volume Block HCF	July 1, 2009 $/HCF	January 1, 2010 $/HCF	July 1, 2010 $/HCF
SFR				
Block 1	0-7	2.977	3.293	3.399
Block 2	8-14	3.229	3.571	3.686
Block 3	Over 14	3.625	4.009	4.139
Multi-Family	All Volume	3.229	3.571	3.686
Commercial	All Volume	3.097	3.425	3.536
Industrial	All Volume	3.097	3.425	3.536
Irrigation	All Volume	3.309	3.660	3.778
Temporary Construction	All Volume	3.309	3.660	3.778

Source: Public Utilities Department, City of San Diego.

Capacity Charges. In February 2007, the City Council and Mayor approved raising the capacity charge by 19.5% to $3,047 per EDU, which was estimated to provide for full cost recovery for Water System expansion projects planned through Fiscal Year 2015. The water used by an average SFR is equated to one EDU and equals 500 gallons per day. Non-residential customers are charged based upon calculated usage or an inventory of plumbing components that are assigned a number of "fixture units," which are converted to EDU's using a conversion factor that equates 20 fixture units to one EDU. The minimum capacity assigned to any user is one EDU.

Capacity charges are not treated as operating income for financial reporting purposes but are considered System Revenues and are deposited in the Water Utility Fund. Pursuant to State law, capacity charges can be applied only for the purpose of paying costs associated with capital expansion, bonds, contracts, or other indebtedness of the Water System related to expansion. Because capacity charges are primarily collected on new construction within the City, revenues obtained from such charges vary based upon construction activity.

The following table sets forth the capacity charges for Fiscal Years 2005 through 2009, which have been adopted by the City Council.

TABLE 11

RECENT RATE HISTORY
FOR WATER CAPACITY CHARGES
Fiscal Years 2005 through 2009

Fiscal Year	Water Capacity Charges (Per EDU)	% Increase/ (Decrease) (1)
2005	$2,550	2.0%
2006	2,550	0.0
2007	2,550	0.0
2008	3,047	19.5
2009	3,047	0.0

Source: Public Utilities Department, City of San Diego.
(1) Figure represents percentage change from prior year.

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The following table sets forth the historical capacity charge revenues from Fiscal Year 2005 through Fiscal Year 2009. Aggregate capacity charge revenues may not equal the amount derived by multiplying the water capacity rate by the number of units because of individual customer account characteristics. Since capacity charge revenue is dependent on development activity within the City, capacity charge revenues are impacted by the slow down in residential construction. For Fiscal Year 2009, the capacity charge revenue was $4,232,469 and the estimated amount for Fiscal Year 2010 is $5,577,700.

TABLE 12

WATER UTILITY FUND
HISTORICAL CAPACITY CHARGE REVENUES
Fiscal Years 2005 through 2009

Fiscal Year	New Equivalent Dwelling Units	Capacity Charge Revenues [(1)]
2005	5,602	$13,113,046
2006	5,713	12,897,678
2007	5,788	13,682,238
2008	4,337	9,697,815
2009	1,826	4,232,469

Source: Office of the Comptroller and Public Utilities Department, City of San Diego.
(1) Audited and included with Capital Contributions on Statement of Revenues, Expenses and Changes in Net Assets in the Comprehensive Annual Financial Report of the indicated Fiscal Year.

Collection of Water Service Charges

In order for a person to receive service and be billed by the City for water fees, he or she must contact the Public Utilities Department to have Water Service initiated. The person initiating the service does not have to be the owner of the property to which the water is delivered. Regardless of customer class, the customer has a meter from which the City measures the amount of the water consumed. The meter is read by the Public Utilities Department to calculate the water fees to be charged to the customer based on his or her customer class.

Pursuant to the approved policies and procedures, 100% of the water used is billed, no matter how far back the water usage occurred, and time extensions for payment are granted by Public Utilities Department management under limited conditions, including health and safety-related reasons, legal negotiations, or the negative impact on other ratepayers in the absence of a grant of extension. Such policies and procedures also provide that the Public Utilities Department has the authority to grant a deferred payment in only two circumstances: a customer receiving a bill greater than 200% of the usage on their normal bill (in which case such customer can only receive a deferred payment plan once during the life of the account, and the total payment must be received within one year) and a customer being back-billed for services received but previously unbilled (in which case the total amount due must be paid within one year or referred to City Treasurer if a longer, deferred-payment plan is required). Further, the approved policies provide that a deposit, for those customers requiring one, will be equal to two average billing periods and a fee of $20 will be imposed per returned check.

Typically, the City seeks to collect unpaid bills by (i) issuing an initial shut-off notice 25 days after a bill is issued; (ii) issuing a final shut-off notice 38 days after a bill is issued; and (iii) shutting off the customer's Water Service 45-51 days after a bill is issued. This procedure results in almost all past due bills being paid. If necessary, the City establishes time payments for customers who are unable to pay a past due amount. Accounts closed with an amount due and unpaid are referred to the City Treasurer for collection activities 75 days after the bill is issued but unpaid. An allowance is taken each Fiscal Year for accounts receivable that are not expected to be paid. During the Fiscal Years 2005 through 2009, accounts receivable amounts outstanding for more than 120 days ranged from $1.72 million to $3.67 million. Water service charges to City utility customers are collected on the municipal water bill, which also includes sewer charges and storm drain fees. Bills are currently invoiced every two months for single family dwellings and most multi-family dwellings and on a monthly basis for all other customers.

The following table sets forth information related to accounts receivable and number of shut-offs.

TABLE 13

WATER CUSTOMER ACCOUNTS RECEIVABLE AND SHUT-OFFS BY FISCAL YEAR
Fiscal Years 2005 through 2009
(Dollar Amounts in Thousands)
(Unaudited)

	2005	2006	2007	2008	2009
Water Sales Revenue (1)	$245,287	$ 258,900	$289,127	$297,225	$324,772
Accounts Receivable (2)	$ 33,622	$ 25,404	$ 28,126	$ 25,995	$ 25,311
Accounts Receivable Over 120 Days (2)	$ 1,727	$ 3,672	$ 3,645	$ 2,939	$ 2,190
% of Total Water Sales Revenues (3)	0.70%	1.40%	1.30%	1.00%	0.67%
No. of Shut-Offs (4)	24,459	21,230	20,451	22,420	23,650

Sources: The City's Comprehensive Annual Financial Reports for the indicated Fiscal Years with respect to "Water Sales Revenue;" Public Utilities Department and Office of the Comptroller, City of San Diego, for all other line items.
(1) Audited. All other items unaudited.
(2) Amounts are as of June 30, and represent the receivable portion of billed customer accounts as of the end of each Fiscal Year. Not included are amounts for unbilled accounts as of June 30.
(3) Percentage of Accounts Receivable over 120 days as compared to Total Water Sales Revenues.
(4) Shut-Offs for non-payment may include multiple shut-offs at the same address throughout the Fiscal Year.

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Revenues

The Water Utility Fund's principal source of revenues is Water Service charges to City residents and commercial enterprises. The following table sets forth the historical sources of water sales revenues of the Water Utility Fund for Fiscal Years 2005 through 2009.

TABLE 14

HISTORICAL SOURCES OF WATER SALES REVENUES (1)
Fiscal Years 2005 through 2009
(In Thousands)

Sources	2005	2006	2007	2008	2009
Retail					
Single Family Residential	$ 92,630	$102,505	$114,461	$126,373	$132,806
Multi-Family (2)	51,505	55,514	61,754	62,404	67,529
Commercial	82,477	82,669	93,042	87,465	100,581
Industrial	3,914	3,880	3,091	2,718	3,050
Reclaimed	3,751	4,452	5,528	5,867	7,737
Outside City	123	246	144	46	52
Wholesale to Other Retailers					
Other Utilities (3)	10,439	8,982	9,776	9,809	10,238
Irrigation Districts	448	652	1,331	2,543	2,779
TOTAL (4)	$245,287	$258,900	$289,127	$297,225	$324,772

Source: The City's Comprehensive Annual Financial Reports for Fiscal Years 2005 through 2009 for Total; Public Utilities Department and Office of the Comptroller, City of San Diego for all other line items.
(1) Referred to as Historical Sources of Service Revenues in the City's previous continuing disclosure agreements.
(2) Previously listed as "Other Domestic" customer type.
(3) Primarily reflects wholesale revenues from California American Water Company.
(4) Audited. All other line items unaudited.

The four annual water rate increases approved in February 2007 and described previously are projected to increase Water Service charge revenues from approximately $289 million in Fiscal Year 2007 to $370 million by Fiscal Year 2011. These revenue estimates include 6.5% annual rate increases in Fiscal Year 2008 through Fiscal Year 2011, but do not include revenues generated by purchase water cost increases that were affected as a result of rate increases implemented by CWA. Table 8 herein sets forth the Water System's Water Service rate increases from Fiscal Year 2005 through Fiscal Year 2009. Rate increases related to increased costs from CWA are approved by the City Council and Mayor following the required Proposition 218 noticing process on an ad hoc basis as cost increases become effective, usually in January of each year.

Operation and Maintenance Expenditures

Operation and Maintenance expenditures include the cost of operating and maintaining water supply, treatment, storage, and distribution facilities. Operation and Maintenance expenditures also include the cost of purchasing water, providing technical services such as laboratory services, administrative costs of the Water System including meter reading and billings, human resources administration and general management of the Public Utilities Department (collectively, "Operation and Maintenance expenditures"). The City used an inflationary factor of 4% in projecting all Operation and Maintenance expenditures, except for salaries and wages, fringe benefits, water purchases, data processing costs, and energy and utility costs. Based on revised labor agreements, the total of salaries, wages and fringe benefits was decreased by an amount equivalent to 6% of total compensation in Fiscal Year 2010. Those amounts are not projected to increase thereafter except for increases to pension benefits and retiree health costs. See "WATER SYSTEM FINANCIAL OPERATIONS – San Diego City Employees' Retirement System – Water System Share of Contributions to Pension System and NPO" and " – Postemployment Healthcare Benefits." Energy and utility expenses were assumed to increase at 8% per year and data processing costs were based on a long-range plan that reflected planned changes to data processing systems.

Water purchases are part of Operation and Maintenance expenditures but are projected separately based on historical factors, required emergency storage factors, known supply availability factors, and projected demand. As of January 1, 2010, the City estimates that the projected water purchase costs will vary from $154 million in Fiscal Year 2010 to $170 million in Fiscal Year 2014, excluding any additional price adjustments from MWD or CWA after Fiscal Year 2010. As described previously, as MWD or CWA price adjustments occur, the City makes corresponding adjustments to its customer rates, subject to the requirements of Proposition 218. The decrease in water purchase costs results from the City's assumption of a 20% supply restriction in each Fiscal Year 2010 through 2014. The current water rate model has been adjusted to reflect water sales for Fiscal Year 2009 based on year to date data and an assumed 20% reduction in water supplies for Fiscal Year 2010 through Fiscal Year 2014, leading to an estimated corresponding 15% reduction in water sales for the same period of time, based on the Public Utilities Department's estimate of supply restrictions that may be in place for those years by CWA. The resulting revenue reduction is offset by reductions in water purchases and other budget reductions made in Fiscal Year 2009 that carry forward into future years. Actual water sales through January 2010 of the current Fiscal Year 2010 are approximately 10% less than water sales from the prior Fiscal Year.

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The following table sets forth the statements of revenues, expenses and changes in fund net assets for the Water Utility Fund for Fiscal Years 2005 through 2009.

TABLE 15

STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS FOR THE WATER UTILITY FUND
Fiscal Years 2005 through 2009
(In Thousands)
(Audited)

	2005	2006	2007	2008	2009
OPERATING REVENUES					
Sales of Water	$245,287	$258,900	$289,127	$297,225	$324,772
Charges for Services	1,027	1,031	1,147	33	0
Revenue from Use of Property	4,701	4,833	6,162	6,115	5,418
Usage Fees	1,756	1,943	1,594	1,235	1,272
Other	14,878	13,860	12,262	14,018	11,257
TOTAL OPERATING REVENUES	267,649	280,567	310,292	318,626	342,719
OPERATING EXPENSES					
Maintenance and Operations	92,959	94,433	97,821	100,360	95,979
Cost of Purchased Water Used	102,096	110,263	124,880	121,186	133,499
Taxes	1,457	570	163	162	162
Administration	37,762	35,370	30,964	36,722	33,258
Depreciation	27,277	29,230	27,644	29,870	39,627
TOTAL OPERATING EXPENSES	261,551	269,866	281,472	288,300	302,525
OPERATING INCOME (LOSS)	6,098	10,701	28,820	30,326	40,194
NONOPERATING REVENUES (EXPENSES)					
Earnings on Investments (1)	7,258	6,966	11,461	15,536	12,478
Federal Grant Assistance	640	424	283	1,427	192
Other Agency Grant Assistance	694	359	284	272	1,070
Gain (Loss) on Sale/Retirement of Capital Assets	(26,141)	(9,819)	(5,076)	(3,494)	(2,436)
Debt Service Interest Expense	(12,737)	(23,935)	(26,370)	(29,919)	(28,081)
Other	32	(67)	175	980	751
TOTAL NONOPERATING REVENUES (EXPENSES)	(30,254)	(26,072)	(19,243)	(15,198)	(16,026)
INCOME (LOSS) BEFORE CONTRIBUTIONS AND TRANSFERS	(24,156)	(15,371)	9,577	15,128	24,168
Capital Contributions	41,954	44,262	80,859	31,526	30,277
Transfers from Other Funds	3,377	220	352	578	439
Transfers from Governmental Funds	27	-	84	3,867	3,443
Transfers to Other Funds	(319)	(158)	(234)	(93)	(99)
Transfer to Governmental Funds	(1,046)	(1,481)	(1,713)	(834)	(530)
CHANGE IN NET ASSETS	19,837	27,472	88,925	50,172	57,698
Net Assets at Beginning of Year	1,179,114	1,198,951	1,226,423	1,315,348	1,365,520
NET ASSETS AT END OF YEAR	$1,198,951	$1,226,423	$1,315,348	$1,365,520	$1,423,218

Source: Comprehensive Annual Financial Reports for Fiscal Years 2005 through 2009.
(1) Earnings on Investments include interest earned on the Construction Fund for the City's outstanding bonds.

The following table sets forth the debt service coverage for Fiscal Years 2005 through 2009.

TABLE 16

CALCULATION OF HISTORIC DEBT SERVICE COVERAGE
Fiscal Years 2005 through 2009
(Dollar Amounts in Thousands)
(Unaudited)

						Parity Obligations				All Obligations [1]	
Fiscal Year Ended June 30	System Revenues	Total Expenses [2]	Net System Revenue	Less: Interest Earnings on Reserve Fund	Adjusted Net System Revenues	Total Debt Service	Less: Interest Earnings	Adjusted Debt Service	Adjusted Debt Service Coverage	Total Debt Service (Parity and Subordinated)	Aggregate Debt Service Coverage
2005	$294,904	$234,392	$60,512	($1,262)	$59,250	$21,355	($1,262)	$20,093	2.95x	$34,861	1.74x
2006	303,453	242,180	61,273	(1,228)	60,045	21,355	(1,228)	20,127	2.98	35,549	1.72
2007	336,599	255,486	81,113	(1,346)	79,767	21,351	(1,346)	20,005	3.99	40,759	1.99
2008	350,770	258,813	91,957	(1,481)	90,476	21,354	(1,481)	19,873	4.55	43,082	2.13
2009	364,413	263,280	101,133	(2,668)	98,465	21,354	(2,668)	18,686	5.27	49,600	2.04

Source: Statistical section (unaudited) of Comprehensive Annual Financial Report for the Fiscal Year Ended June 30, 2009.
(1) All Obligations include Outstanding Parity Obligations and the Outstanding Subordinated Obligations, which includes the Existing SRF Loan.
(2) Amounts reflect the Maintenance and Operation costs of the Water System.

Management's Discussion and Analysis

The following discussion relates to certain items set forth in Table 15. Certain of the following information in connection with the financial condition and results of operations of the Water Utility Fund for Fiscal Year 2009, is unaudited and should be read in conjunction with certain of the information contained in "APPENDIX A – BASIC FINANCIAL STATEMENTS, REQUIRED SUPPLEMENTARY INFORMATION AND CERTAIN EXCERPTS FROM THE COMPREHENSIVE ANNUAL FINANCIAL REPORT OF THE CITY OF SAN DIEGO FOR THE FISCAL YEAR ENDED JUNE 30, 2009" and specifically the portion of the basic financial statements relating to the operation of the Water Utility Fund.

Operating Revenues. Total operating revenues for Fiscal Year 2009 were $342.7 million, which represented an increase of $24.1 million from the previous Fiscal Year. The increase was primarily due to a rate increase of 6.5% on July 1, 2008, and another rate increase of approximately 8.5% on January 1, 2009, and reflects a slight decrease of approximately 240 million cubic feet from the prior year in water delivery. This was a 2.5% decrease in delivery quantity from the prior Fiscal Year.

Operating Expenses. Total operating expenses for Fiscal Year 2009 were $302.5 million, an increase of $14.2 million from Fiscal Year 2008. Such increase was primarily the result of an increase in the cost of purchased water of $12.3 million and an increase in depreciation of $9.7 million. Administrative expenditures during Fiscal Year 2009 were decreased by $3.5 million.

Operation and Maintenance expenses included the operation of three treatment facilities as well as operation and maintenance of approximately 3,222 miles of distribution mains and associated pump stations. Operation and Maintenance expenditures were 32% of Operating Expenses and totaled $96.0 million for Fiscal Year 2009. This was a decrease of $4.4 million or 4.3% less than the corresponding amount for Fiscal Year 2008.

Non-operating Revenues. Non-operating revenues for Fiscal Year 2009 decreased by $3.7 million from non-operating revenues received in Fiscal Year 2008. This decrease was primarily due to a decrease in federal grant assistance and a decrease on investment earnings.

Non-operating Expenses. Non-operating expenses decreased by $2.9 million to $30.5 million during Fiscal Year 2009. This decrease was due to a $1.0 million decrease in losses attributable to the retirement of capital assets and a decrease in debt service interest expense of $1.8 million.

Cash Flow from Operations. Net cash provided by operating activities for Fiscal Year 2009 was $67.0 million, an increase of approximately $8.6 million from the previous year. This change is generally attributable to an increase in receipts from customers and users, a decrease in payments to employees, a decrease in receipts from interfund services, and an increase in payments to suppliers.

Reserves. As of June 30, 2009, the Water Utility Fund had total reserves of approximately $133.7 million. This is in compliance with a reserve policy adopted by the City during Fiscal Year 2009.

Outstanding Obligations. As of June 30, 2009, the Water Utility Fund had outstanding debt of approximately $918.4 million. More detailed information about the Water Utility Fund's long-term debt is presented in the notes to the financial statements attached hereto as "APPENDIX A – BASIC FINANCIAL STATEMENTS, REQUIRED SUPPLEMENTARY INFORMATION AND CERTAIN EXCERPTS FROM THE COMPREHENSIVE ANNUAL FINANCIAL REPORT OF THE CITY OF SAN DIEGO FOR THE FISCAL YEAR ENDED JUNE 30, 2009," including certain information regarding the Public Utilities Department's bond service coverage ratio requirements.

Rate Stabilization Fund; Other Funds and Accounts

The City has established within the Water Utility Fund two reserve funds: the Rate Stabilization Fund ("Rate Stabilization Fund") and the Secondary Purchase Fund ("Secondary Purchase Fund"). Amounts in the Rate Stabilization Fund are to be used exclusively for the operation and maintenance of the Water System and such Fund is maintained pursuant to the Master Installment Purchase Agreement. The Rate Stabilization Fund has no associated budgeted amount from year to year and amounts therein are intended to provide a source of funds to mitigate future rate increases. Deposits into the Rate Stabilization Fund are made from current Water System revenues and subject to the discretion of the City Council. Amounts may be deposited into the Rate Stabilization Fund from time to time but such amounts are typically deposited at the end of the Fiscal Year. When deposited in the Rate Stabilization Fund, Net System Revenues for purposes of calculating bond coverage ratios are reduced by the amount of the deposit. Amounts may be withdrawn from the Rate Stabilization Fund through the normal procedures established by the City Comptroller, including approval of the Chief Financial Officer, or by City Council action in the form of an ordinance to appropriate the amounts from the Rate Stabilization Fund into a specific program for expenditure. When withdrawn from the Rate Stabilization Fund, the amounts are deemed System Revenues for purposes of calculating bond coverage requirements.

The Secondary Purchase Fund has no associated budgeted amount from year to year and any deposits thereto are subject to the discretion of the City. Amounts in the Secondary Purchase Fund, which may come from any moneys available, are intended to be equal to 6% of the annual budget for the purchase of water and may be used as an emergency reserve for the purchase of water in the event of a drought or other emergency that unexpectedly disrupts the City's normal supply of water or for any operating and maintenance expense. Amounts may be withdrawn from the Secondary Purchase Fund and appropriated for program expenditures through City Council action in the form of an ordinance. There is no requirement to replenish any amounts withdrawn from the Secondary Purchase Fund. To the extent that amounts are deposited in the Secondary Purchase Fund from current Water System Revenues, System Revenues are reduced by the amount of such deposit for purposes of calculating debt service coverage requirements. Amounts withdrawn from the Secondary Purchase Fund are deemed System Revenues. There are currently no expected transfers to or from the Secondary Purchase Fund, other than those necessary to maintain the 6% annual water purchases target.

The City has also established within the Water Utility Fund, the Operating Reserve ("Operating Reserve"), which is funded at an amount necessary to provide for a certain number of days of operations in the event of an emergency or catastrophe that results in loss of revenues. Such amount is calculated based on the annual operating budget for the Fiscal Year (less water purchases and amounts in the Appropriated Reserve (as defined below)). The Operating Reserve is required to be replenished during any Fiscal Year in which amounts were withdrawn. As of June 30, 2009, amounts in the Operating Reserve equaled approximately $20,477,026, which accounts for approximately 55 days of operating costs. The Fiscal Year 2010 budget included approximately $19.9 million for the Operating Reserve, which accounts for approximately 60 days of operating costs. The City is in the process of gradually increasing such reserve to a level sufficient for 70 days of operating costs by Fiscal Year 2013.

Other reserves established by the City include an SRF Loan Reserve (the "SRF Loan Reserve") for payment of principal and interest on the Existing SRF Loan; two Debt Service Reserve Funds (the "Debt Service Reserve Funds") for payment of principal and interest on its bonds; an Emergency Reserve (the "Emergency Reserve") annually budgeted at $5.0 million to provide for emergency capital expenditures or other unanticipated capital needs; and an Appropriated Reserve (the "Appropriated Reserve") annually budgeted in an amount determined by the Public Utilities Department in its discretion to provide for unanticipated needs that may arise during the course of the year, including payment of unanticipated operating expenses, which requires the approval of the Director of the Public Utilities Department, and payment of unanticipated capital needs, which requires approval of the City Council.

In Fiscal Year 2008, the City established a Dedicated Reserve for Efficiencies and Savings (the "DRES") to save funds obtained by increasing efficiencies, changing priorities or other actions related to reducing costs of the CIP or operations and maintenance of the Water System. The funds in the DRES may be used for accelerating CIP project schedules and reducing the need for future rate increases. At the end of each Fiscal Year, any savings not required for compliance with established reserve policies will be transferred into the DRES. At the end of four years, any funds transferred into the DRES and not used for capital improvements will be used to lower future rates for the Water System.

The following table sets forth the cash and cash equivalents, including reserves, of the Water Utility Fund as of June 30, 2009.

TABLE 17

WATER UTILITY FUND CASH AND CASH EQUIVALENTS (INCLUDING RESERVES)
(In Thousands)

	As of 6/30/2009 (1)
Cash and Investments	$225,556
Restricted Cash and Investments	263,883
Less Investments Not Meeting the Definition of Cash Equivalents	(256,088)
Cash and Cash Equivalents at Year End (3)	**$233,351**
	As of 6/30/2009 (2)
Rate Stabilization Reserve	$20,500
Secondary Purchase Reserve	7,513
Operating Reserve	20,477
SRF Loan Reserve	1,376
Dedicated Reserve for Efficiencies and Savings (DRES)	2,252
Emergency Reserve	5,000
Unreserved Cash and Cash Equivalents	176,233
Cash and Cash Equivalents at Year End (3)	**$233,351**

(1) Source: The City's Comprehensive Annual Financial Report for the Fiscal Year Ended June 30, 2009.
(2) Source: Public Utilities Department and Comptroller's Office, City of San Diego.
(3) Excludes bond proceeds held in the Acquisition Fund and Trustee-held Debt Service Reserve Funds.

For information on the possible limitation on the City's ability to set rates and charges at levels that would permit the City to make deposits into the Rate Stabilization Fund or the Secondary Purchase Fund as a consequence of Proposition 218, see "WATER SYSTEM FINANCIAL OPERATIONS." See also Table 18 under the caption "WATER SYSTEM FINANCIAL OPERATIONS – Financial Projections and Modeling Assumptions" for currently anticipated deposits into and withdrawals from the Rate Stabilization Fund incident to the currently contemplated CIP.

Financial Projections and Modeling Assumptions

The following table sets forth the estimated and projected operating revenues and expenses for Fiscal Years 2010 through 2014.

TABLE 18

ESTIMATED OPERATING REVENUE AND EXPENSES (1)
Fiscal Year 2010 through 2014
(In Thousands)
(Unaudited)

DESCRIPTION	2010 Projected	2011 Projected	2012 Projected	2013 Projected	2014 Projected
Net Operating Revenues (2)	$68,459	$88,853	$86,154	$83,428	$80,552
Interest Income on Operating Funds	5,239	5,228	6,349	7,105	6,351
Interest Income on Capital Monies	1,989	2,217	2,723	3,298	3,776
Interest Income on Debt Service Reserve Fund	1,086	1,154	1,782	2,418	2,681
Capacity Fee Proceeds	5,578	5,592	5,620	5,676	5,733
Less: Senior Debt Service Reserve Fund Interest (3)	(543)	(646)	(1,087)	(1,475)	(1,636)
Total Adjusted Net System Revenues (4)(5)	$81,808	$102,398	$101,541	$100,450	$97,457
Projected Senior Debt Service	$25,453	$37,302	$46,431	$61,656	$61,657
Less: Senior Debt Service Reserve Fund Interest (3)	(543)	(646)	(1,087)	(1,475)	(1,636)
Adjusted Debt Service	$24,910	$36,656	$45,344	$60,181	$60,021
Senior Debt Service Coverage (4)(5)	328%	279%	224%	167%	162%
Aggregate Debt Service Coverage					
Net Operating Revenues	$68,459	$88,853	$86,154	$83,428	$80,552
Interest Income on Operating Funds	5,239	5,228	6,349	7,105	6,351
Interest Income on Capital Monies	1,989	2,217	2,723	3,298	3,776
Capacity Fee Proceeds	5,578	5,592	5,620	5,676	5,733
Debt Service Reserve Fund Interest(6)	1,086	1,154	1,782	2,418	2,681
Total Net System Revenues (5)	$82,351	$103,044	$102,628	$101,925	$99,093
Projected Senior Debt Service	$25,453	$37,302	$46,431	$61,656	$61,657
Projected Subordinate Debt Service	28,675	28,668	28,672	28,675	28,674
Aggregate Debt Service (7)	$54,128	$65,970	$75,103	$90,331	$90,331
Aggregate Debt Coverage (8)	152%	156%	137%	113%	110%

Source: Public Utilities Department, City of San Diego.

(1) Figures represent a scheduled 6.5% general rate increase in Fiscal Years 2010 and 2011, but figures assume no additional rate increases thereafter. Figures represent projections prior to the prepayment of the Refunded 1998 Certificates and the issuance of the 2010A Bonds. Projections do not reflect anticipated debt service savings resulting from such actions.
(2) Fiscal Year 2010 figures reflect anticipated water conservation of 15% by the end of Fiscal Year 2010. Thereafter, figures reflect 1% growth in water sales from Fiscal Year 2010.
(3) Includes anticipated bond issuances subsequent to Fiscal Year 2010. Does not include restricted Debt Service Reserve Fund interest earnings.
(4) As defined in the Installment Purchase Agreement.
(5) Figures may not add to total due to independent rounding.
(6) Does not include restricted interest earnings.
(7) Includes debt service for Parity Obligations and Subordinated Obligations without adjustment for Debt Service Reserve Fund earnings.
(8) Ratio of total Net System Revenues to Aggregate Debt Service.

The data set forth in Table 18 is based upon various assumptions, including those set forth below, adopted by the Public Utilities Department. The achievement of certain results or other expectations contained in Table 18 involve known and unknown risks, uncertainties, and other factors that may cause actual results, performance, or achievements reflected in Table 18 to be materially different from any future results, performance, or achievements expressed or implied in such Table 18. Although, in the opinion of the Public Utilities Department, such projections are reasonable, there can be no assurance that any or all of such projections will be realized or predictive of future results.

The Public Utilities Department operating projections include the expense of improved and expanded Public Utilities Department facilities that will become operational during the projection period. The Public Utilities Department receives both raw and treated water supplies form CWA. The proportion of these two supplies is based on long-term planning criteria to minimize the long-term costs for water services.

The Water System's account growth projections for Fiscal Year 2014 and beyond are based on San Diego Association of Governments ("SANDAG") 2030 Forecasts, which was approved by the Board of SANDAG in November 2003. SANDAG's growth projections for Fiscal Year 2010 are 1.1% and 1.0% annually thereafter. However, adjustments to the Water System's growth projections for Fiscal Years 2010 through Fiscal Year 2013 reflect recent growth trends based upon the current economic environment. The Water System's account growth rate for Fiscal Years 2010 through Fiscal Year 2012 is 0.25%, increasing to a growth rate of 0.50% in Fiscal Year 2013, and ultimately 1.0% thereafter. These rates are applied to the number of customer accounts. The Public Utilities Department has based the current number of accounts from the Water Utilities Customers Information System Monthly Rate Code Summary (Actual).

Service rates are budgeted to increase 6.5% in Fiscal Years 2010 and 2011. The January 2010 rate adjustment to pass through additional CWA water costs has been included in the analyses on Table 18.

Reclaimed water revenues, which are a component of water sales, are expected to increase from approximately $7.4 million to $11.7 million over the period from Fiscal Year 2010 to Fiscal Year 2014 due to new customers and increased demand from existing customers. Reclaimed revenues will continue to supplant revenues from potable water service charges as existing customers convert from potable to reclaimed water supplies. Revenues will also be lost as customers convert to reclaimed water since reclaimed water is priced below potable water. Reduced water purchases will offset a portion of revenue losses of conversion to reclaimed. However, a large portion of reclaimed water sales are made on a wholesale basis to other water districts and agencies outside of the City, including the Otay Water District, the City of Poway, the Olivenhain Water District, and the International Boundary and Water Commission. These districts and agencies comprise approximately 45% of current reclaimed water used. Reclaimed water used by these districts does not offset potable water sales in the City so they do not have a negative revenue impact to the Water Utility Fund.

The Public Utilities Department is actively pursuing Proposition 50 grants and other grants. Such amounts, however, are not included in the model unless grant agreements have been approved by the Public Utilities Department and the granting agency.

Capital project costs are estimated based on current design, construction management, and construction cost plus a contingency equal to approximately 5% of construction cost. An inflation factor, calculated as described below, is added to the costs in the out-years.

The Public Utilities Department's model reflects capacity charges expected to range between $5.6 million and $5.7 million per year through Fiscal Year 2014.

The Public Utilities Department's model includes the anticipated issuance of additional revenue bonds secured by installment payments pursuant to the Installment Payment Agreement, including bonds in the approximate principal amount of $613.6 million maturing 30 years from their respective dates of issuance. The Public Utilities Department anticipates that the amount of revenue bonds to be issued in the future will be reduced by the amount of the Additional SRF Loans received from DWR, if any.

Interest rates estimated for projected earnings on fund balance are 2.5% for Fiscal Year 2010 and Fiscal Year 2011, 3.0% for Fiscal Year 2012, and 3.5% for Fiscal Year 2013 and Fiscal Year 2014. The interest rate for the projected public financing is reflected in the model to be 6%.

The model assumes annual inflation for Operations and Maintenance expenditures, except salaries and wages (which are assumed at 0%), is 4% based on the consumer price index for all urban consumers. The annual inflation for capital projects is 4% based on the Engineering News Record Construction Cost Index most recent 10-year annual average and 15-year annual average.

The Public Utilities Department's current rate model reflects no increase in salaries and wages until Fiscal Year 2014, consistent with the City's October 2009 Five-Year Financial Outlook (as defined herein). Actual results may be materially different from the assumptions respecting salary and wage increases included in Table 18. To the extent that actual salary and wage increases are higher than the assumed amounts, the Water System's expenditures may materially increase. The Public Utilities Department reduced 72.4 positions in Fiscal Year 2009 (net of hires), to continue both streamlining and re-engineering efforts.

Additional pension costs are reflected in the model based on the Water Utility Fund's proportionate share to fully fund the City's annual required contribution to the Pension System (as defined herein). The Water Utility Fund also contributes its proportional share to the Pension System, which was approximately 4.4% (equal to approximately $6.6 million) for Fiscal Year 2009. See "WATER SYSTEM FINANCIAL OPERATIONS – San Diego City Employees' Retirement System – Water System Share of Contribution to Pension System and NPO" and " – Post-Retirement Healthcare Benefits."

The data in Table 18 is based upon an assumption of the Water Utility Fund's proportionate share of costs for implementation of the Enterprise Resource Planning Program consistent with the Mayor's response to the 2006 Report of the Audit Committee of the City of San Diego (typically referred to as the "Kroll Report"). Additional costs for general government services are reflected based on the reorganization of the City government and the allocation of additional departments not previously included in the calculation.

Outstanding Indebtedness

As of June 1, 2010, the aggregate principal amount of Outstanding Parity Obligations was $625,535,000, and the aggregate principal amount of Outstanding Subordinated Obligations was $276,033,478. After the issuance of the 2010A Bonds and the prepayment of the Refunded 1998 Certificates, the City will have $607,290,000 aggregate principal amount of Outstanding Parity Obligations. The aggregate principal amount of loans payable from Net System Revenues as of June 1, 2010, was $17,573,478, consisting of loans payable to the State of California Water Resources Control Board, which is included in the amount of Outstanding Subordinated Obligations.

See a description of the Public Utilities Department's long-term debt as of June 30, 2009, as presented in Note 6 to the City's audited financial report for Fiscal Year 2009 attached hereto as APPENDIX A. Except for covenants relating to its continuing disclosure undertakings, the Public Utilities Department was and is in compliance with bond covenants and debt service coverage ratio requirements. See "INTRODUCTION – Continuing Disclosure."

Pursuant to Section 90 of the City Charter, general obligation bonded indebtedness for the development, conservation, and furnishing of water shall not exceed 15% of the last preceding assessed valuation of all real and personal property of the City subject to direct taxation. The Public Utilities Department had not issued any general obligation debt as of January 1, 2010.

The following table sets forth the outstanding indebtedness payable from Net System Revenues as of June 1, 2010. See "THE REFUNDING PLAN" for a description of the payments and prepayments to be effected with proceeds of the 2010A Bonds. After the issuance of the 2010A Bonds and the prepayment of the Refunded 1998 Certificates, the City will have $607,290,000 aggregate principal amount of Outstanding Parity Obligations.

TABLE 19

OUTSTANDING DEBT
As of June 1, 2010

Series	Final Maturity	Outstanding Principal Amount	Principal Amount to be Refunded
Parity Obligations:			
1998 Certificates (1)	August 1, 2028	$141,320,000	$141,320,000
2009A Bonds	August 1, 2038	156,155,000	0
2009B Bonds	August 1, 2039	328,060,000	0
Total Parity Obligations:		$625,535,000	$141,320,000
Subordinated Obligations:			
2002 Subordinated Bonds	August 1, 2032	$258,460,000	0
State Revolving Fund Loan	July 1, 2025	17,573,478	0
Total Subordinated Obligations:		$276,033,478	0
Total Outstanding Obligations:		$901,568,478	$141,320,000

Source: Debt Management Department, City of San Diego.

(1) To be prepaid in full with a portion of the proceeds of the 2010A Bonds and other moneys transferred from certain funds and accounts established under the 1998 Trust Agreement.

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Annual Debt Service Requirements

The following table sets forth the amounts required in each Fiscal Year, commencing on July 1, 2010, for the payment of principal of and interest on existing Outstanding Obligations (excluding the Existing SRF Loan) payable from the Water Utility Fund after giving effect to the issuance of the 2010A Bonds and the prepayment of the Refunded 1998 Certificates. See "SECURITY AND SOURCES OF PAYMENT FOR THE 2010A BONDS."

TABLE 20

DEBT SERVICE ON ALL OUTSTANDING OBLIGATIONS [(1)]

As of July 1, 2010

			2010A Bonds					
Fiscal Year Ending June 30	Outstanding Series 2009A Bonds	Outstanding Series 2009B Bonds	Principal	Interest	Total Principal and Interest	Total Parity Obligations Debt Service	Outstanding 2002 Subordinated Bonds	Total Debt Service
2011	$ 8,679,925	$ 21,736,381		$ 3,698,640	$ 3,698,640	$ 34,114,946	$ 27,292,513	$ 61,407,458
2012	8,679,025	21,734,969		6,310,475	6,310,475	36,724,469	27,296,456	64,020,925
2013	8,677,225	21,735,794		6,310,475	6,310,475	36,723,494	27,299,238	64,022,731
2014	8,680,375	21,734,356		6,310,475	6,310,475	36,725,206	27,298,400	64,023,606
2015	8,680,775	21,736,869		6,310,475	6,310,475	36,728,119	27,295,813	64,023,931
2016	9,557,475	21,735,494		6,310,475	6,310,475	37,603,444	26,924,438	64,527,881
2017	21,964,100	21,738,694		6,310,475	6,310,475	50,013,269	13,733,800	63,747,069
2018	21,959,225	21,739,144		6,310,475	6,310,475	50,008,844	13,735,350	63,744,194
2019	21,959,975	21,737,853		6,310,475	6,310,475	50,008,303	13,737,250	63,745,553
2020	21,958,725	21,735,438		6,310,475	6,310,475	50,004,638	13,732,525	63,737,163
2021	21,959,700	21,739,063		6,310,475	6,310,475	50,009,238	13,733,925	63,743,163
2022	21,958,719	21,734,525		6,310,475	6,310,475	50,003,719	13,735,138	63,738,856
2023	4,071,638	21,734,613	$ 12,510,000	5,997,725	18,507,725	44,313,975	13,736,875	58,050,851
2024	4,072,138	21,734,969	13,150,000	5,356,225	18,506,225	44,313,331	13,735,325	58,048,656
2025	4,073,013	21,737,700	15,910,000	4,629,725	20,539,725	46,350,438	13,732,525	60,082,963
2026	4,074,013	21,738,450	18,815,000	3,761,600	22,576,600	48,389,063	13,737,263	62,126,325
2027	4,070,013	21,734,200	19,805,000	2,771,344	22,576,344	48,380,556	13,733,413	62,113,969
2028	4,070,763	21,738,575	20,880,000	1,703,363	22,583,363	48,392,700	13,734,625	62,127,325
2029	4,070,888	21,737,663	22,005,000	577,631	22,582,631	48,391,181	13,734,500	62,125,681
2030	4,070,138	21,734,456	—	—	—	25,804,594	13,736,875	39,541,469
2031	4,069,881	21,737,409	—	—	—	25,807,291	13,735,375	39,542,666
2032	4,069,444	21,737,938	—	—	—	25,807,381	13,733,625	39,541,006
2033	4,071,394	21,734,094	—	—	—	25,805,488	13,735,000	39,540,488
2034	4,070,338	21,738,594	—	—	—	25,808,931	—	25,808,931
2035	4,070,881	21,734,153	—	—	—	25,805,034	—	25,805,034
2036	4,072,500	21,735,756	—	—	—	25,808,256	—	25,808,256
2037	4,069,800	21,735,088	—	—	—	25,804,888	—	25,804,888
2038	4,072,256	21,735,750	—	—	—	25,808,006	—	25,808,006
2039	4,074,213	21,734,075	—	—	—	25,808,288	—	25,808,288
2040	—	21,736,763	—	—	—	21,736,763	—	21,736,763
Total [(2)]:	$253,928,550	$652,088,822	$123,075,000	$97,911,477	$220,986,477	$1,127,003,849	$396,900,244	$1,523,904,093

Source: Debt Management Department, City of San Diego.

(1) Excludes debt service on the Existing SRF Loan.

(2) Amounts have been rounded; total may not equal the sum of the components.

Labor Relations

General. The City has five labor organizations which represent classified employees. They are the International Association of Firefighters Local 145 ("IAFF Local 145"), the San Diego Police Officers Association (the "POA"), the Municipal Employees Association (the "MEA"), the American Federation of State, County and Municipal Employees, Local 127 ("AFSCME Local 127"), and the California Teamsters Local 911 ("Local 911"), who represent lifeguards. A sixth labor organization, the Deputy City Attorneys' Association (the "DCAA"), represents unclassified deputy city attorneys.

As of May 18, 2010, there were 785.5 regular full-time employees of the Water Department, of which 463 are represented by the MEA and 282 are represented by AFSCME Local 127. The remaining 40.5 employees are unrepresented. The two bargaining units represent approximately 95% of the Water Department employees.

Contracts for Fiscal Years 2010 through 2011. On April 14, 2009, the City Council unanimously approved the terms of the labor agreements for Fiscal Years 2010 and 2011 for the MEA, the IAFF Local 145 and the DCAA. Negotiations with the remaining two bargaining units, AFSCME Local 127 and the POA, did not end in agreement. The City Council imposed on both unions the terms and conditions of employment contained in the Mayor's last, best and final offer for Fiscal Year 2010. Pursuant to the labor agreements for the bargaining units and the terms and conditions approved for AFSCME Local 127 and POA, all five bargaining units and the City's unclassified and unrepresented employees were held to a general salary freeze and subject to a 6% reduction in overall compensation, which was effected through salary reductions, decreases in the City-paid allotment for employee health care, retirement and other employment benefits, fewer paid holidays, mandatory furloughs and elimination of the employer contribution to San Diego City Employees' Retirement System employee pickup/offset and to the mandatory match of the supplemental pension savings plan. Each bargaining unit reached the 6% target through a different combination of the aforementioned measures. The compensation reductions also apply to management and unrepresented City employees, including the Mayor, his staff, and some independent departments. Departments not under the Mayor, including some City Council offices, did not participate in some or all of the compensation reductions.

Contracts for Fiscal Years 2011 through 2012. The City has reached a final agreement with Local 911 and has pending agreements with the POA and AFSCME Local 127 for Fiscal Years 2011 through 2012. The contracts call for a continuation of the 6% reduction in overall compensation. There are no salary increases contained in the agreements.

Insurance and Liability Claims

The Public Utilities Department is self-insured for workers' compensation and long-term disability and for public liability claims exposure up to $4 million per occurrence. For liability between $4 million and $50 million, the Public Utilities Department is covered by the City, which purchases insurance in collaboration with the California State Association of Counties–Excess Insurance Authority, a statewide joint powers authority risk pool, in layers for its public liability exposure.

The City participates in the joint purchase of property insurance and flood insurance through the California State Association of Counties–Excess Insurance Authority pool, which includes flood and earthquake coverage for scheduled locations, including bond financed locations of the Water System. This joint purchase of the City's "all risk" property insurance, insuring approximately $2.73 billion of City property, provides coverage for loss to City property under the primary policy up to approximately $25 million per occurrence, with a $25,000 deductible. Depending on availability and affordability of such earthquake insurance, the City may elect not to purchase such coverage in the future. The City does not maintain any casualty insurance on the pipelines of the Water System because such insurance is not commercially available.

The following table reflects the public liability expense and cash payments for liability claims of the Water System for Fiscal Years 2005 through 2009.

TABLE 21

LIABILITY CLAIMS
PUBLIC LIABILITY EXPENSE AND CASH PAYMENTS
Fiscal Years 2005 through 2009
(Unaudited)

Fiscal Year	Public Liability Expense(1)	Cash Payments
2005	$ 966,319	$1,146,732
2006	2,852,333	3,028,169
2007	4,794,657	2,483,122
2008	3,251,170	1,676,075
2009	2,408,517	2,012,355

Source: Comptroller's Office, City of San Diego.
(1) Public Liability Expense includes actual cash payments plus the change in accrued liabilities from the previous Fiscal Year.

Investment of Funds

General. Amounts in the funds and accounts of the Water Utility Fund are invested by the City Treasurer in the Treasurer's Pooled Investment Fund (the "City Pool") described below and the City accounts for such amounts separately from other funds of the City.

City Pool. In accordance with the Charter of the City and authority granted by the City Council, the City Treasurer is responsible for investing the unexpended cash in the City Pool. Responsibility for the daily investment of funds in the City Pool is delegated to the City's Chief Investment Officer. The City and certain related entities are the only participants in the City Pool; there are no other City Pool participants either voluntary or involuntary in the City Pool. The investment objectives of the City Pool are preservation of capital, liquidity and return.

Oversight and Reporting Requirements. The City Treasurer provides an investment report on a monthly basis to the Chief Financial Officer, the City Comptroller and the City Council and annually presents the Investment Policy to the Chief Financial Officer, the Investment Advisory Committee and the City Council. The Investment Advisory Committee is comprised of two City employees, currently the Chief Financial Officer and the Director of Debt Management, and three investment professionals from the private sector and is charged with overseeing the review of the City's Investment Policy and practices of the City Treasurer and recommending changes thereto. Investments in the City Pool are audited annually by an independent firm of certified public accountants as part of the overall audit of the City's financial statements.

The City's investments division uses outside services to provide investment portfolio valuations and accounting and reporting services. These services provide monthly portfolio valuation, investment performance statistics, and other portfolio reports that are distributed to the Office of the City Treasurer accounting section and the Office of the Comptroller of the City for review and reconciliation. The Office of the City Treasurer's accounting section prepares a series of monthly reports, including the portfolio market valuation, and distributes these to the Mayor, City Council, Chief Financial Officer, and other officials.

Authorized Investments. Investments in the City Pool are governed by State law and further restricted by the City's Investment Policy. The Investment Policy is prepared with safety of principal being the foremost objective. Permitted investments include U.S. Treasury securities, U.S. Agency securities, U.S. Agency mortgage backed securities, corporate medium term notes, money market instruments, non-negotiable Federal Deposit Insurance Corporation-insured certificates of deposit and the Local Agency Investment Fund (California State Pool). Reverse repurchase agreements ("reverse repos") are restricted to 20% of the base value of the portfolio and are governed by various maturity restrictions as well. The main operating funds of the City are managed in two separate portfolios. In its management of the "Liquidity" portfolio, comprising approximately 35% of total funds, the City invests in a variety of debt securities with maturities ranging from one day to approximately one year. The remaining 65% of funds are managed in a separate "Core" portfolio that consists of a variety of debt securities ranging from one day to five years; performance is measured against the Merrill Lynch one- to three-year U.S. Treasury Index. The 35% Liquidity/65% Core portfolio split serves as a guideline. The actual split may vary due to market conditions or other factors. Safety of principal and liquidity are paramount considerations in the management of both portfolios.

Pool Liquidity and Other Characteristics. The City Pool (including both the "Liquidity" and the "Core" portfolios) is highly liquid. Based on unaudited month-end data as of March 31, 2010, approximately 13% of the pool investments mature within 62 days, 16% within 92 days, 24% within 184 days, 39% within 1 year, 77% within 2 years, 98% within 3 years, and 100% within 5 years (on a cumulative basis). As of March 31, 2010, the City Pool had a weighted average maturity of 1.34 years (488 days) and its weighted average yield was 1.015%. For purposes of calculating weighted average maturity, the City Treasurer treats investments in the State-wide Local Agency Investment Fund (California State Pool) as maturing within one day. The Liquidity portfolio had a duration of 0.37 years and the Core portfolio had a duration of 1.78 years as of March 31, 2010. Duration is a measure of the price volatility of the portfolio and reflects an estimate of the projected increase or decrease in the value of the portfolio based upon a decrease or increase in interest rates. Accordingly, the Liquidity portfolio should decrease in market value by 0.37% for every 1% increase in market interest rates while the Core portfolio should decrease in market value by 1.78% for every 1% increase in market interest rates. The City Pool's composition is designed with a goal of having sufficient liquid funds available to meet disbursement requirements. The composition and value of investments under management in the City Pool will vary from time to time depending on cash flow needs of the City, maturity or sale of investments, purchase of new securities, and fluctuations in interest rates.

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The following table sets forth the City Pool results at March 31, 2010.

TABLE 22

CITY OF SAN DIEGO POOLED INVESTMENT FUND
at March 31, 2010
(In Thousands)
(Unaudited)

Investment Instrument	Book Value	Fair Value	Percent of Total [1]
U.S. Treasury Bills and Notes	$ 881,235	$ 883,223	42.94%
Federal Agency Securities [2]	770,534	771,644	37.54
Medium Term Notes (Corporate) [3]	194,360	196,183	9.47
Money Market Instruments [4]	156,317	156,277	7.62
Local Agency Investment Fund	49,957	49,957	2.43
TOTAL INVESTMENTS	$2,052,403	$2,057,284	100.00%

Source: Office of the City Treasurer, City of San Diego.
(1) Based on book value.
(2) Federal National Mortgage Association ("Fannie Mae") securities and Federal Home Loan Mortgage Corporation ("Freddie Mac") securities represent 29.82% and 20.16%, respectively, of total Federal Agency Securities, which is approximately 11.19% and 7.57%, respectively, of the City Pool.
(3) These notes consist of both fixed and floating interest rate securities. The notes with floating interest rates are reset at intervals ranging from one day to three months. 70.63% of these notes were issued under the Temporary Liquidity Guarantee Program and are backed by the full faith and credit of the Federal Deposit Insurance Corporation.
(4) These securities consist of commercial paper, negotiable certificates of deposit, Certificate of Deposit Account Registry Service certificate of deposit, term and overnight repurchase agreements, money market mutual funds, banker's acceptances, bank notes, and/or thrift notes.

The City Pool is not invested in any structured investment vehicles, mortgage-backed securities or other asset-backed securities. In addition, the City has no outstanding swap arrangements or liquidity facilities.

San Diego City Employees' Retirement System

The City faces significant financial challenges in addressing an unfunded pension liability to San Diego Employees' Retirement System (the "SDCERS"), which, as of June 30, 2009, was approximately $2.106 billion. The challenges posed by the unfunded pension liability are significant and, together with significant costs related to postemployment healthcare benefits, pose a threat to the future fiscal health of the City. However, as explained below under the caption, "Water System Share of Contribution to Pension System and NPO," the Water System's proportionate share of the City's annual required contributions to the Pension System is budgeted at approximately 5% (equal to approximately $7.71 million, assuming a City pension payment of $154.2 million) for Fiscal Year 2010. Estimates of the Water System's share of the City's annual contributions of approximately $11.5 million for each of Fiscal Years 2008 through 2011 were included in the 2007 Rate Case model that served as the basis for the annual rate increases in effect through Fiscal Year 2011 that were approved by the City Council. For Fiscal Years 2009 and 2010, the actual contributions required from the Water Utility Fund were less than the amounts that were assumed in the 2007 Rate Case model.

The City's annual required contribution ("ARC") payment for Fiscal Year 2011 will be $231.7 million if paid on July 1, 2010. The Water Utility Fund's expected proportionate share of the ARC payment is 5.18%, which would result in a contribution by the Water Utility Fund of approximately $12.0 million for Fiscal Year 2011.

The amounts and percentages set forth under this caption relating to the City's Pension System, including, for example, actuarial accrued liabilities and funded ratios, are based upon numerous demographic and economic assumptions, including investment return rates, inflation rates, salary increase rates, cost of living adjustments, postemployment mortality, active member mortality, and rates of retirement. The prospective purchasers of the Series 2010A Bonds are cautioned to review and carefully assess the reasonableness of the assumptions set forth in the documents that are cited as the sources for the information under this caption. In addition, the prospective purchasers of the Series 2010A Bonds are cautioned that such sources and the underlying assumptions speak as of their respective dates, and are subject to change, any one of which could cause a significant change in the UAAL (as defined below).

SDCERS is considered part of the City's financial reporting entity and is included in the City's CAFR as a pension system trust fund. SDCERS does prepare its own CAFR, the most recent of which is for Fiscal Year 2009.

UAAL and its Calculation. According to the June 30, 2009 Annual Actuarial Valuation of SDCERS, prepared by Cheiron, Inc. ("Cheiron") dated as of January 8, 2010 (the "2009 Valuation"), the funded ratio (the actuarial value of assets available for benefits to total actuarial accrued liability) of the City's portion of the SDCERS fund[1] was 66.5%, and the SDCERS fund had an unfunded actuarial accrued liability (the "UAAL") of $2.106 billion. Thus, for every dollar of benefits due (all vested liabilities), SDCERS had $0.66 in assets available for payment as of June 30, 2009. The UAAL is the difference between total actuarially accrued liabilities (the "AAL"), which was approximately $6.282 billion as of June 30, 2009, and the actuarially calculated assets allocated to funding, which was approximately $4.175 billion as of June 30, 2009.

Global financial markets experienced significant volatility in Fiscal Year 2009, and SDCERS experienced an actuarial investment loss of $811.4 million in the City's plan during that period. According to the City's June 30, 2008 Annual Actuarial Valuation (the "2008 Valuation") and the 2009 Valuation, the actuarial value of assets (City's portion) as of June 30, 2008 and June 30, 2009 were $4.660 billion and $4.175 billion, respectively. The market value of assets (City's portion) as of June 30, 2008 and June 30, 2009, as reported in the 2008 Valuation and the 2009 Valuation, were $4.409 billion and $3.479 billion, respectively. A decline in the actuarial value of assets over time will result in an increase to the City's ARC in comparison to the amounts estimated in the Fiscal Years 2011-2015 Five-Year Financial Outlook; however, the impact on the Water Utility Fund would be expected to be minimal. See " – Water System Share of Contributions to Pension System and NPO" below.

Actuarial Assumptions. The following are the principal actuarial assumptions used by SDCERS' actuary in preparing the valuation as of June 30, 2009:

1. Investment Return Rate: 7.75% a year, net of administrative expenses, compounded annually.

2. Inflation Rate: 4.00% a year, compounded annually.

3. Interest Credited to Member Contributions: 7.75% compounded annually.

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[1] The City participates in SDCERS along with the San Diego Regional Airport Authority ("Airport Authority") and the San Diego Unified Port District ("Port District"). The Information herein refers only to the City's participation in SDCERS and not to the participation of the Airport Authority or the Port District.

4. Salary Increase Rates: Comprised of a 4.00% inflation rate and 0.5% to 8.0% merit component.

5. Annual Cost-of-Living Adjustments: 2.00% per year, compounded annually.

6. Additional Assumptions: Additional assumptions were used regarding rates of separation from active membership, post-retirement mortality, active member mortality, and rates of retirement.

"Smoothing" Methodology. In determining the actuarial value of its assets, SDCERS, as permitted by applicable actuarial guidelines, uses an expected value of assets "smoothing" methodology to reduce the impact of market volatility on plan assets. The market value of assets represents, as of the valuation date, the value of the assets as if they were liquidated on that date. The actuarial value of assets is a value that attempts to smooth annual investment return performance over multiple years to reduce annual contribution volatility. The actuarial value of assets is used to determine SDCERS' contribution rates for the City. As of June 30, 2009, the market value of plan assets was $3.479 billion, and the actuarial value was $4.175 billion. By the smoothing method used in the 2009 Valuation, the calculation of the actuarial value of assets at June 30, 2009 started with the actuarial value of assets at June 30, 2008, added to that 100% of the actuarially assumed rate of return, plus the contribution towards plan assets, less payments out from plan assets, plus 25% of the difference between the expected actuarial value of assets at June 30, 2009 (using the above calculation) and the actual market value of assets at June 30, 2009. In no event will the actuarial value of assets ever be less than 80% of the market value of assets nor greater than 120% of the market value of assets. The impact of this smoothing methodology will vary each year depending upon the year's actual market value compared to the expected value of assets, either as a net gain or a net loss. The City expects SDCERS to employ the smoothing method used in the 2009 Valuation to valuations for future Fiscal Years. As a result of the smoothing methodology, even a healthy increase in the market value of the SDCERS' plan assets as of June 30, 2010 would have a limited impact on improving the Fiscal Year 2012 ARC. For example, holding all other actuarial assumptions constant, an annual investment return of 25% for Fiscal Year 2010 is estimated to result in an ARC of $244.2 million on a citywide basis for Fiscal Year 2012 (compared to an ARC of $231.7 million for Fiscal Year 2011). This is primarily due to the fact that, because of the smoothing methodology, approximately 45% of Fiscal Year 2009's market loss has yet to be captured in future ARC calculations and only 25% of any Fiscal Year 2010 gains will be included in the Fiscal Year 2012 ARC calculation.

City Contributions to SDCERS. The City's ARC consists of: (i) the "normal cost," being the present value of the benefits that SDCERS expects to become payable in the future attributable to a current year's employment, and (ii) payments made to amortize the UAAL. SDCERS currently amortizes the UAAL over several different periods: the amortization of changes in the UAAL due to assumption changes is over 30 years, the amortization of changes in the UAAL due to benefit changes is over five years, and the outstanding balance of the Fiscal Year 2007 UAAL is amortized over 20 years (such that, as of Fiscal Year 2009, 18 years of amortization remain), and subsequent yearly gains and losses are amortized over 15 years. Finally, if necessary, there is an additional UAAL cost component to ensure that there is no negative amortization in any year, all as approved by the SDCERS Board of Administration in its administrative capacity pursuant to its plenary authority over the Pension System. For several years, the City was paying less than the full ARC. The reasons for this are numerous, including prior agreements between the City and SDCERS, earnings on pension assets at greater than the previous actuarially assumed rate of 8% being credited against contributions, payments pursuant to litigation settlements that were mistakenly characterized as "contingent" and therefore not made in certain years, and other reasons explained in detail in Note 12 to the City's 2009 audited financial statements. See APPENDIX A – "BASIC FINANCIAL STATEMENTS, REQUIRED SUPPLEMENTARY INFORMATION AND CERTAIN EXCERPTS FROM THE COMPREHENSIVE ANNUAL

FINANCIAL REPORT OF THE CITY OF SAN DIEGO FOR THE FISCAL YEAR ENDED JUNE 30, 2009" attached hereto.

Due to the City's prior practice of funding the Pension System at less than actuarially required levels, the City has a Net Pension Obligation ("NPO"), which is the cumulative difference between the annual pension cost ("Annual Pension Cost") to the City of the Pension System and the actual contribution in a particular year. The Annual Pension Cost is equal to (i) the ARC, (ii) one year's interest on the NPO, and (iii) an adjustment to the ARC to offset, approximately, the amount included in item (i) for amortization of the past contribution deficiencies.

In Fiscal Year 2009, the City's total pension contribution, which includes contributions to both the core pension plan and the Preservation of Benefits Plan (referenced in the Fiscal Year 2009 CAFR as the "Preservation of Benefits Plan"), was $163.6 million. The City's NPO at the end of Fiscal Year 2009 was $177.8 million. The City's core pension ARC for Fiscal Year 2010, not inclusive of the Preservation of Benefits Plan ARC, is $154.2 million and has been paid in full. The City anticipates contributing $1.4 million for the Preservation of Benefits Plan for Fiscal Year 2010 and $1.5 million to the Preservation of Benefits Plan in Fiscal Year 2011.

The following table sets forth the City's portion of SDCERS historical funding progress for Fiscal Years 2005 through 2009.

TABLE 23

CITY OF SAN DIEGO
SCHEDULE OF FUNDING PROGRESS
Fiscal Years 2005 through 2009
(In Thousands)

Valuation Date (June 30)	Valuation Assets	AAL	Funded Ratio	UAAL(1)
2005(1)(2)	$2,983,080	$4,436,017	67.25%	$1,452,937
2006(1)	3,981,932	4,982,700	79.92	1,000,768
2007(3)	4,413,411	5,597,653	78.84	1,184,242
2008(3)	4,660,346	5,963,550	78.15	1,303,204
2009(3)	4,175,229	6,281,593	66.47	2,106,364

Sources: City of San Diego Comprehensive Annual Financial Report with respect to data for Fiscal Years 2005 through 2008 and 2009 Valuation with respect to data for Fiscal Year 2009.
(1) Projected Unit Cost method used for determining actuarial accrued liability.
(2) For Fiscal Year 2005, the actuarial accrued liability, the UAAL and the funded ratio have been adjusted to reflect the impact of the Corbett contingent settlement benefit. The actuarial valuation provided by the actuary for Fiscal Year 2005 does not include this contingent benefit in the funded ratio. However, the valuations prepared by the actuary for Fiscal Years 2006 through Fiscal Year 2009 do include the impact of the Corbett contingent settlement benefit. See Note 12 to the City's Fiscal Year 2009 audited financial report attached hereto as APPENDIX A.
(3) Reflects revised actuarial methodologies. The actuarial accrued liability was calculated using the Entry Age Normal method beginning in Fiscal Year 2007. Prior to Fiscal Year 2007, the Projected Unit Cost method was used.

Water System Share of Contributions to Pension System and NPO. For Fiscal Year 2009, the Water System's proportionate share to fully fund the City's contribution to the pension system was $6.6 million, and for Fiscal Year 2010 such share is $6.85 million. The Water System's 2007 Rate Case projection assumed an annual payment of $11.5 million for the Water Utility Fund's proportionate share of the City's ARC for Fiscal Years 2008 through 2011. The City expects that the $11.5 million estimate included in the Water System's 2007 Rate Case projection will be sufficient to pay the Water Utility Fund's proportionate share to fully fund the City's contribution to the Pension System for Fiscal Years

2010 and 2011. The Water System's share of the NPO at June 30, 2009, is approximately $8.5 million. See the City's Fiscal Year 2009 audited financial statements attached hereto, line item entitled "Non-Current Liabilities Net Pension Obligation" under the table entitled "Proprietary Funds Statement of Net Assets."

The following table sets forth, for Fiscal Years 2008 through 2011, the City's total pension payments (consisting of its ARC for pension and its contribution for the Preservation of Benefits Plan), the pension contributions included in the Water System's 2007 Rate Case projection and the corresponding actual, budgeted or projected amounts.

TABLE 24

CITY OF SAN DIEGO AND WATER UTILITY FUND
PENSION CONTRIBUTION
Fiscal Years 2008 through 2011
(In Millions)

Fiscal Year ending June 30	ARC(1)	Total City Pension Contribution(2)	Department Rate Case Projection(3)	Actual/ Budgeted/Projected(2)
2008	$140.1	$166.6	$11.50	$8.80(4)
2009	165.7	163.6	11.50	6.60(4)
2010	155.2	155.6	11.50	6.85(5)
2011	230.9(6)(7)	230.8(6)	11.50	12.00(5)

Sources: Fiscal Years 2008 and 2009: Comprehensive Annual Financial Report, Comptroller's Office, City of San Diego; Fiscal Years 2010 and 2011: Financial Management Department, City of San Diego, except for information under the heading "Department Rate Case Projection," which was provided by the Public Utilities Department.

(1) Includes core pension ARC and Preservation of Benefits Plan ARC. Pursuant to IRS guidelines, the City may not pre-fund the Preservation of Benefits Plan. Therefore, plan contributions may differ from the ARC in any given year. See footnote (2).

(2) Fiscal Year 2008 and 2009: Audited; Fiscal Year 2010: Budgeted; and Fiscal Year 2011: Projection. Fiscal Year 2008: Includes $137.7 million core pension contribution pursuant to SDCERS June 30, 2006 Actuarial Valuation, $1 million Preservation of Benefits Plan contribution, and $27.9 million in additional voluntary contributions. Fiscal Year 2009: Includes $161.7 million core pension contribution pursuant to SDCERS June 30, 2007 Actuarial Valuation, $1.2 million Preservation of Benefits Plan contribution, and $700,000 in additional voluntary contributions. Fiscal Year 2010: Includes $154.2 million core pension contribution pursuant to SDCERS June 30, 2008 Actuarial Valuation and a budgeted $1.4 million Preservation of Benefits Plan contribution. Fiscal Year 2011: Includes $229.1 million core pension contribution pursuant to SDCERS June 30, 2009 Actuarial Valuation and revised ARC in accordance with SDCERS Board Action on May 28, 2010, and a projected $1.7 million Preservation of Benefits Plan contribution.

(3) Reflects projections as of the date of the 2007 Rate Case.

(4) Actual. The Water Utility Fund's proportionate share to fully fund the City's pension contribution (excluding contributions for the Preservation of Benefits Plan), was 5.3% for Fiscal Year 2008 and 4.00% for Fiscal Year 2009. The Public Utilities Department contributes to the Preservation of Benefits Plan only if its employees receive benefits thereunder. The Public Utilities Department was not required to contribute to the Preservation of Benefits Plan in Fiscal Year 2008 or 2009. The Public Utilities Department's contribution to the Preservation of Benefits Plan, if any, for subsequent Fiscal Years will be determined at the end of the respective fiscal years. See footnote (6) below for a discussion of adjustments to the proportionate share.

(5) Fiscal Year 2010 budgeted amount and Fiscal Year 2011 projected amount, assuming the Water Utility Fund's proportionate share to fully fund the City's pension contribution (excluding contributions for the Preservation of Benefits Plan), is 4.4% and 5.2%, respectively. The Water Utility Fund's proportionate share is established at the beginning of a Fiscal Year and may increase or decrease during the year and from year to year depending on a variety of factors, including the number of covered employees attributable to the Water Utility Fund, the retirement benefits accruing to such employees, and end-of-the-year payroll adjustments.

(6) Revised ARC in accordance with SDCERS Board Action on May 28, 2010, whereby the employee portion of the City safety members will increase by approximately $3.3 million. This will reduce the City General Fund share of the Fiscal Year 2011 ARC by approximately $2.6 million. No reduction will be seen in the Water Utility Fund's Fiscal Year 2011 pension contribution.

(7) The Fiscal Year 2011 Preservation of Benefits Plan ARC is $1.8 million.

Actual and budgeted amounts set forth above reflect amounts necessary for the City to satisfy its pension contribution requirement for each Fiscal Year and may be more or less than the amounts projected in the 2007 Rate Case. To date, amounts included in the 2007 Rate Case projection have exceeded in total the amounts actually required to satisfy the Water System's pension contribution requirement.

In addition to the City's ARC payment, the City has entered into a court-approved class action settlement in the case of *William J. McGuigan v. City of San Diego, et. al.*, that requires the City to make a payment of the remaining settlement amount of approximately $32.8 million plus any interest accrued under the settlement to SDCERS by June 8, 2011. Due to the unreasonable hardship that would result if the City were required to make this payment within the prescribed time period, the City will seek to modify the settlement agreement to allow the City to pay the remaining settlement amount over four years. The modified settlement, if approved by the Court, would not significantly affect the Water Utility Fund's payment of its proportionate share of the McGuigan settlement. If the modified settlement is approved, the Water Utility Fund's payment would be approximately $2.0 million if made on the expected payment date of June 30, 2010. If the settlement is not modified, the Water Utility Fund's proportionate share of the payment would be would be approximately $2.1 million if paid on June 8, 2011. This lawsuit involved the underfunding of the pension system by the City and all payments made under the settlement are credited against the UAAL.

Postemployment Healthcare Benefits

The City provides retiree healthcare benefits, also known as other postemployment benefits ("OPEB"), to certain health-eligible retired employees through a plan administered by SDCERS. The City's OPEB plan includes approximately 5,400 retirees, 8,900 active employees, and 600 terminated vested members as of June 30, 2009. Historically, OPEB expenses were funded on a pay-as-you-go basis. Beginning in Fiscal Year 2008, the City entered into an agreement with the California Public Employees Retirement System ("CalPERS") as a participating employer in the CalPERS Employers Retirement Benefits Trust ("CERBT") to pre-fund future OPEB expenses. In Fiscal Year 2009, the City contributed approximately $25.6 million to SDCERS to pay current OPEB expenses and contributed an additional amount of approximately $23.9 million to the CERBT. In Fiscal Year 2010, the City budgeted approximately $32.1 million to SDCERS to pay current OPEB expenses and budgeted an additional contribution of approximately $25 million to CERBT. As of December 31, 2009, the balance on the CERBT was approximately $50.3 million.

The Water System's proportionate share of the City's pay-as-you-go contribution for OPEB was approximately $1.9 million for Fiscal Year 2009. The Water Utility Fund's proportionate share of the contribution to CERBT was approximately $1.8 million. For Fiscal Year 2010, the Water Utility Fund is budgeted to contribute approximately $2.4 million and $1.9 million, respectively, as its proportionate share of the City's pay-as-you-go OPEB contribution and the CERBT contribution.

As of the date of this Official Statement, the City has not fully funded its ARC for OPEB (i.e., the sum of the normal cost of the postemployment benefits plus amortization of the OPEB UAAL). The City has not projected the amounts necessary to fully fund its OPEB ARC payments beyond the amounts set forth in its October 2009 Five-Year Financial Outlook and does not expect to fully fund its OPEB ARC payment in that timeframe, as outlined in the October 2009 Five-Year Financial Outlook. All future contributions for postemployment healthcare benefits will be credited toward the City's ARC for retiree healthcare liabilities in accordance with Governmental Accounting Standards Board ("GASB") Statement No. 43, "Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans" ("GASB 43"), and GASB Statement No. 45, "Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions" ("GASB 45"). See Note 13 to the Fiscal Year 2009 audited financial statements attached hereto in APPENDIX A.

In connection with compliance with GASB 43 and GASB 45, the City has calculated its net OPEB obligation ("NOPEBO") as of June 30, 2009 to be approximately $93.9 million. The NOPEBO is the cumulative difference between the City's annual OPEB cost and City's contributions to OPEB in a particular year, including the OPEB liability or asset at transition, if any. Annual OPEB cost is equal to (i) the ARC for OPEB, (b) one year's interest on the NOPEBO from prior years (which the City determined to be zero at the beginning of Fiscal Year 2008, the transition year, in accordance with GASB 45), and (c) an adjustment to the ARC for OPEB to offset the effect of actuarial amortization of past under- or over-contributions. The Water System's proportionate share of the City's NOPEBO as of June 30, 2009 was $6.6 million. The City intends to pre-fund the CERBT with approximately $25 million on an annual basis, as described in Note 13 to the Fiscal Year 2009 audited financial statements attached hereto in APPENDIX A.

An actuarial valuation of the City's postemployment medical benefit program as of June 30, 2009 (the "2009 OPEB Valuation"), was performed by Buck Consultants for the purpose of determining the City's annual cost in accordance with GASB 45. The valuation, dated September 17, 2009, reflected a discount rate of 6.69% based on the City's actual and expected contributions to CERBT, inflation factors for increases in healthcare costs and premium costs, and a 30-year amortization period (open basis). According to the 2009 OPEB Valuation, using the assumptions described above and consistent with GASB 45, the UAAL for OPEB for all retirees, deferred retirement participants, vested terminated and active members was $1.32 billion and the ARC for OPEB will be $120.32 million for Fiscal Year 2011 (as reported in the actuarial valuation dated June 30, 2009).

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The following table sets forth the retiree health contributions included in the Water System's 2007 Rate Case projection for Fiscal Years 2008 through 2011 and the corresponding actual, budgeted or projected amounts, which have been lower than the projected amounts set forth in the 2007 Rate Case. Amounts budgeted for future years may be lower than amounts set forth in the 2007 Rate Case projection. The City expects that such amount will be sufficient to pay the Water System's proportionate share to fund the City's contribution to OPEB for such years. Projections set forth in the Water System's 2007 Rate Case include amounts through Fiscal Year 2011, years through which water rates were approved by the City Council.

TABLE 25

WATER SYSTEM
RETIREE HEALTH CONTRIBUTION
Fiscal Years 2008 through 2011
(In Millions)

Fiscal Year ending June 30	ARC	Total City Retiree Health Contribution [2]	Rate Case Projection	Actual/ Budgeted/Projected[1]
2008	$91.6	$53.6	$3.7	$3.9[2]
2009	104.5	49.5	5.7	3.7[2]
2010	113.4	57.1	6.0	4.3[3]
2011	120.3	57.8	6.0	4.3[4]

Source: The City of San Diego Comprehensive Annual Financial Report for the Fiscal Year ended June 30, 2008 and June 30, 2009; City of San Diego Financial Management Department and the Public Utilities Department.

(1) Consists of the Water Utility Fund's proportionate share of pay-as-you-go postemployment healthcare benefits and its proportionate share of contributions to CalPERS for OPEB. The Water Utility Fund's proportionate share of OPEB for Fiscal Year 2008 was 7.28% and for Fiscal Year 2009 was 7.47%. Proposed and projected amounts reflect an assumed Water Utility Fund proportionate share of 7.56% for Fiscal Year 2010 and 7.4% for Fiscal Year 2011. The Water Utility Fund's proportionate share may increase or decrease from year to year depending on a variety of factors, including the number of covered employees attributable to the Water Utility Fund and the retirement benefits accruing to such employees.
(2) Actual.
(3) Proposed Budget.
(4) Projected Public Utilities Department contribution based on the Water Utility Fund's proportionate share (see footnote (1) above) of the City's aggregate pay-as-you-go postemployment healthcare contributions and OPEB contributions through CalPERS, as set forth in the June 30, 2009 Annual Actuarial Valuation.

RISK FACTORS

Investment in the 2010A Bonds involves risks that may not be appropriate for certain investors. The following is a discussion of certain risk factors that should be considered, in addition to other matters set forth herein, in evaluating the 2010A Bonds for investment. The information set forth below does not purport to be an exhaustive listing of the risks and other considerations that may be relevant to an investment in the 2010A Bonds. In addition, the order in which the following information is presented is not intended to reflect the relative importance of any such risks.

Limited Obligations

The obligation of the City to pay the 2010A Installment Payments securing the 2010A Bonds is a limited obligation of the City and is not secured by a legal or equitable pledge or charge or lien upon any property of the City or any of its income or receipts, except the Net System Revenues. The obligation of the City to make the 2010A Installment Payments does not constitute an obligation of the City to levy or pledge any form of taxation or for which the City has levied or pledged any form of taxation. The City is obligated under the 2010A Supplement to make the 2010A Installment Payments solely from Net System Revenues.

No assurance can be made that Net System Revenues, estimated or otherwise, will be realized by the City in amounts sufficient to pay the 2010A Installment Payments. Among other matters, drought, general and local economic conditions, and changes in law and government regulations (including initiatives and moratoriums on growth) could adversely affect the amount of Net System Revenues realized by the City. In addition, the realization of future Net System Revenues is subject to, among other things, the capabilities of management of the City, the ability of the City to provide water to its customers, and the ability of the City to establish, maintain, and collect rates and charges sufficient to pay for Operation and Maintenance expenditures and the 2010A Installment Payments. See "WATER SYSTEM FINANCIAL OPERATIONS – Establishment of Water Service Charges."

Water System Expenses and Collections

The Operation and Maintenance expenditures related to the Water System are expected to increase in the next five years. See "WATER SYSTEM FINANCIAL OPERATIONS – Financial Projections and Modeling Assumptions." However, there can be no assurance that the City's projected future Maintenance and Operation costs of the Water System will actually be as projected by the Public Utilities Department and described in this Official Statement. In addition, demands on the Water System will increase due to population growth and regulatory requirements in the future. As described herein, the City is in the process of implementing the Long-Range Water Resources Plan and the attendant CIP to provide a framework for meeting future water requirements. Increases in expenses could require a significant increase in rates or charges in order to pay for CIP projects, including those anticipated under the City's Long-Range Water Resources Plan, and payment of the 2010A Installment Payments securing the 2010A Bonds. Also, any such rate increases could increase the likelihood of nonpayment by purchasers of water from the City and could also decrease demand from such purchasers. Further, although the City has covenanted to prescribe, revise, and collect rates and charges for Water Service in amounts necessary to pay the 2010A Installment Payments, there can be no assurance that such amounts will be collected in the amounts and at the times necessary to pay the 2010A Installment Payments sufficient to provide for the payment of the 2010A Bonds.

Water System Demand

There can be no assurance that the local demand for the services provided by the Water System will be maintained at levels described in this Official Statement. Because of changes in demographics within the boundaries of the City, it is possible for the demand for water services to decline over the term of the 2010A Bonds. A significant decline in demand might create a situation in which the City could not increase rates sufficiently to offset the decrease in subscribers or usage. This would reduce the City's ability to make the 2010A Installment Payments, which could in turn adversely impact the Authority's ability to make payments of the principal of or interest on the 2010A Bonds.

Rate-Setting Process Under Proposition 218

Proposition 218, which added Articles XIIIC and XIIID to the State Constitution, affects the City's ability to impose future rate increases and no assurance can be given that future rate increases will not encounter majority protest opposition or be challenged by initiative action authorized under Proposition 218. In the event that future proposed rate increases cannot be imposed as a result of majority protest or initiative, the City might thereafter be unable to generate Net System Revenues in the amounts required by the 2010A Supplement to pay the 2010A Installment Payments. See "CONSTITUTIONAL

LIMITATIONS ON TAXES AND WATER RATES AND CHARGES – Article XIIIC" and " – Article XIIID."

Notwithstanding the foregoing, the City has covenanted to fix, prescribe, and collect rates and charges for Water Service at a level at least sufficient to meet its debt requirements, as set forth under "SECURITY AND SOURCES OF PAYMENT FOR THE 2010A BONDS – Rate Covenant," and to use its best efforts to effect Water Service rate increases in compliance with Proposition 218. The current water rates approved by the City Council have been imposed in compliance with Proposition 218. See "CONSTITUTIONAL LIMITATIONS ON TAXES AND WATER RATES AND CHARGES – Article XIIIC" and " – Article XIIID."

Statutory and Regulatory Compliance

Laws and regulations governing treatment and delivery of water are enacted and promulgated by federal, state and local government agencies. Compliance with these laws and regulations is and will continue to be costly and, as more stringent standards are developed to ensure safe drinking water standards and the provision of water for other purposes, such costs will likely increase.

Claims against the Water System for failure to comply with applicable laws and regulations could be significant. Such claims are payable from assets of the Water System or from other legally available sources. In addition to claims by private parties, changes in the scope and standards for public agency water systems such as that operated by the Public Utilities Department may also lead to administrative orders issued by federal or State regulators. Future compliance with such orders can also impose substantial additional costs on the Water Utility Fund. No assurance can be given that the cost of compliance with such laws, regulations, and orders would not adversely affect the ability of the Water System to generate Net System Revenues sufficient to pay the 2010A Installment Payments. See "WATER SYSTEM REGULATORY REQUIREMENTS – Compliance Order by the California Department of Public Health."

Although the City has covenanted in the Master Installment Purchase Agreement to fix, prescribe, and collect rates and charges for the Water Service that will yield Net System Revenues for each Fiscal Year sufficient to pay debt service on the 2010A Bonds, no assurance can be given that the cost of compliance with such laws and regulations will not materially adversely affect the ability of the Water System to generate Net System Revenues sufficient to pay the 2010A Installment Payments.

Risks Relating to the Water Supply

Drought Risks. The ability of the Water System to operate effectively can be affected by the water supply available to the City, which is situated in an arid and semi-desert environment. If the water supply decreases significantly, whether by operation of mandatory supply restrictions, prohibitively high water costs or otherwise, Water System sales will diminish and Net System Revenues available to pay the 2010A Installment Payments may be adversely affected. While suppliers of water to the City, including CWA and MWD, have planned and managed reserve supplies to account for normal occurrences of drought conditions, decreased runoff from the Sierra Nevada snow pack, environmental issues in the Sacramento-San Joaquin Delta, and a severe drought in the Colorado River Basin are restricting the ability to transport water supplies to Southern California.

Due to drought conditions and court-ordered restrictions, on June 4, 2008, California Governor Arnold Schwarzenegger issued an Executive Order proclaiming a condition of statewide drought (the "Executive Order"). The Executive Order directs DWR to expedite existing conservation grant programs, facilitate water transfers, conduct a water conservation and outreach campaign in cooperation with local water agencies and organizations, and take additional drought response and water conservation actions. The Executive Order orders State and local agencies to identify public water systems at risk of health and safety impacts due to drought and water delivery limitations, and to mitigate these impacts. The Executive Order encourages local water agencies and districts to work cooperatively on actions to reduce water consumption locally and regionally.

Additionally, on February 27, 2009, Governor Arnold Schwarzenegger proclaimed a state of emergency (the "Proclamation") and ordered immediate action to manage the crisis. In the Proclamation, the Governor uses his authority to direct all State government agencies to utilize their resources, implement a State emergency plan and provide assistance for people, communities, and businesses impacted by the drought. Among other things, the Proclamation:

- requests that all urban water users immediately increase their water conservation activities in an effort to reduce their individual water use by 20%; and

- directs State agencies to immediately implement a water use reduction plan and take immediate water conservation actions and requests that federal and local agencies also implement water use reduction plans for facilities within their control.

The Proclamation states that, if the emergency conditions have not been sufficiently mitigated by March 30, 2009, the Governor will consider additional steps. DWR's report on drought conditions issued on March 30, 2009, pursuant to the Proclamation, concluded that increased spring precipitation did not improve the State's overall water supply situation enough to make up for two previous dry years and low reservoir conditions. The report listed DWR's anticipated actions to address the drought, which include expediting distribution of State bond funds for water management projects; planning, proposing legislation and providing public education for Statewide water conservation; finalizing plumbing standards for use of recycled water inside buildings; and preparing a contingency plan in case of drought continuing in calendar year 2010. Subsequent to the Governor's Proclamation, DWR increased the forecasted State Water Project Table "A" Allocations, from 15% to 20% on March 18, 2009, from 20% to 30% on April 15, 2009, and from 30% to 40% on May 20, 2009. DWR and the California Department of Food and Agriculture have also been directed to recommend measures to reduce the economic impacts of the drought, including but not limited to water transfers, through-Delta emergency transfers, water conservation measures, efficient irrigation practices, and improvements to the California Irrigation Management Information System.

MWD, which supplies water to the City through CWA, is currently supplementing supplies from the Colorado River and the SWP by drawing on its stored water supplies to meet near-term demands and anticipates additional actions to stretch reserve supplies. The City has taken into account the effect of the current drought on operations in the Public Utilities Department's Fiscal Year 2010 budget by assuming in its operating budget for Fiscal Year 2010 a 15% reduction in water sales and deliveries. This is expected to result in reduced revenues that are expected to be offset by reductions in its operating budget, which includes reductions to water purchase quantities. As described under the caption "WATER SUPPLY – Drought Related Developments," the City has also taken various actions to address the drought conditions, including declaring a Level 2 Drought Alert Condition, which imposes mandatory conservation practices on all Public Utilities Department customers. Such actions may also result in reduced revenues. In addition, the City has initiated the IPR Project to determine the feasibility of using highly treated reclaimed water to augment the City's drinking water supply. However, the City cannot currently predict the results or the impact of the IPR Project.

Earthquakes, Wildfires, and Other Natural Disasters. Although the City has not experienced any significant damage from seismic activities, the geographic area in which the City is located is subject to unpredictable seismic activity. Southern California is characterized by a number of geotechnical conditions that represent potential safety hazards, including expansive soils and areas of potential liquefaction and landslide. Earthquakes or other natural disasters could interrupt operation of the Water

System and thereby interrupt the ability of the City to realize Net System Revenues sufficient to pay the 2010A Installment Payments securing the payment of the 2010A Bonds. The San Andreas, Rose Canyon, Elsinore, and San Jacinto fault zones are all capable of producing earthquakes in the San Diego area. In anticipation of such potential disasters, the City designs and constructs all facilities of the Water System to the seismic codes in effect at the time of design of the project. The Water System has not experienced any significant losses of facilities or services as a result of earthquakes.

Water conveyance facilities generally consist of pipelines and connections, flow control facilities, and pumping stations, which are not typically vulnerable to damage by wildfires. The above ground facilities within the Water System are designed to be tolerant to damage by wildfires through the use of fire resistant material where possible, such as concrete and masonry blocks. In addition, the Public Utilities Department works closely with the City's fire department to ensure that proper vegetative clearances are maintained in and around the properties and facilities of the Water System. The Public Utilities Department watches for wildfires that may threaten the facilities of the Water System and operations and maintenance crews are dispatched to ensure that all above-ground facilities remain safe and operational. Further, during fires, the Public Utilities Department works closely with the City's fire department and law enforcement officers to monitor and protect facilities of the Water System to ensure continuous operation. The Water System did not sustain damage from the October 2007 wildfires in the County.

As described under the caption "WATER SYSTEM SERVICE AREA AND FACILITIES – Existing Water System Facilities – Raw Water Reservoirs," the City is also cooperating with CWA on the Emergency Storage Project, pursuant to which a system of reservoirs, interconnected pipelines and pumping stations is being created to improve the availability of water to the San Diego region in the event of an interruption in imported water deliveries. Currently, the pipelines that carry imported water for CWA, a portion of which is purchased by the Public Utilities Department, extend for hundreds of miles and cross several major fault lines en route to the County. A severe earthquake, drought or other significant disaster could cut off the County's imported water supply for up to six months. As part of the Emergency Storage Project, CWA is increasing the height and storage of San Vicente Reservoir and connecting Lake Hodges to the imported water system, which will increase the amount of water locally available in an emergency.

Although the City has implemented disaster preparedness plans and made improvements to Water System facilities in connection with such natural disasters, there can be no assurance that these or any additional measures will be adequate in the event that a natural disaster occurs, nor that costs of preparedness measures will be as currently anticipated. Further, damage to components of the Water System could cause a material increase in costs for repairs or a corresponding material adverse impact on Net System Revenues. **The City is not obligated under the Master Installment Purchase Agreement to procure and maintain, or cause to be procured and maintained, nor does the City plan to procure and maintain, earthquake insurance on the Water System.**

Environmental Considerations. Quagga (dreissena rostriformis bugensis) and Zebra (dreissena polymorpha) mussels are small freshwater bivalve mollusks native to Ukraine. Within the United States and in other areas of the world, they are considered an invasive species with significant adverse impact on the ecosystem. Presence of the invasive Quagga mussel has been verified in water bodies supplied by the lower Colorado River, beginning in January 2007. The first identification of mussel presence in the San Diego region occurred in August 2007. It is suspected that Quagga mussels were transported into the Colorado River basin by recreational vessels traveling from infested waters from the eastern United States. Once introduced into the Colorado River basin, the Quagga mussels have been transported through the imported water supply into the City's reservoirs. To date, the City has found Quagga mussels in San Vicente, El Capitan, Otay, Murray, Miramar, and Hodges Reservoirs. Quagga mussels pose a significant risk to the aquatic life and ecosystem within reservoirs and to the operation and maintenance of the Water System. At this time, the ultimate impact is unknown; however, it has the potential to generate significant capital and annual operational and maintenance costs.

Security of the Water System. Military conflicts and terrorist activities may adversely impact the operations and finances of the Water System. The Public Utilities Department continually plans and prepares for emergency situations and immediately responds to ensure the quality and service of water is maintained. The Public Utilities Department prepares for emergencies such as earthquake, fire, power failure, or possible water contamination in a variety of ways, including: extensively monitoring the entire water treatment and distribution system on a routine basis throughout the year, in part by taking thousands of water samples; routinely training staff on critical security and safety; conducting disaster drills to improve coordination efforts throughout the region; collaborating with the DPH, law enforcement and fire-rescue agencies in order to improve multiple agency response to water emergencies; implementing a water quality notification plan to keep customers informed in emergency situations; and implementing additional security measures at all water treatment plants, reservoirs, and other local and remote water facilities. However, there can be no assurance that any existing or additional safety and security measures will prove adequate in the event that terrorist activities are directed against the Water System or that costs of security measures will not be greater than presently anticipated. Further, damage to certain components of the Water System could require the City to increase expenditures for repairs to the Water System significantly enough to adversely impact the City's ability to pay debt service on the 2010A Bonds. The Public Utilities Department's CIP has made use of and is continuing to use Homeland Security grants to enhance security of various facilities throughout the Water System. In addition, the City has established the Operating Reserve, which is currently funded at a minimum 45 days of operating costs (to be gradually increased to 70 days of operating costs in Fiscal Years 2010 to 2011), which may be used under certain circumstances for repairs to the Water System. See "WATER SYSTEM FINANCIAL OPERATIONS – Rate Stabilization Fund; Other Funds and Accounts."

Suppliers of water to the City have also taken actions to increase the security of water from the Colorado River Aqueduct and the SWP. MWD has reported that it has increased ground and air patrols of the Colorado River Aqueduct. In addition, MWD has increased the frequency of monitoring and testing at all treatment plants in addition to various sites along the Colorado River Aqueduct. Although MWD has constructed redundant systems and other safeguards, no assurance can be given that existing or additional safety and security measures will prove adequate in the event that terrorist activities are directed against the Water System to prevent a disruption of MWD's ability to deliver water to its member agencies, including CWA, from which the Public Utilities Department purchases a substantial portion of its water supplies, through the Colorado River Aqueduct or the SWP, or that costs of security measures will not be greater than presently anticipated, which could adversely impact the City's ability to pay the 2010A Installment Payments.

Utility Costs. Power outages may cause difficulties in receiving an adequate water supply and thus increase the cost of water. No assurance can be given that any future significant reduction or loss of power would not materially adversely affect the operations of the Water System. Also, the Public Utilities Department cannot guarantee that prices for electricity or gas will not increase, which could adversely affect the Water System's financial condition, although the rate increases previously approved by the City for Fiscal Years 2008 through 2011 allow for 8% inflation in gas and electric costs. The Public Utilities Department also cannot guarantee that additional increases in water rates charged by CWA, the City's wholesale provider, or other charges imposed by CWA or MWD will not be proposed. Such increases in water rates and such other charges as well as increases in electricity and gas costs are eligible to be "passed through" to the City's water customers as increased water rates in accordance with the City's Municipal Code. Such "pass-through" rate increases are subject to Proposition 218 notice requirements. See "CONSTITUTIONAL LIMITATIONS ON TAXES AND WATER RATES AND CHARGES – Article XIIIC" and " – Article XIIID."

Impact of Current Fiscal Crisis on Water System Revenues

The United States financial market is presently experiencing continued volatility precipitated by major economic disruptions, which occurred in 2008 and much of 2009. While indications are that the severe economic recession ended in the second half of 2009 and the United States economy has returned to economic growth in the fourth quarter of 2009, credit and liquidity problems continue. The City cannot predict the extent of the fiscal problems that will be encountered in this or in any future Fiscal Years, and it is not clear what measures will be taken by the State or federal government to address the current fiscal crisis. Accordingly, the City cannot predict the final outcome of future State or federal actions or the impact that such actions will have on the Water System's finances and operations.

The Public Utilities Department's current water rate model reflects an assumed 15% reduction in water sales for Fiscal Year 2010. In general, the resulting revenue reduction is offset by reductions in water purchases and other budget reductions that also carry forward into future years. See "WATER SYSTEM FINANCIAL OPERATIONS – Operation and Maintenance Expenditures." The Public Utilities Department also prepared a projection that included an assumed 15% reduction in water sales from Fiscal Year 2010 through Fiscal Year 2014, which projection continued to reflect the generation of Net System Revenues in amounts sufficient to pay the Installment Payments. In addition, pursuant to the Master Installment Purchase Agreement, the City is obligated to fix, prescribe, and collect rates and charges for the Water Service that will be at least sufficient to yield the greater of (1) Net System Revenues sufficient to pay during each Fiscal Year all Obligations, including the Installment Payments, payable in such Fiscal Year or (2) Adjusted Net System Revenues during each Fiscal Year equal to 120% of the Adjusted Debt Service for such Fiscal Year. The Master Installment Purchase Agreement also prohibits the City from reducing the rates and charges then in effect, unless the Net System Revenues from such reduced rates and charges will at all times be sufficient to meet the requirements of the Installment Purchase Agreement. Further, the Indenture provides that upon the occurrence and continuance of any Event of Default thereunder, including nonpayment of principal of or interest on the 2010A Bonds, the holders of the 2010A Bonds may proceed to enforce their beneficial rights by mandamus, or other suit, action or proceeding at law or in equity, which includes an action for specific performance by the City with respect to its rate covenant and any other agreement contained in the Installment Purchase Agreement. See also "RISK FACTORS – Rate-Setting Process Under Proposition 218" and "CONSTITUTIONAL LIMITATIONS ON TAXES AND WATER RATES AND CHARGES – Article XIIIC" and " – Article XIIID" for a description of limitations on the rate-setting process under the State Constitution.

However, the City cannot predict the extent to which the current or any future financial crisis, alone or together with the drought conditions described under the caption "RISK FACTORS – Risks Relating to the Water Supply – Drought Risks," will impact its ability to generate Net System Revenues in the amounts required by the Installment Purchase Agreement to pay Installment Payments. In particular, the City cannot predict the extent to which an economic recession and credit crisis will affect future water demands, the impact of any reduced demand on the Water System's finances and operations or whether a sustained fiscal crisis would create sufficient pressure on the City Council to effect a reduction in water fees.

Acceleration; Limitations on Remedies

The Indenture provides that, upon and during the continuance of an Event of Default thereunder, the Trustee may, subject to certain conditions, declare the principal of all 2010A Bonds then Outstanding and the interest accrued thereon to be due and payable immediately. The foregoing notwithstanding, the remedy of acceleration is subject to the limitations on legal remedies against public entities in the State, including a limitation on enforcement obligations against funds needed to serve the public welfare and interest. Also, any remedies available to the Owners of the 2010A Bonds upon the occurrence of an

Event of Default under the Indenture are in many respects dependent upon judicial actions, which are often subject to discretion and delay and could prove both expensive and time consuming to obtain.

Further, enforceability of the rights and remedies of the Owners of the 2010A Bonds, and the obligations incurred by the City, may become subject to the federal bankruptcy code and applicable bankruptcy, insolvency, reorganization, moratorium, or similar laws relating to or affecting the enforcement of creditor's rights generally, now or hereafter in effect, equity principles that may limit the specific enforcement under State law of certain remedies, the exercise by the United States of America of the powers delegated to it by the Constitution, the reasonable and necessary exercise, in certain exceptional situations, of the police powers inherent in the sovereignty of the State and its governmental bodies in the interest of serving a significant and legitimate public purpose, and the limitations on remedies against counties in the State. Bankruptcy proceedings, or the exercise of powers by the federal or State government, if initiated, could subject the Owners of the 2010A Bonds to judicial discretion and interpretation of their rights in bankruptcy or otherwise and consequently may entail risks of delay, limitation, or modification of their rights.

Absence of Market for the Bonds

There can be no assurance that there will ever be a secondary market for purchase or sale of the 2010A Bonds and from time to time there may be no market for such 2010A Bonds, depending upon prevailing market conditions and the financial condition or market position of firms who may make the secondary market.

Loss of Tax Exemption on 2010A Bonds

As discussed under the caption "TAX MATTERS," interest on the 2010A Bonds could become included in gross income for purposes of federal income taxation, retroactive to the date the 2010A Bonds were issued, as a result of future acts or omissions of the City or the Authority in violation of their respective covenants in the Indenture and the Installment Purchase Agreement.

Economic, Political, Social, and Environmental Conditions

Prospective investors are encouraged to evaluate current and prospective economic, political, social, and environmental conditions as part of an informed investment decision. Changes in economic, political, social, or environmental conditions on a local, state, federal, and/or international level may adversely affect investment risk generally. Such conditional changes may include (but are not limited to) fluctuations in business production, consumer prices, or financial markets, unemployment rates, technological advancements, shortages or surpluses in natural resources or energy supplies, changes in law, social unrest, fluctuations in the crime rate, political conflict, acts of war or terrorism, environmental damage, and natural disasters.

CONSTITUTIONAL LIMITATIONS ON TAXES AND WATER RATES AND CHARGES

Article XIIIA

Article XIIIA of the State Constitution provides that the maximum ad valorem tax on real property cannot exceed 1% of the "full cash value," which is defined as "the county assessor's valuation of real property as shown on the 1975-76 tax bill under 'full cash value' or, thereafter, the appraised value of real property when purchased, newly constructed, or a change in ownership has occurred after the 1975 assessment," subject to exceptions for certain circumstances of transfer or reconstruction and except with respect to certain voter approved debt. The "full cash value" is subject to annual adjustment to reflect increases, not to exceed 2% per year, or decreases in the consumer price index or comparable local data, or to reflect reduction in property value caused by damage, destruction or other factors.

Article XIIIA requires a vote of two-thirds of the qualified electorate to impose special taxes, while generally precluding the imposition of any additional ad valorem, sales or transaction tax on real property. As amended, Article XIIIA exempts from the 1% tax limitation any taxes above that level required to pay debt service on certain voter-approved general obligation bonds for the acquisition or improvement of real property. In addition, Article XIIIA requires the approval of two-thirds of all members of the State Legislature to change any State laws resulting in increased tax revenues.

Under California law, any fee that exceeds the reasonable cost of providing the service for which the fee is charged is a "special tax," which under Article XIIIA must be authorized by a two-thirds vote of the electorate. Under Article XIIID, fees and charges for water, sewer, and refuse collection services are subject to majority protest, but are not subject to the two-third vote requirement of Article XIIIA. The reasonable cost of providing water services has been determined by the State Controller to include depreciation and allowance for the cost of capital improvements. In addition, the California courts have determined to date that fees such as capacity fees will not be special taxes if they approximate the reasonable cost of constructing the water or wastewater capital improvements contemplated by the local agency imposing the fee. See "WATER SYSTEM FINANCIAL OPERATIONS – Revenues."

Article XIIIB

Article XIIIB of the California Constitution limits the annual appropriations of proceeds of taxes by State and local government entities to the amount of appropriations of the entity for the prior fiscal year, as adjusted for changes in the cost of living, changes in population, and changes in services rendered by the entity. User fees and charges are considered proceeds of taxes only to the extent they exceed the reasonable costs incurred by a governmental entity in supplying the goods and services for which such fees and charges are imposed.

To the extent that assessments, fees, and charges collected by the City are used to pay the costs of maintaining and operating the Water System and payments due on the 2010A Bonds (including the funding of the Reserve Fund), the City believes as of the date hereof that such moneys should not be subject to the annual appropriations limit of Article XIIIB.

Article XIIIC

On November 5, 1996, the voters of the State approved Proposition 218, a constitutional initiative, entitled the "Right to Vote on Taxes Act" ("Proposition 218"). Proposition 218 added Articles XIIIC and XIIID to the California Constitution and contained a number of interrelated provisions affecting the ability of local governments, including the City, to levy and collect both existing and future taxes, assessments, fees, and charges.

Section 1 of Article XIIIC requires majority voter approval for the imposition, extension, or increase of general taxes and Section 2 thereof requires two-thirds voter approval for the imposition, extension, or increase of special taxes. These voter approval requirements of Article XIIIC reduce the flexibility of the City to raise revenues by the levy of general or special taxes and, given such voter approval requirements, no assurance can be given that the City will be able to enact, impose, extend, or increase any such taxes in the future to meet increased expenditure requirements. The City has not enacted, imposed, extended, or increased any tax since the effective date of Proposition 218.

Section 3 of Article XIIIC expressly extends the initiative power to give voters the power to reduce or repeal local taxes, assessments, fees, and charges, regardless of the date such taxes, assessments, fees, or charges were imposed. Section 3 expands the initiative power to include reducing or repealing assessments, fees, and charges, which had previously been considered administrative rather than legislative matters and therefore beyond the initiative power. This extension of the initiative power is not limited by the terms of Article XIIIC to fees imposed after November 6, 1996, the effective date of Proposition 218, and absent other legal authority could result in the reduction in any existing taxes, assessments, or fees and charges imposed prior to November 6, 1996.

"Fees" and "charges" are not expressly defined in Article XIIIC or in SB 919, the Proposition 218 Omnibus Implementation Act enacted in 1997 to prescribe specific procedures and parameters for local jurisdictions in complying with Article XIIIC and Article XIIID ("SB 919"). Such terms are, however, defined in Article XIIID, discussed below. On July 24, 2006, the California Supreme Court ruled in *Bighorn-Desert View Water Agency v. Virjil (Kelley)* (the "*Bighorn Decision*") that charges for ongoing water delivery are property-related fees and charges within the meaning of Article XIIID and are also fees or charges within the meaning of Section 3 of Article XIIIC. The California Supreme Court held that such water service charges may, therefore, be reduced or repealed through a local voter initiative pursuant to Section 3 of Article XIIIC.

In the *Bighorn Decision*, the Supreme Court did state that nothing in Section 3 of Article XIIIC authorizes initiative measures that impose voter-approval requirements for future increases in fees or charges for water delivery. The Supreme Court stated that water providers may determine rates and charges upon proper action of the governing body and that the governing body may increase a charge that was not affected by a prior initiative or impose an entirely new charge.

The Supreme Court further stated in the *Bighorn Decision* that it was not holding that the initiative power is free of all limitations and was not determining whether the initiative power is subject to the statutory provision requiring that water and wastewater service charges be set at a level that will pay debt service on bonded debt and operating expenses. Such initiative power could be subject to the limitations imposed on the impairment of contracts under the contract clause of the United States Constitution. Additionally, SB 919 provides that the initiative power provided for in Proposition 218 "shall not be construed to mean that any owner or beneficial owner of a municipal security, purchased before or after November 5, 1996 (the date of adoption of Proposition 218), assumes the risk of, or in any way consents to, any action by initiative measure that constitutes an impairment of contractual rights" protected by the United States Constitution. No assurance can be given that the voters of the City will not, in the future, approve initiatives that repeal, reduce or prohibit the future imposition or increase of assessments, fees or charges, including the City's Water Service fees and charges, which are the source of Net System Revenues pledged to the payment of debt service on the 2010A Bonds and other Outstanding Obligations.

Notwithstanding the fact that Water Service charges may be subject to reduction or repeal by voter initiative undertaken pursuant to Section 3 of Article XIIIC, the City has covenanted to levy and charge rates that meet the requirements of the Master Installment Purchase Agreement in accordance with applicable law.

Article XIIID

Article XIIID defines a "fee" or "charge" as any levy other than an *ad valorem tax*, special tax, or assessment, imposed upon a parcel or upon a person as an incident of property ownership, including a user fee or charge for a property-related service. A "property-related service" is defined as "a public service having a direct relationship to a property ownership." As discussed above, in the *Bighorn Decision*, the California Supreme Court held that a public water agency's charges for ongoing water delivery are fees and charges within the meaning of Article XIIID. Article XIIID requires that any agency imposing or increasing any property-related fee or charge must provide written notice thereof to the record owner of each identified parcel upon which such fee or charge is to be imposed and must conduct a public hearing with respect thereto. The proposed fee or charge may not be imposed or increased if a majority of owners of the identified parcels file written protests against it. As a result, the local government's ability to increase such fee or charge may be limited by a majority protest.

The City's Water Service charges have two components, a base fee based on meter size and a commodity charge based on the volume of water consumed. The City has ratified prior increases in its water rates and charges, and believes it has complied with the applicable and material notice and protest procedures of Article XIIID for its current water rates and charges. As of the date of this Official Statement, there has not been and there is no pending litigation challenging any of the City's water fees and charges approved since the effective date of Proposition 218. While the City Attorney currently believes, based upon the judicial precedent in place during the period of these prior rate increases, that a reviewing court could reasonably uphold the validity of those increases, neither the City nor the City Attorney can provide any assurances as to the outcome of a challenge to the prior increases in the City's water rates and charges that were not approved in accordance with the notice and hearing requirements of Article XIIID if one were brought.

In addition, Article XIIID also includes a number of limitations applicable to existing, new, or increased fees and charges, including provisions to the effect that (i) revenues derived from the fee or charge shall not exceed the funds required to provide the property-related service; (ii) such revenues shall not be used for any purpose other than that for which the fee or charge was imposed; (iii) the amount of a fee or charge imposed upon any parcel or person as an incident of property ownership shall not exceed the proportional cost of the service attributable to the parcel; and (iv) no such fee or charge may be imposed for a service unless that service is actually used by, or immediately available to, the owner of the property in question. Property-related fees or charges based on potential or future use of a service are not permitted.

Article XIIID establishes procedural requirements for the imposition of assessments, which are defined as any charge upon real property for a special benefit conferred upon the real property. Standby charges are classified as assessments. Procedural requirements for assessments under Article XIIID include conducting a public hearing and mailed protest procedure, with notice to the record owner of each parcel subject to the assessment. The assessment may not be imposed if a majority of the ballots returned oppose the assessment, with each ballot weighted according to the proportional financial obligation of the affected parcel. To provide guidance to City staff regarding the conduct of Proposition 218 "property-related fee" protest proceedings, the City Council adopted Resolution R-2007-655 in January 2007 establishing additional procedures for submitting protests against proposed increases to water rates, including the provision of notice of a proposed change in water fees to all owners of record on each identified parcel and all water customers of the City as reflected in the billing records of the City at the time the notice is given, and additional procedures for the tabulation of protests against proposed increases to water rates, including guidelines for determining when a valid protest has been submitted.

The City and the City Attorney believe that as of the date of this Official Statement that current water fees and charges that are subject to Proposition 218 materially comply with the provisions thereof. Should it become necessary to increase the water fees and charges above current levels, the City would be required to comply with the requirements of Article XIIID in connection with such proposed increase. To date, there have been no legal challenges to water rate increases implemented by the City pursuant to Proposition 218 or otherwise. As of the date of this Official Statement and under existing standards as of such date, the City and the City Attorney believe that rates and charges may be established at levels that are expected to permit deposits to a Rate Stabilization Fund or maintenance of uncommitted cash reserves. See "WATER SYSTEM FINANCIAL OPERATIONS – Financial Projections and Modeling Assumptions."

The City and the City Attorney believe that current water capacity fees are not subject to Proposition 218. Furthermore, as of the date of this Official Statement, the City and the City Attorney are unaware of any legal challenges to this position.

The interpretation and application of Proposition 218 will ultimately be determined by the courts or through implementing legislation with respect to a number of the matters described above, and it is not possible at this time to predict with certainty the outcome of such determination or the nature or scope of any such legislation.

TAX MATTERS

Bond Counsel Opinion

In the opinion of Goodwin Procter LLP, Los Angeles, California, Bond Counsel to the Authority, based upon an analysis of existing laws, regulations, rulings, and judicial decisions and assuming, among other matters, the accuracy of certain representations and compliance with certain covenants and requirements, interest on the 2010A Bonds is excluded from gross income for United States federal income tax purposes under Section 103 of the Internal Revenue Code of 1986, as amended (the "Code"), and is exempt from State of California personal income taxes. Bond Counsel is further of the opinion that interest on the 2010A Bonds is not a specific preference item for purposes of the United States federal individual or corporate alternative minimum taxes. Bond Counsel observes, however, that such interest is included in adjusted current earnings in calculating federal corporate alternative minimum taxable income. A copy of the proposed form of opinion of Bond Counsel with respect to the 2010A Bonds is set forth in APPENDIX C attached hereto and will accompany the 2010A Bonds.

The Code imposes various restrictions, conditions, and requirements relating to the exclusion from gross income for United States federal income tax purposes of interest received by persons such as the owners of the 2010A Bonds. The Authority has made certain representations and covenanted to comply with certain restrictions, conditions, and requirements designed to ensure that interest on the 2010A Bonds will not be included in gross income for United States federal income tax purposes. Inaccuracy of these representations or failure to comply with those covenants may result in interest on the 2010A Bonds being included in gross income for United States federal income tax purposes, possibly from the date of issuance of the 2010A Bonds. The opinion of Bond Counsel assumes the accuracy of those representations and compliance with those covenants. Bond Counsel has not undertaken to determine (or to inform any person) whether any actions taken (or not taken) or events occurring (or not occurring) after the date of issuance of the 2010A Bonds may adversely affect the tax status of interest on the 2010A Bonds.

Bond Counsel has not undertaken to advise in the future whether any events after the date of issuance of the 2010A Bonds may affect the United States federal or State tax status of interest on the 2010A Bonds or the tax consequences of ownership of the 2010A Bonds. No assurance can be given that future legislation, including amendments to the Code or interpretations thereof, if enacted into law, will not contain provisions that could directly or indirectly reduce the benefit of the excludability of the interest on the 2010A Bonds from gross income for United States federal income tax purposes.

Although Bond Counsel has rendered an opinion that interest on the 2010A Bonds is excluded from gross income for United States federal and State personal income tax purposes, a U.S. holder's United States federal and State tax liability may otherwise be affected by the ownership or disposition of the 2010A Bonds. The nature and extent of such other tax consequences will depend upon the U.S. holder's particular circumstances, including other items of income or deduction. Bond Counsel has expressed no opinion regarding any such other tax consequences. Accordingly, before purchasing any of the 2010A Bonds, all potential purchasers should consult their tax advisors concerning collateral tax consequences with respect to the 2010A Bonds.

Risk of Audit by Internal Revenue Service

The Internal Revenue Service (the "IRS") has an ongoing program of auditing tax-exempt obligations to determine whether, in the view of the IRS, interest on such tax-exempt obligations is includable in the gross income of the owners thereof for United States federal income tax purposes. No assurances can be given as to whether or not the IRS will commence an audit of the 2010A Bonds. If an audit is commenced, under current procedures the IRS is likely to treat the Authority as the taxpayer and the owners of the 2010A Bonds may have no right to participate in such procedure.

Bond Counsel's opinion represents its legal judgment based upon its review of existing law, regulations, rulings, judicial decisions, and other authorities, and upon the covenants and representations of the parties and such other facts as it has deemed relevant to render such opinion, and is not a guarantee of a result. Bond Counsel is not obligated to defend the tax-exempt status of the 2010A Bonds. Neither the Authority nor Bond Counsel is responsible to pay or reimburse the costs of any owner with respect to any audit or litigation relating to the 2010A Bonds.

Original Issue Discount and Premium

If the 2010A Bonds' "stated redemption price at maturity" (generally the sum of all payments required under the 2010A Bonds other than payments of stated interest payable at least annually over the term of such 2010A Bonds) exceeds their issue price by more than a de minimis amount, the difference constitutes "original issue discount" or "OID" the accrual of which, to the extent properly allocable to each owner thereof, is treated as interest on the 2010A Bonds that is excluded from gross income for United States federal income tax purposes. OID with respect to any maturity of the 2010A Bonds accrues daily over the term to maturity of such 2010A Bonds on the basis of a constant interest rate compounded semiannually (with straight-line interpolations between compounding dates). Any accruing OID is added to the adjusted basis of such 2010A Bonds to determine taxable gain or loss upon disposition (including sale, redemption, or payment on maturity) of such 2010A Bonds. U.S. holders of the 2010A Bonds should consult their own tax advisors with respect to the tax consequences of ownership of 2010A Bonds with original issue discount.

In general, if the 2010A Bonds are issued for an amount greater than the stated principal amount of the 2010A Bonds, the 2010A Bonds will be considered to have "amortizable bond premium." No deduction is allowable for the amortizable bond premium in the case of bonds, like the 2010A Bonds, the interest on which is excluded from gross income for United States federal income tax purposes. However, the amount of tax-exempt interest received, and a U.S. holder's basis in a 2010A Bond issued with acquisition premium, would be reduced by the amount of amortizable bond premium properly allocable to such U.S. holder. U.S. holders of 2010A Bonds should consult their own tax advisors with respect to the proper treatment of amortizable bond premium in their particular circumstances.

Information Reporting and Backup Withholding

Information reporting requirements apply to interest on tax-exempt obligations, including the 2010A Bonds. In general, such requirements are satisfied if the interest recipient completes, and provides the payor, with a Form W-9 "Request for Taxpayer Identification Number and Certification," or unless the recipient is one of a limited class of exempt recipients, including corporations. A recipient not otherwise exempt from information reporting who fails to satisfy the information reporting requirements will be subject to "backup withholding," which means that the payor is required to deduct and withhold a tax from the interest payment, calculated in the manner set forth in the Code. For the foregoing purpose, a "payor" generally refers to the person or entity from whom a recipient receives its payments of interest or who collects such payments on behalf of the recipient.

If an owner purchasing a 2010A Bond through a brokerage account has executed a Form W-9 in connection with the establishment of such account, as generally can be expected, no backup withholding should occur. In any event, backup withholding does not affect excludability of the interest on the 2010A Bonds from gross income for Federal income tax purposes. Any amounts withheld pursuant to backup withholding would be allowed as a refund or a credit against the owner's Federal income tax once the required information is furnished to the IRS.

CONTINUING DISCLOSURE

Pursuant to the Continuing Disclosure Certificate of the City (the "Disclosure Certificate"), the City has agreed to provide, or cause to be provided, to the Municipal Securities Rulemaking Board in the manner prescribed by the SEC certain annual financial information and operating data concerning the City. The annual report to be filed by the City is to be filed not later than 270 days following the end of the City's Fiscal Year (currently June 30), commencing with the Annual Report for Fiscal Year 2010, and is to include audited financial statements of the City. See "APPENDIX D – FORM OF CONTINUING DISCLOSURE CERTIFICATE."

Beginning in March 2004, the City failed to comply with undertakings related to 21 bond issues for each of Fiscal Years 2003 through 2007 due to the unavailability of the City's audited financial statements. The circumstances regarding the unavailability of the City's audited financial statements are described under the caption entitled "INTRODUCTION –2006 SEC Order and Related Matters." Each required annual report and audited financial statement was subsequently filed. Prior to March 2004, the City had never failed to comply with its undertakings with regard to Rule 15c2-12.

The City has timely filed the annual reports and financial statements for Fiscal Year 2008 with respect to securities secured by the Water Utility Fund, the Sewer Utility Fund, and the City's General Fund. The City Council received and filed the City's CAFR for Fiscal Year 2009 on February 1, 2010, and corresponding continuing disclosure filings have been prepared and filed in a timely manner.

The City's covenants in the Continuing Disclosure Certificate have been made in order to assist the Underwriters in complying with the Rule. A failure by the City to comply with any of the covenants therein is not an event of default under the Indenture.

LITIGATION

As of the date of this Official Statement, there is no litigation pending against the City or the Authority or, to the knowledge of its respective executive officers, threatened, seeking to restrain or enjoin the issuance, sale, execution, or delivery of the 2010A Bonds or in any way contesting or affecting the validity of the 2010A Bonds or the authorizations or any proceedings of the City or the Authority taken with respect to the issuance or sale thereof, or the pledge or application of any moneys or security provided for the payment of the 2010A Bonds or the use of the proceeds of the 2010A Bonds.

There are no pending lawsuits that, in the opinion of the City Attorney, challenge the validity of the 2010A Bonds, the corporate existence of the City or the Authority, or the title of the executive officers thereof to their respective offices. In connection with this review, attention has been given to not only litigation pending against the City, but also litigation pending against the City's Public Utilities Department. The Office of the City Attorney has prepared the following summary, as of the date of this Official Statement, of certain claims and lawsuits for which the estimated loss to the City as of such date exceeds $1 million ("Material Litigation") pending against the Water Utility Fund for construction claims and certain other alleged liabilities arising during the ordinary course of operations of the Water System:

Colony Hills Homeowners Association, Akeson v. City of San Diego. On March 4, 2008, the Colony Hills Homeowners Association (the "HOA") and 40 property owners within the HOA filed a lawsuit against the City claiming that on August 8, 2006, a water main broke and caused flooding along a private street in La Jolla belonging to the HOA, resulting in approximately $180.8 million in alleged damages, including damage from soil subsidence, hillside failure, road failure and diminished property value. The City's experts opined that the breaks in the City's water mains did not cause the subsidence; rather, that the subsidence caused the breaks in the City's water mains. The City filed a Cross Complaint against the HOA and several homeowners.

Following mediation, the City, the HOA, all Plaintiffs, and the Whalen Family Trust (an uphill property owner), negotiated a proposed global settlement that went before the City Council in Closed Session for approval on February 2, 2010. The settlement was approved in Closed Session on that date. The proposed settlement requires the City to construct a re-routed water main. The cost of this project is currently estimated to be approximately $1.2 to $1.4 million. A portion of this cost will be paid using $700,000 in settlement monies the City has received from Cross-Defendants in the case. The total cost to the City under the settlement is expected to be approximately $515,000 to $715,000, inclusive of out of pocket expenses, and will be paid from the Water Utility Fund.

Crabbe, et al. v. City of San Diego (also known as the Mount Soledad Landslide Litigation). 113 property owners, owning 64 separate single family residences filed a lawsuit against the City claiming a landslide which occurred in the 5700 block of Soledad Mountain Road on October 3, 2007, resulted in substantial damages to the property owners' homes, as well as diminished property value and emotional distress. The property owners claim the cause of the landslide was the failure of City infrastructure. In the event of an adverse ruling, the possible liability facing the City was estimated to be in the range of $0 to $38 million. Trial of phase one, addressing solely the causation of the landslide, began on August 17, 2009, and concluded on September 17, 2009. The Court issued its ruling on October 1, 2009 in favor of the City. This ruling rendered the remaining issues in the case moot. Thereafter, the City entered into a global settlement agreement with all plaintiffs to resolve the litigation.

In order to reach a final settlement of the litigation, the City agreed to pay $173,584 plus up to an additional $75,000 to demolish one of the damaged homes. The City incurred in excess of $3 million in attorneys' fees with Butz, Dunn & DeSantis. In addition to attorneys' fees, the City incurred in excess of $3 million in expert fees and costs. The City is attempting to recoup these costs through its insurance carriers, which initially issued coverage and defense denials.

The summaries and estimated losses to the City of the Material Litigation set forth above are based on the City's reasonable estimates as of the date of this Official Statement, based on information available at such time, are subject to change without notice and the City disclaims any responsibility to update any information provided below for any matters relating to these claims and lawsuits or any new claims or lawsuits that may be brought to the attention of the City after the date hereof.

The City believes, as of the date of this Official Statement and subject to the assumptions and limitations in the paragraph above, that it has sufficient defenses against such claims and lawsuits and that the aggregate amount of the uninsured liabilities of the City that may result from adverse rulings, judgments or settlements in any or all of such pending Material Litigation should not have a material adverse effect on the Water Utility Fund's financial position.

ADDITIONAL INFORMATION

On June 8, 2010, a San Diego County civil grand jury released a report on the City's fiscal condition which made a number of recommendations, including that the Mayor and City Council convene a panel of experts to evaluate the legal and financial ramifications of the City declaring bankruptcy. The City is not considering bankruptcy and neither the Mayor nor the City Attorney believes a bankruptcy filing is appropriate. The City is required to respond to the grand jury recommendations by September 6, 2010. The City has no obligation to implement any grand jury recommendation.

CERTAIN LEGAL MATTERS

Goodwin Procter LLP, Los Angeles, California, Bond Counsel, will render an opinion with respect to the 2010A Bonds in substantially the forms set forth in APPENDIX C hereto. Copies of such opinion will be furnished to the Underwriters at the time of delivery of the Bonds. Certain legal matters will be passed upon for the Authority and the Corporation by Goodwin Procter LLP, for the City and the Authority by Jan I. Goldsmith, City Attorney, and for the Underwriters by their counsel, Nixon Peabody LLP, Los Angeles, California.

RATINGS

Fitch, Moody's, and S&P have assigned the 2010A Bonds their ratings of "AA," "Aa2," and "AA–," respectively, to the 2010A Bonds. Such ratings reflect only the views of such organizations and any desired explanation of the significance of such ratings should be obtained from the rating agency furnishing the same, at the following addresses: Standard & Poor's Ratings Services, 55 Water Street, New York, New York 10041; Fitch Ratings, One State Street Plaza, New York, New York 10004; Moody's Investors Service, Inc., 7 World Trade Center, 250 Greenwich Street, New York, New York 10007. Generally, a rating agency bases its rating on the information and materials furnished to it and on investigations, studies and assumptions of its own.

There is no assurance such ratings will continue for any given period of time or that such ratings will not be revised downward or withdrawn entirely by the rating agencies, if in the judgment of such rating agencies, circumstances so warrant. Any such downward revision or withdrawal of such ratings may have an adverse effect on the market price of the 2010A Bonds. The City undertakes no obligation to oppose any downward revision, suspension or withdrawal.

UNDERWRITING

The 2010A Bonds are being purchased by the Underwriters named on the cover page to this Official Statement (collectively, the "Underwriters"). Morgan Stanley is serving as the representative of the Underwriters. The Underwriters have agreed, subject to certain conditions, to purchase the 2010A Bonds at a purchase price of $130,771,035.61 (equal to the original principal amount thereof, plus an original issue premium of $8,309,754.65, less an underwriters' discount of $613,719.04). The Underwriters may offer and sell the 2010A Bonds to certain dealers and others at prices lower than the offering prices. The offering prices may be changed from time to time by the Underwriters.

Morgan Stanley, parent company of Morgan Stanley & Co. Incorporated, one of the underwriters of the 2010 Bonds, has entered into a retail brokerage joint venture with Citigroup Inc. As part of the joint venture, Morgan Stanley & Co. Incorporated will distribute municipal securities to retail investors through the financial advisor network of a new broker-dealer, Morgan Stanley Smith Barney LLC. This distribution arrangement became effective on June 1, 2009. As part of this arrangement, Morgan Stanley

& Co. Incorporated will compensate Morgan Stanley Smith Barney LLC for its selling efforts with respect to the 2010 Bonds.

PROFESSIONAL ADVISORS

Montague DeRose and Associates, LLC, Westlake Village, California served as Financial Advisor to the City with respect to the sale of the 2010A Bonds. The Financial Advisor has not undertaken to make an independent verification or to assume responsibility for the accuracy, completeness, or fairness of the information contained in this Official Statement.

FINANCIAL STATEMENTS

The City's basic financial statements contained in the City's CAFRs include the financial statements of the Water Utility Fund. The City's Fiscal Year 2009 basic financial statements have been audited by Macias Gini & O'Connell LLP (the "Independent Auditor"), independent certified public accountants, as stated in their report.

Those portions of the City's basic financial statements contained in the CAFR for Fiscal Year 2009 relating to the Water Utility Fund, including all of the City's basic financial statements for Fiscal Year 2009 audited by the Independent Auditor, are included in APPENDIX A. APPENDIX A also includes the unaudited management's discussion and analysis, unaudited required supplementary information with respect to the City's Pension System and CERBT, and General Fund budgetary information. Certain of the data and information set forth in APPENDIX A do not pertain to the Water Utility Fund but have been included in APPENDIX A for purposes of context. The unaudited letter of transmittal from the Mayor and unaudited statistical information regarding debt service coverage on Parity Obligations and aggregate debt service on all Obligations are also included in APPENDIX A. The City's CAFRs are available in their entirety on the City's website at http://www.sandiego.gov. However, the information presented there is not part of this Official Statement, is not incorporated by reference herein and should not be relied upon in making an investment decision with respect to the 2010A Bonds. The City's General Fund does not secure payment of debt service on the 2010A Bonds.

The Independent Auditor did not review this Official Statement and the City did not request the consent of the Independent Auditor to append the City's financial statements to this Official Statement. Accordingly, the Independent Auditor did not perform any procedures relating to any of the information in this Official Statement.

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MISCELLANEOUS

This Official Statement has been duly approved, executed and delivered by the Authority and the City.

There are appended to this Official Statement a summary of certain provisions of the principal and legal documents, portions of the City's CAFR for Fiscal Year 2009, including financial statements of the Water Utility Fund, the proposed form of opinion of Bond Counsel, and a general description of the City and a description of the Book-Entry Only System. The Appendices are integral parts of this Official Statement and must be read together with all other parts of this Official Statement.

This Official Statement is not to be construed as a contract or agreement between the Authority or the City and the purchasers or holders of any of the 2010A Bonds. Any statements made in this Official Statement involving matters of opinion, whether or not expressly so stated, are intended merely as an opinion and not as representations of fact. The information and expressions of opinion herein are subject to change without notice and neither the delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the financial condition, results of operations, or any other affairs of the City, the Authority, or the Corporation since the date hereof.

PUBLIC FACILITIES FINANCING AUTHORITY OF THE CITY OF SAN DIEGO

By: /s/ Joseph W. Craver
Chairperson, Board of Commissioners

THE CITY OF SAN DIEGO

By: /s/ Mary Lewis
Chief Financial Officer

APPENDIX A

BASIC FINANCIAL STATEMENTS, REQUIRED SUPPLEMENTARY INFORMATION AND CERTAIN EXCERPTS FROM THE COMPREHENSIVE ANNUAL FINANCIAL REPORT OF THE CITY OF SAN DIEGO FOR THE FISCAL YEAR ENDED JUNE 30, 2009

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INTRODUCTORY SECTION

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THE CITY OF SAN DIEGO

December 21, 2009

Citizens and Interested Parties,

The San Diego economy has been severely impacted by the ongoing recession and recent economic data is mixed regarding the timing of any potential recovery. Federal stimulus funds contributed to positive GDP growth nationally in the third quarter of calendar year 2009 and local leading economic indicators have increased in each of the past six months showing some economic stabilization. However, State and local unemployment rates are at twenty-five year highs and property foreclosures continue to adversely affect home values. Lower consumer spending has significantly reduced economic activity in the City, resulting in decreased government revenues. Continued revenue reductions will affect the ability of the City to provide services to its citizens.

The City's fiscal challenges have been exacerbated by the State's ongoing budget crisis. The State legislature suspended the requirements of Proposition 1A (2004) in an effort to balance the State's FY 2010 budget. Proposition 1A is intended to prevent local revenues from being taken by the State; however, Proposition 1A can be suspended with the declaration of a fiscal emergency by the Governor and a vote of two-thirds of the Legislature. In fiscal year 2010, the State will borrow approximately $1.9 billion in property tax revenue from local jurisdictions to help balance the State budget; the City's share of this is approximately $35.8 million. However, the City will recover this property tax revenue during fiscal year 2010 through a securitization program established by the California Statewide Communities Development Authority. The State also passed Assembly Bill (AB) 26 4x, which requires redevelopment agencies statewide to pay a total of $2.05 billion of their property tax revenues to the State over the next two years. The impact to the City's Redevelopment Agency (RDA) will be approximately $56 million in fiscal year 2010 and $11 million in fiscal year 2011. The State continues to struggle to balance its budget resulting in ongoing uncertainty with respect to the City's expected revenues.

Economic Development Activities

The City addressed the economic downturn in fiscal year 2009 by increasing community investment, promoting business growth and retention, and by competing successfully for federal stimulus funds. The City division of Economic Growth Services (EGS) worked to create and retain jobs and taxable investment in the City of San Diego. EGS consists of two focused work units: the Business Expansion, Attraction, and Retention Team and the Government Incentives Team. These two teams work directly with businesses, business organizations, and City departments to create a business-friendly environment that promotes a stable economy. Economic growth, energy independence, revenue enhancement, and community revitalization are accomplished by attracting new companies, retaining and/or expanding existing companies, making San Diego competitive in emerging markets, and revitalizing older business communities.

Due to the economic downturn, Economic Growth Services has placed a strong emphasis on its business retention mission. In fiscal year 2009 EGS developed and executed successful business retention efforts for Sony Electronics, Cricket Corporation, Circle Foods, Lockheed Martin, Eli Lilly, and CamelBak. These efforts resulted in the creation or retention of approximately 2,900 San Diego based jobs. In the current fiscal year, EGS worked with Alliant Techsystems, Inc to retain or create 200 San Diego based jobs. The capital investments made by the companies EGS assisted in fiscal year 2009 and fiscal year 2010 represent a cumulative investment of more than $368 million of construction and renovation activity for our local economy.

The "Certificate of Deposit Account Registry Service" (CDARS) is a deposit-placement service designed to allow FDIC-insured depository institutions to accept deposits of more than $100,000 (currently $250,000) and obtain full coverage for the depositor by spreading the funds among as many separate FDIC insured institutions as necessary so that no institution holds more than $250,000 (principal plus interest) for each depositor. To support local reinvestment, the City increased its CDARS investment from $5 million to $15 million in fiscal year 2009. The City plans to increase the allowable investment in the CDARS program to approximately $40 million in fiscal year 2010. The authorized CDARS investment program allows the City to invest millions of dollars into fully insured FDIC non-negotiable certificates of deposit. The initial deposit is split among small community banks throughout the country so that any single Certificate of Deposit at a financial institution does not exceed the $250,000 FDIC insurance limit. The banks participating in the CDARS network send an equal amount of funds back to local San Diego banks to ensure that they retain funds equal to the City's initial deposit for reinvestment in the local community. The City's investment in the CDARS program assures that the full amount deposited at local banks stays in San Diego for reinvestment in the community.

According to the stimulus tracking website Recovery.org, California received more American Recovery and Reinvestment Act (ARRA) dollars than any other state and the San Diego region received the second largest total of stimulus dollars of any region in California (trailing Los Angeles). As of November 19, 2009, the San Diego region received 201 projects totaling over $2.1 billion. The City of San Diego can expect to see at least $340 million in stimulus funding. Of this amount, approximately $290 million is for Federal projects and will not come directly through the City; the remaining $50 million is expected to come to the City over the next six months. Projects including the modernization of Otay Mesa's Port of Entry and the San Ysidro border expansion project will alleviate congestion and improve the productivity and efficiency of US/Mexico border relations. This money will come either directly to the City in the form of block grants and competitive awards ($49 million) or to our partner agencies in which the City participates, such as the San Diego Association of Governments and the San Diego Workforce Partnership ($126 million), or to federal agencies pursuing major construction projects within the City of San Diego ($164 million not including military projects). These ARRA funds will be used on transportation, housing, public safety and energy projects that will not only create jobs but will provide long term benefits for the City and the region.

Fiscal Challenges

The City of San Diego has faced significant financial challenges over the last several years and has made a determined effort to improve its overall financial condition and the quality of its financial statements, internal controls, and disclosure controls and procedures. A few of the City's achievements include (1) the release of audited financial statements for fiscal years 2003-2008 in a two year period; (2) the implementation of an annual five-year financial outlook as a prudent planning tool; (3) the strengthening of the City's General Fund reserves; (4) fully funding the Annual Required Contribution (ARC) to the City's pension system since fiscal year 2006; (5) new pension plans for police and for non-public safety employees hired on or after July 1, 2009; (6) participation in a California Public Employees' Retirement System (CALPERs) trust for pre-funding of post-employment healthcare benefits for retired City employees; (7) rating upgrades from the national rating agencies, including, in the case of one agency, the reinstatement of the City's credit rating; and (8) re-entering the public bond market in 2009 and issuing $1.6 billion in debt (new money and refunding) after a five year absence.

The City issued the Fiscal Year 2010 First Quarter Budget Monitoring Report on November 17, 2009, which presented a review of actual expenditures and receipts through September 2009 and projects annual expenditures and revenues for the General Fund through year end. Based on this analysis, the City expects a shortfall of approximately $7.5 million in fiscal year 2010, primarily as a result of declining sales tax and Transient Occupancy Tax (TOT) revenues. The decline in major revenues is partially offset by conservative spending and a hiring freeze that has been in effect since August 2009.

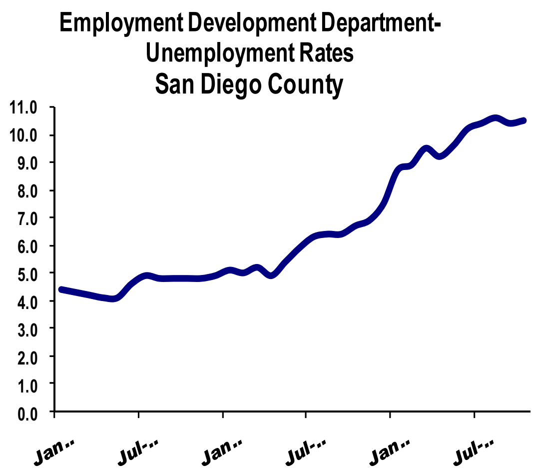
The Five Year Financial Outlook (Outlook) issued on October 1, 2009, identified a projected deficit for fiscal year 2011 of $179 million. The sensitivity analysis in the Outlook estimates a deficit range of $168 to $200 million, primarily resulting from the possible fluctuation of three major revenues: property tax; sales tax; and TOT. On November 24, the Mayor presented a proposed 18 month budget for the remainder of fiscal year 2010 and fiscal year 2011 to remediate the projected fiscal year 2011 deficit of $179 million. On December 14, 2009 the City Council adopted the fiscal year 2010 budget revisions and the fiscal year 2011 proposed budget. The fiscal year 2011 budget framework approved by the City Council includes a combination of transfers, new revenue, and annual expenditure reductions that will impact services to City residents. Further action, including labor negotiations and additional City Council approval, will be necessary to implement all recommended adjustments. If the budget is implemented on January 1, 2010 as recommended, savings of approximately $24 million in fiscal year 2010 will be set aside to assist in balancing the fiscal year 2011 budget.

The City publicly issued a $125 million Tax and Revenue Anticipation Notes (TRAN) on July 1, 2009 and does not currently foresee the need to issue additional notes to meet any General Fund liquidity needs for the remainder of fiscal year 2010. The City treasury holds approximately $2 billion that is invested primarily in US Treasuries and agencies, and consistent with the City's investment policy, has sufficient liquidity to meet all currently foreseeable cash demands. The General Fund reserves are approximately $79 million as of the issuance of this report, which includes $55 million set aside in an Emergency Reserve Fund that can be accessed by a two-thirds vote of City Council.

Readers of these financial statements should pay particular attention to Notes 12, 13, 18, and 22, concerning Pension Plans, Other Post Employment Benefits, Contingencies, and Subsequent Events, respectively. The notes, along with the other financial and operational data included in the City's CAFR, must be read in their entirety to obtain a complete understanding of the City's financial position as of June 30, 2009.

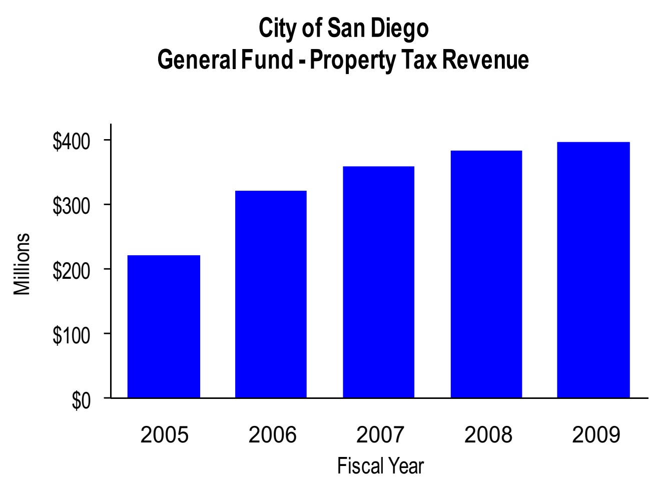
Our Underlying Fundamentals

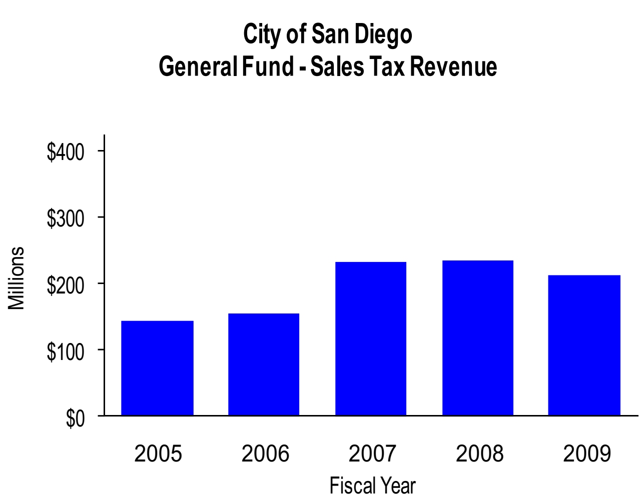
The City has a diversified economy, with the principal employers being government, high-tech industries, particularly biotech and telecommunications, and the tourism industry. The City's economic base is also anchored by higher education and major scientific research institutions, including the University of California, San Diego, San Diego State University, Scripps Research Institute, the Salk Institute for Biological Studies, and the San Diego Supercomputer Center.



Like all regions around the country, San Diego County's economy has been impacted by the economic recession. In the past three years unemployment has more than doubled, rising from an average in 2006 of 4.0% to 10.5% as of October 2009. The recession has slowed both residential and commercial development within our region. This combined with a contraction in business payrolls and reduced travel spending has driven the unemployment rate to historic levels.

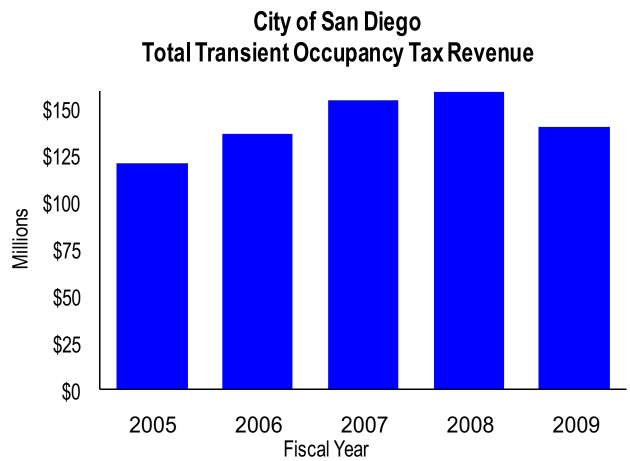
The City's property tax revenue has grown over the last five years, although at a decreasing rate. In fiscal year 2009 General Fund property tax revenues were $398.7 million compared to $384.3 million in fiscal year 2008, representing a 3.8% growth. However, due to the continued decline in home prices, the budgeted fiscal year 2010 property tax revenue in the General Fund was projected to decline 4.0% over fiscal year 2009 actuals. Subsequently, based on updated information from the County, the City revised its estimate for property tax revenue for fiscal year 2010 showing a smaller decrease of 1.5% over the fiscal year 2009 actual property tax revenue.





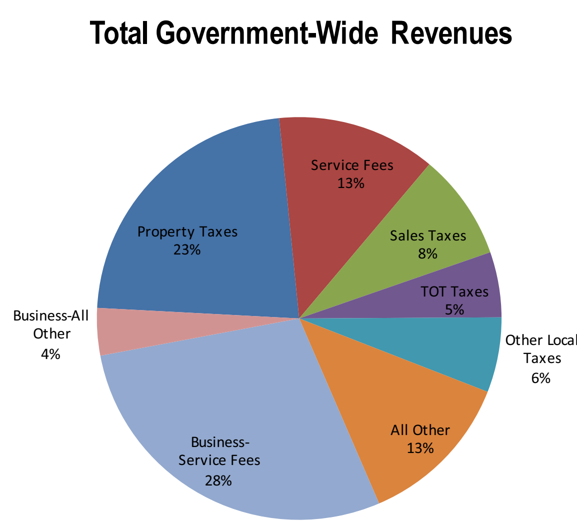
The impact of lower business and consumer spending has had a significant effect on sales tax revenues. In fiscal year 2009, actual General Fund sales tax revenues (including safety sales tax) were $212.9 million, a 9.6% decline from 2008 sales tax revenues of $235.6 million. For fiscal year 2010, the City budgeted a decline of 1.3% in sales tax revenues. However, the first quarter actual sales tax receipts were significantly below the budgeted amount. The City's adjusted projection for fiscal year 2010 is now $191.2 million, or 10.2% lower than actual revenue received for fiscal year 2009.

San Diego remains a top tourist destination due to the region's natural attractions; however, the tourism industry has not escaped the impact of the deteriorating economy. The City's Transient Occupancy Tax (TOT) rate is currently 10.5% and is allocated according to the Municipal Code. As such, the General Fund receives 52% of these revenues to be used for general governmental purposes, and the TOT fund receives the remaining 48% for the purpose of promoting the City as a tourism destination. The General Fund portion of TOT represents approximately 7% of the revenue from the fiscal year 2010 General Fund Adopted Budget. In fiscal year 2009, San Diego experienced an 11.7% decrease in TOT revenue from fiscal year 2008. For fiscal year 2010, the City budgeted an increase of 2.9% in TOT tax over 2009 actuals. Based on receipts from the first three months of fiscal year 2010, the City adjusted its estimate for TOT tax receipts to $127.6 million which reflects a 9.3% decline from fiscal year 2009 actuals.

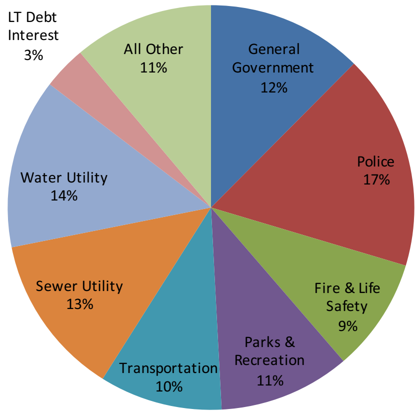


Financial Health

The City's total government-wide revenues, which are generated through a combination of governmental and business-type activities, have remained approximately the same over the prior three years, improving by 1%. While property tax revenues and business-type charges for services revenue for water and wastewater services have grown during this period, sales tax and TOT have declined. For fiscal year 2010, property tax revenue is projected to decline by 1.5%. Other major revenue sources are also trending flat to declining as well. Total government-wide revenues for fiscal year 2009 were $2.7 billion; governmental activities were $1.8 billion and business-type activities were $.9 billion, and are illustrated in the chart to the right.



Total Government-Wide Expenses



Over the last three years, the City's total government-wide expenses have increased approximately 4%. These expenses supported all public services and the significant fiscal obligations of the City, including funding of the City's pension system, post-employment healthcare benefits, and capital improvements. Total expenses for fiscal year 2009 were $2.5 billion. Governmental activities were $1.7 billion, of which 38% was spent on public safety for police, fire, and life safety services. Business-type activities were $.8 billion, of which 85% of these expenses were for water and wastewater expenses.

Pension Funding Progress ***(Thousands)***

Actuarial Valuation Date	Actuarial Value of Assets	UAAL	Funded Ratio
6/30/2005	$ 2,983,080	$ 1,452,937	67.3%
6/30/2006	3,981,932	1,000,768	79.9%
6/30/2007	4,413,411	1,184,242	78.8%
6/30/2008	4,660,346	1,303,204	78.2%

The City's unfunded pension liability remains a significant obligation of the City. The City has aggressively confronted this deficit, fully funding the City's Annual Required Contribution (ARC) beginning in fiscal year 2006, and has made significant additional payments in excess of the ARC into the pension fund in certain years. The San Diego City Employees' Retirement System (SDCERS) is the administrator of the City's employee pension funds. On an annual basis, the pension fund portfolio and future pension obligations are evaluated by an independent actuary to determine the full pension liability. The June 30, 2008 valuation calculated the unfunded pension liability to be approximately $1.303 billion. The June 30, 2009 actuarial report is not complete as of the issuance of this report.

In fiscal year 2009, the global financial markets experienced significant declines. The effects of the market declines have been wide ranging and impact even the most diversified investment portfolios. The SDCERS investment portfolio is no exception. SDCERS employs a long-term investment strategy. The City's ARC is determined using an asset smoothing methodology which dampens the volatility of the market value of assets which occurs from fluctuations in market conditions. The ARC payment for fiscal year 2011 has not been determined by the SDCERS actuary as of the issuance of this report; however, it has been estimated by the SDCERS actuary, presented to the Board on July 17, 2009 and September 18, 2009, to be approximately $224 million. This is an increase of $70 million, or 45%, over the ARC payment of $154 million the City is obligated to fund in fiscal year 2010. Any significant increase in the fiscal year 2011 ARC payment will require the City to reduce operating expenses which will affect services and programs.

Retiree Healthcare Liabilities ***(Thousands)***

Actuarial Valuation Date	Actuarial Value of Assets	UAAL	Funded Ratio
6/30/2008	$ 29,637	$ 1,206,070	2.4%
6/30/2009	41,497	1,317,880	3.1%

In fiscal year 2008, Governmental Accounting Standards Board Statement 45 ("GASB 45") went into effect requiring all municipal governments to report on Other Post Employment Benefits (retiree healthcare costs) in a manner similar to reporting on pension benefits. The City's actuarial valuation for retiree healthcare costs estimated an unfunded actuarial accrued liability (UAAL) of $1.318 billion as of June 30, 2009. The City is participating in a trust administered by CalPERS to fund this long-term liability and, to date, has contributed $54 million to the CalPERS trust. The fair value of these assets as of June 30, 2009 was $41.5 million. The City is not currently fully funding the ARC for retiree healthcare, which is $120.3 million for fiscal year 2011. The amount budgeted for fiscal year 2010 is $57.1 million, of which $32.1 million will fund the pay-go portion and $25 million is expected to be transferred to the CalPERS trust by fiscal year end.

Governmental Funds (Tax Supported Operations)

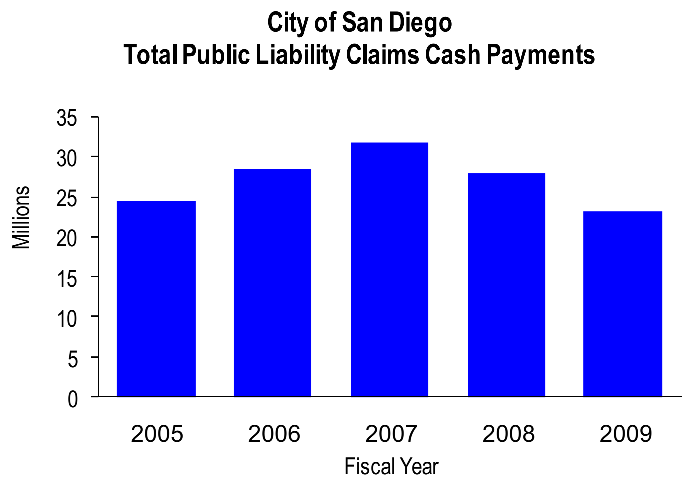
The City's General Fund finished fiscal year 2009 with unrestricted cash and investments of approximately $87 million. As a fiscal precaution against natural disasters or unforeseen events, the City maintains an emergency reserve fund that can only be accessed for qualifying emergencies as declared by the Mayor and/or City Council and approved by at least a 2/3 vote of the City Council. The General Fund Reserve Policy set a funding goal of 7.0% of General Fund revenue by the end of fiscal year 2009. The General Fund reserve was actually 7.7% of General Fund revenue at June 30, 2009, resulting in a total reserve balance of $78.3 million. This balance is reported within the General Fund Balance Sheet as Undesignated Fund Balance. The reserves are currently cash funded within the City Treasury's pooled cash portfolio. The goal is to establish General Fund reserves at 8% of revenues by fiscal year 2012.

The Fiscal year 2010 Budget adopted in June 2009 reflected a reduction of expense growth by reducing program expenditures and imposing an across the board 6% reduction in compensation for all City employees. The City also was successful in redesigning the pension benefit package for most employees hired after July 1, 2009. Due to a projected decline in the City's major revenues, management addressed the City's projected budgetary imbalance by proposing, and City Council then adopting, a Fiscal year 2010 Budget that reduced spending on current services while also attempting to mitigate service level reductions. Council adopted a Fiscal year 2010 Budget in June 2009 that balanced estimated revenues to expenditures.

During fiscal year 2009, total long-term liabilities of the City's governmental activities increased by $198 million. This was primarily the result of the capital improvement 2009A lease revenue bond issue for $103 million for various capital improvement projects and an increase to the Net Other-Postemployment Benefits Obligation of $45 million. Overall, our annual interest costs for governmental activities were approximately $84 million in fiscal year 2009, which represents approximately 5% of our total governmental activities expenses.

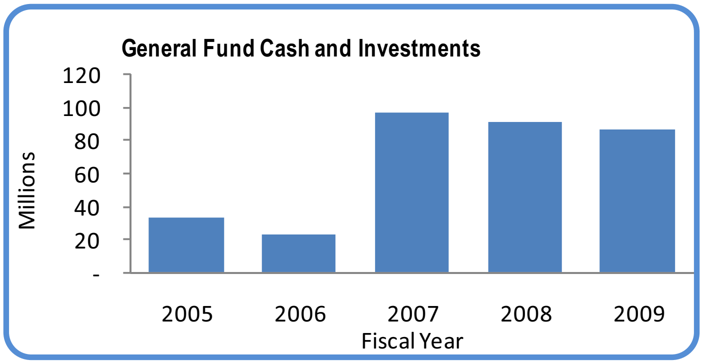
The City's capital assets are essential to providing services to its residents and maintaining the quality of its environment. During fiscal year 2009, total capital assets for governmental activities increased by $120 million. This was funded by a combination of developer contributions, grant monies, and city-funded capital improvement programs.

The City's capital improvement backlog is estimated to be approximately $800 to $900 million according to the most recent Five Year Financial Outlook. This amount is the most recent estimate and includes the cost of needed repairs to City facilities, streets and storm drains but does not include alleys, sidewalks or soft costs. The City is in the process of assessing and updating its cost estimate for its capital improvement backlog. These costs have been deferred because the City has not had the necessary funding resources. As mentioned above, the City issued $103 million in bonds to fund deferred projects during fiscal year 2009. The bond proceeds will be used to fund deferred capital improvement projects within the City.



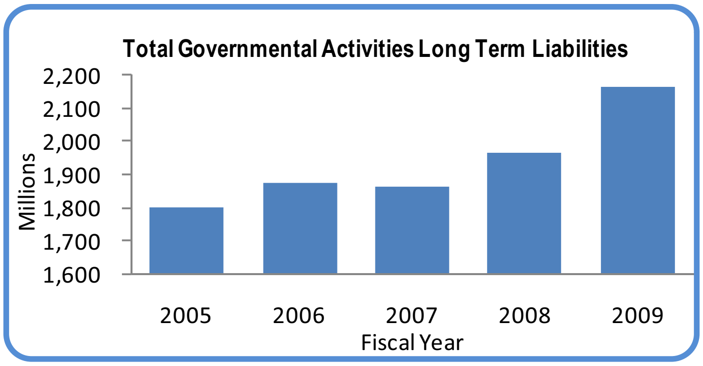
The City's Public Liability Fund, which accounts for governmental fund-related claims, has a deficit of approximately $49 million as of June 30, 2009. This deficit includes an accrued liability for actuarially calculated claims costs, incurred but not reported claims, and allocated and unallocated losses of approximately $59 million, offset with the cash reserves collected in the fund. This fund has seen significantly higher claims since fiscal year 2005, largely as a result of the legal claims and investigations stemming from the pension fund underpayment and related financial disclosure issues; however, most of these unusual costs were paid through fiscal year 2007 and fiscal year 2008. The Workers' Compensation Fund, which accounts for both governmental and business-type claims, has a deficit of $114 million as of June 30, 2009. This deficit includes an accrued liability for actuarially calculated liabilities for open and unreported claims, as well as a provision for the allocated loss adjustment expense totaling approximately $148 million, offset with the cash reserves collected in the fund. The total liability for workers compensation has declined since fiscal year 2007 due to a downward trend in the number of claims and the effect of State legislation regarding workers compensation reform enacted in 2004. Per the City Reserve Policy, the City has budgeted funds annually to establish cash reserves to reach the goal of 50% of the estimated outstanding liabilities in each fund. While the City is committed to funding reserves in the Worker's Compensation and Public Liability funds, and has included funding for these reserves in the fiscal year 2010 budget, the goal of funding 50% of outstanding liabilities in both funds by 2014 is being reassessed given the economic downturn and continued decline in General Fund revenues.

Governmental Activities Key Indicators



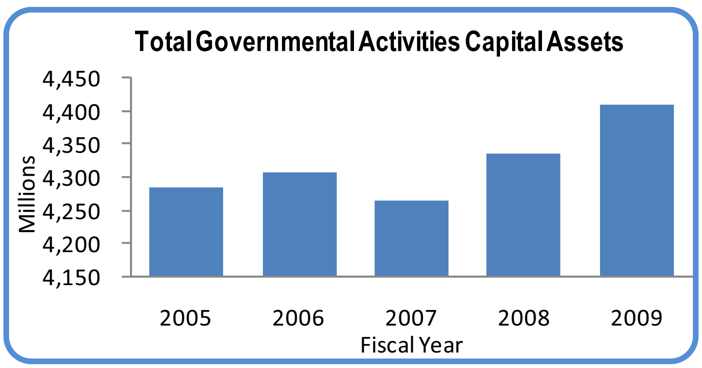
General Fund Cash

Continued expenditure savings due to vacancies and management imposed reductions in discretionary spending have helped the City to maintain a relatively stable cash position.



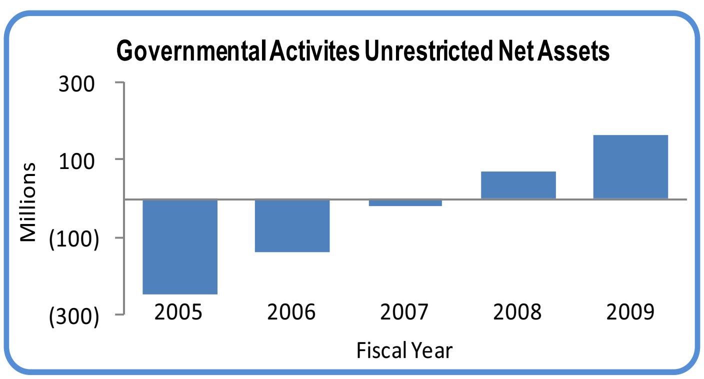
Total Long Term Liabilities

The City issued $103 million in Lease Revenue Bonds to finance various public improvements during FY 2009. The City's obligation related to Other Post-employment Benefits also increased $45 million in FY 2009, together creating an increase in total long term liabilities of approximately 10.1%.



Capital Assets

Capital Assets increased by approximately $120 million during FY 2009. This included capital expenditures related to the City's new ERP system, seismic retrofitting of the City's bridge infrastructure, and infrastructure and improvements to repair street damage resulting from the Mt. Soledad landslide.



Unrestricted Net Assets

Unrestricted Net Assets increased approximately $92 million in FY 2009. This was primarily the result of Redevelopment Agency revenues exceeding expenses to fund multi-year capital improvements.

Business-Type Activities

The majority of the City's business-type activities are related to utilities that provide water and wastewater services. The Water and Metropolitan Wastewater Departments have been consolidated into a single Public Utilities Department and continue to serve several regional agencies outside of the City's boundaries. The utilities operations are mainly supported by fees charged to customers. The Independent Rate Oversight Committee (an independent committee of stakeholders) monitors utility rates and expenditures on behalf of the ratepayers.

The City's Water Utility Fund issued $485 million of Water Revenue and Revenue Refunding Bonds, Series 2009A and 2009B during fiscal year 2009 to prepay outstanding principal of $207 million of Subordinated Water Revenue Notes, Series 2007A and 2008B; refund $94 million of Certificates of Undivided Interest, Series 1998 monies; and to finance capital improvements on the water system. The publicly offered Water 2009A and 2009B Revenue Refunding Bonds are secured by and payable solely from net system revenues of the Water Utility Fund. The City's Wastewater Utility Fund issued $1.089 billion of Senior Sewer Revenue Bonds to finance capital improvements to the wastewater system; fully refund $224 million in wastewater revenue notes; and to refund approximately $683 million in wastewater revenue bonds. The net change in these notes and bonds payable during fiscal year 2009 is the primary reason the business-type long term liabilities increased $344 million over fiscal year 2008.

For the year ended June 30, 2009, the City's business-type activities closed with restricted and unrestricted cash and investment balances totaling $1.2 billion, an increase over fiscal year 2008 of approximately $319 million as a result of the debt issues discussed above.

While the City's capital assets for business-type activities have continued to increase in value, deferred maintenance remains an ongoing challenge. The City maintains a network of over 3,000 miles of water pipes and over 3,000 miles of sewer and waste water lines.

Compliance with environmental regulations generally requires infrastructure construction, including the replacement of water distribution systems, treatment plant upgrades, the replacement of wastewater collection systems, and improving sewage treatment capacity. The City has agreed with various state and federal regulators to build significant infrastructure upgrades. In June 2009, the City received tentative approval of a third five-year waiver permit from the Environmental Protection Agency (EPA) and the state Regional Water Quality Control Board to continue operating the Point Loma Wastewater Treatment Plant at advanced primary treatment level. The City is still working with the California Coastal Commission to receive final wording on a consistency determination in support of this EPA decision. The resolution is anticipated in early 2010.

The City is also facing challenges to the future of its water supplies. A persistent regional drought and judicial decisions regarding management of the State Water Project has put significant pressure on San Diego's regional water supplies. The City of San Diego imports as much as 90% of its water supply. The reliability of that supply has been reduced because of court decisions, weather conditions, the diminishing availability of stored water, and dwindling supplies of new water. The City continues to work with its water wholesalers (the San Diego County Water Authority and the Metropolitan Water District of Southern California) to address these supply issues but currently operates under a mandatory water conservation target to achieve an 8% reduction in overall use. The City's performance from June through September has averaged a monthly reduction of over 12%. The availability of water has legal implications and could potentially affect City Council findings regarding state mandated water supply assessments for future development. These assessments must demonstrate the long-term availability of water for large projects before those projects can be approved by local jurisdictions. At this time, it is unclear what effect limitations to water supplies would have on the City's economy and its revenues as the most recent project assessments have all been able to find potable water offsets through the increased use of reclaimed water. The Mayor also proposed and the City Council approved in October 2009 a revised Landscape Ordinance in advance of the state's requirement to do so by January 2010. The City is also moving forward with the California Department of Public Health to undertake a demonstration project intended to verify that highly treated municipal wastewater can be placed in a drinking water reservoir.

Best Practice Operating Improvements

The City took a major leap forward on July 1, 2009 when it went live with its new SAP Enterprise Resource Planning (ERP) financial system. After two years of planning, the City successfully began the transition to an integrated financial system which allowed us to eliminate over a dozen legacy software applications. Throughout fiscal year 2010, core functionality modules will be implemented, eliminating even more costly legacy software applications and hardware. The addition of the ERP system and a well trained workforce are expected to significantly improve the City's financial operations and reporting capabilities.

Internal controls over financial operations and reporting continue to be a focus issue for the City. As part of the ERP system, the City has invested in an integrated internal controls module called Governance, Risk and Compliance (GRC). GRC, coupled with new process and procedure documents, are expected to improve our internal control environment. In addition, the City has established a comprehensive plan and has the proper staffing in place to complete the remediation of weaknesses in internal controls over financial reporting within 14 months.

The Five Year Financial Outlook

In October 2009, the City released an updated Five-Year Financial Outlook (the Outlook) for fiscal years 2011 through 2015. This document is an examination of the City's long range fiscal condition and financial challenges. The City updates the Outlook periodically to account for changed circumstances.

The City's General Fund was the primary focus of the 2011-2015 Outlook. Approximately 68% of the City's major revenues consist of four revenue sources: property tax, sales tax, TOT, and franchise fees. Nearly 70% of the City's General Fund expenditures are personnel expenses. Negative economic factors have resulted in a downward revision to revenue projections for the fiscal year 2010 annual budget, which served as a base for the Outlook. The Outlook discussed risks and opportunities that affect fiscal decisions and the City's ability to accomplish its strategic financial goals over the next five-year period. These goals include:

- Meet contractual obligations and fund mandated programs
- Contribute the full payment of the Annual Required Contribution (ARC) for the City's pension system
- Maintain or enhance General Fund and other reserves according to the City's Reserve Policy
- Preserve City services to the fullest extent possible

Five Year Outlook for Fiscal Years 2011 - 2015						
GENERAL FUND		**Forecast FY 2011**	**Forecast FY 2012**	**Forecast FY 2013**	**Forecast FY 2014**	**Forecast FY 2015**
Projected Revenues						
	Property Tax	$ 396.4	$ 404.5	$ 416.7	$ 433.4	$ 450.7
	Sales Tax	182.7	192.7	200.2	208.1	218.8
	Transit Occupancy Tax	71.9	74.1	76.7	79.7	82.9
	Franchise Fees	75.0	76.7	78.5	80.3	82.2
	Other Revenues	335.6	346.1	353.3	355.3	362.0
		1,061.6	**1,094.1**	**1,125.4**	**1,156.8**	**1,196.6**
Projected Expenses						
	Salary, Wages & Benefits	611.8	620.9	627.2	636.2	622.7
	Operating Expenses	351.5	363.1	366.0	382.5	390.6
	Pension Expense	217.8	206.5	225.2	242.5	258.7
	Retiree Healthcare Expense	43.2	46.8	50.4	54.2	57.8
	General Fund Reserves	4.2	7.9	2.5	2.5	3.2
	Liability Funding	12.2	7.8	10.1	4.8	-
		1,240.7	**1,253.0**	**1,281.4**	**1,322.7**	**1,333.0**
General Fund Projected Shortfall		**$ (179.1)**	**$ (158.9)**	**$ (156.0)**	**$ (165.9)**	**$ (136.4)**

The impact of continued declines in major revenue sources and increased costs for pension funding are the leading factors in the fiscal year 2011 forecasted budget deficit of $179 million.

Because of the severity of the budget shortfall, the Mayor has indicated that cuts to services and programs will be inevitable in order for the City to maintain a balanced budget. Within the City, this will mean a workforce reduction combined with expenditure savings from reduced or eliminated programs and services. The Mayor's budget plan for fiscal year 2011 does not include contributions to fund reserves; however, the plan proposes that reserves will not be spent and will be maintained at current levels.

Looking Forward

These are difficult economic times, and the City has set challenging goals for its future. The City believes these goals are achievable with continued fiscal discipline and greater government efficiency. In some revenue categories, San Diego has relatively low taxes and fees compared to most other large municipalities in the United States. San Diego enjoys an ideal location with agreeable weather year round. The diversity of industry, education and tourism well positions the City for an early economic rebound when the economy begins its eventual recovery.

Out of these challenging times, San Diego is restructuring its operations, services and programs so that the City will emerge with a sound, fundamentally sustainable municipal business model. We have addressed the issues that have created prior difficulties for this City, and we are structuring ourselves for long-term solvency and flexibility. We will continue to live within our means and balance our annual budgets.

Purpose, Background, and Scope of this Report

San Diego City Charter § 111 requires the City to submit an annual report, including a Statement of Net Assets, and requires that all accounts of the City be audited by an independent auditor. Pursuant to this requirement, the Comprehensive Annual Financial Report ("CAFR") of the City of San Diego ("City") for the fiscal year ended June 30, 2009, is hereby submitted. The audit firm of Macias Gini & O'Connell LLP has issued an unqualified opinion on the City of San Diego's financial statements. The independent auditor's report is located at the front of the financial section of this report.

The CAFR has been prepared in conformance with the principles and standards for reporting as set forth by the Governmental Accounting Standards Board (GASB). Responsibility for both the accuracy of the data and the completeness and fairness of the presentation, including all disclosures, rests with the management of the City and its related agencies. The City's objective is to provide you with reasonable, rather than absolute, assurance that the financial statements are free of any material misstatements. Additionally, the City continues to construct and improve a comprehensive internal control framework in order to ensure acceptable management of taxpayer funds.

To the best of our knowledge and belief, the data as presented, is accurate in all material respects; it is presented in a manner designed to present fairly the financial position and results of operations of the governmental activities, business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining funds of the City and its related agencies; and all disclosures necessary to enable the reader to gain an understanding of the City's, as well as its related agencies', financial activities have been included.

A narrative introduction, overview, and analysis of the financial statements can be found in Management's Discussion and Analysis (MD&A), which immediately follows the independent auditor's report. The MD&A complements this letter of transmittal and should be read in conjunction with it. The CAFR is organized into three sections:

- The introductory section includes information about the organizational structure of the City, the City's economy, and selected other financial information.

- The financial section is prepared in accordance with governmental accounting standards. It includes the MD&A (unaudited), the independent auditor's report, the audited basic financial statements, notes to the basic financial statements, required supplementary information (unaudited), and supplementary information (unaudited).

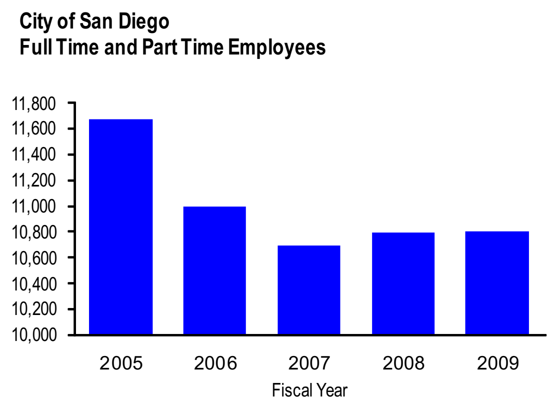
- The statistical section contains historical statistical data on the City's financial data and debt statistics, as well as miscellaneous physical, demographic, economic, and social data of the City. This section of the CAFR is unaudited.

Profile of the City of San Diego

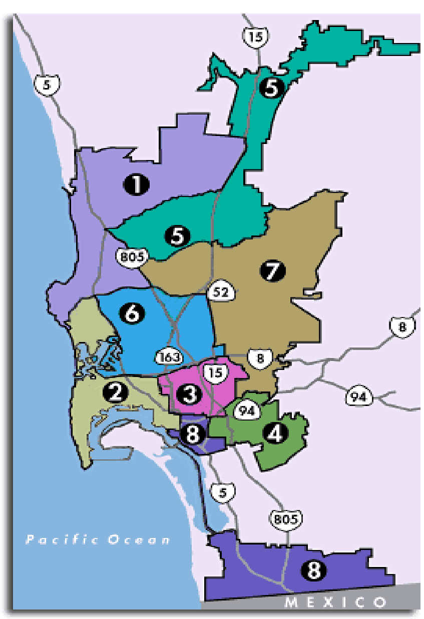
The City of San Diego was incorporated in 1850. The City comprises 342 square miles and, as of January 1, 2009, the California Department of Finance estimates the population to be 1,353,993. The City, with approximately 10,800 employees, provides a full range of governmental services including police and fire protection, sanitation and health services, the construction and maintenance of streets and infrastructure, recreational activities and cultural events, and the maintenance and operation of the water and sewer utilities.

Governing Structure

The City operates under and is governed by the laws of the State of California and its own Charter, as periodically amended since its adoption by the electorate in 1931. The City is currently operating under a Strong-Mayor form of government. The departure, on an interim trial basis, from the City's previous Council-Manager form of government was approved by a vote of the public and became effective January 1, 2006. The Mayor is elected at large to serve a four-year term.



City of San Diego Council District Map



Under the Strong-Mayor form of government, the Mayor is the Chief Executive Officer of the City and has direct oversight over all City functions and services except for the City Council, Personnel, City Clerk, Independent Budget Analyst (IBA), City Attorney, and City Auditor departments. Under this form of government, the City Council is composed of eight members and is presided over by the Council President, who is selected by a majority vote of the City Council. The Mayor presides over City Council in closed session meetings of the Council. The Council retains its legislative authority; however, all City Council resolutions and ordinances are subject to a veto of the Mayor except for certain ordinances including emergency declarations and the City's annual Salary and Appropriations Ordinances. The City Council may override a Mayoral veto with five votes. The City Attorney, who is elected for a four-year term, serves as the chief legal advisor of and attorney for the City and all departments.

During the County's primary election held on June 3, 2008, voters approved Proposition B which requires City Council to place a measure on the June 2010 ballot to allow voters to decide whether the Strong-Mayor form of government should become permanent effective January 1, 2011. Additionally, Proposition B provides for the public to decide whether the number of City Council districts should increase from eight to nine, and therefore, a corresponding increase of City Council votes required to override the Mayor's veto from five to six. Additionally, voters approved Proposition C, which separated the City Auditor's Office from the Comptroller's Office and made the Office of the IBA permanent. Under this amendment, the City Auditor serves a ten-year term and is supervised by an Audit Committee consisting of two Councilmembers and three members of the public with auditing expertise, who are appointed by the City Council. This amendment also provides that the Mayor will appoint, with City Council confirmation, the Chief Financial Officer. In addition, the Mayor's appointment of the City Treasurer no longer requires City Council confirmation.

Current Elected Officials
(As of the issuance of this report)

Mayor Jerry Sanders

District 1
Councilmember Sherri Lightner

District 5
Councilmember Carl DeMaio

District 2
Council President Pro Tem
Kevin Faulconer

District 6
Councilmember Donna Frye

District 3
Councilmember Todd Gloria

District 7
Councilmember Marti Emerald

District 4
Councilmember Tony Young

District 8
Council President Ben Hueso

City Attorney
Jan Goldsmith

<u>Other City Officials</u>

Jay M. Goldstone, Chief Operating Officer

Mary Lewis, Chief Financial Officer

Kenton C. Whitfield, City Comptroller

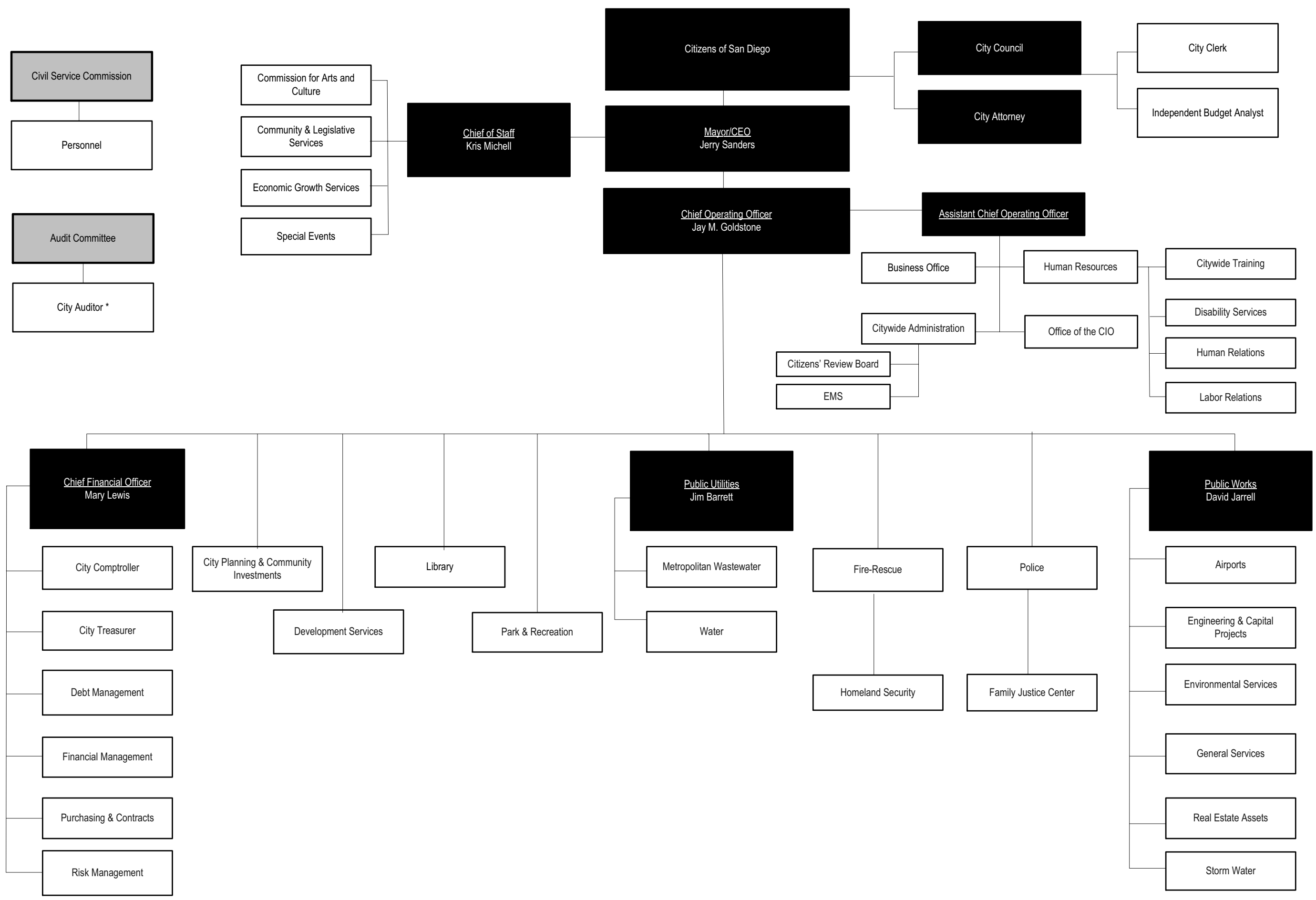
Gail R. Granewich, City Treasurer

Elizabeth Maland, City Clerk

Andrea Tevlin, Independent Budget Analyst

Eduardo Luna, City Auditor

City of San Diego Organization Chart
(As of the issuance of this Report)



* Proposition C, passed in June 2008, provides that the City Auditor shall report to and be accountable to the Audit Committee. To complete the enacting measure for Proposition C, the City Auditor must be appointed by the City Manager (Mayor), in consultation with the Audit Committee, and confirmed by the City Council. This organization chart reflects the reporting structure called for in Proposition C, which will be in effect following that Council action.

Financial Reporting Entity

In accordance with Governmental Accounting Standards Board (GASB) Statement 14, the following component units are incorporated into the accompanying financial statements:

- Centre City Development Corporation (CCDC)
- Convention Center Expansion Financing Authority (CCEFA)
- City of San Diego Metropolitan Transit Development Board Authority (MTDB)
- San Diego City Employees' Retirement System (SDCERS)
- Public Facilities Financing Authority (PFFA)
- Redevelopment Agency of the City of San Diego (RDA)
- San Diego Convention Center Corporation (SDCCC)
- San Diego Data Processing Corporation (SDDPC)
- San Diego Facilities and Equipment Leasing Corporation (SDFELC)
- San Diego Housing Commission (SDHC)
- San Diego Industrial Development Authority (SDIDA)
- San Diego Open Space Park Facilities District #1
- Community Facilities and Other Special Assessment Districts
- Tourism Marketing District
- Southeastern Economic Development Corporation (SEDC)
- Tobacco Settlement Revenue Funding Corporation (TSRFC)

Additionally, the City participates in a joint venture operation with a private company to provide for emergency medical and medical transportation services. This joint venture is a limited liability company named San Diego Medical Services Enterprise, LLC. The financial impact of the joint venture is displayed in the General Fund within the governmental funds statement of revenues, expenditures and changes in fund balance and in the government-wide statement of activities.

Budgetary Process

Pursuant to the City Charter, an annual budget is presented by the Mayor to the City Council for consideration. Set forth in this budget are the anticipated revenues and expenditures of the General Fund, certain special revenue funds, enterprise funds, and certain debt service funds for the ensuing fiscal year. Additionally, project-length financial plans are presented to and adopted by the City Council for the capital projects funds. The legal level of budgetary control for the City's general fund is exercised at the salaries and wages and non-personnel expenditures level. Budgetary control for the other budgeted funds, including those of certain component units, is maintained at the total fund appropriation level. Copies of the City's budgets are available at the Financial Management Office located at 202 C Street, MS8A, San Diego, CA 92101.

The City continues to look for ways to improve the effectiveness and efficiency of its operations. The focus now is on crafting policy that will ensure a continued commitment to strong financial stewardship.

Sincerely,

Jerry Sanders
Mayor

Jay M. Goldstone
Chief Operating Officer

Mary Lewis
Chief Financial Officer

Kenton C. Whitfield
City Comptroller

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FINANCIAL SECTION

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MACIAS GINI & O'CONNELL LLP
Certified Public Accountants & Management Consultants

SAN DIEGO
402 W. Broadway, Suite 400
San Diego, CA 92101
619.573.1112

SACRAMENTO

OAKLAND

WALNUT CREEK

LOS ANGELES

NEWPORT BEACH

INDEPENDENT AUDITOR'S REPORT

To the Honorable Mayor and Members of the City Council
of the City of San Diego, California

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of San Diego, California (City), as of and for the year ended June 30, 2009, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the San Diego Housing Commission, a discretely presented component unit, which statements reflect 90%, 95% and 85% of the total assets, total net assets and total revenues, respectively, of the aggregate discretely presented component unit totals. Also, we did not audit the Southeastern Economic Development Corporation, a blended component unit, which statements reflect less than 1% in each of the total assets, total net assets and total revenues categories, respectively, of the aggregate remaining fund information. Those financial statements were audited by other auditors whose reports thereon has been furnished to us, and our opinion, insofar as it relates to the amounts included for the San Diego Housing Commission and the Southeastern Economic Development Corporation is based solely on the reports of the other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the reports of the other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City as of June 30, 2009, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1 to the basic financial statements, the City adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations,* effective July 1, 2008.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 21, 2009, on our consideration of the City's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis, schedules of funding progress and schedule of contributions from employer and other contributing entities, and general fund budgetary information on pages 35 through 48, 168, and 172 through 174, respectively, are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City's basic financial statements. The introductory section, supplementary information, and, statistical section are presented for purposes of additional analysis and are not a required part of the basic financial statements. The supplementary information has been subjected to the auditing procedures applied by us and the other auditors in the audit of the basic financial statements and, in our opinion, based on our audit and the report of other auditors, is fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory and statistical sections have not been subjected to the auditing procedures applied by us and the other auditors in the audit of the basic financial statements and, accordingly, we express no opinion on them.

Macias Gini & O'Connell LLP

Certified Public Accountants

San Diego, California
December 21, 2009

MANAGEMENT'S DISCUSSION AND ANALYSIS
(Unaudited)
(In Thousands)
June 30, 2009

As management of the City of San Diego (City), we offer readers of the City financial statements this narrative overview and analysis of the financial activities of the City for the fiscal year ended June 30, 2009.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the City's basic financial statements. The City's basic financial statements are comprised of 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.

GOVERNMENT-WIDE FINANCIAL STATEMENTS

The focus of the government-wide financial statements is on reporting on the operating results and financial position of the government as an economic entity. These statements are intended to report the entity's operational accountability to its readers, giving information about the probable medium and long-term effects of past decisions on the government's financial position.

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 the financial position of the City is improving or deteriorating.

The statement of activities presents information showing changes in the City's net assets during the fiscal year 2009. All changes in net assets are reported when the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. The focus is on both gross and net costs of City functions, which are supported by general revenues. This Statement also distinguishes 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: General Government and Support; Public Safety - Police; Public Safety - Fire and Life Safety and Homeland Security; Parks, Recreation, Culture and Leisure; Transportation; Sanitation and Health; and Neighborhood Services. The business-type activities of the City include: Airports; City Store; Development Services; Environmental Services; Golf Course; Recycling; Sewer Utility; and Water Utility.

The government-wide financial statements include the City (known as the primary government) and the following legally separate, discretely presented component units: San Diego Convention Center Corporation (SDCCC); and San Diego Housing Commission (SDHC). Financial information for these component units is reported separately from the financial information presented for the primary government. Blended component units, also legally separate entities, are a part of the government's operations and are combined with the primary government.

Included within the primary government as blended component units:

- Centre City Development Corporation (CCDC)
- City of San Diego Metropolitan Transit Development Board Authority (MTDB Authority)
- City of San Diego Tobacco Settlement Revenue Funding Corporation (TSRFC)
- Community Facilities and Other Special Assessment Districts
- Convention Center Expansion Financing Authority (CCEFA)
- Public Facilities Financing Authority (PFFA)
- Redevelopment Agency of the City of San Diego (RDA)
- San Diego City Employees' Retirement System (SDCERS)
- San Diego Data Processing Corporation (SDDPC)

- San Diego Facilities and Equipment Leasing Corporation (SDFELC)
- San Diego Industrial Development Authority (SDIDA)
- San Diego Open Space Park Facilities District #1
- Southeastern Economic Development Corporation (SEDC)
- Tourism Marketing District (TMD)

The government-wide financial statements can be found beginning on page 52 of this report.

FUND FINANCIAL STATEMENTS

A fund is a grouping of related accounts that is 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 funds of the City can be divided into 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. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spendable resources, as well as balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

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 of 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 individual governmental 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 a major fund. Data from the other governmental funds are combined into a single, aggregated presentation. Individual fund data for each of these nonmajor governmental funds is provided in the Supplementary Information section of this report.

The City adopts an annual appropriated budget for its General Fund. A budgetary comparison statement has been provided for the General Fund to demonstrate compliance with this budget and is presented as required supplementary information.

The basic governmental funds financial statements can be found beginning on page 56 of this report.

PROPRIETARY FUNDS

The City maintains two different types of proprietary funds, enterprise funds and internal service 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 its various business-type activities, such as Sewer and Water Utilities. Internal Service funds, such as Fleet Services, Central Stores, Publishing Services, and Self Insurance, are used to report activities that provide centralized supplies and/or services to the City. All internal service funds, except for the Special Engineering Fund, have been included within governmental activities in the government-wide financial statements since they predominantly benefit governmental functions. The Special Engineering Fund, which services exclusively Sewer and Water activities, has been included within business-type activities in the government-wide financial statements.

Proprietary fund statements provide the same type of information as the government-wide financial statements, only in more detail. The proprietary funds financial statements provide separate information for the Sewer and Water funds, which are considered to be major funds of the City. Data for the nonmajor proprietary funds are combined into a single, aggregated presentation, and the internal service funds are combined into a single, aggregated presentation as well. Included in the Supplementary Information section of this report are individual fund data for the nonmajor proprietary funds and the internal service funds. The basic proprietary funds financial statements can be found beginning on page 60 of this report.

FIDUCIARY FUNDS

Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are not available to support the City's operations. The accounting used for fiduciary funds is much like that used for proprietary funds.

The basic fiduciary funds financial statements can be found beginning on page 63 of this report.

NOTES TO THE FINANCIAL STATEMENTS

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found beginning on page 65 of this report.

OTHER INFORMATION

In addition to the basic financial statements and accompanying notes, this report also presents certain required supplementary information concerning the City's progress in funding its obligation to provide pension and postemployment healthcare benefits to its employees, and the General Fund's budgetary comparison schedule. Required supplementary information can be found beginning on page 170 of this report.

The individual fund data referred to earlier in connection with nonmajor governmental funds, nonmajor proprietary funds, internal service funds, and fiduciary funds are presented immediately following the required supplementary information on pensions and the General Fund budgetary comparison schedule, beginning on page 199 of this report.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

CITY OF SAN DIEGO'S SUMMARY OF NET ASSETS
(In Thousands)

	Governmental Activities		Business-Type Activities		Total Primary Government	
	2009	2008	2009	2008	2009	2008
Capital Assets	$ 4,455,525	$ 4,335,317	$ 4,766,721	$ 4,634,918	$ 9,222,246	$ 8,970,235
Other Assets	2,110,185	2,096,751	1,357,070	1,031,815	3,467,255	3,128,566
Total Assets	6,565,710	6,432,068	6,123,791	5,666,733	12,689,501	12,098,801
Net Long-Term Liabilities	2,164,276	1,965,991	2,413,033	2,068,569	4,577,309	4,034,560
Other Liabilities	143,231	312,696	110,479	108,455	253,710	421,151
Total Liabilities	2,307,507	2,278,687	2,523,512	2,177,024	4,831,019	4,455,711
Net Assets:						
Invested in Capital Assets,						
Net of Related Debt	3,530,937	3,518,704	2,970,351	2,933,012	6,501,288	6,451,716
Restricted	564,605	564,042	42,485	39,436	607,090	603,478
Unrestricted	162,661	70,635	587,443	517,261	750,104	587,896
Total Net Assets	$ 4,258,203	$ 4,153,381	$ 3,600,279	$ 3,489,709	$ 7,858,482	$ 7,643,090

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the City, assets exceeded liabilities by $7,858,482 at June 30, 2009, an increase of $215,392 over fiscal year 2008.

$6,501,288, or approximately 82%, of total Net Assets represent the City's investment in capital assets (e.g., land, structures and improvements, equipment, distribution and collections systems, infrastructure, and construction-in-progress), less any outstanding debt used to acquire these assets. The City uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending. Although the City's investment in 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 generally are not used to liquidate these liabilities.

$607,090, or approximately 8%, of total Net Assets represent resources that are subject to external restrictions on how they may be used. The remaining balance of $750,104, or approximately 10%, is available to finance ongoing services and obligations to the City's citizens and creditors.

Unrestricted Net Assets increased by $162,208, or approximately 28%. Approximately $70,000 of this increase was in the Business-Type activities, primarily attributed to Council approved rate increases. Governmental activities increased by approximately $92,000. This was primarily the result of revenues exceeding expenses for RDA by approximately $70,000. RDA projects are multi-year in nature, and therefore, revenues collected on an annual basis are often budgeted for future larger construction phases of the projects. In addition, RDA experienced increased property tax revenues from fiscal year 2008 to 2009. Another material increase was a $20,000 increase to debt service reserves not legally restricted but internally set aside.

CITY OF SAN DIEGO'S SUMMARY OF CHANGES IN NET ASSETS
(In Thousands)

	Governmental Activities		Business-Type Activities		Total Primary Government	
	2009	2008	2009	2008	2009	2008
Revenues:						
Program Revenues						
Charges for Current Services	$ 345,532	$ 289,985	$ 771,725	$ 772,602	$ 1,117,257	$ 1,062,587
Operating Grants and Contributions	93,244	75,126	1,739	2,312	94,983	77,438
Capital Grants and Contributions	110,802	78,347	60,863	58,400	171,665	136,747
General Revenues						
Property Taxes	607,857	576,605	-	-	607,857	576,605
Transient Occupancy Taxes	140,657	159,348	-	-	140,657	159,348
Other Local Taxes	161,485	151,267	-	-	161,485	151,267
Grants and Contributions not Restricted to						
Specific Programs	8,488	6,251	-	-	8,488	6,251
Sales Taxes	229,651	269,757	-	-	229,651	269,757
Investment Income	75,245	96,725	31,004	41,224	106,249	137,949
Other	51,598	85,785	8,257	7,850	59,855	93,635
Total Revenues	1,824,559	1,789,196	873,588	882,388	2,698,147	2,671,584
Expenses:						
General Government and Support	303,581	322,157	-	-	303,581	322,157
Public Safety-Police	418,549	382,907	-	-	418,549	382,907
Public Safety-Fire, Life Safety, Homeland Security	220,787	204,822	-	-	220,787	204,822
Parks, Recreation, Culture and Leisure	258,038	231,955	-	-	258,038	231,955
Transportation	239,305	212,255	-	-	239,305	212,255
Sanitation and Health	77,447	51,772	-	-	77,447	51,772
Neighborhood Services	116,735	91,110	-	-	116,735	91,110
Debt Service:						
Interest on Long-Term Debt	84,070	82,211	-	-	84,070	82,211
Airports	-	-	5,140	4,109	5,140	4,109
City Store	-	-	321	788	321	788
Development Services	-	-	47,260	51,461	47,260	51,461
Environmental Services	-	-	35,718	37,279	35,718	37,279
Golf Course	-	-	11,864	11,142	11,864	11,142
Recycling	-	-	20,067	20,511	20,067	20,511
Sewer Utility	-	-	314,125	322,552	314,125	322,552
Water Utility	-	-	329,748	321,123	329,748	321,123
Total Expenses	1,718,512	1,579,189	764,243	768,965	2,482,755	2,348,154
Change in Net Assets Before Transfers:	106,047	210,007	109,345	113,423	215,392	323,430
Transfers	(1,225)	3,551	1,225	(3,551)	-	-
Net Change in Net Assets	104,822	213,558	110,570	109,872	215,392	323,430
Net Assets - July 1	4,153,381	3,939,823	3,489,709	3,379,837	7,643,090	7,319,660
Net Assets - June 30	$ 4,258,203	$ 4,153,381	$ 3,600,279	$ 3,489,709	$ 7,858,482	$ 7,643,090

GOVERNMENTAL ACTIVITIES

Governmental activities increased the City's net assets by $104,822 during fiscal year 2009. Variances from fiscal year 2008 of more than 10% are discussed below.

- Charges for Services increased by $55,547, or approximately 19%. The Special Engineering Fund was closed out during fiscal year 2009, and all Water and Sewer engineering positions were transferred to the General Fund. Charges for Services revenue increased as a result of those engineers billing Water and Sewer capital improvement projects.

- Operating Grants and Contributions increased by $18,118, or approximately 24%, mainly due to an increase in Community Development Block Grant (CDBG) revenues. This was primarily the result of CDBG funded projects for non-City owned assets for various public improvements.

- Capital Grants and Contributions increased by $32,455, or approximately 41%, which was caused by several factors. The City was awarded two new grants related to a 2007 landslide in the La Jolla area. The first was a Homeland Security grant for the Desert View Drive Area of La Jolla ($6,800), and the second was a federal grant for the Mount Soledad Road area ($11,900). In addition, there were increased revenues recognized for several other Capital Outlay grants including a Seismic Retrofit federal grant ($5,500), a Prop1B State Grant ($4,500), and a La Jolla/Pacific Beach/Ocean Beach/Mission Bay Water grant ($1,200). Donated capital assets increased by $8,900, which included park land turned over to the City ($3,200) and land exchanged with the County for open space ($2,600). These increases were offset by a decrease of approximately $9,400 in CDBG related capital projects for city-owned public improvements.

- Transient Occupancy Taxes decreased by $18,691, or approximately 12%, primarily due to the economic downturn in San Diego's tourism industry.

- Grants and Contributions not Restricted to Specific Programs increased by $2,237, or approximately 36%, primarily due to one-time revenue received by RDA for the sale of downtown condominium units, pursuant to a participation agreement with a developer.

- Sales Taxes decreased by $40,106, or approximately 15%. The General Fund's sales tax revenue decreased by approximately $22,700, primarily due to declining retail sales as part of the overall downturn in the economy. TransNet's sales tax revenue decreased by approximately $15,000. In fiscal year 2008 the City was awarded $4,900 for the Bike Lanes and Major Corridor Programs, and in fiscal year 2009 the City was not awarded any new funds for these programs. In addition, SANDAG deferred approximately $5,500 in sales tax disbursements to the City because the City was in violation of a SANDAG Board ruling which states that the City cannot maintain a balance in excess of 30% of the yearly apportionment. SANDAG deferred disbursement until the balance in the fund is reduced to meet the 30% rule.

- Investment Income decreased by $21,480, or approximately 22%, primarily due to declining interest rates during 2008 and a decrease in interest income from the reinvestment of the investment pool's assets at these record low interest rates.

- Other Revenue decreased by $34,187, or approximately 40% primarily due to a $20,200 decrease in Proceeds from Land Sales. Due to the real estate market decline, the City has not sold the remaining parcels that were designated for disposition as part of the portfolio management plan for the City. There were also decreases in developer contributions in the Impact Fees Fund of $9,300 and the Facilities Benefit Assessment Fund of $2,400. These decreases were attributed to several communities, mainly Centre City ($7,000), but also including smaller decreases in Uptown Urban Communities, Pacific Highlands Ranch, and Scripps Miramar Ranch.

- Parks, Recreation, Culture and Leisure expense increased by $26,083, or approximately 11%, primarily due to the creation of the new Tourism Marketing District (TMD). Fiscal Year 2009 was the first full year for the TMD, causing an increase in expenditures of approximately $9,500. There were also increases in depreciation of governmental capital assets in the amount of $6,700 and Net Pension Obligation expense of $6,900.

- Transportation expense increased by $27,050, or approximately 13%, primarily due to the Underground Surcharge expenses. Since the underground program is funded by SDG&E franchise revenues, which came in lower than anticipated during fiscal year 2008, expenditures for the undergrounding of utility lines increased by approximately $17,000 during fiscal year 2009 when revenues came in higher. Expenses related to the addition of the new Right of Way Design Program also increased by approximately $6,400.

- Sanitation and Health expense increased by $25,675, or approximately 50%, primarily due to an increase in the General Fund's Storm Water department expenditures. The City's Storm Drain and Street Sweeping programs were transferred to the Storm Water department from the Streets and Public Safety-Police departments, which accounted for an increase of approximately $20,200. In addition, the Convention Center Fund paid $5,900 for a one-time capacity fee adjustment for the annual cost of effluent dewatering.

- Neighborhood Services expense increased by $25,625, or approximately 28%. This increase was primarily the result of a settlement agreement with the County of San Diego regarding the Grantville Redevelopment Project area for $39,200. This was partially offset by a decrease of approximately $9,300 which was attributed to a prior year loss on the disposition of an RDA parcel of land in the Centre City Project area, related to the Renaissance Hotel project. The loss was mostly due to timing differences in revenue and expense recognition because advances from the developer were recognized in prior years as the funds were used to acquire the property.

BUSINESS-TYPE ACTIVITIES

Business-type activities increased the City's net assets by $110,570 during fiscal year 2009. Variances from fiscal year 2008 of more than 10% are discussed below.

- Investment Income decreased by $10,220, or approximately 25%, primarily due to a bottoming out of declining interest rates around December 2008 and a decrease in interest income from the reinvestment of the Investment Pool's assets at these record low interest rates.

- Airports expense increased by $1,031, or approximately 25%, primarily due to higher personnel costs. This was the result of filling supervisory positions, as well as emergency repairs and maintenance performed on buildings and runways.

- City Store expense decreased by $467, or approximately 59%, primarily due to the City Store operations being shut down during fiscal year 2009.

FINANCIAL ANALYSIS OF THE GOVERNMENT'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 is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the City'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.

As of the end of fiscal year 2009, the City's governmental funds reported combined ending fund balances of $1,740,792, an increase of $149,488 from fiscal year 2008. Approximately $999,926 constitutes unreserved fund balance, which is available for spending at the government's direction. The remainder of fund balance is reserved to indicate that it is not available for new spending because it has already been committed (1) to liquidate contracts and purchase orders of the period, (2) to pay debt service, (3) to generate income to pay for the perpetual funding of various programs, or (4) for a variety of other purposes.

The General Fund is the principal operating fund of the City. At the end of fiscal year 2009, undesignated fund balance of the General Fund was $78,347, while total fund balance was $114,392. This represents a $10,389 decrease from the fiscal year 2008 total fund balance.

PROPRIETARY FUNDS

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

As of the end of fiscal year 2009, Unrestricted Net Assets of the Sewer Utility Fund are $292,441. Unrestricted Net Assets increased approximately $48,724, or approximately 20%, mainly due to increased charges for services as a result of Council approved rate increases.

As of the end of fiscal year 2009, Unrestricted Net Assets of the Water Utility Fund are $232,899. Unrestricted Net Assets increased by $21,054, or approximately 10%, mainly due to increased sales of water as a result of Council approved rate increases.

GENERAL FUND BUDGETARY HIGHLIGHTS

The original budget for expenditures and transfers out was $24,744 higher than the final budget due to increases (decreases) in appropriations primarily attributed to the following:

- ($10,548) for General Governmental and Support. This variance was mostly attributed to the departments below:
    - ($11,016) for Citywide Programs. The majority of the budget adjustment ($7,614) is due to employee leveraged pick up savings being reimbursed to employees out of the UAAL fund instead of the General Fund. City Elections budget decreased by ($1,975) due to fewer propositions on the November ballot and no run-off elections. The remaining ($1,427) is made up of a decrease in the amount of Mission Bay revenue transferred to the Park Improvement Fund and other miscellaneous adjustments.
    - $ 8,377 due to an increase in the General Fund Appropriated Reserve.
    - ($1,200) for City Treasurer. This decrease was due to the first quarter budget adjustments approved by City Council, which reduced funding for supplies and services, as well as personnel costs.
    - ($3,853) for City Comptroller, Facilities Maintenance, Field Engineering, and Project Implementation and Technical Services. This decrease was mainly due to the first quarter budget adjustments approved by City Council, which reduced funding for supplies and services, as well as personnel costs.
    - ($ 2,837) for City Planning and Development, Community Services, Customer Services, Office of Ethics and Integrity, and Public Safety. This decrease was due to the first quarter budget adjustments approved by City Council, which eliminated these four departments.
- ($7,902) for Public Safety-Police. The majority of the budget reduction was in personnel, which was attributed to vacant positions, the decrease in recruits from the Police Academy, and overtime savings.
- $10,414 for Public Safety-Fire and Life Services and Homeland Security. The increase in budget was primarily due to over budget expenditures related to overtime Strike Team activities for wildfires and other Federal Emergency Management Agency requirements, unanticipated retirements, and an increase in reimbursable Emergency Medical Services.
- ($1,560) for Parks, Recreation, Culture and Leisure. This decrease was mainly due to the first quarter budget adjustments approved by City Council.
- ($4,561) for Transportation. This decrease was due to vacant reimbursable positions in the Streets Department and a budget reduction in supplies and services approved by City Council in December.
- ($10,273) for Sanitation and Health. The decrease was primarily due to the first quarter budget adjustments approved by City Council, which reduced funding for Storm Drain Repairs, Contracts, Pollution Prevention, and personnel costs.

- $818 for Principal Retirement. This increase was due to capital lease payments for Police and Parking Enforcement vehicles, as well as equipment, vehicles and helicopters for the Public Safety-Fire and Life Safety and Homeland Security department.

- $194 for Interest Expense. This increase was due to capital lease payments for Police and Parking Enforcement vehicles, as well as equipment, vehicles and helicopters for the Public Safety-Fire and Life Safety and Homeland Security.

Actual revenues received for the General Fund were $64,787 less than budgeted. Sales Tax and Transient Occupancy Tax were under budget by $10,700 and $8,424, respectively, due to the downturn in the economy. Other Local Taxes were under budget by $4,545 mainly due to Property Transfer Tax which came in lower than anticipated. This was the result of reduced home sales and shortfalls in SDG&E and Refuse Collection Franchise Fees. Revenue from Use of Money and Property came in $10,099 under budget, due to declining market values for the City's investment pool. Revenue from Federal Agencies came in $11,433 under budget. $2,347 was budgeted to come in during fiscal year 2009 but was actually accrued as fiscal year 2008 revenue. Charges for Current Services came in $2,101 over budget due to the Engineering Department's work on Water and Sewer capital improvement projects. Other revenue was $21,562 less than budgeted, which was due to Engineering's charges to Water and Sewer capital projects being received in the Charges for Services category, rather than in Other Revenue, where it was originally budgeted.

Actual expenditures for the General Fund were $45,464 less than budgeted. $20,136 was attributed primarily to an increase in the budget of the General Fund Appropriated Reserve without corresponding expenditures, and lower than anticipated allocations from the General Fund Fringe Benefits Reserve. The Fringe Benefits Reserve is used to compensate departments for fringe expenditures in excess of the Revised Budget. In addition, several categories had appropriation savings: Public Safety-Police had personnel and supplies and services savings of $6,827; Sanitation and Health had savings of $9,168 mainly due to vacant positions and delays in contractual expenditures for the Storm Water department; Parks, Recreation, Culture, and Leisure had savings of $3,331 largely due to conservative spending in non-personnel costs. The remaining $6,002 was primarily due to personnel savings in Neighborhood Services and non-personnel savings in Transportation.

CAPITAL ASSET AND DEBT ADMINISTRATION

CITY OF SAN DIEGO'S CAPITAL ASSETS
(Net of Accumulated Depreciation)
(In Thousands)

	Governmental Activities		Business-Type Activities		Total Primary Government	
	2009	2008	2009	2008	2009	2008
Land, Easements, Rights of Way	$ 1,768,968	$ 1,755,956	$ 93,240	$ 89,988	$ 1,862,208	$ 1,845,944
Construction-in-Progress	192,741	165,880	291,283	174,065	484,024	339,945
Structures and Improvements	826,488	827,912	1,253,903	1,422,839	2,080,391	2,250,751
Equipment	169,387	133,317	156,891	102,069	326,278	235,386
Distribution and Collection Systems	-	-	2,971,404	2,845,957	2,971,404	2,845,957
Infrastructure	1,497,941	1,452,252	-	-	1,497,941	1,452,252
Totals	$ 4,455,525	$ 4,335,317	$ 4,766,721	$ 4,634,918	$ 9,222,246	$ 8,970,235

CAPITAL ASSETS

In accordance with GASB Statement No. 34, all major infrastructure assets (such as streets, signals, bridges, and drains) are capitalized by the City in the government-wide statements. While capital assets of both governmental and proprietary funds are capitalized at the government-wide level, only proprietary assets are reported at the fund level. Governmental funds are reported on a modified accrual basis at the fund level. Differences between reporting at the fund level and government-wide level for these governmental assets will be explained in both the reconciliation and the accompanying notes to the financial statements.

The City's investment in capital assets (including infrastructure) for governmental and business-type activities as of June 30, 2009 was $9,222,246 (net of accumulated depreciation). There was an overall increase in the City's investment in capital assets over fiscal year 2008 of approximately $252,011. Readers interested in more detailed information on capital asset activity should refer to Note 4 Capital Assets.

HIGHLIGHTS OF FISCAL YEAR 2009 CAPITAL IMPROVEMENT ACTIVITIES

<u>Governmental Activities</u>

- Phase 1 of the Enterprise Resource Planning (ERP) System Core Project to provide a replacement of the legacy software currently used by the Offices of the Chief Financial Officer (CFO) and Business and Support Services was completed and implemented city-wide on July 1, 2009. As identified in the Kroll report, the legacy system was no longer meeting the City's requirement for responsible financial management, efficient human resources management, or IT operational efficiency. The project is being funded primarily through a lease purchase agreement with IBM Credit LLC and cash from SDDPC. The City's fiscal year 2009 capital expenditures for this project were $19,501.

- Construction continued on the reconstruction of Soledad Mountain Road following the October 2007 landslide that destroyed a large section of the 5700 block of Soledad Mountain Road and Desert View Drive Alley. The project is funded by TransNet, as well as state and federal grants. The City's fiscal year 2009 capital expenditures for this project were $12,594.

- Construction continues on the North Harbor Drive Bridge over the Navy Estuary. This project will provide for the seismic retrofitting of the bridge as well as stabilization of the existing piers, and joining the paired piers together at the waterline to increase support during seismic events. The City's fiscal year 2009 capital expenditures for this project were $9,953.

- Construction was completed on the Bird Rock Coastal Traffic Flow Improvements. This project provides traffic calming measures to reduce speed and improve safety and walkability on La Jolla Boulevard. The project provides three modern roundabouts on La Jolla Boulevard, as well as three mini roundabouts on connecting residential streets. La Jolla Boulevard will also be reduced from four to two lanes. The project was funded by SANDAG, TransNet, Developer Impact Fees, and federal and state grants. The City added $6,207 in capital infrastructure assets related to this project in fiscal year 2009.

- Construction was completed on the widening of Genesee Avenue from Interstate 5 to Campus Point Drive. This project provided for the widening of 2,500 feet of Genesee Avenue to a modified six-lane primary arterial including Class II bicycle lanes. The project was funded by Facility Benefit Assessments. The City added $6,500 in capital infrastructure assets related to this project in fiscal year 2009.

- Construction continued on Phase II of the Logan Heights Branch Library. This project provides for a new 25,000 square foot library at 28th Street and Ocean Boulevard to serve the Logan Heights Community. The project is funded by various grants and the Library System Improvement Fund. The City's fiscal year 2009 capital expenditures for this project were $5,540.

- Construction was completed on the Carmel Valley Community Park South. This project provided for the development of a 15 useable acre community park in the Torrey Hills and Carmel Valley Neighborhoods south of State Route 56, located in Carmel Valley Neighborhood 8A. The City added $8,816 in capital infrastructure assets related to this project in fiscal year 2009.

- Construction began on the First Avenue Bridge Rehabilitation and Retrofit project. This project will provide for seismic retrofits to the abutments, expansion joints and bracing of the First Ave Bridge; as well as extensive hardware restoration and replacement. The project is part of the Uptown Community Plan. The City's fiscal year 2009 capital expenditures for this project were $3,714.

- Construction continued on the Bayshore Bikeway. The project provides for construction of a Class I bikeway from the northern end of 13th Street to Main Street at the I-5 interchange at the Southeast corner of San Diego Bay and will complete the missing segment of the planned bike path around San Diego Bay from Point Loma to Coronado. The project is funded by TransNet Major Corridor funds. The City's fiscal year 2009 capital expenditures for this project were $3,217.

Business-Type Activities

During fiscal year 2009, the Water Utility Fund added approximately $147,500 in capital improvement projects (CIP). Upgrades and expansion of the Miramar Water Treatment Plant, Otay Water Treatment Plant and the Alvarado Water Treatment Plant continued, along with water main replacements. Capital asset write-offs for fiscal year 2008 were approximately $8,100, and were primarily related to losses on abandoned projects and retirements of developer contributed assets.

During fiscal year 2009, the Sewer Utility Fund added approximately $49,500 in CIP, of which the Metropolitan system CIP increased approximately $4,900. Municipal system CIP increased approximately $44,600 and included the following major projects: Caltrans/SR–905 Otay Mesa Trunk Sewer, Pipeline Rehabilitation Phase C-1, and the continued replacement of sewer mains and upgrades to the sewer infrastructure. Capital asset write-offs for fiscal year 2008 were approximately $3,500, and were primarily related to losses on abandoned projects and retirements of developer contributed assets.

HIGHLIGHTS OF APPROVED FISCAL YEAR 2010 CAPITAL IMPROVEMENT PROJECTS (CIP) BUDGET

The Annual Approved Capital Improvements Budget for Fiscal Year 2010 is $478,400 which is a decrease of $108,600, or approximately 18.5% from the fiscal year 2009 budget of $587,000. The decrease in the Fiscal Year 2010 budget is primarily due to one-time financing and Proposition 1B funds which were included in the Fiscal Year 2009 Annual Capital Improvement budget for deferred maintenance needs. Water and Sewer projects comprise over 59.3% of the total CIP budget. Engineering & Capital Projects and General Services projects comprise 25.4%, and 2.5% of the total CIP budget, respectively. Funding for governmental projects include: TransNet funds; Facilities Benefit Assessments; Developer Impact Fees; developer contributions; federal, state, local, and private contributions; land sale proceeds; and deferred maintenance bonds. Highlights of the key budgets by department are as follows:

Governmental Activities

- Engineering and Capital Projects: $121,500 (25.4% of total CIP budget). Key projects include the undergrounding of City utilities to augment the California Public Utilities Commission (CPUC) Rule 20A funds, and conversion of City-owned street lighting and resurfacing of roadways associated with the undergrounding of utilities. The $48,900 annual allocation for these projects is entirely funded by the Underground Surcharge Fund. Other significant projects include: $11,100 for ADA improvements, $10,200 for Carroll Canyon Road, $3,500 for North Torrey Pines Road, and $3,000 for 43rd Street and Logan/National Ave Intersection.

- General Services: $12,200 (2.5% of total CIP budget). Key budgets include: $11,800 for deferred maintenance projects.

- Parks and Recreation: $29,400 (6.1% of total CIP budget). Planned project types for fiscal year 2010 include play area upgrades, joint use fields, accessibility improvements, comfort stations, picnic shelters, sports field and security lighting, new park development, and golf course improvements and upgrades.

- OneSD Support: $9,900 (2.1% of total CIP budget). This budget is for completion of the Enterprise Resource Planning (ERP) System.

- City Planning and Community Investments: $5,500 (1.1% of total CIP budget). This budget is for downtown parking improvement projects.

Business-Type Activities

The fiscal year 2010 Water Utility CIP budget is $149,800. There are no phase funded projects budgeted for fiscal year 2010. Significant projects include: $43,000 for water main replacements; $37,900 for the Alvarado Water Treatment Plant–Upgrade and Expansion; $15,700 for the Miramar Water Treatment Plant–Upgrade and Expansion; $9,400 for the North City Reclamation System.

The fiscal year 2010 Sewer Utility CIP budget is $134,100. There are no phase funded projects budgeted for fiscal year 2010. Significant projects include: $74,300 for pipeline repair, replacement, and rehabilitation; $39,200 for replacement of trunk sewers; $8,900 for repair and upgrade of pump stations; and $7,600 for the repair and upgrade of treatment plants.

CITY OF SAN DIEGO'S OUTSTANDING DEBT
(In Thousands)

	Governmental Activities		Business-Type Activities		Total Primary Government	
	2009	2008	2009	2008	2009	2008
Capital Lease Obligations	$ 89,519	$ 61,262	$ -	$ 166	$ 89,519	$ 61,428
Contracts Payable	4,715	2,615	-	-	4,715	2,615
Notes Payable	4,786	5,662	-	430,830	4,786	436,492
Loans Payable	44,815	34,777	90,326	95,875	135,141	130,652
Section 108 Loans	33,532	35,896	-	-	33,532	35,896
General Obligation Bonds	6,315	8,580	-	-	6,315	8,580
Revenue Bonds/COP's/ Lease Revenue Bonds	579,500	498,950	2,166,906	1,425,445	2,746,406	1,924,395
Special Assessment/ Special Tax Bonds	152,270	144,805	-	-	152,270	144,805
Tax Allocation Bonds	534,547	548,643	-	-	534,547	548,643
Tobacco Settlement Asset-Backed Bonds	95,380	99,370	-	-	95,380	99,370
Pooled Financing Bonds	33,460	34,115	-	-	33,460	34,115
Totals	$ 1,578,839	$ 1,474,675	$ 2,257,232	$ 1,952,316	$ 3,836,071	$ 3,426,991

LONG-TERM DEBT

At the end of fiscal year 2009, the City, including blended component units, had total debt outstanding of approximately $3,836,071. Of this amount, $6,315 is comprised of debt backed by the full faith and credit of the City. The remainder of the City's debt represents revenue bonds, lease revenue bonds, certificates of participation (COPs), special assessment bonds, tax allocation bonds, tobacco settlement asset-backed bonds, pooled financing bonds, contracts payable, notes payable, loans payable, Section 108 loans, SRF loans, and capital lease obligations.

Governmental Activities

- The City issued $12,365 of Community Facilities District No. 4 (Black Mountain Ranch Villages) Special Tax Bonds, Series 2008 A, to finance public improvements required in connection with the district, to fund the Reserve Fund, and to pay costs of issuance related to the 2008A Bonds. The 2008A bonds were issued pursuant to the Mello-Roos Community Facilities Act of 1982 and are limited obligations of the district.

- The City (PFFA) sold $103,000 of Lease Revenue Bonds, Series 2009A, on a private placement basis, for the purpose of financing various capital improvement projects. The 2009A bonds are secured from base rental payments and bear interest at a rate of 3.89% through June 1, 2010. Thereafter the rate will be fixed to equal the purchaser's internal cost of funds rate plus a fixed spread of 3.00%, but not to exceed 12% until the final maturity date of December 1, 2018.

- Total principal payments for long-term debt were $64,542. $48,356 of this amount was for outstanding bonds, $2,809 was for loans payable, $876 was for notes payable, and $12,501 was for capital leases. Readers interested in more detailed information regarding Governmental Activities Long Term Liabilities should refer to Note 5.

Business-Type Activities

- The City (PFFA) issued $157,190 of Water Revenue Bonds, Refunding Series 2009A for the following purposes: to prepay $57,000 of outstanding principal on the Subordinated Water Revenue Notes, Series 2007A; to partially refund $94,165 of Certificates of Undivided Interest, Series 1998; to fund the reserve; and to pay costs of issuance related to the Series 2009A Bonds. The publicly offered Water 2009A Revenue Refunding Bonds are secured by and payable solely from net system revenues of the Water Utility Fund.

- The City (PFFA) issued $453,775 of Senior Sewer Revenue Bonds, Series 2009A for the following purposes: to finance capital improvements to the Wastewater System; to pay in full $223,830 of Subordinate Sewer Revenue Notes, Series 2007; to partially refund $36,635 of Sewer Revenue Bonds, Series 1997A and $13,410 of Sewer Revenue Bonds, Series 1997B; to fund the reserve; and to pay costs of issuance related to the Series 2009A Bonds. The publicly offered Sewer 2009A Revenue Bonds are secured by and payable solely from wastewater system net revenues.

- The City (PFFA) issued $634,940 of Senior Sewer Revenue Refunding Bonds, Series 2009B for the following purposes: to fully refund $160,220 of outstanding Sewer Revenue Bonds, Series 1993; to partially refund $211,455 of Sewer Revenue Bonds, Series 1995; to partially refund $80,255 of Sewer Revenue Bonds, Series 1997A and $29,385 of Sewer Revenue Bonds, Series 1997B; to partially refund $97,845 of Sewer Revenue Bonds, Series 1999A and $54,015 of Sewer Revenue Bonds, Series 1999B; to fund the reserve; and to pay costs of issuance related to the Series 2009A Bonds. The publicly offered Sewer 2009B Revenue Refunding Bonds are secured by and payable solely from wastewater system net revenues.

- The City (PFFA) issued $328,060 of Water Revenue Bonds, Series 2009B for the following purposes: to finance capital improvements to the Water System; to prepay $150,000 of outstanding principal on the Subordinated Water Revenue Notes, Series 2008A; to fund the reserve; and to pay costs of issuance related to the series 2009B Bonds. The publicly offered Water 2009B Revenue Bonds are secured by and payable solely from net system revenues of the Water Utility Fund.

- Total principal payments for long-term debt were $1,269,049, of which $832,504 was for outstanding bonds, including $786,910 of bonds refunded or redeemed in advance of scheduled maturity date, and $45,594 of scheduled bond principal payments. $430,830 was for outstanding notes prepaid, $5,549 was for loans payable, and $166 was for capital leases. Readers interested in more detailed information regarding Business-Type Activities Long Term Liabilities should refer to Note 6.

As of the issuance of this report, the credit ratings on the City of San Diego's outstanding General Obligation Bonds, Revenue Bonds, Lease Revenue Bonds, and COPs are as follows:

	Moody's Investors Service	Fitch Ratings	Standard & Poor's
General Obligation Bonds	A2	A+	A
General Fund Backed Lease Revenue Bonds	Baa1/Baa2	A	A-
Outlook	Stable	Stable	Positive
Wastewater System Bonds	A2	AA-	A+
Outlook	Stable	Stable	Stable
Water System Bonds	A1/A2	AA-/A+	AA-/A+
Outlook	Stable	Stable	Stable

Section 90 of the City Charter provides that the general obligation bonded indebtedness for the development, conservation and furnishings of water shall not exceed 15% of the last preceding assessed valuation of all real and personal property of the City subject to direct taxation, and that the bonded indebtedness for other municipal improvements shall not exceed 10% of such valuation. The City's current outstanding general obligation balances as of June 30, 2009 are significantly less than the current debt limitations for water and other purposes, which are $5,962,975 and $3,975,316, respectively (see Statistical Section, Table 12).

It has been the City's practice, as provided for in Section 90.1 of the City Charter, to issue revenue bonds for the purpose of constructing water facilities. Per Section 90.1, revenue bonds do not constitute an indebtedness of the City, but an obligation payable from the revenues received by the utility. Section 90.2 authorizes the issuance of Revenue Bonds for the purpose of constructing improvements to the City's sewer system.

Additional information on the City's long-term debt can be found in the accompanying notes to the financial statements.

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of the City's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Office of the City Comptroller, 202 C Street, San Diego, California 92101, or e-mailed to comptroller@sandiego.gov. This financial report is also available on the City's website at www.sandiego.gov, under the Office of the City Comptroller. Additional information intended for the investor community is available on the Investor Information web page also located on the City's website listed above.

Basic Financial Statements

STATEMENT OF NET ASSETS
June 30, 2009
(In Thousands)

	Primary Government			Component Units	
	Governmental Activities	Business-Type Activities	Total	San Diego Convention Center Corporation	San Diego Housing Commission
ASSETS					
Cash and Investments	$ 1,320,591	$ 675,673	$ 1,996,264	$ 21,756	$ 94,458
Receivables:					
Taxes - Net	86,059	-	86,059	-	-
Accounts - Net of Allowance for Uncollectibles					
(Governmental $34,534, Business-Type $3,019)	39,226	79,546	118,772	2,537	6,991
Claims - Net	155	2	157	-	-
Contributions	360	-	360	-	-
Special Assessments - Net	2,993	-	2,993	-	-
Notes	122,948	-	122,948	-	169,532
Accrued Interest	4,421	2,535	6,956	-	18,288
Grants	35,702	3,606	39,308	-	-
Investment in Joint Venture	1,824	-	1,824	-	-
Advances to Other Agencies	5,777	-	5,777	-	-
Internal Balances	(7,929)	7,929	-	-	-
Inventories of Water in Storage	-	36,947	36,947	-	-
Inventories	2,033	622	2,655	15	54
Land Held for Resale	39,413	-	39,413	-	-
Prepaid Expenses	5,313	461	5,774	1,057	1,623
Restricted Cash and Investments	431,547	535,647	967,194	-	699
Deferred Charges	19,752	14,102	33,854	-	-
Capital Assets - Non-Depreciable	1,961,709	384,523	2,346,232	-	36,545
Capital Assets - Depreciable	2,493,816	4,382,198	6,876,014	16,404	60,683
TOTAL ASSETS	6,565,710	6,123,791	12,689,501	41,769	388,873

STATEMENT OF NET ASSETS
June 30, 2009
(In Thousands)

	Primary Government			Component Units	
	Governmental Activities	Business-Type Activities	Total	San Diego Convention Center Corporation	San Diego Housing Commission
LIABILITIES					
Accounts Payable	$ 46,526	$ 45,932	$ 92,458	$ 5,679	$ 2,905
Accrued Wages and Benefits	31,314	12,003	43,317	-	415
Other Accrued Liabilities	210	-	210	1,796	2,638
Interest Accrued on Long-Term Debt	24,488	17,761	42,249	-	124
Long-Term Liabilities Due Within One Year	158,140	76,352	234,492	3,077	1,753
Due to Other Agencies	188	11,308	11,496	-	-
Unearned Revenue	34,794	7,494	42,288	9,986	2,342
Contract Deposits	-	8,596	8,596	-	-
Sundry Trust Liabilities	5,711	-	5,711	-	-
Customer Deposits Payable	-	4,566	4,566	-	-
Deposits/Advances from Others	-	2,819	2,819	-	965
Long-Term Liabilities Due After One Year:					
Arbitrage Liability	533	-	533	-	-
Compensated Absences	39,534	6,356	45,890	-	-
Liability Claims	230,316	29,352	259,668	-	-
Capital Lease Obligations	73,556	-	73,556	531	-
Contracts Payable	4,715	-	4,715	-	-
Notes Payable	4,786	-	4,786	500	26,671
Loans Payable	36,107	84,673	120,780	-	-
Section 108 Loans Payable	31,075	-	31,075	-	-
Net Bonds Payable	1,364,345	2,147,103	3,511,448	-	-
Estimated Landfill Closure and Postclosure Care	-	19,336	19,336	-	-
Pollution Remediation Obligation	-	620	620	-	-
Net Other Post Employment Benefit Obligation	73,504	19,767	93,271	-	-
Net Pension Obligation	147,665	29,474	177,139	-	-
TOTAL LIABILITIES	2,307,507	2,523,512	4,831,019	21,569	37,813
NET ASSETS					
Invested in Capital Assets, Net of Related Debt	3,530,937	2,970,351	6,501,288	13,510	69,458
Restricted for:					
Capital Projects	293,284	-	293,284	-	-
Debt Service	-	4,372	4,372	-	-
Low-Moderate Income Housing	135,581	-	135,581	-	-
Nonexpendable Permanent Endowments	13,280	-	13,280	-	-
Other	122,460	38,113	160,573	1,452	128,863
Unrestricted	162,661	587,443	750,104	5,238	152,739
TOTAL NET ASSETS	$ 4,258,203	$ 3,600,279	$ 7,858,482	$ 20,200	$ 351,060

The accompanying notes are an integral part of the financial statements.

STATEMENT OF ACTIVITIES
Year Ended June 30, 2009
(In Thousands)

Functions/Programs	Expenses	Program Revenues: Charges for Services	Program Revenues: Operating Grants and Contributions	Program Revenues: Capital Grants and Contributions
Primary Government:				
Governmental Activities:				
General Government and Support	$ 303,581	$ 152,630	$ 13,449	$ 323
Public Safety - Police	418,549	42,178	14,054	-
Public Safety - Fire and Life Safety and Homeland Security	220,787	20,449	16,144	1
Parks, Recreation, Culture and Leisure	258,038	80,795	2,282	19,376
Transportation	239,305	18,360	10,572	77,277
Sanitation and Health	77,447	9,306	2,097	-
Neighborhood Services	116,735	21,814	34,646	13,825
Debt Service:				
Interest	84,070	-	-	-
TOTAL GOVERNMENTAL ACTIVITIES	1,718,512	345,532	93,244	110,802
Business-Type Activities:				
Airports	5,140	4,929	-	1,806
City Store	321	242	-	-
Development Services	47,260	37,310	-	-
Environmental Services	35,718	31,726	83	-
Golf Course	11,864	16,201	-	-
Recycling	20,067	16,027	227	-
Sewer Utility	314,125	322,571	167	28,780
Water Utility	329,748	342,719	1,262	30,277
TOTAL BUSINESS-TYPE ACTIVITIES	764,243	771,725	1,739	60,863
TOTAL PRIMARY GOVERNMENT	$ 2,482,755	$ 1,117,257	$ 94,983	$ 171,665
Component Units:				
San Diego Convention Center Corporation	$ 38,365	$ 30,774	$ 4,129	$ 143
San Diego Housing Commission	179,548	26,095	169,456	-
TOTAL COMPONENT UNITS	$ 217,913	$ 56,869	$ 173,585	$ 143

General Revenues:
- Property Taxes
- Transient Occupancy Taxes
- Other Local Taxes
- Developer Contributions and Fees
- Grants and Contributions not Restricted to Specific Programs
  - Sales Taxes
- Investment Income
- Gain on Sale of Capital Assets
- Miscellaneous

Transfers

TOTAL GENERAL REVENUES AND TRANSFERS

CHANGE IN NET ASSETS

Net Assets at Beginning of Year

NET ASSETS AT END OF YEAR

Net Revenue/(Expense) and Changes in Net Assets

Primary Government: Governmental Activities	Primary Government: Business-Type Activities	Primary Government: Total	Component Units: San Diego Convention Center Corporation	Component Units: San Diego Housing Commission
$ (137,179)	$ -	$ (137,179)	$ -	$ -
(362,317)	-	(362,317)	-	-
(184,194)	-	(184,194)	-	-
(155,585)	-	(155,585)	-	-
(133,096)	-	(133,096)	-	-
(66,043)	-	(66,043)	-	-
(46,450)	-	(46,450)	-	-
(84,070)	-	(84,070)	-	-
(1,168,934)	-	(1,168,934)	-	-
-	1,595	1,595	-	-
-	(79)	(79)	-	-
-	(9,950)	(9,950)	-	-
-	(3,909)	(3,909)	-	-
-	4,337	4,337	-	-
-	(3,813)	(3,813)	-	-
-	37,393	37,393	-	-
-	44,510	44,510	-	-
-	70,084	70,084	-	-
(1,168,934)	70,084	(1,098,850)	-	-
-	-	-	(3,319)	-
-	-	-	-	16,003
-	-	-	(3,319)	16,003
607,857	-	607,857	-	-
140,657	-	140,657	-	-
161,485	-	161,485	-	-
16,148	-	16,148	-	-
8,488	-	8,488	-	-
229,651	-	229,651	-	-
75,245	31,004	106,249	289	5,543
1,922	-	1,922	-	-
33,528	8,257	41,785	579	-
(1,225)	1,225	-	-	-
1,273,756	40,486	1,314,242	868	5,543
104,822	110,570	215,392	(2,451)	21,546
4,153,381	3,489,709	7,643,090	22,651	329,514
$ 4,258,203	$ 3,600,279	$ 7,858,482	$ 20,200	$ 351,060

The accompanying notes are an integral part of the financial statements.

GOVERNMENTAL FUNDS
BALANCE SHEET
JUNE 30, 2009
(In Thousands)

	General Fund	Other Governmental Funds	Total Governmental Funds
ASSETS			
Cash and Investments	$ 86,667	$ 1,085,808	$ 1,172,475
Receivables:			
Taxes - Net	69,438	16,621	86,059
Accounts - Net of Allowance for Uncollectibles (General Fund $7,032, Other Governmental $26,606)	13,891	24,159	38,050
Claims - Net	130	16	146
Special Assessments	-	2,993	2,993
Notes	-	122,948	122,948
Accrued Interest	906	3,497	4,403
Grants	-	35,702	35,702
From Other Funds	1,500	26	1,526
Interfund Loan Receivable	-	33,460	33,460
Advances to Other Funds	-	7,959	7,959
Advances to Other Agencies	-	5,777	5,777
Land Held for Resale	-	39,413	39,413
Prepaid Items	886	1,351	2,237
Investment in Joint Venture	1,824	-	1,824
Restricted Cash and Investments	-	431,547	431,547
TOTAL ASSETS	$ 175,242	$ 1,811,277	$ 1,986,519
LIABILITIES			
Accounts Payable	$ 3,789	$ 34,295	$ 38,084
Accrued Wages and Benefits	27,642	736	28,378
Other Accrued Liabilities	-	210	210
Due to Other Funds	2,095	5,993	8,088
Due to Other Agencies	-	188	188
Unearned Revenue	663	34,054	34,717
Deferred Revenue	26,661	58,784	85,445
Sundry Trust Liabilities	-	5,711	5,711
Advances from Other Funds	-	7,959	7,959
Interfund Loan Payable	-	36,947	36,947
TOTAL LIABILITIES	60,850	184,877	245,727

GOVERNMENTAL FUNDS
BALANCE SHEET
JUNE 30, 2009
(In Thousands)

	General Fund	Other Governmental Funds	Total Governmental Funds
FUND EQUITY:			
Fund Balances:			
Reserved for Land Held for Resale	-	39,413	39,413
Reserved for Notes Receivable	-	118,907	118,907
Reserved for Encumbrances	32,071	250,665	282,736
Reserved for Advances	-	13,736	13,736
Reserved for Low and Moderate Income Housing	-	95,668	95,668
Reserved for Permanent Endowments	-	13,280	13,280
Reserved for Debt Service	-	175,302	175,302
Reserved for Minority Interest in Joint Venture	1,824	-	1,824
Unreserved, Reported in General Fund:			
Designated for Unrealized Gains	1,943	-	1,943
Designated for Subsequent Years' Expenditures	207	-	207
Undesignated	78,347	-	78,347
Unreserved, Reported in:			
Special Revenue Funds	-	221,089	221,089
Debt Service Funds	-	265,236	265,236
Capital Projects Funds	-	430,479	430,479
Permanent Funds	-	2,625	2,625
TOTAL FUND EQUITY	114,392	1,626,400	1,740,792
TOTAL LIABILITIES AND FUND EQUITY	$ 175,242	$ 1,811,277	

Amounts reported for governmental activities in the Statement of Net Assets are different because:	
Capital assets used in governmental activities are not financial resources, and therefore, are not reported in the funds.	4,329,571
Other assets and liabilities used in governmental activities are not financial resources, and therefore, are either deferred or not reported in the funds.	105,197
Internal Service funds are used by management to charge the costs of activities such as Fleet Services, Print Shop, Self Insurance, and Central Stores to individual funds. The assets and liabilities of certain Internal Service Funds are included in governmental activities in the Statement of Net Assets.	6,826
Certain liabilities, including bonds payable, are not due and payable in the current period, and therefore, are not reported in the funds.	(1,924,183)
Net Assets of governmental activities	$ 4,258,203

The accompanying notes are an integral part of the financial statements.

GOVERNMENTAL FUNDS
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
YEAR ENDED JUNE 30, 2009
(In Thousands)

	General Fund	Other Governmental Funds	Total Governmental Funds
REVENUES			
Property Taxes	$ 398,743	$ 204,831	$ 603,574
Special Assessments	-	63,500	63,500
Sales Taxes	212,918	20,222	233,140
Transient Occupancy Taxes	73,765	66,892	140,657
Other Local Taxes	72,432	98,760	171,192
Licenses and Permits	31,249	8,100	39,349
Fines, Forfeitures and Penalties	32,467	1,939	34,406
Revenue from Use of Money and Property	41,461	66,323	107,784
Revenue from Federal Agencies	4,268	66,118	70,386
Revenue from Other Agencies	8,915	43,541	52,456
Revenue from Private Sources	-	21,593	21,593
Charges for Current Services	133,117	70,315	203,432
Other Revenue	5,296	20,415	25,711
TOTAL REVENUES	1,014,631	752,549	1,767,180
EXPENDITURES			
Current:			
General Government and Support	243,057	101,873	344,930
Public Safety - Police	389,390	17,267	406,657
Public Safety - Fire and Life Safety and Homeland Security	195,596	30,100	225,696
Parks, Recreation, Culture and Leisure	116,391	95,368	211,759
Transportation	72,635	90,334	162,969
Sanitation and Health	67,867	10,393	78,260
Neighborhood Services	17,255	56,530	73,785
Capital Projects	-	138,634	138,634
Debt Service:			
Principal Retirement	818	56,391	57,209
Interest	3,106	75,553	78,659
Cost of Issuance	-	1,001	1,001
TOTAL EXPENDITURES	1,106,115	673,444	1,779,559
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	(91,484)	79,105	(12,379)
OTHER FINANCING SOURCES (USES)			
Transfers from Proprietary Funds	6,267	1,979	8,246
Transfers from Other Funds	105,059	216,685	321,744
Transfers to Proprietary Funds	(4,043)	(2,547)	(6,590)
Transfers to Other Funds	(26,031)	(295,713)	(321,744)
Net Loss from Joint Venture	(157)	-	(157)
Proceeds from the Sale of Capital Assets	-	2,157	2,157
Capital Leases	-	30,392	30,392
Contracts Issued	-	2,100	2,100
Loans Issued	-	10,483	10,483
Special Tax Bonds Issued	-	12,365	12,365
Revenue Bonds Issued	-	103,000	103,000
Discount on Bonds Issued	-	(129)	(129)
TOTAL OTHER FINANCING SOURCES (USES)	81,095	80,772	161,867
NET CHANGE IN FUND BALANCES	(10,389)	159,877	149,488
Fund Balances at Beginning of Year	124,781	1,466,523	1,591,304
FUND BALANCES AT END OF YEAR	$ 114,392	$ 1,626,400	$ 1,740,792

The accompanying notes are an integral part of the financial statements.

City of San Diego
Reconciliation of the Statement of Revenues, Expenditures, and
Changes in Fund Balances of Governmental Funds
to the Statement of Activities
Year Ended June 30, 2009
(In Thousands)

Net change in fund balances - total governmental funds (page 58)	$ 149,488
Governmental funds report capital outlays as expenditures. However, in the Statement of Activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which capital outlays exceeded depreciation in the current period.	121,730
The net effect of various miscellaneous transactions involving capital assets (i.e., donations, retirements, and transfers) is to decrease net assets.	(17,686)
Revenues in the Statement of Activities that do not provide current financial resources are not reported as revenues in the funds.	10,410
The issuance of long-term debt (i.e., bonds, leases) provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net assets. This amount is the net effect of these differences in the treatment of long-term debt and related items.	(100,854)
Some expenses reported in the Statement of Activities do not require the use of current financial resources (i.e., compensated absenses, net pension obligation), and therefore are not accrued as expenses in governmental funds.	(92,248)
Internal Service funds are used by management to charge the costs of activities such as Fleet Services, Publishing Services, Central Stores, Self Insurance, and others to individual funds. The net revenue of certain internal service activities is reported with governmental activities.	33,982
Change in net assets of governmental activities (page 55)	$ 104,822

The accompanying notes are an integral part of the financial statements.

PROPRIETARY FUNDS
STATEMENT OF NET ASSETS
JUNE 30, 2009
(In Thousands)

	Business-Type Activities - Enterprise Funds				
	Sewer Utility	Water Utility	Other Enterprise Funds	Total	Internal Service Funds
ASSETS					
Current Assets:					
Cash and Investments	$ 345,933	$ 225,556	$ 104,184	$ 675,673	$ 148,116
Receivables:					
Accounts - Net of Allowance for Uncollectibles (Sewer $930, Water $1,749, Other Enterprise $340, Internal Service $896)	35,172	43,573	801	79,546	1,176
Claims - Net	-	-	2	2	9
Contributions	-	-	-	-	360
Accrued Interest	1,420	604	511	2,535	18
Grants	-	1,822	1,784	3,606	-
From Other Funds	-	-	3,609	3,609	5,980
Inventories of Water in Storage	-	36,947	-	36,947	-
Inventories	-	620	2	622	2,033
Prepaid Expenses	3	456	2	461	3,076
Total Current Assets	382,528	309,578	110,895	803,001	160,768
Non-Current Assets:					
Restricted Cash and Investments	231,212	263,883	40,552	535,647	-
Deferred Charges	7,114	6,988	-	14,102	-
Interfund Loan Receivable	3,487	-	-	3,487	-
Capital Assets - Non-Depreciable	118,881	240,760	24,882	384,523	1,984
Capital Assets - Depreciable	2,710,102	1,611,573	60,523	4,382,198	123,970
Total Non-Current Assets	3,070,796	2,123,204	125,957	5,319,957	125,954
TOTAL ASSETS	3,453,324	2,432,782	236,852	6,122,958	286,722
LIABILITIES					
Current Liabilities:					
Accounts Payable	11,995	32,367	1,570	45,932	8,442
Accrued Wages and Benefits	7,682	2,145	2,176	12,003	2,936
Interest Accrued on Long-Term Debt	6,162	11,598	1	17,761	269
Long-Term Debt Due Within One Year	54,663	19,705	1,984	76,352	55,267
Due to Other Funds	510	558	147	1,215	1,812
Due to Other Agencies	10,262	1,046	-	11,308	-
Unearned Revenue	-	817	6,677	7,494	77
Contract Deposits	3,503	4,756	337	8,596	-
Current Liabilities Payable from Restricted Assets:					
Customer Deposits Payable	-	4,566	-	4,566	-
Total Current Liabilities	94,777	77,558	12,892	185,227	68,803
Non-Current Liabilities:					
Deposits/Advances from Others	250	-	2,569	2,819	-
Compensated Absences	2,323	2,036	1,997	6,356	3,795
Liability Claims	27,776	1,576	-	29,352	178,126
Capital Lease Obligations	-	-	-	-	21,221
Loans Payable	67,100	17,573	-	84,673	-
Net Revenue Bonds Payable	1,251,957	895,146	-	2,147,103	-
Estimated Landfill Closure and Postclosure Care	-	-	19,336	19,336	-
Pollution Remediation Obligation	-	620	-	620	-
Net Other Post Employment Benefit Obligation	6,916	6,578	6,273	19,767	2,978
Net Pension Obligation	10,785	8,477	10,212	29,474	2,925
Total Non-Current Liabilities	1,367,107	932,006	40,387	2,339,500	209,045
TOTAL LIABILITIES	1,461,884	1,009,564	53,279	2,524,727	277,848
NET ASSETS					
Invested in Capital Assets, Net of Related Debt	1,698,249	1,186,697	85,405	2,970,351	97,195
Restricted for Debt Service	750	3,622	-	4,372	-
Restricted for Closure/Postclosure Maintenance	-	-	38,113	38,113	-
Unrestricted	292,441	232,899	60,055	585,395	(88,321)
TOTAL NET ASSETS	$ 1,991,440	$ 1,423,218	$ 183,573	3,598,231	$ 8,874
Adjustment to reflect the consolidation of Internal Service Fund activities related to Enterprise Funds.				2,048	
Net assets of Business-Type activities				$ 3,600,279	

The accompanying notes are an integral part of the financial statements.

PROPRIETARY FUNDS
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
YEAR ENDED JUNE 30, 2009
(In Thousands)

	Business-Type Activities - Enterprise Funds				
	Sewer Utility	Water Utility	Other Enterprise Funds	Total	Internal Service Funds
OPERATING REVENUES					
Sales of Water	$ -	$ 324,772	$ -	$ 324,772	$ -
Charges for Services	318,474	-	58,789	377,263	160,937
Revenue from Use of Property	-	5,418	-	5,418	-
Usage Fees	-	1,272	45,672	46,944	81,001
Other	4,097	11,257	1,974	17,328	883
TOTAL OPERATING REVENUES	322,571	342,719	106,435	771,725	242,821
OPERATING EXPENSES					
Benefit and Claim Payments	-	-	-	-	58,416
Maintenance and Operations	119,470	95,979	81,621	297,070	46,347
Cost of Materials Issued	-	-	-	-	29,149
Cost of Purchased Water Used	-	133,499	-	133,499	-
Taxes	-	162	-	162	-
Administration	71,300	33,258	34,138	138,696	55,715
Depreciation	76,554	39,627	5,797	121,978	26,513
TOTAL OPERATING EXPENSES	267,324	302,525	121,556	691,405	216,140
OPERATING INCOME (LOSS)	55,247	40,194	(15,121)	80,320	26,681
NONOPERATING REVENUES (EXPENSES)					
Earnings on Investments	13,454	12,478	5,075	31,007	5,182
Federal Grant Assistance	-	192	27	219	-
Other Agency Grant Assistance	167	1,070	283	1,520	123
Loss on Sale/Retirement of Capital Assets	(3,525)	(2,436)	(814)	(6,775)	(236)
Debt Service Interest Expense	(46,151)	(28,081)	(3)	(74,235)	(971)
Other	5,244	751	2,262	8,257	10,461
TOTAL NONOPERATING REVENUES (EXPENSES)	(30,811)	(16,026)	6,830	(40,007)	14,559
INCOME BEFORE CONTRIBUTIONS AND TRANSFERS	24,436	24,168	(8,291)	40,313	41,240
Capital Contributions	28,780	30,277	1,806	60,863	198
Transfers from Other Funds	616	439	276	1,331	163
Transfers from Governmental Funds	1,238	3,443	2,617	7,298	5,723
Transfers to Other Funds	(59)	(99)	(63)	(221)	(1,273)
Transfers to Governmental Funds	(3,550)	(530)	(2,464)	(6,544)	(4,539)
CHANGE IN NET ASSETS	51,461	57,698	(6,119)	103,040	41,512
Net Assets at Beginning of Year	1,939,979	1,365,520	189,692		(32,638)
NET ASSETS AT END OF YEAR	$ 1,991,440	$ 1,423,218	$ 183,573		$ 8,874
Adjustment to reflect the consolidation of Internal Service Fund activities related to Enterprise Funds.				7,530	
Change in net assets of Business-Type activities				$ 110,570	

The accompanying notes are an integral part of the financial statements.

PROPRIETARY FUNDS
STATEMENT OF CASH FLOWS
YEAR ENDED JUNE 30, 2009
(In Thousands)

	Business-Type Activities - Enterprise Funds				
	Sewer Utility	Water Utility	Other Enterprise Funds	Total	Internal Service Funds
CASH FLOWS FROM OPERATING ACTIVITIES					
Receipts from Customers and Users	$ 327,771	$ 277,717	$ 90,607	$ 696,095	$ 3,182
Receipts from Interfund Services Provided	2,688	65,945	18,305	86,938	250,022
Payments to Suppliers	(120,624)	(262,356)	(41,838)	(424,818)	(104,650)
Payments to Employees	(41,702)	(567)	(61,907)	(104,176)	(90,710)
Payments for Interfund Services Used	(34,733)	(13,779)	(7,609)	(56,121)	(2,739)
NET CASH PROVIDED BY (USED FOR) OPERATING ACTIVITIES	133,400	66,960	(2,442)	197,918	55,105
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES					
Transfers from Other Funds	616	406	276	1,298	162
Transfers from Governmental Funds	1,238	186	2,617	4,041	2,550
Transfers to Other Funds	(26)	(99)	(62)	(187)	(1,273)
Transfers to Governmental Funds	(998)	(477)	(2,464)	(3,939)	(4,307)
Operating Grants Received	167	1,012	238	1,417	123
Proceeds from Advances and Deposits	-	235	2,569	2,804	-
Payments for Advances and Deposits	-	-	(25)	(25)	-
NET CASH PROVIDED (USED FOR) NONCAPITAL FINANCING ACTIVITIES	997	1,263	3,149	5,409	(2,745)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES					
Proceeds from Contracts, Notes and Loans	-	-	-	-	10,362
Proceeds from Revenue Bonds	217,469	179,729	-	397,198	-
Proceeds from Capital Contributions	10,361	7,631	973	18,965	-
Acquisition of Capital Assets	(55,809)	(150,587)	(6,580)	(212,976)	(49,169)
Proceeds from the Sale of Capital Assets	-	5,707	-	5,707	3,358
Principal Payments on Capital Leases	-	-	(166)	(166)	(7,055)
Principal Payments on Contracts, Notes and Loans	(4,654)	(895)	-	(5,549)	-
Principal Payments on Revenue Bonds	(31,700)	(13,894)	-	(45,594)	-
Interest Paid on Long-Term Debt	(44,670)	(29,625)	(11)	(74,306)	(1,046)
NET CASH PROVIDED BY (USED FOR) CAPITAL AND RELATED FINANCING ACTIVITIES	90,997	(1,934)	(5,784)	83,279	(43,550)
CASH FLOWS FROM INVESTING ACTIVITIES					
Sales of Investments	988,652	1,671,625	-	2,660,277	-
Purchases of Investments	(1,173,015)	(1,759,692)	-	(2,932,707)	-
Interest Received on Investments	13,671	13,914	5,632	33,217	5,202
NET CASH PROVIDED BY (USED FOR) INVESTING ACTIVITIES	(170,692)	(74,153)	5,632	(239,213)	5,202
Net Increase (Decrease) in Cash and Cash Equivalents	54,702	(7,864)	555	47,393	14,012
Cash and Cash Equivalents at Beginning of Year	291,240	241,215	144,181	676,636	134,104
CASH AND CASH EQUIVALENTS AT END OF YEAR	$ 345,942	$ 233,351	$ 144,736	$ 724,029	$ 148,116
Reconciliation of Cash and Cash Equivalents at End of Year to the Statement of Net Assets:					
Cash and Investments	$ 345,933	$ 225,556	$ 104,184	$ 675,673	$ 148,116
Restricted Cash & Investments	231,212	263,883	40,552	535,647	-
Less Investments not meeting the definition of cash equivalents	(231,203)	(256,088)	-	(487,291)	-
Total Cash and Cash Equivalents at End of Year	$ 345,942	$ 233,351	$ 144,736	$ 724,029	$ 148,116
Reconciliation of Operating Income (Loss) to Net Cash Provided by (Used For) Operating Activities:					
Operating Income (Loss)	$ 55,247	$ 40,194	$ (15,121)	$ 80,320	$ 26,681
Adjustments to Reconcile Operating Income (Loss) to Net Cash Provided By (Used For) Operating Activities:					
Depreciation	76,554	39,627	5,797	121,978	26,513
(Increase) Decrease in Assets:					
Accounts Receivable - Net	2,455	281	63	2,799	(955)
Claims Receivable - Net	-	-	(2)	(2)	2
Contributions Receivable	-	-	-	-	39
Due from Other Funds	-	-	464	464	-
Inventories	-	(511)	76	(435)	72
Prepaid Expenses	5	(10)	10	5	(710)
Increase (Decrease) in Liabilities:					
Accounts Payable	(3,287)	(9,719)	8	(12,998)	(8,252)
Accrued Wages and Benefits	(2,052)	328	193	(1,531)	(296)
Due to Other Funds	(696)	(684)	(134)	(1,514)	(131)
Due to Other Agencies	7,365	(1,525)	-	5,840	-
Unearned Revenue	-	(326)	(372)	(698)	(49)
Contract Deposits	189	237	62	488	-
Arbitrage Liability	(157)	(429)	-	(586)	-
Compensated Absences	(197)	18	(505)	(684)	(362)
Liability Claims	(11,374)	(6,012)	-	(17,386)	2,331
Estimated Landfill Closure and Postclosure Care	-	-	907	907	-
Pollution Remediation Obligation	-	620	-	620	-
Net OPEB Obligation	3,878	3,919	3,652	11,449	1,237
Net Pension Obligation	226	201	198	625	(2,401)
Other Nonoperating Revenue	5,244	751	2,262	8,257	11,386
Total Adjustments	78,153	26,766	12,679	117,598	28,424
NET CASH PROVIDED BY (USED FOR) OPERATING ACTIVITIES	$ 133,400	$ 66,960	$ (2,442)	$ 197,918	$ 55,105
Noncash Investing, Capital, and Financing Activites:					
Capital Leases	$ -	$ -	$ -	$ -	$ 10,366
Developer Contributed Assets	18,419	22,646	-	41,065	198
Increase (Decrease) in Capital Assets related Accounts Payable	7,632	4,530	(382)	11,780	(6,246)
Noncash Retirement of Capital Assets	(3,525)	(8,142)	(814)	(12,481)	(318)
Contributions of Capital Assets from Governmental Activities	-	3,257	-	3,257	3,174
Proceeds of Refunding Bonds Issued	907,050	301,165	-	1,208,215	-
Repayment of Refunding Bonds to Escrow	(907,050)	(301,165)	-	(1,208,215)	-
Interest Fund Credits for Debt Service Payments	(13,281)	(5,186)	-	(18,467)	-

The accompanying notes are an integral part of the financial statements.

FIDUCIARY FUNDS
STATEMENT OF FIDUCIARY NET ASSETS
June 30, 2009
(In Thousands)

	Pension & Employee Savings Trust	Investment Trust	Agency
ASSETS			
Cash or Equity in Pooled Cash and Investments	$ 4,616	$ 4,637	$ 29,253
Cash with Custodian/Fiscal Agent	371,762	-	-
Investments at Fair Value:			
Short Term Investments	33,311	-	-
Domestic Fixed Income Securities (Bonds)	861,555	-	-
International Fixed Income Securities (Bonds)	143,677	-	-
Domestic Equity Securities (Stocks)	1,444,848	-	-
International Equity Securities (Stocks)	614,246	-	-
Real Estate Equity and Real Estate Securities	350,498	-	-
Defined Contribution Investments	673,922	-	-
Receivables:			
Accounts - Net	-	-	120
Contributions	16,957	-	-
Accrued Interest	13,135	38	15
Loans	32,559	-	-
Securities Sold	81,077	-	-
Prepaid Expenses	73	-	-
Securities Lending Collateral	395,085	-	-
Restricted Cash and Investments	-	-	10,205
Capital Assets - Depreciable	1,275	-	-
TOTAL ASSETS	5,038,596	4,675	$ 39,593
LIABILITIES			
Accounts Payable	6,113	-	$ -
Accrued Wages and Benefits	783	-	-
Deposits/Advances from Others	7,200	-	10,977
Sundry Trust Liabilities	-	-	28,616
DROP Liability	360,758	-	-
Net Other Post Employment Benefit Obligation	607	-	-
Net Pension Obligation	628	-	-
Securities Lending Obligations	395,085	-	-
Securities Purchased	203,700	-	-
TOTAL LIABILITIES	974,874	-	$ 39,593
NET ASSETS			
Held in Trust for Pension Benefits and Other Purposes	$ 4,063,722	$ 4,675	

The accompanying notes are an integral part of the financial statements.

FIDUCIARY FUNDS
STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS
Year Ended June 30, 2009
(In Thousands)

	Pension & Employee Savings Trust	Investment Trust	Total
ADDITIONS			
Employer Contributions	$ 248,677	$ -	$ 248,677
Employee Contributions	95,345	-	95,345
Retiree Contributions	7,483	-	7,483
Contributions to Pooled Investments	-	4,574	4,574
Earnings on Investments:			
Investment Income (Loss)	(1,012,535)	159	(1,012,376)
Investment Expense	(19,661)	-	(19,661)
Net Investment Income (Loss)	(1,032,196)	159	(1,032,037)
Securities Lending Income:			
Gross Earnings	11,607	-	11,607
Borrower Rebates	(4,944)	-	(4,944)
Administrative Expenses (Lending Agent)	(1,754)	-	(1,754)
Net Securities Lending Income	4,909	-	4,909
Other Income:			
Litigation Proceeds	325	-	325
TOTAL OPERATING ADDITIONS	(675,457)	4,733	(670,724)
DEDUCTIONS			
DROP Interest Expense	27,098	-	27,098
Benefit and Claim Payments	373,495	-	373,495
Distributions from Pooled Investments	-	4,484	4,484
Administration	15,057	-	15,057
TOTAL OPERATING DEDUCTIONS	415,650	4,484	420,134
CHANGE IN NET ASSETS	(1,091,107)	249	(1,090,858)
Net Assets at Beginning of Year	5,154,829	4,426	5,159,255
NET ASSETS AT END OF YEAR	$ 4,063,722	$ 4,675	$ 4,068,397

The accompanying notes are an integral part of the financial statements.

NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED JUNE 30, 2009

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (In Thousands)

The City of San Diego (the "City") adopted its current charter on April 7, 1931 and operates as a municipality in accordance with State laws. Since adoption, the City Charter has been amended several times. The most recent amendments were added with voter approval of Propositions C and D in the November 4, 2008 election. Proposition C amended the City Charter to designate the use of lease revenues from Mission Bay Park, exceeding certain thresholds, 75% for capital improvements in Mission Bay Park and 25% for capital improvements in other coastal and regional parks. Proposition D amended the Municipal Code section 56.54 to make consumption of alcoholic beverages unlawful at all City parks.

The accounting policies of the City conform to accounting principles generally accepted in the United States of America ("GAAP") as applicable to governmental units. The following is a summary of the City's significant accounting policies:

a. Financial Reporting Entity

As required by GAAP, these financial statements present the primary government and its component units, entities for which the primary government is considered to be financially accountable.

Blended component units, although legally separate entities, are, in substance, part of the primary government's operations and as a result, data from these units are combined with data of the primary government (references within this document to "the City" are referring to the primary government). Component units should be included in the reporting entity financial statements using the blending method if either of the following criteria is met:

i. The component unit's governing body is substantively the same as the governing body of the primary government (the City).

ii. The component unit provides services entirely, or almost entirely, to the primary government or otherwise exclusively, or almost exclusively, benefits the primary government even though it does not provide services directly to it.

Included within the reporting entity as blended component units are the following:

- Centre City Development Corporation
- City of San Diego/Metropolitan Transit Development Board Authority
- Community Facilities and Other Special Assessment Districts
- Convention Center Expansion Financing Authority
- Public Facilities Financing Authority
- Redevelopment Agency of the City of San Diego
- San Diego Data Processing Corporation
- San Diego Facilities and Equipment Leasing Corporation
- San Diego Industrial Development Authority
- San Diego Open Space Park Facilities District #1
- Southeastern Economic Development Corporation
- San Diego City Employees' Retirement System
- Tobacco Settlement Revenue Funding Corporation
- Tourism Marketing District

A brief description of each blended component unit follows:

- Centre City Development Corporation, Inc. (CCDC) is a not-for-profit public benefit corporation established in 1975 to administer certain redevelopment projects in downtown San Diego and to provide redevelopment advisory services to the Redevelopment Agency of the City of San Diego. The City Council elects the Board of Directors. CCDC's budget and governing board are approved by the Redevelopment Agency of the City of San Diego and services are provided exclusively to the primary government. CCDC is reported as a governmental fund. Financial statements can be requested from Centre City Development Corporation, 401 B Street- Fourth Floor, San Diego, California 92101.

- The City of San Diego/Metropolitan Transit Development Board Authority (MTDB Authority) is a financing authority which was established in 1988 to acquire and construct mass transit guide ways, public transit systems, and related transportation facilities primarily benefiting the residents of the City of San Diego. The Mayor appoints, with Council confirmation, two public members and the MTS Board appoints one MTS boardmember to the governing board of the MTDB Authority. The MTDB Authority primarily provides services to the primary government. The MTDB Authority is reported as a governmental fund. Financial statements can be requested from the Office of the City Comptroller, 202 C Street, San Diego, California 92101.

- The City maintains various Community Facilities, Maintenance Assessment, and Business Improvement Districts to pay for the construction, maintenance and improvement of community facilities and infrastructure. The governing body of Special Assessment Districts and Community Facilities Districts (special districts) is the City Council. Among its duties, it approves the budgets of special districts, parcel fees, special assessments, and special taxes. The special districts are reported in governmental fund types.

- The Convention Center Expansion Financing Authority (CCEFA) was established in 1996 to acquire and construct the expansion of the existing convention center. During the period reported, the CCEFA was governed by a board consisting of the Mayor [the City Manager] the Director of the Port of San Diego, and a member of the Board of Commissioners for the Port of San Diego. Under the strong mayor form of government, the City Manager position does not exist and therefore is currently vacant. The CCEFA provides services which primarily benefit the primary government. CCEFA is reported as a governmental fund. Financial statements can be requested from the Office of the City Comptroller, 202 C Street, San Diego, California 92101.

- The Public Facilities Financing Authority (PFFA) was established in 1991 by the City and the Redevelopment Agency to acquire and construct public capital improvements. PFFA is governed by a board of commissioners composed of the City Treasurer, the assistant executive director of the Redevelopment Agency and three members of the public appointed by the Mayor and confirmed by the Council. PFFA provides services exclusively to the primary government. Financing for governmental funds is reported as a governmental activity and financing for enterprise funds is reported as a business-type activity. Financial statements can be requested from the Office of the City Comptroller, 202 C Street, San Diego, California 92101.

- The Redevelopment Agency of the City of San Diego (RDA) was established in 1958 in order to provide a method for revitalizing deteriorating and blighted areas of the City and began functioning in 1969 under the authority granted by the community redevelopment law. The City Council is the governing board sitting as the Board of Directors of the RDA, and the RDA is reported as a governmental fund. Complete stand-alone financial statements can be requested from the Office of the City Comptroller, 202 C Street, San Diego, California 92101.

- San Diego Data Processing Corporation (SDDPC) was formed in 1979 as a not-for-profit public benefit corporation for the purpose of providing data processing services. SDDPC's budget and governing board are approved by the City Council. SDDPC provides services almost exclusively to the primary government. SDDPC is reported as an Internal Service Fund. Financial statements can be requested from San Diego Data Processing Corporation, 5975 Santa Fe Street, San Diego, California 92109.

- The San Diego Facilities and Equipment Leasing Corporation (SDFELC) is a not-for-profit public benefit corporation established in 1987 for the purpose of acquiring and leasing to the City real and personal property to be used in the municipal operations of the City. The SDFELC is governed by a three member board consisting of the City Attorney, the Chief Financial Officer and the Mayor (as City Manager) and services are provided exclusively to the primary government. Financing for governmental funds is reported as a governmental activity and financing for enterprise funds is reported as a business-type activity. Financial statements can be requested from the Office of the City Comptroller, 202 C Street, San Diego, California 92101.

- The San Diego Industrial Development Authority (SDIDA) was established in 1983 by the City for the purpose of providing an alternate method of financing to participating parties for economic development purposes. The City Council is the governing board. SDIDA is reported as a governmental fund. Financial statements can be requested from the Office of the City Comptroller, 202 C Street, San Diego, California 92101.

- The San Diego Open Space Park Facilities District #1 (SDOSPFD) was established in 1978 by the City for the purpose of acquiring open space properties to implement the Open Space Element of the City's General Plan. The boundaries are contiguous with those of the City. The City Council is the governing board. SDOSPFD is reported as a governmental fund. Financial statements can be requested from the Office of the City Comptroller, 202 C Street, San Diego, California 92101.

- Southeastern Economic Development Corporation (SEDC) is a not-for-profit public benefit corporation organized in 1980 by the City to administer certain redevelopment projects in southeast San Diego and to perform economic development services in its area of influence. SEDC's budget and governing board are approved by the Redevelopment Agency and services are provided exclusively to the primary government. SEDC is reported as a governmental fund. Financial statements can be requested from the Southeastern Economic Development Corporation, 995 Gateway Center Way, Suite 300, San Diego, California 92102.

- San Diego City Employees' Retirement System (SDCERS) was established in 1927 by the City and administers retirement, post employment healthcare, disability, and death benefits. Currently, SDCERS also administers the Port of San Diego and the San Diego County Regional Airport Authority defined benefit plans.

  SDCERS is a legally separate, blended component unit of the City of San Diego. It is managed by a Board of Administration, the majority of which is appointed by the City of San Diego, and a Pension Administrator who does not report to, or work under the direction of the elected officials or appointed managers of the City of San Diego. SDCERS provides services almost exclusively to the primary government. Additionally, during the period reported, SDCERS utilized legal counsel independent of the City of San Diego. As such, the City does not maintain direct operational oversight of SDCERS or its financial reports.

  SDCERS is reported as a pension and employee savings trust fund. Complete stand-alone financial statements can be requested from the San Diego City Employees' Retirement System, 401 West A Street, Suite 400, San Diego, California 92101.

- The Tobacco Settlement Revenue Funding Corporation (TSRFC) is a not-for-profit public benefit corporation established in 2006 for the purpose of acquiring the tobacco settlement revenues allocated to the City from the State of California, pursuant to the Master Settlement Agreement. TSRFC is governed by the Board of Directors which consists of the Chief Operating Officer, the Chief Financial Officer, and one independent director. The independent director shall be appointed by the Mayor or the remaining directors. TSRFC is reported as a governmental fund. Financial statements can be requested from the Office of the City Comptroller, 202 C Street, San Diego, California, 92101.

- The Tourism Marketing District (TMD) is an assessment district created, in fiscal year 2008, by the City on behalf of larger hotel and motel operators within the City. The TMD provides for tourism development, including coordinated joint marketing and promotion of San Diego, in order to maintain and expand the tourism industry. The TMD procedural ordinance establishes a method by which benefited businesses may be assessed for the cost of activities associated with tourism development within their respective area. The governing body of the TMD is the City Council. Among its duties, TMD will initiate proceedings to establish a district upon submission of a written petition, signed by the business owners in the proposed district who will pay more than 50 percent of the assessments proposed to be levied, and will approve the district management plan which includes an annual budget, frequency for levying assessments, and number of years assessments will be levied. The TMD is reported as a governmental fund.

Discretely presented component units, which are also legally separate entities, have financial data reported in a separate column from the financial data of the primary government to demonstrate they are financially and legally separate from the primary government.

There are two entities which are discretely presented component units:

- San Diego Convention Center Corporation (SDCCC)

  SDCCC is a not-for-profit public benefit corporation originally organized to market operate and maintain the San Diego Convention Center. San Diego Theaters Inc. is a non-profit subsidiary of SDCCC created in 2003 to operate the San Diego Civic Theater and the restored Balboa Theater. The City is the sole member of SDCCC and acts through the San Diego City Council in accordance with the City Charter and the City's Municipal Code. The City appoints seven voting members out of the nine-member Board of Directors of SDCCC. The City is liable for any operating deficits and would be secondarily liable for any debt issuances of SDCCC. SDCCC is discretely presented because it provides services directly to the citizens. Complete stand-alone financial statements can be requested from San Diego Convention Center Corporation, 111 West Harbor Drive, San Diego, California 92101.

- San Diego Housing Commission (SDHC)

  SDHC is a government agency which was formed by the City under Ordinance No. 2515 on December 5, 1978 in accordance with the Housing Authority Law of the State of California. SDHC primarily serves low-income families by providing rental assistance payments, rental housing, loans and grants to individuals and not-for-profit organizations and other services. Members of the Board of Commissioners are appointed by the Mayor and confirmed by the City Council. SDHC is discretely presented because it provides services directly to the citizens. Complete stand-alone financial statements can be requested from San Diego Housing Commission, 1122 Broadway, Suite 300, San Diego, California 92101.

Each blended and discretely presented component unit has a June 30 fiscal year-end.

b. Government-Wide and Fund Financial Statements

The government-wide financial statements (i.e., the Statement of Net Assets and the Statement of Activities) report information on all of the non-fiduciary activities of the primary government and its component units. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. Likewise, the primary government is reported discretely from certain legally separate component units for which the primary government is financially accountable.

The Statement of Activities demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenues. Direct expenses are those that are clearly identifiable as to a specific function or segment. Direct expenses reported include administrative and overhead charges. Program revenues include (1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and (2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenues and contributions.

Separate financial statements are provided for governmental funds, proprietary funds, and fiduciary funds, the latter of which are excluded from the government-wide financial statements. Major individual governmental funds and major individual enterprise funds are reported as separate columns in the fund financial statements.

c. Measurement Focus, Basis of Accounting, and Financial Statement Presentation

Government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting, as are the proprietary and fiduciary funds financial statements. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements have been met.

The business-type activities and proprietary funds financial statements apply all effective pronouncements of the Governmental Accounting Standards Board ("GASB"). In addition, these statements apply all Accounting Principles Board Opinions ("APBO") and Financial Accounting Standards Board ("FASB") Statements and Interpretations issued on or before November 30, 1989, except those that conflict with GASB pronouncements. The City has elected not to apply all FASB Statements and Interpretations issued after November 30, 1989.

As a general rule, the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are payments-in-lieu of taxes and other charges between the government's water and sewer functions and various other functions of the government. Elimination of these charges would distort the direct costs and program revenues reported for the various functions concerned.

All internal service funds, except for the Special Engineering Fund, have been included within governmental activities in the government-wide financial statements since they predominantly benefit governmental functions. The Special Engineering Fund, which services exclusively water and sewer activities, has been included within business-type activities in the government-wide financial statements.

Amounts reported as program revenues include (1) charges to customers for goods, services, or privileges provided, (2) operating grants and contributions, and (3) capital grants and contributions, including special assessments. General revenues include all taxes and investment income.

Governmental funds financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period.

Revenues which are considered susceptible to accrual include: real and personal property taxes; other local taxes; franchise fees; fines, forfeitures and penalties; motor vehicle license fees; rents and concessions; interest; and state and federal grants and subventions, provided they are received within 60 days from the end of the fiscal year.

Licenses and permits, including parking citations and miscellaneous revenues are recorded as revenues when received in cash because they generally are not measurable until actually received.

Expenditures are recognized when the related fund liability is incurred except for (1) principal and interest of general long-term debt which are recognized when due; and (2) employee annual leave and claims and judgments from litigation which are recorded in the period due and payable since such amounts will not currently be liquidated with expendable available financial resources.

The governmental funds financial statements do not present long-term debt, but the related debt is shown in the reconciliation of the Governmental Funds Balance Sheet to the Government-Wide Statement of Net Assets. Bond premiums, discounts and issuance costs are recognized during the current period.

Permanent Funds, also referred to as Endowment Funds, are governmental funds used to report resources that are legally restricted to the extent that only earnings, and not principal, may be used for purposes that support City programs. The City has received endowments for the following programs: Mt. Hope Cemetery; Carmel Valley Sewer Maintenance; North Park Branch Library; Jacaranda Tree planting and maintenance in City rights-of-way; Rancho Bernardo Branch Library; La Jolla/Riford Branch Library; Los Penasquitos Canyon Preserve; Montezuma Road Median Maintenance; Southcrest Oak Estates II landscape maintenance; Sycamore Estates property maintenance; and, the Fortuna Mountain Conservation Bank management within Mission Trails Regional Park. The amount of investment earnings available for expenditure is reported as Undesignated Fund Balance in the fund level financial statements. The endowment principal is reported as Restricted for Nonexpendable Permanent Endowments in the Statement of Net Assets. The State law governing the spending of endowment funds investment earnings is California Probate Code Section 18504.

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the City's proprietary funds are charges to customers for sales and services. Operating expenses for proprietary funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

Fiduciary funds are used to account for assets held by the City in a trustee capacity or as an agent for individuals, private organizations, and/or other governmental units, and include pension and employee savings trust, investment trust, and agency funds. Pension and Employee Savings Trust Funds are reported using the same measurement focus and basis of accounting as Proprietary Funds. Agency funds are reported using the accrual basis of accounting.

The following is the City's major governmental fund:

<u>General Fund</u> - The General Fund is the principal operating fund of the City. It is used to account for all financial resources, except those required to be accounted for in another fund.

The following are the City's major Enterprise Funds:

<u>Sewer Utility Fund</u> - The sewer utility fund is used to account for the operation, maintenance and development of the City's sewer system. The City's sewer utility fund includes activities related to the performance of services for Participating Agencies.

<u>Water Utility Fund</u> - The water utility fund is used to account for operating and maintenance costs, replacements, betterments, expansion of facilities, and payments necessary in obtaining water from the Colorado River and the State Water Project.

The following are the City's other fund types:

Internal Service Funds - These funds account for vehicle and transportation, printing, engineering, data processing, and storeroom services provided to City departments on a cost-reimbursement basis. Internal service funds also account for self-insurance activities, including workers' compensation and long-term disability programs, which derive revenues from rates charged to benefiting departments. This fund type also accounts for the public liability reserve, which was established for the purpose of paying liability claims.

Pension and Employee Savings Trust Funds - These funds account for the San Diego City Employees' Retirement System, the Supplemental Pension Savings Plan (SPSP), and the 401(k) Plan.

Investment Trust Fund - This fund was established to account for equity that legally separate entities have in the City Treasurer's investment pool. The Automated Regional Justice Information System (ARJIS), the San Diego Graphic Information Source (SanGIS), and the Abandoned Vehicle Abatement (AVA) are all legally separate entities which have cash invested in the City Treasurer's investment pool.

Agency Funds - These funds account for assets held by the City as an agent for individuals, private organizations, and other governments, including federal and state income taxes withheld from employees, parking citation revenues on behalf of other agencies, and certain employee benefit plans.

d. Property Taxes

The County of San Diego (the "County") assesses, bills, and collects property taxes on behalf of numerous special districts and incorporated cities, including the City of San Diego. The City's collections of the current year's taxes are received through periodic apportionments from the County.

The County's tax calendar is from July 1 to June 30. Property taxes attach as a lien on property on January 1. Taxes are levied on July 1 and are payable in two equal installments on November 1 and February 1, and become delinquent after December 10 and April 10, respectively. Since the passage of California's Proposition 13, beginning with fiscal year ended 1979, general property taxes are based either on a flat 1% rate applied to the 1975-76 full value of the property or on 1% of the sales price of any property sold or of the cost of any new construction after the 1975-76 valuation. Taxable values of properties (exclusive of increases related to sales and new construction) can increase by a maximum of 2% per year. The Proposition 13 limitation on general property taxes does not apply to taxes levied to pay the debt service on any indebtedness approved by the voters prior to June 6, 1978 (the date of passage of Proposition 13).

At the government-wide level, property tax revenue is recognized in the fiscal year for which the taxes have been levied. Property taxes received after the fiscal year in which they were levied are not considered available as a resource that can be used to finance the current year operations of the City and, therefore, are recorded as deferred revenue in the governmental funds. The City provides an allowance for uncollected property taxes of approximately 5% of the outstanding current balance which is analyzed each year against most recent data from the County.

Property owners can appeal the assessment value of their property to the County Assessment Appeals Board. If successful, the County Assessor may reduce the taxable value of a property and/or provide a refund to affected property owners. Reductions of taxable property value within the City of San Diego will have a negative impact on future tax collections until assessed valuations increase.

e. Cash and Investments

The City's cash and cash equivalents for Statement of Cash Flows purposes are considered to be cash on hand, demand deposits, restricted cash, and investments held by the City Treasurer in a cash management investment pool and reported at fair value. Cash equivalents reported in the Statement of Cash Flows for the Water and Sewer Utilities do not include restricted investments represented as Restricted Cash and Investments with a maturity date greater than ninety days.

The City's cash resources are combined to form a cash and investment pool managed by the City Treasurer (the pool). The pool is not registered as an investment company with the Securities and Exchange Commission (SEC) nor is it a 2a7–like pool. The investment activities of the Treasurer in managing the pool are governed by California Government Code § 53601 and the City's Investment Policy, which is reviewed by the Investment Advisory Committee and approved annually by the City Council. Interest earned on pooled investments is allocated to participating funds and entities based upon their average daily cash balance during the allocation month. Fair value adjustments to the pool are recorded annually; however, the City Treasury reports on market values monthly. The value of the shares in the pool approximates the fair value of the pool.

The pool participates in the California State Treasurer's Local Agency Investment Fund (LAIF). Investments in LAIF are governed by State statutes and overseen by a five member Local Investment Advisory Board. The fair value of the City's position in LAIF may be greater or less than the value of the shares. Investments in LAIF are valued in these financial statements using a fair value factor provided by LAIF applied to the value of the City's shares in the investment pool.

It has been the City's policy to allow the General Fund to receive interest earned by certain governmental funds, internal service funds and agency funds, unless otherwise expressly stated in the resolutions creating individual funds. During the fiscal year ended June 30, 2009, approximately $8,887 interest was assigned from various funds to the General Fund. These transactions caused an increase to the "transfers from other funds" amount for the General Fund and caused a like increase to the "transfer to other funds" amount for the fund disbursing the interest. In the case of negative interest, these transactions caused an increase to the "transfers from other funds" amount for the fund transferring the negative interest and caused a like increase to the "transfer to other funds" amount for the General Fund.

Certain governmental funds maintain investments outside of the City's investment pool. These funds are supervised and controlled by a five member Funds Commission which is appointed by the Mayor and confirmed by the City Council. The Funds Commission engages money managers to direct the investments of these funds. Additionally, the City and its component units maintain individual accounts pursuant to bond issuances and major construction contracts which may or may not be related to debt issuances. The investment of these funds is governed by the policies set forth in individual indenture and trustee agreements. Certain component units of the City also participate in LAIF separately from the City Treasurer's investment pool.

All City investments are reported at fair value in accordance with the GASB 31, *Accounting and Financial Reporting for Certain Investments and External Investment Pools.* Note 3 of the notes to the financial statements contain additional information on permissible investments per the City investment policy and other policies applicable to the cash and investments reported herein.

The discharge of fiduciary duties by SDCERS' Board is governed by Section 144 of the City Charter and Article XVI, Section 17 of the California State Constitution. Investment decisions are made on a risk versus return basis in a total portfolio context. SDCERS' Board has the authority to delegate investment management duties to outside advisors, to seek the advice of outside investment counsel, and to provide oversight and monitoring of the investment managers it hires. Furthermore, under the California State Constitution and other relevant authorities, SDCERS' Board may, at its discretion, and when prudent in the informed opinion of the Board, invest funds in any form or type of investment, financial instrument, or financial transaction, unless otherwise limited by the San Diego City Council. SDCERS' agents, in

SDCERS' name, manage all investments.

SDCERS' investments are reported at fair value in the accompanying Statement of Fiduciary Net Assets. SDCERS' custodian, State Street Bank & Trust Company, provides the market values of exchange traded assets. In the case of debt securities acquired through private placements, SDCERS' contract investment advisors compute fair value based on market yields and average maturity dates of comparable quoted securities. Short-term investments are reported at cost or amortized cost, which approximates fair value. Real estate equity investment fair values are based on either annual valuation estimates provided by SDCERS' contract real estate advisors or by independent certified appraisers. Fair value of investments in commingled funds of publicly traded securities are based on the funds' underlying asset values determined from published market prices and quotations from major investment firms.

f. Inventories

Inventories reported in the government-wide financial statements and the proprietary funds financial statements, which consist of water in storage and supplies, are valued at the lower of cost or market. Such inventories are expensed when consumed using primarily the first-in, first-out (FIFO) and weighted-average methods, respectively. Inventory supplies of governmental funds are recorded as expenditures when purchased.

g. Land Held for Resale

Land Held for Resale, purchased by RDA, is reported in the government-wide and fund financial statements at the lower of cost or net realizable value.

h. Deferred Charges

In the government-wide and proprietary funds financial statements, Deferred Charges represent the unamortized portion of bond issuance costs. These costs will be amortized over the life of the related bonds using a method which approximates the effective interest method.

i. Capital Assets

Non-Depreciable Capital Assets, which include land and construction-in-progress, are reported in the applicable governmental or business-type activities column in the government-wide financial statements, as well as in the Proprietary Funds financial statements.

Depreciable Capital Assets, which include structures and improvements, equipment, distribution and collection systems, and infrastructure, are reported net of accumulated depreciation in the applicable governmental or business-type activities column in the government-wide financial statements, as well as in the proprietary funds financial statements. To meet the criteria for capitalization, an asset must have a useful life in excess of one year and in the case of equipment outlay, must equal or exceed a capitalization threshold of five thousand dollars. All other capital assets such as land, structures, infrastructure, and distribution and collection systems are capitalized regardless of cost. Subsequent improvements are capitalized to the extent that they extend the initial estimated useful life of the capitalized asset, or improve the efficiency or capacity of that asset. Costs for routine maintenance are expensed as incurred. Interest expense incurred during the construction phase of business-type capital assets are reflected in the capitalized value of the asset constructed. During fiscal year 2009, $18,041 of interest expense incurred was capitalized, which is calculated net of related interest revenue of $1,835.

Capital assets, when purchased or constructed, are recorded at historical cost or estimated historical cost. Donated capital assets are recorded at the estimated fair value on the date of donation. Depreciation of capital assets is computed using the straight-line method over the estimated useful life of the asset as follows:

Assets	Years
Structures and Improvements	
Buildings	40 - 50
Building Improvements	15 - 40
Equipment	
Automobiles and Light Trucks	5 - 10
Construction and Maintenance Vehicles	5 - 20
General Machinery and Office Equipment	3 - 30
Distribution and Collection Systems	
Sewer Pipes and Water Mains	15 - 150
Reservoirs	100 - 150
Infrastructure	
Pavement and Traffic Signals	12 - 50
Bridges	75
Hardscape	20 - 50
Flood Control Assets	40 - 75

j. Unearned/Deferred Revenue

In the government-wide and all fund level financial statements, unearned revenue represents amounts received which have not been earned. The government-wide financial statements include revenues earned from developer credits, which are not reported in governmental funds because they are non-monetary transactions. In the governmental funds financial statements, deferred revenue represents revenues which have been earned but have not met the recognition criteria based on the modified accrual basis of accounting.

k. Interfund Transactions

The City has the following types of interfund transactions:

Loans – amounts provided with a requirement for repayment. Interfund loans are normally reported as interfund receivables (i.e. Due from Other Funds) in lender funds and interfund payables (i.e. Due to Other Funds) in borrower funds. The non-current portions of long-term interfund loans receivable are reported as advances. There is one interfund loan between the Facilities Benefit Assessments (FBA) Fund and the Sewer Utility Fund, for developer fees owed for the Carmel Valley Trunk sewer project, which is reported as an Interfund Loan Receivable/Payable at the fund level and included with Internal Balances on the government-wide Statement of Net Assets.

Services provided and used – sales and purchases of goods and services between funds for a price approximating their external exchange value. Interfund services provided and used are reported as revenues in seller funds and expenditures or expenses in purchaser funds. Unpaid amounts are reported as interfund receivables and payables in the fund balance sheets or fund statements of net assets.

Reimbursements – repayments from the funds responsible for particular expenditures or expenses to the funds that initially paid for them. Reimbursement is reported as expenditures or expenses in the reimbursing fund and a reduction of expenditures or expenses in the paying fund.

Transfers – flows of assets (such as cash or goods) without equivalent flows of assets in return, and without a requirement for repayment. In governmental funds, transfers are reported as other financing uses in the funds making transfers and as other financing sources in the funds receiving transfers. In proprietary funds, transfers are reported after non-operating revenues and expenses.

l. Long-Term Liabilities

In the government-wide and proprietary funds financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary funds statements of net assets. Capital appreciation bond accretion, bond premiums and discounts, and bond refunding gains and losses are amortized over the life of the bonds using a method which approximates the effective yield method. Net bonds payable reflects amortized bond accretion and unamortized bond discounts, premiums and refunding gains and losses.

m. Sundry Trust Liabilities

Under approval of certain agreements, developers submit to RDA an initial deposit to ensure the developer proceeds diligently and in good faith to negotiate and perform all of the obligations under the agreement. These deposits can normally be used for administrative costs of RDA. In the government-wide financial statements and in the fund financial statements, the unspent portion of these deposits, called Sundry Trust Liabilities, are reported as liabilities of RDA.

n. Compensated Absences

The City provides combined annual leave to cover both vacation and sick leave. It is the City's policy to permit employees to accumulate between 8.75 weeks and 17.5 weeks of earned but unused annual leave, depending on hire date. Accumulation of these earnings will be paid to employees upon separation from service.

The liability for compensated absences reported in the government-wide, proprietary, and fiduciary fund financial statements consists of unpaid, accumulated vacation and sick leave balances. The liability has been calculated using the vesting method, in which leave amounts for both employees who currently are eligible to receive termination payments and other employees who are expected to become eligible in the future to receive such payments upon termination are included. The liability has been calculated based on the employees' current salary level and includes salary related costs (e.g. Social Security and Medicare Tax). A liability for these amounts is reported in governmental funds only if they have matured, for example, as a result of employee resignations and retirements.

o. Claims and Judgments

The costs of claims and judgments are accrued when incurred and measurable in the government-wide financial statements and both proprietary and fiduciary funds financial statements. In governmental funds, the costs of claims and judgments are recorded as expenditures when payments are due and payable.

p. Non-Monetary Transactions

The City, as part of approving new development in the community planning process, requires that certain public facilities be constructed per the provisions of community financing plans. Historically, the City has agreed to pay a pro rata share of these assets. In lieu of providing direct funding for these assets, the City often provides developers with credits (also referred to as FBA credits) for future permit fees. These credits are earned by the developer upon successful completion of construction phases and when City engineers have accepted the work. The credits are recognized as permit revenue upon issuance and a corresponding capital asset is recorded in the government-wide financial statements.

q. Net Assets

In the government-wide and proprietary funds financial statements, net assets are categorized as follows:

- Invested in Capital Assets, Net of Related Debt consists of capital assets, net of accumulated depreciation, and reduced by outstanding debt attributed to the acquisition of these assets.
- Restricted Net Assets consist of assets with restrictions imposed on them by external creditors, grantors, contributors, laws and regulations of other governments, or law through constitutional provisions or enabling legislation. It is the City's policy to first apply restricted resources when an expense is incurred for purposes which both restricted and unrestricted net assets are available. As of June 30, 2009, the amount of restricted net assets due to enabling legislation was approximately $147,994.
- Unrestricted Net Assets consist of net assets that do not meet the definition of Invested in Capital Assets, Net of Related Debt or Restricted Net Assets.

r. Fund Balance

In the fund financial statements, portions of fund equity of governmental funds have been reserved for specific purposes. Reservations are created to either (1) satisfy legal covenants that require a portion of the fund balance to be segregated, or (2) identify the portion of the fund balance that is not appropriable for future expenditures.

Designated fund balance indicates that portion of fund equity for which the City has made tentative plans. Undesignated fund balance indicates that portion of fund equity which is available for appropriation in future periods.

s. Reserves

City Charter Section 91 titled "General Reserve Fund" was approved by the voters on November 6, 1962. This section requires the City Council to create and maintain a General Reserve Fund for the purpose of keeping the payment of running expenses of the City on a cash basis. Section 91 requires the reserve be maintained in an amount sufficient to meet all legal demands against the City Treasury for the first four months or other necessary period of each fiscal year prior to the collection of taxes. This fund may be expended only in the event of a public emergency by the affirmative vote of two-thirds of the City Council. The argument for this charter section given by the Citizens Charter Review Committee, commissioned in 1962, was to "strengthen the financial position of the City through the more efficient utilization of tax monies by reducing the amount of taxes collected and lying idle during a great part of the year, and through focusing responsibility for fiscal policies on the elected City Council."

On February 28, 1984, the City Attorney's Office issued Opinion No. 84-3 which addresses issues in regards to the City's compliance with the funding requirements of Charter Section 91. Such opinion stated, "To the extent that the legislative body approves the issuance of short term notes, commonly referred to as Tax or Revenue Anticipation Notes, pursuant to Section 92 titled "Borrowing Money on Short Term Notes"; or authorizes temporary loans to any tax-supported fund from any other funds in the treasury pursuant to Section 93 titled "Loans and Advances", the General Reserve Fund required under section 91 can be reduced." Therefore, the funding requirements of Charter Section 91 have been satisfied through a combination of the General Fund reserve of $78,347 reported within the General Fund column of the Governmental Funds Balance Sheet in Undesignated Fund Balance, and the provisions set forth in Charter Sections 92 and 93 for the fiscal year ended June 30, 2009.

In September 2007, the City Attorney's Office issued a new opinion that supersedes, in part, the opinion issued on February 28, 1984. The revised opinion states that the Charter Section 91 General Reserve must be a separate, legal fund. This fund, separate from the General Fund, must be funded if not at a "four month operating expenditure" level then at a level of such "other necessary funding." The City Attorney's Opinion referenced the guidance of the Government Finance Officer's Association, which recommends a level between 5% and 15% of operating expenditures as the benchmark for interpreting the required funding level that meets the intent of the City's voters. Per the City Attorney's opinion, the City created a separate General Reserve in fiscal year 2008, and the General Fund reserve monies were transferred to that separate reserve and reported therein in all future financial statements. The City Council also approved the Mayor's "City Reserve Policy" with Ordinance 19679 on November 13, 2007. This is a formal fiscal reserve policy that establishes a General Fund Reserve that will be set at a minimum of 8% of annual General Fund Revenues. The policy provides that the City shall reach this level of funding no later than fiscal year 2012. The General Fund Reserve is reported within the General Fund Undesignated Fund Balance as stated above.

The City also has an internal reserve policy in relation to certain governmental long term liabilities which are repaid with Transient Occupancy Tax revenues. When the liabilities are incurred by the City, the City creates policy reserves equal to one half of the annually required lease payments in the form of a rate stabilization reserve for each liability. The purpose of the internal reserve is to make the lease payments when they are due; even if there are unanticipated fluctuations in the Transient Occupancy Tax receipts that could potentially impact the timely payment of lease payments for such liabilities. The City maintains cash funded debt service reserve funds or surety guarantees with trustees in accordance with the bond indentures that exist for these liabilities.

As of June 30, 2009, the following is a schedule of all such internal stabilization reserves (in whole dollars) by fund:

Internal Stabilization Reserve	CAFR Section	CAFR Column	Amount	
Convention Center Expansion	Special Revenue	Transient Occupancy Tax	$	6,850,531
Petco Park (PFFA-Ballpark)	Special Revenue	Transient Occupancy Tax		5,657,279
Balboa Park (SDFELC)	Special Revenue	Transient Occupancy Tax		3,286,878
Trolley (MTDB)	Special Revenue	Public Transportation		2,043,591
			$	17,838,279

These reserve funds were closed and the balances transferred to the General Fund in the FY2010 operating budget.

t. Participating Agencies Revenue Recognition

The Regional Wastewater Disposal Agreement between the City of San Diego (City) and the Participating Agencies (PA) in the Metropolitan Sewerage System allow for quarterly invoicing of local area member municipalities and utility districts to collect and process sewage waste using the City's facilities. The invoicing is based on an estimated allocation of costs associated with each PA and may not represent that agency's proportionate allocation of actual maintenance and operating costs of the sewerage system, resulting in an overstatement or understatement of revenue reported in the Sewer Utility Statement of Revenues, Expenses, and Changes in Fund Net Assets.

During fiscal year 2009 the City invoiced approximately $43,484, net of $13,966 in credits (expenses) and reimbursements (revenues) as a result of the audits of fiscal year 2006 and 2007 activity. In addition, the City has also recognized and accrued approximately $4,514 in estimated credits applicable to fiscal year 2008, which has been recorded as a liability on the Sewer Utility Statement of Net Assets. In prior years, credits of $2,543 and $8,078 were recorded in the Sewer Utility fund financial statements for fiscal years 2005 and 2004, respectively.

u. Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of certain assets and liabilities, disclosure of contingent assets and liabilities, and the related amounts of revenues and expenses. Actual results could differ from those estimates. Management believes that the estimates are reasonable.

v. New Governmental Accounting Standards Implemented During Fiscal Year Ended June 30, 2009

The requirements for the following accounting standards are effective for the purpose of implementation, for the City, for fiscal year ended June 30, 2009.

In November 2006, GASB issued Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*, which addresses accounting and financial reporting standards for pollution (including contamination) remediation obligations, which are obligations to address the current or potential detrimental effects of existing pollution by participating in pollution remediation activities such as site assessments and clean ups. The Statement generally requires the government to estimate the components of expected pollution remediation outlays and determine whether outlays for those components should be accrued as a liability or, if appropriate, capitalized when goods and services are acquired. This would only be required if any one of five obligating events has occurred. If deemed appropriate, the liability will be accrued in the government-wide and proprietary fund financial statements and all required disclosures can be found in Note 18 Contingencies.

In November 2007, GASB issued Statement No. 52, *Land and Other Real Estate Held as Investments by Endowments*, which requires endowments to report their land and other real estate investments at fair value. Governments are also required to report changes in fair value as investment income. As of June 30, 2009 the City does not have land or other real estate assets invested in any of the Endowment Funds, which are reported in the Permanent Fund financial statements.

In March 2009, GASB issued Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. The objective of this Statement is to identify the sources of accounting principles and the framework for selecting the principles used in the preparation of the financial statements. The GAAP hierarchy was previously included in the auditing standards of the American Institute of Certified Public Accountants (AICPA). This Statement improves financial reporting by contributing to the GASB's efforts to codify all GAAP for state and local governments so that they derive from a single source.

In March 2009, GASB issued Statement No. 56, *Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statement on Auditing Standards*. The objective of this Statement is to incorporate in the GASB authoritative literature certain accounting and financial reporting guidance presented in the AICPA Statements on Auditing Standards. The three issues addressed are related party transactions, going concern consideration, and subsequent events. This Statement does not establish new accounting standards but rather incorporates existing guidance into the GASB standards.

2. RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS (In Thousands)

Certain adjustments are necessary to reconcile governmental funds to governmental activities (which includes all internal service funds except the Special Engineering Fund). The reconciliation of these adjustments is as follows:

a. Explanation of certain differences between the Governmental Funds Balance Sheet and the Government-wide Statement of Net Assets:

The Governmental Funds Balance Sheet includes a reconciliation between "Total Fund Balances-Governmental Funds" and "Total Net Assets-Governmental Activities" as reported in the Government-wide Statement of Net Assets. One element of the reconciliation states, "Other assets and liabilities used in governmental activities are not financial resources (uses), and therefore, are either deferred or not reported in the funds." The details of this $105,197 difference are as follows:

Deferred Charges, net, July 1, 2008	$ 19,875
Issuance Costs	1,001
Amortization Expense	(1,124)
Deferred Charges, net, June 30, 2009	19,752
Deferred Revenue:	
Taxes Receivable	24,783
Notes Receivable	4,041
Motor Vehicle License Receivable	1,032
Special Assessments Receivable	2,077
Grants and Other Receivables	53,512
Deferred Revenue, net, June 30, 2009	85,445
Net Adjustment to increase "Total Fund Balances-Governmental Funds" to arrive at "Total Net Assets-Governmental Activities"	$ 105,197

Another element of the reconciliation states, "Certain liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds." The details of this ($1,924,183) difference are as follows:

Interest Accrued on Long-Term Debt	$ (24,219)
Arbitrage Liability	(533)
Compensated Absences	(66,585)
Liability Claims	(52,190)
Capital Leases Payable	(60,760)
Contracts Payable	(4,715)
Notes Payable	(4,786)
Loans Payable	(44,815)
Section 108 Loans Payable	(33,532)
Net Bonds Payable	(1,402,100)
Accretion of Interest on Capital Appreciation Bonds	(14,682)
Net Pension Obligation	(144,740)
Net OPEB Obligation	(70,526)
Net adjustment to decrease "Total Fund Balances-Governmental Funds" to arrive at "Total Net Assets-Governmental Activities"	$ (1,924,183)

Another element of the reconciliation states, "Internal Service Funds are used by management to charge the costs of activities such as Fleet Services, Publishing Services, Self Insurance, and Central Stores to individual funds. The assets and liabilities of certain Internal Service Funds are included in the governmental activities in the Statement of Net Assets. The details of this $6,826 difference are as follows:

Assets:	
Capital Assets - Non Depreciable	$ 1,984
Capital Assets - Depreciable	123,970
Internal Balances	(2,048)
Other Assets	160,768
Liabilities:	
Compensated Absences	(7,861)
Liability Claims	(221,789)
Capital Lease Obligations	(28,759)
Net Other Post Employment Benefits Obligation	(2,978)
Net Pension Obligation	(2,925)
Other Liabilities	(13,536)
Net adjustment to increase "Total Fund Balances-Governmental Funds" to arrive at "Total Net Assets-Governmental Activities"	$ 6,826

b. Explanation of certain differences between the Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances and the Government-wide Statement of Activities:

The Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances includes a reconciliation between "Net Change in Fund Balances-Total Governmental Funds" and "Changes in Net Assets of Governmental Activities" as reported in the Government-wide Statement of Activities. One element of that reconciliation explains, "Governmental funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense." The details of this $121,730 difference are as follows:

Capital Projects	$ 138,634
Other Capital Activities	108,076
Depreciation Expense	(124,980)
Net Adjustment to increase "Net Changes in Fund Balances-Total Governmental Funds" to arrive at "Changes in Net Assets of Governmental Activities"	$ 121,730

Another element of the reconciliation states "The net effect of various miscellaneous transactions involving capital assets (i.e., donations, retirements, and transfers) is to decrease net assets." The details of this ($17,686) are as follows:

In the Statement of Activities, only the net gain on the sale of land is reported. However, in the governmental funds, the proceeds from the sale increase financial resources. Thus, the change in net assets differs from the change in fund balances by the net book value of the capital assets sold/retired.	$ (6,587)
Transfers of capital assets to Business-Type activities decrease net assets in the Statement of Activities, but do not appear in the governmental funds because they are not financial resources.	(3,594)
The Statement of Activities reports losses arising from the retirement of existing depreciable capital assets. Conversely, governmental funds do not report any gain or loss on retirements of capital assets.	(7,505)
Net adjustment to decrease "Net Change in Fund Balances-Total Governmental Funds" to arrive at "Changes in Net Assets of Governmental Activities"	$ (17,686)

Another element of the reconciliation states, "Internal Service Funds are used by management to charge the costs of activities such as Fleet Services, Publishing Services, Central Stores, Self Insurance, and others to individual funds." The net expense of certain Internal Service activities is reported with governmental activities. The details of this $33,982 are as follows:

Allocated Operating Profit	$ 18,508
Nonoperating Revenues (Expenses):	
Loss on Sale/Retirement of Capital Assets	(235)
Other Nonoperating Revenues	14,798
Transfers	713
Capital Contributions	198
Net adjustment to increase "Net Changes in Fund Balances-Total Governmental Funds" to arrive at "Changes in Net Assets of Governmental Activities"	$ 33,982

Another element of the reconciliation states "The issuance of long-term debt (i.e., bonds, leases) provides current financial resources to governmental funds, while the repayment of the principal consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net assets." The details of this ($100,854) difference are as follows:

Debt Issued or Incurred:	
Capital Leases	$ (30,392)
Contracts Payable	(2,100)
Loans Payable	(10,483)
Special Assessment/Special Tax Bonds	(12,365)
Revenue Bonds	(103,000)
Principal Repayments:	
Capital Leases	5,445
Contracts/Notes Payable	876
Loans Payable	168
Section 108 Loans	2,364
G.O. Bonds	2,265
Revenue Bonds	22,450
Special Assessment Bonds/Special Tax Bonds	4,900
Tax Allocation Bonds	14,096
Tobacco Settlement Asset-Backed Bonds	3,990
Pooled Financing Bonds	655
Loans Payable Modification (See Note 5)	277
Net adjustment to decrease "Net Changes in Fund Balances-Total Governmental Funds" to arrive at "Changes in Net Assets of Governmental Activities"	$ (100,854)

Another element of the reconciliation states that "Some expenses reported in the Statement of Activities do not require the use of current financial resources (i.e., compensated absences, net pension obligation) and therefore are not accrued as expenses in governmental funds." The details of this ($92,248) difference are as follows:

Compensated Absences	$ 16
Liability Claims	(39,200)
Net Pension Obligation/Net OPEB Obligation	(48,630)
Accrued Interest	(2,438)
Current Year Premiums/Discounts and Interest Accretion Less Amortization of Bond Premiums	(1,873)
Issuance Costs Less Current Year Amortization	(123)
Net adjustment to decrease "Net Changes in Fund Balances-Total Governmental Funds" to arrive at "Changes in Net Assets of Governmental Activities"	$ (92,248)

3. CASH AND INVESTMENTS (In Thousands)

The following is a summary of the carrying amount of cash and investments:

	Governmental Activities	Business-Type Activities	Fiduciary Statement of Net Assets other than SDCERS	Subtotal	SDCERS Fiduciary Statement of Net Assets	Grand Total
Cash and Cash or Equity in						
Pooled Cash and Investments	$ 1,383,731	$ 723,517	$ 45,512	$ 2,152,760	$ 3,199	$ 2,155,959
Cash and Investments with Fiscal Agent	156,258	175,593	26	331,877	371,736	703,613
Investments at Fair Value	212,149	312,210	673,922	1,198,281	3,448,135	4,646,416
Securities Lending Collateral	-	-	-	-	395,085	395,085
TOTAL	$ 1,752,138	$ 1,211,320	$ 719,460	$ 3,682,918	$ 4,218,155	$ 7,901,073

a. Cash and Cash or Equity in Pooled Cash and Investments

Cash and Cash or Equity in Pooled Cash and Investments represents petty cash, cash at the bank in demand deposit and/or savings accounts, and cash in escrow for contract retention payables. Furthermore, it represents equity in pooled cash and investments, which is discussed in further detail below.

As provided for by California Government Code, the cash balances of substantially all funds and certain outside entities are pooled and invested by the City Treasurer for the purpose of increasing interest earnings through investment activities. The respective funds' shares of the total pooled cash and investments are included in the table above, under the caption Cash and Cash or Equity in Pooled Cash and Investments.

The following represents a summary of the items included in the Cash and Cash or Equity in Pooled Cash and Investments line item:

Cash on Hand - Petty Cash	$ 206
Deposits - Held in Escrow Accounts	10,205
Deposits - Cash and Cash Equivalents (Not Pooled)	2,146
Deposits - Cash and Cash Equivalents (Pooled)	1,024
Deposits - Certificates of Deposit (CDARS)	15,000
Pooled Investments in the City Treasury	2,127,378
Total Cash and Cash or Equity in Pooled Cash and Investments	$ 2,155,959

A summary of the investments held by the City Treasurer's investment pool as of June 30, 2009 is presented in the table below:

Investment	Fair Value	Book Value	Interest Rate % Range		Maturity Range
U.S. Treasury Bills	$ 190,408	$ 188,884	0.29-2.10%	*	7/2/2009-11/27/2009
U.S. Treasury Notes & Bonds	966,025	961,686	0.88-4.88%		11/15/2009-5/15/2012
U.S. Agency Discount Notes	114,889	113,578	0.34-2.55%	*	8/14/2009-3/30/2010
U.S. Agency Notes & Bonds	533,169	529,225	0.50-4.63%		9/28/2009-6/20/2012
Commercial Paper	119,949	119,800	0.12-0.75%	*	7/1/2009-10/16/2009
Corporate Notes & Bonds	151,832	151,520	1.25-6.88%		8/10/2009-6/22/2012
Local Agency Investment Fund (LAIF)	39,718	39,667	1.91%	**	2/21/2010
Repurchase Agreement	11,388	11,388	0.07%		7/1/2009
Certificates of Deposit (CDARS)	15,000	15,000	2.20-2.21%		4/29/2010-5/6/2010
	$ 2,142,378	$ 2,130,748			

* Discount Rates

** LAIF - Fair Value is adjusted to account for LAIF factor. Maturity range is based on weighted average maturity of 235 days.

The following represents a condensed statement of net assets and changes in net assets for the City Treasurer's cash and investment pool as of June 30, 2009:

Statement of Net Assets	
Deposit - Cash and Cash Equivalents (Pooled)	$ 1,024
Deposits - Certificates of Deposit (CDARS)	15,000
Investments of Pool Participants	2,127,378
Accrued Interest Receivable of Internal Pool Participants	7,227
Accrued Interest Receivable of External Pool Participants	38
Total Cash, Investments, and Interest Receivable	$ 2,150,667
Equity of Internal Pool Participants	$ 2,145,992
Equity of External Pool Participants (SanGIS, ARJIS & AVA) **	4,675
Total Equity	$ 2,150,667

**Voluntary Participation

Statement of Changes in Net Assets	
Net Assets Held for Pool Participants at July 1, 2008	$ 2,063,901
Net Change in Investments by Pool Participants	86,766
Total Net Assets Held for Pool Participants at June 30, 2009	$ 2,150,667

b. Cash and Investments with Fiscal Agents

Cash and Investments with Fiscal Agents represents cash and investments held by fiscal agents resulting from bond issuances. More specifically, these funds represent reserves held by fiscal agents or trustees as legally required by bond issuances and liquid investments held by fiscal agents or trustees which are used to pay debt service. Under the Fiduciary Statement of Net Assets, Cash and Investments with Fiscal Agent represents the City's balance for the Preservation of Benefit Plan (POB Plan). The POB Plan is a qualified governmental excess benefit arrangement (QEBA) under Internal Revenue Code (IRC) section 415(m) and is discussed in further detail in Note 12.

The San Diego City Employees' Retirement System (SDCERS) portion of Cash and Investments with Fiscal Agents represents funds held as cash collateral from market neutral portfolios (domestic fixed income investment strategy). Furthermore, it represents transaction settlements, held in each investment manager's portfolio, which are invested overnight by SDCERS' custodial bank.

c. Investments at Fair Value

Investments at Fair Value represents investments of the City's Supplemental Pension Savings Plan, 401(k) Plan, San Diego City Employees' Retirement System (SDCERS), investments managed by the City Treasurer (which are not part of the pool), investments reported by San Diego Data Processing Corporation (SDDPC), and investments managed by the Funds Commission (e.g. Cemetery Perpetuity, Effie Sergeant, Gladys Edna Peters, Los Penasquitos Canyon, and the Edwin A. Benjamin Library funds).

d. Investment Policy

In accordance with City Charter Section 45 and under authority annually approved by the City Council, the City Treasurer is responsible for the safekeeping and investment of the unexpended cash in the City Treasury according to the City Treasurer's Investment Policy (Policy). This Policy applies to all of the investment activities of the City except for the pension trust funds, the proceeds of certain debt issues, which are managed and invested at the direction of the City Treasurer in accordance with the applicable indenture or by Trustees appointed under indenture agreements or by fiscal agents, and the assets of trust funds, which are placed in the custody of the Funds Commission by Council ordinance.

City staff reviews the Policy annually and may make revisions based upon changes to the California Government Code and the investment environment. These suggested revisions are presented to the Investment Advisory Committee (IAC) for review and comment. The IAC consists of two City representatives and three outside financial professionals with market and portfolio expertise not working for the City of San Diego. The City Council reviews the Policy and considers approval on an annual basis.

The IAC evaluates the horizon returns, risk parameters, security selection, and market assumptions the City's investment staff is using when explaining the City's investment returns. The IAC also meets semi-annually to review the previous two quarters' investment returns and make recommendations to the City Treasurer on proposals presented to the IAC by the Treasurer's staff.

The Policy is governed by the California Government Code (CGC), Sections 53600 et seq. The following table presents the authorized investments, requirements, and restrictions per the CGC and the Policy:

Investment Type	Maximum Maturity (1)		Maximum % of Portfolio		Maximum % with One Issuer		Minimum Rating	
	CGC	City Policy	CGC	City Policy	CGC	City Policy	CGC	City Policy
U.S. Treasury Obligations (bills, bonds, or notes)	5 years	5 years	None	None	None	None	None	None
U.S. Agencies	5 years	5 years	None	(2)	None	(2)	None	None
Bankers' Acceptances (6)	180 days	180 days	40%	40%	30%	10%	None	(3)
Commercial Paper (6)	270 days	270 days	25%	25%	10%	10%	P1	P1
Negotiable Certificates (6)	5 years	5 years	30%	30%	None	10%	None	(3)
Repurchase Agreements	1 year	1 year	None	None	None	None	None	None
Reverse Repurchase Agreements (4)	92 days	92 days	20%	20%	None	None	None	None
Local Agency Investment Fund	N/A	N/A	None	None	None	None	None	None
Non-Negotiable Time Deposits (6)	5 years	5 years	None	25%	None	10%	None	(3)
Medium Term Notes/Bonds (6)	5 years	5 years	30%	30%	None	10%	A	A
Municipal Securities of California Local Agencies (6)	5 years	5 years	None	20%	None	10%	None	A
Mutual Funds	N/A	N/A	20%	5%	10%	None	AAA	AAA
Notes, Bonds, or Other Obligations	5 years	5 years	None	None	None	None	None	AA
Mortgage Pass-Through Securities	5 years	5 years	20%	20%	None	None	AA	AAA
Financial Futures (5)	N/A	None	None	None	None	None	None	None

Footnotes:

(1) In the absence of a specified maximum, the maximum is 5 years.

(2) No more than one-third of the cost value of the total portfolio at time of purchase can be invested in the unsecured debt of any one agency.

(3) Credit and maturity criteria must be in accordance per Section X of the City's Investment Policy.

(4) Maximum % of portfolio for Reverse Repurchase Agreements is 20% of base value.

(5) Financial futures transactions would be purchased only to hedge against changes in market conditions for the reinvestment of bond proceeds.

(6) Investment types with a 10% maximum with one issuer are further restricted per the City's Investment Policy: 5% per issuer and an additional 5% with authorization by City Treasurer.

According to the Policy, the City may enter into repurchase and reverse repurchase agreements only with primary dealers of the Federal Reserve Bank of New York with which the City has entered into a master repurchase agreement.

Additionally, the Policy authorizes investment in other specific types of securities. The City may invest in floating rate notes with coupon resets based upon a single fixed income index (which would be representative of an eligible investment), provided that security is not leveraged. Structured notes issued by U.S. government agencies that contain imbedded calls or options are authorized as long as those securities are not inverse floaters, range notes, or interest only strips derived from a pool of mortgages. A maximum of 8% of the "cost value" of the pooled portfolio may be invested in structured notes.

In fiscal year 2009, the City invested $15 million as part of the Certificate of Deposit Account Registry Service (CDARS). The CDARS investment was deposited with two institutions, $5 million with Neighborhood National Bank and $10 million with First Business Bank. Under the City Treasurer's Investment Policy, this type of investment is subject to a 1% limit of total portfolio value for the City's pooled investments. The CDARS investment program is permissible per California Government Code (CGC) Section 53601.8 and is subject to a 30% limit of total portfolio value.

Ineligible investments prohibited from use in the portfolio include, but are not limited to, common stocks and long-term corporate notes/bonds. A copy of the City Treasurer's Investment Policy can be requested from the City Treasurer, 1200 3rd Avenue, Suite 100, San Diego, CA 92101.

Other Investment Policies

The City currently has a Funds Commission whose role is to supervise and control all trust, perpetuity, and investment funds of the City and such pension funds as shall be placed in its custody. The statutory authority for the Funds Commission is created in City Charter Article V, Section 41(a). While the duties described in the creation document form broad authority for the Funds Commission, in practice, the Funds Commission only oversees investments related to a small number of permanent endowments. The allowable investments for these funds are different than those as prescribed in the City Treasurer's Investment Policy. Each permanent endowment fund has its own separate investment policy. Copies of the individual investment policies can be requested from the City Treasurer, 1200 3rd Avenue, Suite 100, San Diego, CA 92101.

The City and its component units have funds invested in accordance with various bond indenture and trustee agreements. The investment of these bond issuances is in accordance with the Permitted Investments section and applicable account restrictions outlined in the Indenture of each bond issuance. The Permitted Investments section in each Indenture will vary based upon the maturity, cash flow demands, and reserve requirements associated with each issuance. In general, the Permitted Investments section of each Indenture will closely resemble the City Treasurer's Investment Policy, but may include certain investment options not authorized by applicable law for the City Treasurer's Investment Policy (CGC §53601). Copies of the individual bond indentures can be requested from the City Treasurer's Investment Division, 1200 3rd Avenue, Suite 1624, San Diego, CA 92101.

City of San Diego – Disclosures for Specific Risks

e. Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Market or interest-rate risk for the City's pooled investments is intended to be mitigated by establishing two portfolios, a liquidity portfolio and a core portfolio. Target durations are based upon the expected short and long-term cash needs of the City. The liquidity portfolio is structured with an adequate mix of highly liquid securities and maturities to meet major cash outflow requirements for at least six months (per CGC Section 53646). The liquidity portfolio uses the Merrill Lynch 3-6 month Treasury Index as a benchmark with a duration of plus or minus 40% of the duration of that benchmark.

The core portfolio uses the Merrill Lynch 1-3 year Treasury Index as a benchmark with a duration of plus or minus 20% of the duration of that benchmark. It consists of high quality liquid securities with a maximum maturity of 5 years and is structured to meet the longer-term cash needs of the City. Information about the sensitivity of the fair value of the City's investments to market interest rate fluctuations is presented in the table below.

As of June 30, 2009, the City's investments (in thousands) by maturity are as follows:

	Years				Fair Value
Pooled Investments with City Treasurer:	Under 1	1-3	3-5	Over 5	(In Thousands)
U.S. Treasury Bills	$ 190,408	$ -	$ -	$ -	$ 190,408
U.S. Treasury Notes	163,352	802,673	-	-	966,025
U.S. Agencies - Federal Farm Credit Bank	45,014	30,631	-	-	75,645
U.S. Agencies - Federal Home Loan Bank	170,603	111,858	-	-	282,461
U.S. Agencies - Federal Home Loan Mortgage Corporation	59,997	65,361	-	-	125,358
U.S. Agencies - Federal National Mortgage Association	40,000	124,594	-	-	164,594
Commercial Paper	119,949	-	-	-	119,949
Corporate Notes	12,073	139,759	-	-	151,832
Non-Negotiable Certificate of Deposit (CDARS deposit)	15,000	-	-	-	15,000
Repurchase Agreement	11,388	-	-	-	11,388
State Local Agency Investment Fund	39,718	-	-	-	39,718
	867,502	1,274,876	-	-	2,142,378
Non-Pooled Investments with City Treasurer:					
U.S. Treasury Bills	118,574	-	-	-	118,574
U.S. Treasury Notes	11,059	2,756	-	-	13,815
U.S. Agencies - Federal Farm Credit Bank	-	11,186	-	-	11,186
U.S. Agencies - Federal Home Loan Bank	15,031	-	-	-	15,031
U.S. Agencies - Federal Home Loan Mortgage Corporation	37,221	-	-	-	37,221
U.S. Agencies - Federal National Mortgage Association	18,200	10,253	-	-	28,453
Commerical Paper	165,146	-	-	-	165,146
Repurchase Agreements	122,812	-	-	-	122,812
	488,043	24,195	-	-	512,238
Investments with Fiscal Agents, Funds Commission, and Blended Component Units:					
U.S. Treasury Bills	23,595	-	-	-	23,595
U.S. Treasury Bonds and Notes	8,894	38,440	-	425	47,759
U.S. Agencies - Federal Home Loan Bank	94,146	-	-	-	94,146
U.S. Agencies - Federal Home Loan Mortgage Corporation	45,773	-	-	-	45,773
U.S. Agencies - Federal National Mortgage Association	23,077	-	-	-	23,077
Commercial Paper	6,054	-	-	-	6,054
Common Stock	2,429	-	-	-	2,429
Corporate Bonds and Notes	124	1,001	538	3,192	4,855
Guaranteed Investment Contracts	-	-	-	13,716	13,716
Money Market Mutual Funds	78,977	-	-	-	78,977
Mortgage Backed Securities - Commercial	-	-	-	89	89
Mortgage Backed Securities - Government	-	-	-	31	31
Mutual Funds - Equity	279,612	-	-	-	279,612
Mutual Funds - Fixed Income	-	-	396,244	1,537	397,781
Cash (with Fiscal Agents)	26	-	-	-	26
	562,707	39,441	396,782	18,990	1,017,920
Total Investments	$ 1,918,252	$ 1,338,512	$ 396,782	$ 18,990	3,672,536
Total Deposits					13,375
Total Cash on Hand					206
Total Investments, Deposits, and Cash on Hand (Includes SDCERS Pooled Cash and Investments with the City - $3,199)					$ 3,686,117

f. Credit Risk

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. As of June 30, 2009, the City's investments and corresponding credit ratings are as follows:

Pooled Investments with City Treasurer:	Moody's	S&P	Fair Value	Percentage
U.S. Treasury Bills	Exempt	Exempt	$ 190,408	8.89%
U.S. Treasury Notes	Exempt	Exempt	966,025	45.10%
U.S. Agencies - Federal Farm Credit Bank	Aaa	N/A	75,645	3.53%
U.S. Agencies - Federal Home Loan Bank [1]	Aaa	N/A	262,517	12.25%
U.S. Agencies - Federal Home Loan Bank [1]	P-1	N/A	19,944	0.93%
U.S. Agencies - Federal Home Loan Mortgage Corporation [1]	Aaa	N/A	70,413	3.29%
U.S. Agencies - Federal Home Loan Mortgage Corporation [1]	P-1	N/A	54,945	2.56%
U.S. Agencies - Federal National Mortgage Association [1]	Aaa	N/A	124,594	5.82%
U.S. Agencies - Federal National Mortgage Association [1]	P-1	N/A	40,000	1.87%
Commercial Paper	P-1	N/A	119,949	5.60%
Corporate Notes	Aaa	N/A	123,055	5.74%
Corporate Notes	Aa1	N/A	5,157	0.24%
Corporate Notes	Aa2	N/A	12,073	0.56%
Corporate Notes	A1	N/A	10,544	0.49%
Corporate Notes	A2	N/A	1,003	0.05%
Non-Negotiable Certificates of Deposit (CDARS deposit)	Not Rated	Not Rated	15,000	0.70%
Repurchase Agreements	Not Rated	Not Rated	11,388	0.53%
State Local Agency Investment Fund	Not Rated	Not Rated	39,718	1.85%
Subtotal - Pooled Investments			2,142,378	100.00%
Non-Pooled Investments with City Treasurer:				
U.S. Treasury Bills	Exempt	Exempt	118,574	23.15%
U.S. Treasury Notes	Exempt	Exempt	13,815	2.70%
U.S. Agencies - Federal Farm Credit Bank	Aaa	N/A	11,186	2.18%
U.S. Agencies - Federal Home Loan Bank	P-1	N/A	15,031	2.93%
U.S. Agencies - Federal Home Loan Mortgage Corporation [1]	Aaa	N/A	12,938	2.53%
U.S. Agencies - Federal Home Loan Mortgage Corporation [1]	P-1	N/A	24,283	4.75%
U.S. Agencies - Federal National Mortgage Association [1]	Aaa	N/A	10,253	1.99%
U.S. Agencies - Federal National Mortgage Association [1]	P-1	N/A	18,200	3.55%
Commerical Paper	P-1	N/A	165,146	32.24%
Repurchase Agreements	Not Rated	Not Rated	122,812	23.98%
Subtotal - Non-Pooled Investments			512,238	100.00%

"Exempt" - Per GASB 40, U.S. Treasury Obligations do not require disclosure of credit quality.

"N/A" - S&P rating not applicable, Moody's rating provided.

[1] More than 5% of total investments are with U.S. Agencies whose debt is not backed by full faith and credit of the U.S. Government.

(continued on next page)

Investments with Fiscal Agents, Funds Commission, and Blended Component Units:	Moody's	S&P	Fair Value	Percentage
U.S. Treasury Bills	Exempt	Exempt	$ 23,595	2.32%
U.S. Treasury Bonds and Notes	Exempt	Exempt	47,759	4.69%
U.S. Agencies - Federal Home Loan Bank [1]	Aaa	N/A	42,977	4.22%
U.S. Agencies - Federal Home Loan Bank [1]	P-1	N/A	51,169	5.03%
U.S. Agencies - Federal Home Loan Mortgage Corporation	P-1	N/A	45,773	4.50%
U.S. Agencies - Federal National Mortgage Association	Aaa	N/A	83	0.01%
U.S. Agencies - Federal National Mortgage Association	P-1	N/A	22,994	2.26%
Commercial Paper	P-1	N/A	6,054	0.59%
Common Stock	Not Rated	Not Rated	2,429	0.24%
Corporate Bonds and Notes	Aa2	N/A	483	0.05%
Corporate Bonds and Notes	Aa3	N/A	169	0.02%
Corporate Bonds and Notes	A1	N/A	954	0.09%
Corporate Bonds and Notes	A2	N/A	2,617	0.26%
Corporate Bonds and Notes	A3	N/A	301	0.03%
Corporate Bonds and Notes	Baa1	N/A	229	0.02%
Corporate Bonds and Notes	Baa2	N/A	102	0.01%
Guaranteed Investment Contracts	Not Rated	Not Rated	13,716	1.35%
Money Market Mutual Funds	Aaa	N/A	78,977	7.76%
Mortgage Backed Securities - Commercial	Aaa	N/A	89	0.01%
Mortgage Backed Securities - Government	Not Rated	Not Rated	31	0.01%
Mutual Funds - Equity	Not Rated	Not Rated	279,612	27.47%
Mutual Funds - Fixed Income	Not Rated	Not Rated	397,781	39.05%
Cash (with Fiscal Agents)	Not Rated	Not Rated	26	0.01%
Subtotal - Other Investments			1,017,920	100.00%
Total Investments			3,672,536	
Total Deposits			13,375	
Total Cash on Hand			206	
Total Investments, Deposits, and Cash on Hand*			$ 3,686,117	

*(includes SDCERS Pooled Cash and Investments with the City - $3,199)

"Exempt" - Per GASB 40, US Treasury Obligations do not require disclosure of credit quality.

"N/A" - S&P rating not applicable, Moody's rating provided.

[1] More than 5% of total investments are with U.S. Agencies whose debt is not backed by full faith and credit of the U.S. Government.

Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the relative size of an investment in a single issuer. As of June 30, 2009, the City exceeded the 5% limit of total investments for issuers of various U.S. Agencies. Investments exceeding the 5% limit are referenced in the credit ratings table above. Investments issued or explicitly guaranteed by the U.S. government and investments in mutual funds, external investment pools, and other pooled investments are exempt.

g. Custodial Credit Risk

Deposits

At June 30, 2009, the carrying amount of the City's cash deposits was approximately $18,170, and the bank balance was approximately $35,849, the difference of which is substantially due to outstanding checks. For the balance of cash deposits in financial institutions, approximately $16,008 was covered by federal depository insurance and approximately $19,841 was uninsured. Pursuant to the California Government Code, California banks and savings and loan associations are required to secure the City's deposits not covered by federal depository insurance by pledging government securities as collateral. As such, $18,793 of the City's deposits are pledged at 110% and held by a bank acting as the City's agent, in the City's name. The City is exposed to custodial credit risk for the remaining $1,048, which is uninsured and uncollateralized. The amount subject to custodial credit risk includes approximately $1,048 in deposits relating to San Diego Data Processing Corporation.

The City also has deposits held in escrow accounts with a carrying amount and bank balance of approximately $10,205. For the balance of deposits in escrow accounts, approximately $1,851 was covered by federal depository insurance. The remaining balance of $8,354 was uninsured. Pursuant to the California Government Code, California banks and savings and loans associations are required to secure the City's deposits in excess of insurance by pledging government securities as collateral. As such, $8,354 of the City's deposits in escrow accounts are collateralized and pledged at 110%.

Investments

The City's investments at June 30, 2009 are categorized as described below:

Category 1:	Insured or registered, with securities held by the City or its agent in the City's name.
Category 2:	Uninsured and unregistered, with securities held by the counterparty's trust department or agent in the City's name.
Category 3:	Uninsured and unregistered, with securities held by the counterparty, or by its trust department or agent but not in the City's name.
Non–Categorized:	Includes investments made directly with another party, real estate, direct investments in mortgages and other loans, open-end mutual funds, pools managed by other governments, annuity contracts, and guaranteed investment contracts.

At June 30, 2009, the City had investments exposed to custodial credit risk. Investments within the Cemetery Perpetuity Fund's portfolio were held by Northern Trust Bank, and were not in the City's name. The following summarizes the investment types and amounts that are exposed to custodial credit risk and are classified as Category 3:

Investment Type	Fair Value
U.S. Treasury Bonds and Notes	$ 494
U.S. Agencies	83
Corporate Bonds and Notes	4,855
Mortgage Backed Securities - Commercial	89
Mortgage Backed Securities - Government	31
Common Stock	2,429
Total	$ 7,981

h. Restricted Cash and Investments

Cash and investments at June 30, 2009 that are restricted by legal or contractual requirements are comprised of the following:

Nonmajor Governmental Funds	
Reserved for Debt Service	$ 415,680
Permanent Endowments	15,867
Total Nonmajor Governmental Funds	431,547
Nonmajor Enterprise Funds	
Environmental Services Fund -Funds set aside for landfill site closure and maintenance costs	37,983
Recycling Enterprise Fund - Customer deposits	2,569
Total Nonmajor Enterprise Funds	40,552
Water Utility Enterprise Fund	
Customer deposits	7,317
Interest and redemption funds	256,566
Total Water Utility Enterprise Fund	263,883
Sewer Utility Enterprise Fund	
Interest and redemption funds	231,212
Miscellaneous Agency Funds	
Retention held in escrow	10,205
Total Restricted Cash and Investments	$ 977,399

Summary of Total Cash and Investments
(In Thousands)

Total Unrestricted Cash and Investments	$ 6,923,674
Total Restricted Cash and Investments	977,399
Total Cash and Investments	$ 7,901,073
Total Governmental Activities	$ 1,752,138
Total Business-Type Activities	1,211,320
Total Fiduciary Activities	4,937,615
Total Cash and Investments	$ 7,901,073

San Diego City Employees' Retirement System (SDCERS) – Disclosures for Policy and Specific Risks

Summary of Cash and Investments – San Diego City Employees' Retirement System

Cash or Equity in Pooled Cash and Investments with the City of San Diego	$ 3,199
Cash and Cash Equivalents on Deposit with Custodial Bank and Fiscal Agents	371,736
Investments at Fair Value:	
Short-Term Investments	33,311
Domestic Fixed Income Securities	861,555
International Fixed Income Securities	143,677
Domestic Equity Securities	1,444,848
International Equity Securities	614,246
Directly Owned Real Estate Assets and Real Estate Equity Securities	350,498
Securities Lending Collateral	395,085
Total Cash and Investments for SDCERS	$ 4,218,155

Narratives and tables presented in the following sections (i. through r.) are taken directly from the comprehensive annual financial report of the San Diego City Employees' Retirement System, as of June 30, 2009, issued December 8, 2009.

i. Investment Policy

Investments for the pension trust fund are authorized to be made by the Board of Administration of the SDCERS (Board) in accordance with Section 144 of the City Charter and the California State Constitution Article XVI, Section 17. The Board is authorized to invest in any securities that are allowed by general law for savings banks. The Board may also invest in additional investments as approved by resolution of the San Diego City Council. These investments include, but are not limited to, bonds, notes and other obligations, real estate investments, common stock, preferred stock, and pooled vehicles. Additionally, investment policies permit SDCERS' Board to invest in financial futures contracts provided the contracts do not leverage SDCERS' Trust Fund portfolio. Financial futures contracts are recorded at fair value each day and must be settled at expiration date. Changes in the fair value of the contracts will result in the recognition of a gain or loss under GASB Statement No. 25.

Investment earnings from the pension trust fund are accounted for in accordance with GASB Statement No. 25. Net investment income includes the net appreciation/depreciation in the fair value of investments, interest income, dividend income, and other income not included in the change in the fair value of investments, less total investment expenses (including investment management/custodial fees and all other significant investment-related costs). SDCERS had realized losses that totaled $314,900 for the year ended June 30, 2009. Pursuant to the San Diego Municipal Code, realized gains and losses determine whether contingent benefits will be paid each fiscal year.

SDCERS' investment portfolio includes fixed income strategies to diversify the investment portfolio. The percentage allocated to these strategies is based on efficient model portfolios developed from an annual asset allocation study. The returns of fixed income strategies are in general more consistent than equity returns. SDCERS' target asset allocation policy is reviewed annually to reflect changes in capital market assumptions. As of June 30, 2009, SDCERS' target allocation to fixed income strategies was 29%. The fixed income allocation is externally managed and is comprised as follows: 22% to core-plus domestic fixed income (benchmarked to the Barclays Capital Aggregate Bond Index), 4% to non-U.S. fixed income (benchmarked to the Citigroup Non-U.S. Government Bond Index), and 3% to convertible bond securities (benchmarked to the Merrill Lynch Convertible Index, All Qualities).

SDCERS also has a 5% target allocation to an unsecuritized market neutral strategy which is benchmarked to the Merrill Lynch 1-5 year Government/Corporate Index. The market neutral and convertible bond strategies are intended to minimze interest rate risk, and duration is not relevant in structuring these portfolios. Convertible securities diversify SDCERS' fixed income portfolio and are expected to provide a higher rate of return than traditional fixed income strategies due to their conversion feature. SDCERS' market neutral strategy was added to SDCERS' fixed income strategy in 1998. This strategy uses equity securities held long and sold short with the cash proceeds of the short sales held in a cash account invested in U.S. Government Federal Funds. Both market neutral strategies have a low correlation to fixed income assets and provide additional diversification to the portfolio's fixed income allocation.

A copy of the SDCERS investment policy and additional details on the results of the system's investment activities are available at 401 West A Street, Suite 400, San Diego, CA 92101.

j. Interest Rate Risk

SDCERS does not have a general investment policy that addresses interest rate risk. Each investment manager's specific investment guidelines places limits on each portfolio to manage interest rate risk. SDCERS uses duration to measure how changes in interest rates will affect the value of its fixed income portfolios. Convertible bonds are typically not subject to interest rate risk as convertible bonds are usually positively correlated to interest rate movements compared to other fixed income securities.

The following table displays the durations for SDCERS' domestic and international fixed income strategies based on portfolio holdings as of June 30, 2009.

Fixed Income Portfolios (Domestic and International)
Portfolio Duration Analysis as of June 30, 2009

Type of Security	Effective Duration (in years)	Fair Value [1] (in thousands)
Collateralized Mortgage Obligations		
Collateralized Mortgage Obligations	7.65	$ 104,265
Corporates		
Corporate Bonds	4.07	267,080
Government & Agency Obligations		
FHLMC	3.52	61,308
FNMA	2.80	282,624
GNMA I	5.07	15,006
GNMA II	1.29	954
Treasury Strips	18.90	1,762
Government Issues	5.64	118,705
Municipals	11.71	5,545
Asset-Backed Securities		
Other Asset-Backed Securities	1.13	44,281
Total		$ 901,530

[1] Fair Value does not include convertible bonds, short-term investments, and derivative securities of $137,013. These securities do not exhibit interest rate risk and duration cannot be calculated.

Source: SDCERS' CAFR as of June 30, 2009

k. Investments Highly Sensitive to Interest Rate Changes

Certain terms in fixed income securities may increase the sensitivity of their fair values to changes in interest rates. The Portfolio Duration Analysis table on the previous page discloses the degree to which SDCERS' investments are sensitive to interest rate changes due to the remaining term of maturity. The total value of securities, as of June 30, 2009, that are highly sensitive to interest rate changes due to factors other than term to maturity are presented in the table below.

	Fair Value (in thousands)	Percent of Fixed Income Portfolio
Adjustable Rate Notes	$ 11,133	1.1%
Asset Backed Securities	27,238	2.6%
Floating Rate Notes	66,237	6.4%
Interest Only Strips	1,713	0.2%
Inverse Floating Rate Notes	2,970	0.3%
Range Notes	2,626	0.3%

Source: SDCERS' CAFR as of June 30, 2009

Although SDCERS does not have an investment policy that pertains directly to investments that are highly sensitive to interest changes, this risk is mitigated by diversification of issuer, credit quality, maturity, and security selection.

l. Credit Risk

SDCERS employs two core-plus bond managers that invest in a wide variety of fixed income and derivative securities. One of SDCERS' domestic core-plus fixed income managers has tactical discretion to invest in non-U.S. fixed income securities while the other domestic core-plus fixed income manager is limited to U.S. fixed income investments only. The permitted securities and derivatives for the two domestic core-plus fixed income managers include U.S. Government and Agency obligations, collateralized mortgage obligations, U.S. corporate securities, and asset backed securities. Investment guidelines include minimum average portfolio quality of A rating (market value rated); and minimum credit quality at time of purchase of 80% Baa/BBB and 20% B for a domestic core-plus fixed manager; and Ba/BB for core-plus fixed income manager with tactical discretion to invest in non-U.S. fixed income strategies.

The permitted securities for SDCERS' domestic convertible bond portfolio include convertible bonds, convertible preferred stocks, common stocks, and straight debt and synthetic convertibles. SDCERS' domestic convertible bond portfolio will generally maintain an average rating of at least BB+.

The permitted securities for SDCERS' international fixed income portfolio include international corporate securities, sovereign debt instruments, and international asset backed securities. SDCERS' international fixed income portfolio has the following credit and market risk parameters: minimum average portfolio quality of A rating (market value weighted); and a minimum credit quality at time of purchase of BBB- or equivalent rating by at least one of the major rating agencies.

The table on the following page identifies the credit quality for SDCERS' fixed income strategies based on portfolio holdings as of June 30, 2009.

Credit Quality of SDCERS'
Fixed Income Strategies (Domestic and International)
As of June 30, 2009

S&P Quality Rating	Total Fair Value (in thousands)	Collateralized Mortgage Obligations	Corporates[1]	Government & Agency Obligations[2]	Asset-Backed Securities	Short-Term/ Other
U.S. Treasury	$ 22,140	$ -	$ -	$ 22,140	$ -	$ -
AAA	567,928	83,537	29,611	432,671	22,109	-
AA+	25,931	-	10,046	10,926	4,959	-
AA	28,308	-	19,450	8,121	737	-
AA-	15,950	-	15,950	-	-	-
A+	41,504	-	26,692	2,212	-	12,600
A	58,648	313	57,678	657	-	-
A-	21,786	-	21,786	-	-	-
BBB+	14,733	-	13,581	253	899	-
BBB	10,125	-	4,958	1,384	3,783	-
BBB-	16,460	73	11,896	492	3,999	-
BB+	1,484	528	956	-	-	-
BB	5,529	1,485	4,044	-	-	-
BB-	5,152	1,864	2,143	197	948	-
B+	2,066	-	2,066	-	-	-
B	4,247	-	2,923	-	1,324	-
CCC+	1,849	-	1,849	-	-	-
CCC	2,496	1,541	955	-	-	-
CC	6,239	-	6,239	-	-	-
NR	185,968	14,924	138,737	6,851	5,523	19,933
Totals	$ 1,038,543	$ 104,265	$ 371,560	$ 485,904	$ 44,281	$ 32,533

[1] Corporates include convertible bonds from SDCERS' convertible bond manager.

[2] Includes municipal holdings as well.

Source: SCDERS' CAFR as of June 30, 2009

m. Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the relative size of an investment in a single issuer. As of June 30, 2009, SDCERS had no single issuer that exceeded 5% of total investments, excluding investments issued or explicitly guaranteed by the U.S. Government and investments in mutual funds, external investment pools, and other pooled investments. With respect to the concentration of credit risk by issue, SDCERS' Investment Policy states that not more than 10% of the fixed income portfolio shall be invested in the debt security of any one issue at the time of initial commitment, except for U.S. Government and Agency obligations. While SDCERS does not have a general investment policy on the concentration of credit risk by issuer, each manager's specific investment guidelines place limitations on the maximum holdings in any one issuer.

n. Custodial Credit Risk

Custodial credit risk is the risk that if a financial institution or counterparty fails, SDCERS would not be able to recover the value of its deposits, investments, or securities. SDCERS' exposure to custodial credit risk is further discussed in the following paragraphs.

Deposits

SDCERS' is exposed to custodial credit risk for uncollateralized cash/deposits that are not covered by federal depository insurance. At June 30, 2009, the amount of cash/deposits on deposit with SDCERS' custodial bank totaled $184,200.

Investments

As of June 30, 2009, 100% of SDCERS' investments were held in SDCERS' name. SDCERS is not exposed to custodial credit risk related to these investments.

Securities Lending Collateral

SDCERS is exposed to custodial credit risk for the securities lending collateral such that certain collateral is received in the form of letters of credit, tri-party collateral or securities collateral. The fair value of securities on loan collateralized by these non-cash vehicles totaled $35,000 as of June 30, 2009 and are at risk as the collateral for these loaned securities is not held in SDCERS' name and cannot be sold without a borrower default. The cash collateral held by SDCERS' custodian in conjunction with the securities lending program, which totaled $395,085 as of June 30, 2009, is also at risk as it is invested in a pooled vehicle managed by the custodian. The investment characteristics of the collateral pool are disclosed in the Securities Lending Collateral section.

o. Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. The following table represents SDCERS' securities (in thousands) held in a foreign currency as of June 30, 2009.

Foreign Currency Risk [1]
As of June 30, 2009
(All values are in U.S. Dollars)

Local Currency Name	Cash	Equity	Fixed income	Total
Australian Dollar	$ 689	$ 17,271	$ 11,717	$ 29,677
Brazilian Real	-	6,700	-	6,700
Canadian Dollar	97	11,312	2,570	13,979
Swiss Franc	4	34,855	-	34,859
Danish Krone	4	4,707	14,785	19,496
Euro Currency	989	162,934	69,880	233,803
Pound Sterling	356	116,202	3,647	120,205
Hong Kong Dollar	212	48,001	-	48,213
Indonesian Rupiah	-	1,153	-	1,153
Japanese Yen	1,588	124,209	39,826	165,623
South Korean Won	1	729	-	730
Norwegian Krone	128	121	-	249
New Zealand Dollar	-	605	-	605
Philippine Peso	-	140	-	140
Swedish Krona	103	7,357	4,437	11,897
Singapore Dollar	5	6,953	-	6,958
Taiwan Dollar	37	3,360	-	3,397
South African Rand	-	2,093	-	2,093
Totals	$ 4,213	$ 548,702	$ 146,862	$ 699,777

[1] The foreign exchange exposure in SDCERS' international equity small cap value portfolio (an institutional mutual fund investment) is not included in this disclosure.

Source: SCDERS' CAFR as of June 30, 2009

Foreign currency is comprised of international investment proceeds and income to be repatriated into U.S. dollars and funds available to purchase international securities. Foreign currency is not held by SDCERS as an investment. Foreign currency is held temporarily in foreign accounts until it is able to be repatriated or expended to settle trades. A significant component of the diversification benefit of non-domestic investments comes from foreign currency exposure. As such, SDCERS does not have a policy to hedge against fluctuations in foreign exchange rates. SDCERS' investment managers may hedge currencies at their discretion pursuant to specific guidelines included in their investment management agreements.

p. Derivative Instruments

SDCERS' investment managers, as permitted by specific investment guidelines, may enter into transactions involving derivative financial instruments, consistent with the objectives established by the Board's Investment Policy Statement. These instruments include futures, options and swaps. By Board policy these investment vehicles may not be used to leverage SDCERS' portfolio. These instruments are used primarily to enhance a portfolio's performance and to reduce its risk or volatility. The notional or contractual amount (in thousands) of futures contracts as of June 30, 2009 was $350,600. The fair value (in thousands) of options and swaps included in the short-term investments line on the SDCERS Statement of Plan Net Assets was $7,900 as of June 30, 2009.

Futures contracts are contracts in which the buyer agrees to purchase and the seller agrees to make delivery on a specific financial instrument on a predetermined date and price. Gains and losses on futures contracts are settled daily based on a notional principal value and do not involve an actual transfer of the specific instrument. Futures contracts are standardized and are traded on exchanges. The exchange assumes the risk that counterparty will not pay and generally requires margin payments to minimize such risk.

Option contracts provide the option purchaser with the right, but not the obligation, to buy or sell the underlying security at a set price during a period or at a specified date. The option writer is obligated to buy or sell the underlying security if the option purchaser chooses to exercise the option. SDCERS uses exchange-traded and over-the-counter options. Options are sold and proceeds are received to enhance fixed income portfolio performance. Option contracts sold were predominantly on money market and short-term instruments of less than one-year to maturity. In call option contracts, if interest rates remained steady or declined during the option contract periods, the contracts would expire unexercised. By contrast, in put option contracts, if interest rates rose sufficiently to result in the purchase of the securities on or before the end of the option periods, this would occur at prices attractive to the portfolio manager.

Swap agreements are used to modify investment returns or interest rates on investments. Swap transactions involve the exchange of investment returns or interest rate payments without the exchange of the underlying principal amounts. These swaps could expose investors entering into these types of arrangements to credit risk in the event of non-performance by counterparties.

In January 2009, SDCERS implemented a cash overlay program with the objective of keeping the portfolio performing more closely to its target asset allocations. SDCERS does not have an allocation to cash, but the portfolio will have cash balances held at the investment manager level to settle trades. The overlay program utilizes futures contracts as an inexpensive, highly liquid method of maintaining the portfolio's exposures to the target allocation.

q. Real Estate

SDCERS' target allocation to real estate is 11%. SDCERS' Board established the following portfolio composition target: a minimum of 30% in stable core real estate and a maximum of 70% to enhanced, high return and opportunistic real estate opportunities. No more than 40% of SDCERS' real estate portfolio is allocated to non-U.S. real estate investment opportunities pursuant to a policy adopted by the Board in FY 2007. As of June 30, 2009, unfunded capital commitments totaled $111,300 and real estate investments totaled $350,498.

r. Securities Lending Collateral

SDCERS has entered into an agreement with its custodial bank, State Street, to lend domestic and international equity and fixed income securities to broker-dealers and banks in exchange for pledged collateral that will be returned for the same securities plus a fee in the future. All securities loans can be terminated on demand by either the lender or the borrower.

State Street manages the securities lending program and receives cash and/or securities as collateral. Borrowers are required to deliver collateral equal to 102% of the market value of domestic securities on loan and 105% of the market value of international securities on loan. State Street does not have the ability to pledge or sell collateral securities delivered absent a borrower default.

SDCERS had no credit risk exposure to borrowers because the amounts provided to State Street on behalf of SDCERS, in the form of collateral plus accrued interest, exceeded the amounts broker-dealers and banks owed to the State Street on behalf of SDCERS for securities borrowed. State Street has indemnified SDCERS by agreeing to purchase replacement securities or return cash collateral in the event a borrower fails to return or pay distributions on a loaned security. SDCERS incurred no losses during the fiscal year resulting from a default of the borrowers or State Street. Non-cash collateral (securities and letters of credit) cannot be pledged or sold without a borrower default and are therefore not reported as an asset of SDCERS for financial reporting purposes.

Despite lending securities on a fully collateralized basis, SDCERS may encounter various risks related to securities lending agreements. These risks include operational risk, borrower or counterparty default risk, and collateral reinvestment risk. During the fiscal year, the two collateral pools that SDCERS was invested in and managed by State Street were impacted by market events and the credit crunch. Market values of securities held in collateral pools declined as liquidity evaporated. However, SDCERS' investments in the collateral pools did not realize any losses. State Street is required to maintain its securities lending program in compliance with applicable laws of the United States and all countries in which lending activities take place, and all rules, regulations, and exemptions from time to time promulgated and issued under the authority of those laws.

The SDCERS securities lending transactions, collateralized by cash as of June 30, 2009 had a fair value of $382,500 and a collateral value of $395,085, which were reported in the assets and liabilities in the accompanying Statements of Plan Net Assets for the Group Trust in accordance with GASB Statement No. 28. As of June 30, 2009, the securities lending transactions collateralized by securities, irrevocable letters of credit, or tri-party collateral had a fair value of $35,000 and a collateral value of $36,800, which were not reported in the assets or liabilities in the accompanying Statements of Plan Net Assets for the Group Trust per GASB Statement No. 28. The total collateral pledged to SDCERS at fiscal year end for its securities lending activities was $395,085.

The cash collateral received on lent securities was invested by State Street, together with the cash collateral of other qualified tax-exempt plan lenders, in a collective investment pool. Because the securities loans were terminable at will, their duration did not generally match the duration of the investments made with cash collateral. As of June 30, 2009, the investment pool had an average duration of 42.64 days and an average weighted maturity of 317.62 days for U.S. Dollar (USD) denominated collateral. Beginning in fiscal year 2007, the securities lending program was expanded to allow the acceptance of Euro (EUR) denominated collateral. As of June 30, 2008, the Euro collateral pool had an average duration of 35 days and an average weighted maturity of 508 days.

As of June 30, 2009, SDCERS has lent $417,500 in securities and received collateral of $36,759 and $395,085 in securities and cash, respectively from borrowers. SDCERS' securities lending transactions as of June 30, 2009, are summarized in the following table.

Securities Lending as of June 30, 2009

Security Type	Fair Value of Loaned Securities	Cash Collateral	Fair Value of Securities Collateral
Securities Loaned for Cash Collateral			
US Corporate Bond and Equity (USD)	$ 255,040	$ 263,150	$ -
US Government Agencies (USD)	39,839	40,672	-
Non-US Fixed Income (EUR)	38,307	38,924	-
Non-US Fixed Income (USD)	2,754	2,765	-
Non-US Equity (USD)	46,550	49,574	-
Securities Loaned with Non-Cash Collateral			
US Government Agencies (USD)	11,422	-	11,795
US Corporate Bond and Equity (USD)	124	-	3,011
Non-US Equity (EUR)	-	-	1
Non-US Equity (USD)	23,464	-	21,952
Total	$ 417,500	$ 395,085	$ 36,759

Source: SCDERS' as of June 30, 2009

Discretely Presented Component Units – Disclosures for Policy and Specific Risks

Narratives and tables presented in the following sections (s. through t.) are taken directly from the comprehensive annual financial reports of the San Diego Convention Center Corporation and the San Diego Housing Commission, as of June 30, 2009, respectively.

s. San Diego Convention Center Corporation

Cash deposits and investments for SDCCC were categorized as follows at June 30, 2009:

Cash on hand	$ 59
Deposits	1,449
Certificates of deposit	1,452
Money market account deposits	1,010
Money market mutual funds	17,786
Total cash and investments	$ 21,756

Deposits (In Thousands)

On June 30, 2009, the carrying amount of the San Diego Convention Center Corporation's (SDCCC) cash on hand, deposits, certificates of deposit, and money market account deposits was $3,970 and the bank balance was $4,029. Of the bank balance, $2,317 was covered by federal depository insurance. The remaining uninsured balance of $1,712 was collateralized with the collateral held by an affiliate of the counterparty's financial institution. Neither the money market account deposits nor the certificates of deposit are rated by credit rating agencies. The $1,452 invested in certificates of deposit bear interest rates from 1.3% to 1.6%, and have maturities of less than one year. SDCCC does not have a formal deposit and investment policy that addresses custodial credit risk.

Investments (In Thousands)

At June 30, 2009, SDCCC had a total investment balance of $17,786. The total investment balance includes $17,786 in money market mutual funds. Of the amount invested in money market funds and accounts, $13,634 was covered by the U.S. Treasury Department's temporary Money Market Fund Guarantee Program. The money market mutual funds are not rated by credit rating agencies. SDCCC does not have a formal deposit and investment policy that addresses credit quality risk and places no limit on the amount that may be invested in any one account or fund. Of the total investments not covered by the Guarantee Program or Federal depository insurance, 16.5% were invested in a Dreyfus money market mutual fund. There were no other investment amounts in any single account or fund that exceeded 5% of total uninsured investments.

t. San Diego Housing Commission

Cash, cash equivalents, and investments at June 30, 2009 consisted of the following:

Deposits	$ 4,261
Petty cash	12
Certificates of deposit	2,259
Agency Bonds	49,494
Corporate Bonds	7,103
Investment - Other	1
Local agency investment fund	31,328
Total cash and investments	94,458
Restricted cash and cash equivalents	699
Total	$ 95,157

Deposits (In Thousands)

The carrying amount of the San Diego Housing Commission's (SDHC) deposits and petty cash was $4,273 and the bank balance was $4,737 at June 30, 2009. The bank balances were fully insured and/or collateralized with securities held by the pledging financial institutions in SDHC's name. The California Government Code requires California banks and savings and loan associations to secure SDHC's deposits by pledging securities as collateral. This Code states that collateral pledged in this manner shall have the effect of perfecting a security interest in such collateral superior to those of a general creditor. Thus, collateral for cash deposits is considered to be held in SDHC's name.

At June 30, 2009, SDHC had a carrying amount and bank balance of $2,259 in non-negotiable certificates of deposit. The certificates of deposit were either covered by FDIC insurance or 100% collateralized with securities held by pledging financial institutions.

Investments (In Thousands)

As of June 30, 2009, SDHC's investments included corporate bonds, agency bonds, and California Local Agency Investment Fund (LAIF). SDHC had $7,103 in corporate bonds, which represent an investment in FDIC-guaranteed floating rate corporate debt securities (floaters) explicitly backed by the U.S. government. Unlike fixed rate instruments, the coupon rate on these floating-rate securities resets every 3 months based on the 90 day London Inter-Bank Offer Rate (LIBOR) index plus a margin or basis points. All of SDHC's corporate bonds were rated AAA by Standard & Poor's as of June 30, 2009.

Agency bonds represent the SDHC's investment in Government-Sponsored Enterprises (GSE) Senior Debt bonds and Mortgage-backed Security (MBS) bonds traded on an active secondary market. As of June 30, 2009, SDHC had $49,494 invested in these AAA rated securities, with a weighted average maturity of 791 days.

SDHC participates in the Local Agency Investment Fund (LAIF). As of June 30, 2009, SDHC had $31,328 invested with LAIF. The investment in LAIF represents SDHC's equity in the pooled investments of that fund. The average maturity of LAIF investments was 235 days as of June 30, 2009. LAIF had 14.71% of the pool investment funds in structured notes and asset-backed securities.

Policy

In accordance with state statutes and HUD regulations, SDHC has authorized the CFO or their designee to invest in obligations of the U.S. Treasury, U.S. Government agencies or other investments as outlined in the

Commission Investment Policy. An Investment Committee, consisting of two Commission Board members, monitors the management of funds and compliance with the Commission Investment Policy. There are many factors that can affect the value of investments. Some factors, such as credit risk, custodial risk, concentration of credit risk, and interest rate risk, may affect both equity and fixed income securities. It is the investment policy of SDHC to invest substantially all of its funds in fixed income securities which limits SDHC's exposure to most types of risk.

Interest Rate Risk

In accordance with its investment policy, SDHC manages its interest rate risk by limiting the weighted average maturity of its investment portfolio. This is accomplished by matching portfolio maturities to projected liabilities and by continuously investing a portion of the portfolio in readily available funds to ensure that appropriate liquidity is maintained in order to meet ongoing operations.

Credit Risk

SDHC will minimize credit risk by limiting investments to those listed in the investment policy. In addition, SDHC will pre-qualify the financial institutions, broker/dealers, intermediaries, and advisors with which SDHC will do business in accordance with the investment policy. SDHC will diversify the portion of the investment portfolio not invested in U.S. Treasury Bills, Notes, Bonds, and Collateralized Certificates of Deposit to minimize potential losses from any one type of security or issuer.

Concentration of Credit Risk

Concentration of credit risk is the risk associated with a lack of diversification, such as having substantial investments in a few individual issuers. Investments issued or guaranteed by the U.S. government and investments in external investment pools such as LAIF are not considered subject to concentration of credit risk. SDHC may choose to maintain 100% of its investment portfolio in U.S. Treasury Bills, Notes, Bonds, and Collateralized Certificates of Deposit.

Custodial Credit Risk

At June 30, 2009, SDHC did not have any investments exposed to custodial risk. Bonds are purchased through a Merrill Lynch account in SDHC's name. All securities are held in safekeeping by Merrill Lynch and are covered by Securities Investor Protection Corporation (SIPC) and a separate Lloyd's of London policy for a combined aggregate limit of $600 million.

4. CAPITAL ASSETS (In Thousands)

Capital asset activity for the year ended June 30, 2009 was as follows:

	Primary Government				
	Beginning Balance	Increases	Decreases/ Adjustments	Transfers	Ending Balance
GOVERNMENTAL ACTIVITIES:					
Non-Depreciable Capital Assets:					
Land, Easements, Rights of Way	$ 1,755,956	$ 20,081	$ (6,587)	$ (482)	$ 1,768,968
Construction in Progress	165,880	125,367	(4,149)	(94,357)	192,741
Total Non-Depreciable Capital Assets	1,921,836	145,448	(10,736)	(94,839)	1,961,709
Depreciable Capital Assets:					
Structures and Improvements	1,143,383	13,231	(1,426)	14,600	1,169,788
Equipment	367,004	65,087	(64,151)	2,513	370,453
Infrastructure	3,007,785	56,086	(3,066)	79,746	3,140,551
Total Depreciable Capital Assets	4,518,172	134,404	(68,643)	96,859	4,680,792
Less Accumulated Depreciation For:					
Structures and Improvements	(315,471)	(29,158)	1,426	(97)	(343,300)
Equipment	(233,687)	(34,940)	69,863	(2,302)	(201,066)
Infrastructure	(1,555,533)	(87,395)	383	(65)	(1,642,610)
Total Accumulated Depreciation	(2,104,691)	(151,493)	71,672	(2,464)	(2,186,976)
Total Depreciable Capital Assets - Net of Depreciation	2,413,481	(17,089)	3,029	94,395	2,493,816
Governmental Activities Capital Assets, Net	$ 4,335,317	$ 128,359	$ (7,707)	$ (444)	$ 4,455,525
BUSINESS-TYPE ACTIVITIES:					
Non-Depreciable Capital Assets:					
Land, Easements, Rights of Way	$ 89,988	$ -	$ (5)	$ 3,257	$ 93,240
Construction in Progress	174,065	202,630	(4,772)	(80,640)	291,283
Total Non-Depreciable Capital Assets	264,053	202,630	(4,777)	(77,383)	384,523
Depreciable Capital Assets:					
Structures and Improvements	1,785,713	5,144	(199,367)	18,871	1,610,361
Equipment	342,574	3,100	56,206	2,111	403,991
Distribution & Collection Systems and Other Infrastructure	3,481,401	54,946	119,275	54,381	3,710,003
Total Depreciable Capital Assets	5,609,688	63,190	(23,886)	75,363	5,724,355
Less Accumulated Depreciation For:					
Structures and Improvements	(362,874)	(36,641)	42,954	103	(356,458)
Equipment	(240,505)	(22,918)	14,027	2,296	(247,100)
Distribution & Collection Systems and Other Infrastructure	(635,444)	(62,419)	(40,801)	65	(738,599)
Total Accumulated Depreciation	(1,238,823)	(121,978)	16,180	2,464	(1,342,157)
Total Depreciable Capital Assets - Net of Depreciation	4,370,865	(58,788)	(7,706)	77,827	4,382,198
Business-Type Activities Capital Assets, Net	$ 4,634,918	$ 143,842	$ (12,483)	$ 444	$ 4,766,721

Governmental Activities capital assets net of accumulated depreciation at June 30, 2009 are comprised of the following:

General Capital Assets, Net	$	4,329,571
Internal Service Funds Capital Assets, Net		125,954
Total	$	4,455,525

Business-Type Activities capital assets net of accumulated depreciation at June 30, 2009 are comprised of the following:

Enterprise Funds Capital Assets, Net	$	4,766,721

Depreciation expense was charged to functions/programs of the primary government as follows:

Governmental Activities:

General Government and Support	$	5,914
Public Safety - Police		4,904
Public Safety - Fire and Life Safety		2,892
Parks, Recreation, Culture and Leisure		35,067
Transportation		73,761
Sanitation and Health		290
Neighborhood Services		2,152
Subtotal		124,980
Internal Service		26,513
Total Depreciation Expense	$	151,493

Business-Type Activities:

Airports	$	520
City Store		1
Development Services		267
Environmental Services		3,140
Golf Course		817
Recycling		1,052
Sewer Utility		76,554
Water Utility		39,627
Total Depreciation Expense	$	121,978

Discretely Presented Component Units

Capital asset activities for the City's Discretely Presented Component Units for the year ended June 30, 2009 are as follows:

Discretely Presented Component Unit - San Diego Convention Center Corp.	Beginning Balance	Increases	Decreases/ Adjustments	Ending Balance
Depreciable Capital Assets:				
Structures and Improvements	$ 25,329	$ 1,097	$ (160)	$ 26,266
Equipment	9,317	627	(214)	9,730
Total Depreciable Capital Assets	34,646	1,724	(374)	35,996
Less Accumulated Depreciation For:				
Structures and Improvements	(10,626)	(1,691)	96	(12,221)
Equipment	(6,843)	(735)	207	(7,371)
Total Accumulated Depreciation	(17,469)	(2,426)	303	(19,592)
Capital Assets, Net	$ 17,177	$ (702)	$ (71)	$ 16,404

Discretely Presented Component Unit - San Diego Housing Commission	Beginning Balance	Increases	Decreases/ Adjustments	Ending Balance
Non-Depreciable Capital Assets:				
Land, Easements, Rights of Way	$ 29,544	$ -	$ -	$ 29,544
Construction in Progress	11,720	-	(4,719)	7,001
Total Non-Depreciable Capital Assets	41,264	-	(4,719)	36,545
Depreciable Capital Assets:				
Structures and Improvements	64,273	-	4,499	68,772
Equipment	2,463	162	220	2,845
Total Depreciable Capital Assets	66,736	162	4,719	71,617
Less Accumulated Depreciation For:				
Structures and Improvements	(7,628)	(1,942)	-	(9,570)
Equipment	(939)	(425)	-	(1,364)
Total Accumulated Depreciation	(8,567)	(2,367)	-	(10,934)
Total Depreciable Capital Assets - Net of Depreciation	58,169	(2,205)	4,719	60,683
Capital Assets, Net	$ 99,433	$ (2,205)	$ -	$ 97,228

5. GOVERNMENTAL ACTIVITIES LONG-TERM LIABILITIES (IN THOUSANDS)

a. Long-Term Liabilities

Governmental long-term liabilities as of June 30, 2009 are comprised of the following:

Type of Obligation	Interest Rates	Fiscal Year Maturity Date	Original Amount	Balance Outstanding June 30, 2009
Arbitrage Liability				$ 533
Compensated Absences				74,446
Liability Claims				273,979
Capital Lease Obligations				89,519
Contracts Payable:				
Contract Payable to SDSU Foundation, dated December 1991	variable*	---	$ 1,598	1,598
Amendment to Contract Payable to SDSU Foundation, dated January 1995	variable*	---	117	117
Contract Payable to Western Pacific Housing, Inc., dated April 2004	5.0%	---	3,000	3,000
Total Contracts Payable				4,715
Notes Payable:				
Note Payable to Price Charities, dated April 2001	5.0	2032	5,115	2,506
Note Payable to Price Charities, dated May 2005	8.0	2025	2,100	2,100
Amendment to Note Payable to Price Charities, dated February 2006	8.0	2025	180	180
Total Notes Payable				4,786
Loans Payable:				
International Gateway Associates, LLC, dated October 2001	10.0	2032	1,876	1,788
PCCP/SB Las America, LLC, dated August 2005	10.0	2036	1,247	1,222
Centerpoint, LLC, dated April 2006	5.5	2021	5,246	4,969
Bank of America, N.A. Line of Credit, dated October 2006	variable*	2009	8,530	8,530
California Housing Finance Agency dated October, 2006	3.0	2017	1,250	1,250
California Energy Resources Conservation and Development Commission, dated January 2007	4.5	2021	302	302
California Energy Resources Conservation and Development Commission, dated March 2007	3.95	2019	2,154	1,760
San Diego National Bank, Line of Credit, dated July 2007 City Heights Housing Area	4.05	2011	1,298	1,298
San Diego National Bank, Line of Credit, dated July 2007 City Heights Non-Housing Area	6.42	2011	2,011	2,011
San Diego National Bank, Line of Credit, dated July 2007 Naval Training Center Housing Area	2.58	2011	2,635	2,635
San Diego National Bank, Line of Credit, dated July 2007 Naval Training Center Non-Housing Area	1.0 - 5.49	2011	6,804	11,100
San Diego National Bank, Line of Credit, dated July 2007 North Bay Housing Area	4.05	2011	2,255	2,255
San Diego National Bank, Line of Credit, dated July 2007 North Park Non-Housing Area	1.42 - 4.05	2011	3,695	5,695
Total Loans Payable				44,815
Section 108 Loans Payable				33,532

Type of Obligation	Interest Rates	Fiscal Year Maturity Date	Original Amount	Balance Outstanding June 30, 2009
General Obligation Bonds:				
Public Safety Communications Project, Series 1991	5.0 - 8.0**	2012	$ 25,500	$ 6,315
Total General Obligation Bonds				6,315
Revenue Bonds / Lease Revenue Bonds / COPs:				
MTDB Authority Lease Revenue Refunding Bonds, Series 1994	4.25 - 5.625**	2010	66,570	2,770
Public Facilities Financing Authority Stadium Lease Revenue Bonds, Series 1996 A	6.2 - 7.45**	2027	68,425	56,275
San Diego Facilities and Equipment Leasing Corp. Certificates of Participation, Series 1996 A	4.0 - 5.6**	2011	33,430	6,685
San Diego Facilities and Equipment Leasing Corp. Certificates of Participation Refunding, Series 1996 B	4.0 - 6.0**	2022	11,720	8,050
Convention Center Expansion Financing Authority Lease Revenue Bonds, Series 1998 A	3.8 - 5.25**	2028	205,000	168,065
Centre City Parking Revenue Bonds, Series 1999 A	4.5 - 6.49**	2026	12,105	9,860
Public Facilities Financing Authority Reassessment District Refunding Revenue Bonds, Series 1999 A	2.75 - 4.75**	2018	30,515	11,850
Public Facilities Financing Authority Reassessment District Refunding Revenue Bonds, Series 1999 B	3.5 - 5.10**	2018	7,630	2,930
Public Facilities Financing Authority Fire and Life Safety Lease Revenue Bonds, Series 2002 B	3.55 - 7.0**	2032	25,070	22,280
Centre City Parking Revenue Bonds, Series 2003 B	3.0 - 5.30**	2027	20,515	17,570
MTDB Authority Lease Revenue Refunding Bonds, Series 2003	2.0 - 4.375**	2023	15,255	12,120
San Diego Facilities Equipment Leasing Corp. Certificates of Participation Refunding, Series 2003	1.0 - 4.0**	2024	17,425	8,655
Public Facilities Financing Authority Ballpark Lease Revenue Refunding Bonds, Series 2007 A	5.0 - 5.25**	2032	156,560	149,390
Public Facilities Financing Authority Lease Revenue Bonds, Series 2009 A	variable*	2019	103,000	103,000
Total Revenue Bonds / Lease Revenue Bonds / COPs				579,500
Special Assessment / Special Tax Bonds:				
Otay Mesa Industrial Park Limited Obligation Improvement Bonds, Issued May 1992	5.5 - 7.95**	2013	2,235	250
Miramar Ranch North Special Tax Refunding Bonds, Series 1998	3.75 - 5.375**	2021	59,465	39,650
Santaluz Special Tax Bonds, Improvement Area No.1, Series 2000 A	4.75 - 6.375**	2031	56,020	52,000
Santaluz Special Tax Bonds, Improvement Area No.3, Series 2000 B	4.5 - 6.2**	2031	4,350	4,020
City of San Diego Reassessment District No. 2003-1 Limited Obligation Refunding Bonds	4.25 - 5.8**	2018	8,850	6,210
Piper Ranch Limited Obligation Improvement Bonds, Issued January 2004	2.5 - 6.2**	2034	5,430	4,310
Santaluz Special Tax Bonds, Improvement Area No.1, Series 2004 A	1.7 - 5.5**	2031	5,000	4,500
Santaluz Special Tax Bonds, Improvement Area No.4, Series 2004 A	1.65 - 5.5**	2034	9,965	9,450
Liberty Station Special Tax Bonds, Series 2006 A	5.0 - 5.75**	2037	16,000	15,630
Liberty Station Special Tax Bonds, Series 2008 A	3.74 - 6.3**	2037	3,950	3,885
Black Mountain Ranch Villages Special Tax Bonds Series 2008 A	3.125-6.0**	2038	12,365	12,365
Total Special Assessment / Special Tax Bonds				152,270

(continued on next page)

Type of Obligation	Interest Rates	Fiscal Year Maturity Date	Original Amount	Balance Outstanding June 30, 2009
Tax Allocation Bonds:				
Gateway Center West Redevelopment Project Tax Allocation Bonds, Series 1995	7.8 - 9.75**	2014	$ 1,400	$ 580
Mount Hope Redevelopment Project Tax Allocation Bonds, Series 1995 A	4.4 - 6.0**	2020	1,200	750
Horton Plaza Redevelopment Project Tax Allocation Refunding Bonds, Series 1996 A	3.8 - 6.0**	2016	12,970	6,355
Centre City Redevelopment Tax Allocation Bonds, Series 1999 A	3.0 - 5.125**	2019	25,680	25,200
Centre City Redevelopment Tax Allocation Bonds, Series 1999 B	6.25**	2014	11,360	11,360
Centre City Redevelopment Tax Allocation Bonds, Series 1999 C	3.1 - 4.75**	2025	13,610	11,705
City Heights Redevelopment Tax Allocation Bonds, Series 1999 A	4.5 - 5.8**	2029	5,690	5,060
City Heights Redevelopment Tax Allocation Bonds, Series 1999 B	5.75 - 6.4***	2029	10,141	8,982
Centre City Redevelopment Project Tax Allocation Bonds, Series 2000 A	4.0 - 5.6**	2025	6,100	4,810
Centre City Redevelopment Project Tax Allocation Bonds, Series 2000 B	3.95 - 5.35**	2025	21,390	18,190
Horton Plaza Redevelopment Project Tax Allocation Bonds, Series 2000	4.25 - 5.8**	2022	15,025	13,110
North Bay Redevelopment Project Tax Allocation Bonds, Series 2000	4.25 - 5.875**	2031	13,000	11,200
North Park Redevelopment Project Tax Allocation Bonds, Series 2000	4.1 - 5.9**	2031	7,000	6,035
Centre City Redevelopment Tax Allocation Bonds, Series 2001 A	4.93 - 5.55****	2027	58,425	55,795
Mount Hope Redevelopment Project Tax Allocation Bonds, Series 2002 A	5.0**	2027	3,055	3,055
Centre City Redevelopment Project Tax Allocation Bonds, Series 2003 A	2.5 - 5.0**	2029	31,000	11,980
City Heights Redevelopment Project Tax Allocation Bonds, Series 2003 A	5.875 - 6.5**	2034	4,955	4,955
City Heights Redevelopment Project Tax Allocation Bonds, Series 2003 B	2.5 - 4.25**	2014	865	410
North Park Redevelopment Project Tax Allocation Bonds, Series 2003 A	1.5 - 6.125**	2028	7,145	6,045
North Park Redevelopment Project Tax Allocation Bonds, Series 2003 B	4.75 - 5.0**	2034	5,360	5,360
Horton Plaza Redevelopment Project Tax Allocation Bonds, Series 2003 A	4.65 - 5.1**	2022	6,325	6,325
Horton Plaza Redevelopment Project Tax Allocation Bonds, Series 2003 B	3.25 - 5.45**	2022	4,530	4,300
Horton Plaza Redevelopment Project Tax Allocation Bonds, Series 2003 C	3.49 - 7.74**	2022	8,000	6,565
Centre City Redevelopment Project Tax Allocation Bonds, Series 2004 A	3.5 - 5.25**	2030	101,180	93,410
Centre City Redevelopment Project Tax Allocation Bonds, Series 2004 B	2.26 - 4.58**	2011	9,855	3,035
Centre City Redevelopment Project Tax Allocation Bonds, Series 2004 C	2.26 - 6.18**	2030	27,785	25,035

Type of Obligation	Interest Rates	Fiscal Year Maturity Date	Original Amount	Balance Outstanding June 30, 2009
Centre City Redevelopment Project Tax Allocation Bonds, Series 2004 D	2.26 - 6.28**	2030	$ 8,905	$ 8,035
Centre City Redevelopment Project Tax Allocation Bonds, Series 2006 A	4.25 - 5.25**	2033	76,225	75,025
Centre City Redevelopment Project Tax Allocation Bonds, Series 2006 B	5.66 - 6.2**	2032	33,760	32,880
Centre City Redevelopment Project Tax Allocation Bonds, Series 2008 A	3.74 - 6.3**	2021	69,000	69,000
Total Tax Allocation Bonds				534,547
Tobacco Settlement Asset-Backed Bonds:				
Tobacco Settlement Revenue Funding Corporation Asset-Backed Bonds, Series 2006	7.125**	2023	105,400	95,380
Pooled Financing Bonds:				
Public Facilities Financing Authority Pooled Financing Bonds, Series 2007 A	5.95 - 6.65**	2038	17,230	16,340
Public Facilities Financing Authority Pooled Financing Bonds, Series 2007 B	4.0 - 5.25**	2038	17,755	17,120
Total Pooled Financing Bonds				33,460
Total Bonds Payable				1,401,472
Net Other Postemployment Benefits Obligation				73,504
Net Pension Obligation				147,665
Total Governmental Activities Long-Term Liabilities				$ 2,148,966

* Additional information on the variable rate contracts payable with the SDSU Foundation, the loan payable line of credit from Bank of America, and the PFFA Lease Revenue Bonds, Series 2009 A are discussed further on the following page.

** Interest rates are fixed, and reflect the range of rates for various maturities from the date of issuance to maturity.

*** The City Heights Redevelopment Tax Allocation Bonds, Series 1999 B, are capital appreciation bonds, which mature from fiscal year 2011 through 2029. The balance outstanding at June 30, 2009 does not include accreted interest of $7,695.

**** The Centre City Redevelopment Tax Allocation Bonds, Series 2001 A, partially include capital appreciation bonds, which mature from fiscal year 2015 through 2027. The balance outstanding at June 30, 2009 does not include accreted interest of $6,987.

Arbitrage Rebate Liability is calculated via third party providers in accordance with the provisions of the Internal Revenue Code of 1986, as amended, and the United States Treasury Regulations effective as of July 1, 1993, as amended.

Liability claims are primarily liquidated by the Self Insurance (Internal Service) Fund and Enterprise Funds. Compensated absences are generally liquidated by the general fund and certain internal service funds. Pension liabilities are paid out of the operating funds based on a percentage of payroll.

Public safety general obligation bonds are secured by a pledge of the full faith and credit of the City or by a pledge of the City to levy ad valorem property taxes without limitation. Open space general obligation bonds are backed by Environmental Growth Fund 2/3 franchise fees.

Revenue bonds are secured by a pledge of specific revenue generally derived from fees or service charges related to the operation of the project being financed. Certificates of Participation (COPs) and lease revenue bonds provide long-term financing through a lease agreement, installment sales agreement, or loan agreement that does not constitute indebtedness under the state constitutional debt limitation and is not subject to other statutory requirements applicable to bonds.

Special assessment/special tax bonds are issued by the City to provide funds for public improvements in/and or serving special assessment and Mello-Roos districts created by the City. The bonds are secured by assessments and special taxes levied on the properties located within the assessment districts and the community facilities districts, and are payable solely from the assessments and special taxes collected. The assessments and the special taxes, and any bonds payable from them, are secured by a lien on the properties upon which the assessments and the special taxes are levied. Neither the faith and credit nor the taxing power of the City is pledged to the payment of the bonds.

Section 108 loans are the loan guarantee provisions of the Community Development Block Grant (CDBG) program. Section 108 loans provide the community with a source of financing for economic development, housing rehabilitation, public facilities, and capital improvement and infrastructure projects.

San Diego State University Foundation executed an Agreement for Processing a Redevelopment Plan and Land Use Entitlements with RDA which allows for reimbursement of expenses incurred by the Foundation, in assisting in the preparation and processing of the Redevelopment Plan and Land Use Entitlements in the College Area. The agreement is a variable rate obligation of RDA. The unpaid principal bears interest at the prime rate and is fixed on a quarterly basis, using the prime rate established on the first banking day of each calendar quarter. Interest calculations are made on the quarterly weighted average of the principal balance and are made at the end of the quarter based upon the rate fixed for that quarter. The effective interest rate as of June 30, 2009 is 3.25 percent.

Loans Payable includes a loan agreement with Centerpoint, LLC that was for the purpose of constructing affordable housing and retail space pursuant to the terms of a Disposition and Development Agreement and the first and second implementation agreements. On December 29, 2008 a third implementation agreement was executed that converted the project from the sale of residential dwelling units to rental residential dwelling units. Due to the modification of the size of the dwelling units to be developed and the corresponding reduction in the development costs, the amount of the loan was reduced from $5,245 to $4,969. The corresponding liability has been reduced in the Statement of Net Assets.

Loans Payable includes a line of credit executed by RDA with Bank of America, N.A. on October 31, 2006. The line of credit is to be used to refinance the North Park Theatre, to pay sums of settlement of eminent domain actions relating to the North Park Redevelopment Area and for other redevelopment activities in the North Park Redevelopment Area. The tax-exempt portion of the line of credit has an effective interest rate of 3.23 percent, the taxable portion has an effective interest rate of 4.75 percent as of June 30, 2009, and the effective interest rate will reset on October 31, annually.

Loans Payable also includes six separate non-revolving secured three-year term lines of credit executed by RDA with San Diego National Bank dated July 26, 2007. Four lines of credit are for affordable housing in North Park, City Heights, North Bay and Naval Training Center (NTC) Redevelopment Project Areas. Two lines of credit are for non-housing or general purposes for City Heights and NTC Redevelopment Project Areas. Each advance taken from the lines of credit has a fixed rate that is set on the day of the advance to be equal to either the United States Three-Year Treasury Constant Maturities Index plus one and nine-tenths percentage point or the One-Month LIBOR Rate plus one and one-tenth percentage point and that rate remains constant during the entire period such advance is outstanding.

PFFA Lease Revenue Bonds, Series 2009A were issued for the purpose of financing various capital improvement projects. The Series 2009A bonds are secured from base rental payments and bear interest at a rate of 3.89 percent through June 1, 2010. Thereafter the interest rate will be fixed to equal the purchaser's internal cost of funds rate plus a fixed spread of 3.0 percent, provided that in no event will the interest rate exceed 12 percent, and the new rate will remain constant until the final maturity date of December 1, 2018.

Tobacco Settlement Asset-Backed Bonds are limited obligations of the Tobacco Settlement Revenue Funding Corporation, which is a separate legal California nonprofit public benefit corporation established by the City of San Diego. The Corporation purchased from the City the rights to receive future tobacco settlement revenues due to the City. The Tobacco Settlement Asset-Backed Bonds are payable from and secured solely by pledged tobacco settlement revenues.

b. Amortization Requirements

The annual requirements to amortize such long-term debt outstanding as of June 30, 2009, including interest payments to maturity, are as follows:

Year Ended June 30,	Capital Lease Obligations		Contracts Payable		Notes Payable		Loans Payable	
	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest
2010	$ 15,963	$ 3,551	$ -	$ -	$ -	$ -	$ 8,708	$ 1,616
2011	15,475	2,661	-	-	-	-	25,180	650
2012	15,915	2,056	-	-	-	-	195	351
2013	14,294	1,438	-	-	-	-	205	341
2014	10,152	933	-	-	-	-	216	330
2015-2019	13,413	1,827	-	-	-	-	1,264	1,467
2020-2024	4,307	531	-	-	-	-	480	1,177
2025-2029	-	-	-	-	-	-	772	884
2030-2034	-	-	-	-	-	-	1,045	412
2035-2039	-	-	-	-	-	-	229	35
Unscheduled*	-	-	4,715	1,868	4,786	1,767	6,521	-
Total	$ 89,519	$ 12,997	$ 4,715	$ 1,868	$ 4,786	$ 1,767	$ 44,815	$ 7,263

** The contracts payable to SDSU Foundation in the amount of $1,715, the contract payable to Western Pacific Housing, Inc. in the amount of $3,000, the notes payable to Price Charities of $4,786, the loan payable to Centerpoint, LLC in the amount of $4,969, the loan payable to California Housing Finance Agency in the amount of $1,250, and the loan payable to the California Energy Resources Conservation and Development Commission in the amount of $302 do not have repayment schedules. Annual payments on the San Diego State University debt is based on the availability of tax increment, net of the low-moderate and taxing agency set-asides, as well as project area administration costs. Annual payments on the Western Pacific Housing, Inc., and Price Charities debt are based on available tax increment. Annual payments on the Centerpoint, LLC debt are based upon future receipts of unallocated tax increment or other available sources. Annual payments on the California Housing Agency are deferred for the term of the loan. Annual payments on the California Energy and Resources Conservation and Development Commission will not begin until project completion.*

Year Ended June 30,	Section 108 Loans Principal	Section 108 Loans Interest	General Obligation Bonds Principal	General Obligation Bonds Interest	Revenue Bonds / COPs Principal	Revenue Bonds / COPs Interest	Special Assessment / Special Tax Bonds Principal	Special Assessment / Special Tax Bonds Interest
2010	$ 2,457	$ 1,685	$ 1,975	$ 353	$ 21,955	$ 29,735	$ 5,130	$ 8,408
2011	2,595	1,579	2,100	219	29,776	27,720	5,490	8,152
2012	2,724	1,460	2,240	74	27,567	26,402	5,860	7,870
2013	2,863	1,329			28,870	25,094	6,155	7,561
2014	3,016	1,186	-	-	30,227	23,719	6,430	7,224
2015-2019	13,023	3,659	-	-	163,510	96,248	36,755	30,530
2020-2024	6,158	1,036	-	-	124,740	60,620	29,515	20,969
2025-2029	696	21	-	-	117,650	25,611	28,415	13,088
2030-2034	-	-	-	-	35,205	3,736	21,765	4,470
2035-2039	-	-	-	-	-	-	6,755	707
Total	$ 33,532	$ 11,955	$ 6,315	$ 646	$ 579,500	$ 318,885	$ 152,270	$ 108,979

Year Ended June 30,	Tax Allocation Bonds Principal	Tax Allocation Bonds Unaccreted Appreciation	Tax Allocation Bonds Interest	Tobacco Asset-Backed Bonds Principal	Tobacco Asset-Backed Bonds Interest	Pooled Financing Bonds Principal	Pooled Financing Bonds Interest
2010	$ 19,054	$ 2,163	$ 26,620	$ 3,800	$ 6,796	$ 680	$ 1,883
2011	19,948	2,243	25,727	4,000	6,525	770	1,846
2012	20,884	2,317	24,749	4,400	6,240	825	1,805
2013	24,143	2,388	23,612	4,600	5,927	860	1,762
2014	25,704	2,455	22,327	5,000	5,599	900	1,718
2015-2019	144,897	12,014	90,577	30,900	22,101	5,280	7,821
2020-2024	134,019	8,824	52,561	42,680	8,765	5,725	6,247
2025-2029	102,468	2,181	22,801	-	-	6,880	4,470
2030-2034	43,430	-	4,500	-	-	7,895	2,155
2035-2039	-	-	-	-	-	3,645	445
Subtotal	534,547	34,585	293,474	95,380	61,953	33,460	30,152
Add:							
Accreted Appreciation through June 30, 2009	14,682	-	-	-	-	-	-
Total	$ 549,229	$ 34,585	$ 293,474	$ 95,380	$ 61,953	$ 33,460	$ 30,152

** The Tobacco Asset-Backed Bond Principal Debt Service requirements are based upon expected Turbo Principal payments.*

c. Change in Long-Term Liabilities

Additions to governmental activities long-term debt for contracts, notes and loans payable may differ from proceeds reported on the Statement of Revenues, Expenditures, and Changes in Fund Balances, due to funding received in prior fiscal years being converted from short-term to long-term debt as a result of developers extending the terms of the obligation.

The following is a summary of changes in governmental activities long-term liabilities for the year ended June 30, 2009. The effect of bond accretion, bond premiums, discounts, and deferred amounts on bond refunds are amortized as adjustments to long-term liabilities.

	Governmental Activities				
	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Arbitrage Liability	$ -	$ 533	$ -	$ 533	$ -
Compensated Absences	74,825	62,642	(63,021)	74,446	34,912
Liability Claims	232,448	84,863	(43,332)	273,979	43,663
Capital Lease Obligations	61,262	40,758	(12,501)	89,519	15,963
Contracts Payable	2,615	2,100	-	4,715	-
Notes Payable	5,662	-	(876)	4,786	-
Loans Payable	34,777	10,483	(445)	44,815	8,708
Section 108 Loans Payable	35,896	-	(2,364)	33,532	2,457
General Obligation Bonds	8,580	-	(2,265)	6,315	1,975
Revenue Bonds / COPs	498,950	103,000	(22,450)	579,500	21,955
Unamortized Bond Premiums, Discounts and Deferred Amounts on Refunding	(4,235)	-	203	(4,032)	(203)
Net Revenue Bonds/COP's	494,715	103,000	(22,247)	575,468	21,752
Special Assessment / Special Tax Bonds	144,805	12,365	(4,900)	152,270	5,130
Unamortized Bond Premiums, Discounts and Deferred Amounts on Refunding	(534)	(129)	53	(610)	(53)
Net Special Assessment Bonds	144,271	12,236	(4,847)	151,660	5,077
Tax Allocation Bonds	548,643	-	(14,096)	534,547	19,054
Interest Accretion	12,837	2,080	(235)	14,682	-
Balance with Accretion	561,480	2,080	(14,331)	549,229	19,054
Unamortized Bond Premiums, Discounts and Deferred Amounts on Refunding	5,494	-	(116)	5,378	116
Net Tax Allocation Bonds	566,974	2,080	(14,447)	554,607	19,170
Tobacco Settlement Asset-Backed Bonds	99,370	-	(3,990)	95,380	3,800
Pooled Financing Bonds	34,115	-	(655)	33,460	680
Unamortized Bond Premiums, Discounts and Deferred Amounts on Refunding	(125)	-	17	(108)	(17)
Net Pooled Financing Bonds	33,990	-	(638)	33,352	663
Net Other Postemployment Benefits Obligation	28,872	44,632	-	73,504	-
Net Pension Obligation	141,734	5,931	-	147,665	-
Total	$ 1,965,991	$ 369,258	$ (170,973)	$ 2,164,276	$ 158,140

d. Defeasance and Redemption of Debt

As of June 30, 2009, principal amounts payable from escrow funds established for defeased bonds are as follows:

Defeased Bonds	Amount
Central Imperial Redevelopment Project Tax Allocation Bonds, Series 2000	$ 2,975
Southcrest Redevelopment Project Tax Allocation Bonds, Series 2000	1,520
Total Defeased Bonds Outstanding	$ 4,495

e. Long-Term Pledged Liabilities

Governmental long-term pledged liabilities as of June 30, 2009 are comprised of the following:

Type of Pledged Revenue	Fiscal Year Maturity Date	Pledged Revenue to Maturity	Debt Principal & Interest Paid	Pledged Revenue Recognized
Pledged CDBG Revenue:				
Section 108 Loans Payable		$ 34,763	$ 3,534	$ 3,534
Total Pledged CDBG Revenue		34,763	3,534	3,534
Pledged Developer Revenue:				
Regional Transportation Center Redevelopment Project (Section 108)	2021	2,663	285	285
Total Pledged Developer Revenue		2,663	285	285
Pledged Net Operating Revenue (Parking):				
Centre City Parking Revenue Bonds, Series 1999 A	2026	16,065	957	953
Centre City Parking Revenue Bonds, Series 2003 B	2027	26,879	1,508	1,390
Total Pledged Net Operating Revenue (Parking)		42,944	2,465	2,343
Pledged Special Assessment / Special Tax Revenue:				
Otay Mesa Industrial Park Limited Obligation Improvement Bonds, Issued May 1992	2013	292	72	71
Miramar Ranch North Special Tax Refunding Bonds, Series 1998	2021	52,117	4,371	4,147
Public Facilities Financing Authority Reassessment District Refunding Revenue Bonds, Series 1999 A	2018	13,651	2,330	1,882
Public Facilities Financing Authority Reassessment District Refunding Revenue Bonds, Series 1999 B	2018	3,424	599	470
Santaluz Special Tax Bonds, Improvement Area No.1, Series 2000 A	2031	96,349	4,368	4,287
Santaluz Special Tax Bonds, Improvement Area No.3, Series 2000 B	2031	7,325	316	337
City of San Diego Reassessment District No. 2003-1 Limited Obligation Refunding Bonds	2018	7,899	966	732
Piper Ranch Limited Obligation Improvement Bonds, Issued January 2004	2034	8,311	345	317
Santaluz Special Tax Bonds, Improvement Area No.1, Series 2004 A	2031	7,615	377	370
Santaluz Special Tax Bonds, Improvement Area No.4, Series 2004 A	2034	17,221	625	692
Liberty Station Special Tax Bonds, Series 2006 A	2037	31,193	1,149	1,554
Liberty Station Special Tax Bonds, Series 2008 A	2037	7,760	256	347
Black Mountain Ranch Villages Special Tax Bonds Series 2008 A	2038	25169	358	986
Total Pledged Special Assessment / Special Tax Revenue		278,326	16,132	16,192

(continued on next page)

Type of Pledged Revenue	Fiscal Year Maturity Date	Pledged Revenue to Maturity	Debt Principal & Interest Paid	Pledged Revenue Recognized
Pledged Tax Increment Revenue:				
Contracts				
Contract Payable to SDSU Foundation, dated December 1991	---	$ 3,095	-	$ -
Amendment to Contract Payable to SDSU Foundation, dated January 1995	---	233	-	-
Contract Payable to Western Pacific Housing, Inc., dated April 2004	---	3,476	-	-
Notes				
Note Payable to Price Charities, dated April 2001	2032	4,274	1,045	1,045
Note Payable to Price Charities, dated May 2005	2025	2,100	-	-
Amendment to Note Payable to Price Charities, dated February 2006	2025	180	-	-
Loans				
International Gateway Associates, LLC, dated October 2001	2032	4,776	199	199
PCCP/SB Las America, LLC, dated August 2005	2036	3,571	132	132
Centerpoint, LLC, dated April 2006	2021	4,969	-	-
Bank of America, N.A. Line of Credit, dated October 2006	2009	8,626	330	330
San Diego National Bank, Line of Credit, dated July 2007 City Heights Housing Area	2011	1,419	74	74
San Diego National Bank, Line of Credit, dated July 2007 City Heights Non-Housing Area	2011	2,255	163	163
San Diego National Bank, Line of Credit, dated July 2007 Naval Training Center Housing Area	2011	2,748	55	55
San Diego National Bank, Line of Credit, dated July 2007 Naval Training Center Non-Housing Area	2011	11,651	317	317
San Diego National Bank, Line of Credit, dated July 2007 North Bay Housing Area	2011	2,407	93	93
San Diego National Bank, Line of Credit, dated July 2007 North Park Non-Housing Area	2011	5,952	140	140
Naval Training Center Civic, Arts, and Cultural Center (Section 108)	2025	8,062	509	509

Type of Pledged Revenue	Fiscal Year Maturity Date	Pledged Revenue to Maturity	Debt Principal & Interest Paid	Pledged Revenue Recognized
Bonds				
Gateway Center West Redevelopment Project Tax Allocation Bonds, Series 1995	2014	$ 732	$ 145	$ 145
Mount Hope Redevelopment Project Tax Allocation Bonds, Series 1995 A	2020	1,018	91	91
Horton Plaza Redevelopment Project Tax Allocation Refunding Bonds, Series 1996 A	2016	7,778	1,116	1,110
Centre City Redevelopment Tax Allocation Bonds, Series 1999 A	2019	32,987	1,276	1,209
Centre City Redevelopment Tax Allocation Bonds, Series 1999 B	2014	13,154	710	3,083
Centre City Redevelopment Tax Allocation Bonds, Series 1999 C	2025	17,179	794	780
City Heights Redevelopment Tax Allocation Bonds, Series 1999 A	2029	8,497	430	418
City Heights Redevelopment Tax Allocation Bonds, Series 1999 B	2029	31,130	571	543
Centre City Redevelopment Project Tax Allocation Bonds, Series 2000 A	2025	7,215	445	441
Centre City Redevelopment Project Tax Allocation Bonds, Series 2000 B	2025	27,376	1,458	1,406
Horton Plaza Redevelopment Project Tax Allocation Bonds, Series 2000	2022	18,806	1,353	1,340
North Bay Redevelopment Project Tax Allocation Bonds, Series 2000	2031	19,804	893	834
North Park Redevelopment Project Tax Allocation Bonds, Series 2000	2031	10,676	479	448
Centre City Redevelopment Tax Allocation Bonds, Series 2001 A	2027	109,162	2,567	2,473
Mount Hope Redevelopment Project Tax Allocation Bonds, Series 2002 A	2027	5,355	153	153
Centre City Redevelopment Project Tax Allocation Bonds, Series 2003 A	2029	21,107	3,971	3,886
City Heights Redevelopment Project Tax Allocation Bonds, Series 2003 A	2034	10,371	316	316
City Heights Redevelopment Project Tax Allocation Bonds, Series 2003 B	2014	452	92	92
North Park Redevelopment Project Tax Allocation Bonds, Series 2003 A	2028	9,975	546	546
North Park Redevelopment Project Tax Allocation Bonds, Series 2003 B	2034	11,189	259	259

(continued on next page)

Type of Pledged Revenue	Fiscal Year Maturity Date	Pledged Revenue to Maturity	Debt Principal & Interest Paid	Pledged Revenue Recognized
Horton Plaza Redevelopment Project Tax Allocation Bonds, Series 2003 A	2022	$ 9,487	$ 310	$ 306
Horton Plaza Redevelopment Project Tax Allocation Bonds, Series 2003 B	2022	6,135	327	309
Horton Plaza Redevelopment Project Tax Allocation Bonds, Series 2003 C	2022	10,252	798	770
Centre City Redevelopment Project Tax Allocation Bonds, Series 2004 A	2030	146,086	6,855	6,855
Centre City Redevelopment Project Tax Allocation Bonds, Series 2004 B	2011	3,155	1,965	1,965
Centre City Redevelopment Project Tax Allocation Bonds, Series 2004 C	2030	41,891	2,230	2,152
Centre City Redevelopment Project Tax Allocation Bonds, Series 2004 D	2030	13,570	723	698
Centre City Redevelopment Project Tax Allocation Bonds, Series 2006 A	2033	125,477	4,356	4,268
Centre City Redevelopment Project Tax Allocation Bonds, Series 2006 B	2032	61,393	2,642	2,617
Public Facilities Financing Authority Pooled Financing Bonds, Series 2007 A	2038	32,499	1,409	1,409
Public Facilities Financing Authority Pooled Financing Bonds, Series 2007 B	2038	31,113	1,164	1,164
Centre City Redevelopment Project Tax Allocation Bonds, Series 2008 A	2021	95,878	2,800	9,927
Total Pledged Tax Increment Revenue		1,010,693	46,301	55,070
Pledged Tobacco Settlement Revenue:				
Tobacco Settlement Revenue Funding Corporation Asset-Backed Bonds, Series 2006	2023	$ 157,333	$ 11,056	$ 10,100
Total Pledged Tobacco Settlement Revenue		157,333	11,056	10,100
Total Pledged Revenue		$ 1,526,722	$ 79,773	$ 87,524

6. BUSINESS-TYPE ACTIVITIES LONG-TERM LIABILITIES (In Thousands)

a. Long-Term Liabilities

Business-type activities long-term liabilities as of June 30, 2009 are comprised of the following:

Type of Obligation	Interest Rates	Fiscal Year Maturity Date	Original Amount	Balance Outstanding June 30, 2009
Compensated Absences				$ 12,671
Liability Claims				32,853
Loans Payable:				
Loans Payable to San Diego County Water Authority	-	-	$ 100	100
Loans Payable to State Water Resources Control Board, issued February 9, 2000	1.80%**	2020	10,606	6,301
Loans Payable to State Water Resources Control Board, issued February 9, 2000	1.80**	2022	6,684	4,613
Loans Payable to State Water Resources Control Board, issued March 30, 2001	1.80**	2022	33,720	23,262
Loans Payable to State Water Resources Control Board, issued May 17, 2001	1.80**	2022	7,742	5,340
Loans Payable to State Water Resources Control Board, issued May 17, 2001	1.80**	2021	860	553
Loans Payable to State Water Resources Control Board, issued June 11, 2001	1.80**	2021	2,525	1,623
Loans Payable to State Water Resources Control Board, issued October 3, 2002	1.99**	2020	3,767	2,459
Loans Payable to State Water Resources Control Board, issued October 3, 2002	1.80**	2023	8,068	5,942
Loans Payable to State Water Resources Control Board, issued December 14, 2005	1.89**	2024	10,093	8,257
Loans Payable to Department of Health Services, issued July 6, 2005	2.51**	2026	21,525	18,491
Loans Payable to State Water Resources Control Board, issued October 15, 2006	1.99**	2024	3,858	3,306
Loans Payable to State Water Resources Control Board, issued February 28, 2007	1.89**	2026	11,068	10,079
Total Loans Payable				90,326

(continued on next page)

Type of Obligation	Interest Rates	Fiscal Year Maturity Date	Original Amount	Balance Outstanding June 30, 2009
Bonds Payable:				
Sewer Revenue Bonds, Series 1995	3.9 - 6.0*	2025	$ 350,000	$ 43,850
Sewer Revenue Bonds, Series 1997 A	3.7 - 5.375*	2027	183,000	22,565
Sewer Revenue Bonds, Series 1997 B	3.7 - 5.375*	2027	67,000	8,260
Water Certificate of Undivided Interest, Series 1998	4.0 - 5.375*	2029	385,000	141,320
Sewer Revenue Bonds, Series 1999 A	3.5 - 5.125*	2029	203,350	67,020
Sewer Revenue Bonds, Series 1999 B	3.5 - 5.125*	2029	112,060	37,080
Subordinated Water Revenue Bonds, Series 2002	2.0 - 5.0*	2033	286,945	272,846
Senior Sewer Revenue Bonds, Series 2009 A	2.0-5.375*	2039	453,775	453,775
Senior Sewer Revenue Refunding Bonds Series 2009 B	3.0-5.5*	2025	634,940	634,940
Water Revenue Refunding Bonds, Series 2009 A	2.5-5.25*	2039	157,190	157,190
Water Revenue Bonds, Series 2009 B	2.5-5.75*	2040	328,060	328,060
Total Bonds Payable				2,166,906
Estimated Landfill Closure and Postclosure Care				19,336
Net Other Postemployment Benefits Obligation				19,767
Net Pension Obligation				29,474
Pollution Remediation Obligation				620
Total Business-Type Activities Long-Term Liabilities				$ 2,371,953

** Interest rates are fixed, and reflect the range of rates for various maturities from the date of issuance to maturity.*

*** Effective rate*

b. Amortization Requirements

Annual requirements to amortize long-term debt as of June 30, 2009, including interest payments to maturity, are as follows:

Year Ended June 30	Loans Payable Principal	Loans Payable Interest	Revenue Bonds Payable Principal	Revenue Bonds Payable Interest
2010	$ 5,653	$ 1,780	$ 58,741	$ 97,033
2011	5,765	1,670	63,915	103,683
2012	5,878	1,557	66,420	101,173
2013	5,992	1,443	69,275	98,325
2014	6,109	1,326	72,485	95,112
2015-2019	32,384	4,792	417,635	420,395
2020-2024	25,072	1,677	485,090	307,757
2025-2029	3,373	89	470,265	183,672
2030-2034	-	-	220,205	96,243
2035-2039	-	-	221,720	39,781
2040-2044	-	-	21,155	582
Unscheduled*	100	-	-	-
Total	$ 90,326	$ 14,334	$ 2,166,906	$ 1,543,756

** The loan payable to the San Diego County Water Authority in the amount of $100 does not have an annual repayment schedule. The payment is due if funding for the projects for which the loan was received becomes available from other sources.*

c. Change in Long-Term Liabilities

The following is a summary of changes in long-term liabilities for the year ended June 30, 2009. The effect of bond premiums, discounts and deferred amounts on refunding are reflected as adjustments to long-term liabilities.

	Business-Type Activities				
	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Arbitrage Liability	$ 586	$ -	$ (586)	$ -	$ -
Compensated Absences	13,355	11,949	(12,633)	12,671	6,315
Liability Claims	50,239	(13,794)	(3,592)	32,853	3,501
Capital Lease Obligations	166	-	(166)	-	-
Revenue Notes Payable	430,830	-	(430,830)	-	-
Loans Payable	95,875	-	(5,549)	90,326	5,653
Revenue Bonds Payable	1,425,445	1,573,965	(832,504)	2,166,906	58,741
Unamortized Bond Premiums, Discounts and Deferred Amounts on Refunding	(6,619)	39,748	7,951	41,080	2,142
Net Revenue Bonds Payable	1,418,826	1,613,713	(824,553)	2,207,986	60,883
Estimated Landfill Closure/Postclosure Care	18,429	907	-	19,336	-
Net Other Postemployment Benefits Obligation	8,921	10,846	-	19,767	-
Net Pension Obligation	31,342	-	(1,868)	29,474	-
Pollution Remediation Obligation	-	620	-	620	-
Totals	$ 2,068,569	$ 1,624,241	$ (1,279,777)	$ 2,413,033	$ 76,352

d. Defeasance and Redemption of Debt

PFFA issued Water Revenue Bonds, Series 2009A in the amount of $157,190 and Series 2009B in the amount of $328,060. The bond proceeds were used to fully redeem outstanding Subordinated Water Notes, Series 2007A and Subordinated Water Notes, Series 2008A and for partial redemption of the Water Certificates of Undivided Interest, Series 1998. The Water 2007A and 2008A Notes have been redeemed and the corresponding liabilities have been removed from the Statement of Net Assets. The redemption transaction for the Water 2007A Notes resulted in a total economic loss of approximately $11,161 and a cash flow cost of approximately $21,558. The redemption transaction for the Water 2008A Notes resulted in a total economic loss of approximately $40,412 and a cash flow cost of approximately $92,955. The partial refunding of $94,165 from the remaining outstanding Water Certificates of Undivided Interest, Series 1998 resulted in a total economic gain of approximately $5,580 and a cash flow savings of approximately $8,741. All of the Notes and Certificates that were redeemed or refunded from the Water Revenue Bonds, Series 2009A and 2009B were called or redeemed at a date prior to the end of the fiscal year, and accordingly, there is no defeased debt balance outstanding as of June 30, 2009.

PFFA issued Senior Sewer Revenue Bonds, Series 2009A in the amount of $453,775 and Series 2009B in the amount of $634,940. The bond proceeds were used to fully redeem and refund outstanding Subordinated Sewer Revenue Notes, Series 2007 and Sewer Revenue Bonds, Series 1993. The bond proceeds were also used for a partial redemption of the Sewer Revenue Bonds, Series 1995, Series 1997A, Series 1997B, Series 1999A and Series 1999B. The Subordinated Sewer Notes, Series 2007 were fully redeemed while the Sewer Revenue Bonds, Series 1993, carry a defeased balance in an escrow fund, listed below. Both liabilities have been removed from the Statement of Net Assets. The redemption transaction for the Sewer 2007 Notes resulted in a total economic loss of approximately $23,013 and a cash flow cost of approximately $44,084. The redemption transaction for the Sewer Revenue Bonds, Series 1993 resulted in a total economic gain of approximately $8,457 and a cash flow savings of approximately $13,951. The partial redemption of the Sewer Revenue Bonds, Series 1995 resulted in a total economic gain of approximately $11,086 and a cash flow savings of approximately $18,287. The partial redemption of the Sewer Revenue Bonds, Series 1997A and Series 1997B resulted in a total economic gain of approximately $10,954 and a cash flow savings of approximately $18,190. The partial redemption of the Sewer Revenue Bonds, Series 1999A and Series 1999B resulted in a total economic gain of approximately $7,933 and a cash flow savings of approximately $13,085. The 2007 Notes were fully redeemed and the partial refunding of the Series 1995, 1997 and 1999 bonds, from the Sewer Revenue Bonds, Series 2009A and Series 2009B, were all called or redeemed at a date prior to the end of the fiscal year, and accordingly, there is no defeased debt balance outstanding as of June 30, 2009.

As of June 30, 2009, principal amount payable from the escrow fund established for the defeased bond is as follows:

Defeased Bonds	Balance
Sewer Revenue Bonds, Series 1993	$ 160,220

e. Long-Term Pledged Liabilities

Business-type activities long-term pledged liabilities as of June 30, 2009 are comprised of the following:

Type of Pledged Revenue	Fiscal Year Maturity Date	Pledged Revenue to Maturity	Debt Principal & Interest Paid	Pledged Revenue Recognized
Pledged Net Sewer Systems Revenue:				
Loans				
Loans Payable to State Water Resources Control Board, issued February 9, 2000	2020	$ 7,004	$ 637	$ 637
Loans Payable to State Water Resources Control Board, issued February 9, 2000	2022	5,216	401	401
Loans Payable to State Water Resources Control Board, issued March 30, 2001	2022	26,320	2,025	2,025
Loans Payable to State Water Resources Control Board, issued May 17, 2001	2022	6,038	465	465
Loans Payable to State Water Resources Control Board, issued May 17, 2001	2021	619	52	52
Loans Payable to State Water Resources Control Board, issued June 11, 2001	2021	1,819	151	151
Loans Payable to State Water Resources Control Board, issued October 3, 2002	2020	2,763	251	251
Loans Payable to State Water Resources Control Board, issued October 3, 2002	2023	6,777	484	484
Loans Payable to State Water Resources Control Board, issued December 14, 2005	2024	9,561	637	637
Loans Payable to State Water Resources Control Board, issued October 15, 2006	2024	3,858	258	258
Loans Payable to State Water Resources Control Board, issued February 28, 2007	2026	11,883	699	699

Type of Pledged Revenue	Fiscal Year Maturity Date	Pledged Revenue to Maturity	Debt Principal & Interest Paid	Pledged Revenue Recognized
Bonds and Notes				
Sewer Revenue Bonds, Series 1993	2023	$ -	$ 16,319	$ 16,316
Sewer Revenue Bonds, Series 1995	2025	78,930	23,585	23,581
Sewer Revenue Bonds, Series 1997 A	2027	43,889	12,179	12,177
Sewer Revenue Bonds, Series 1997 B	2027	16,066	4,458	4,457
Sewer Revenue Bonds, Series 1999 A	2029	126,138	13,207	12,352
Sewer Revenue Bonds, Series 1999 B	2029	69,789	7,308	7,118
Subordinated Sewer Revenue Notes, Series 2007	2009	-	11,192	11,190
Senior Sewer Revenue Bonds, Series 2009 A	2039	858,509	-	-
Senior Sewer Revenue Refunding Bonds Series 2009 B	2025	911,622	-	-
Total Pledged Net Sewer Systems Revenue		2,186,801	94,308	93,251
Pledged Net Water Systems Revenue:				
Loans				
Loans Payable to Department of Health Services, issued July 6, 2005	2026	22,703	1,376	1,376
Bonds and Notes				
Water Certificate of Undivided Interest, Series 1998	2029	256,934	21,354	20,002
Subordinated Water Revenue Bonds, Series 2002	2033	424,199	18,037	17,200
Subordinated Water Revenue Notes, Series 2007 A	2009	-	2,301	2,301
Subordinated Water Revenue Notes, Series 2008 A	2010	-	4,551	6,532
Water Revenue Refunding Bonds, Series 2009 A	2039	262,608	-	-
Water Revenue Bonds, Series 2009 B	2040	661,977	-	-
Total Pledged Net Water Systems Revenue		1,628,421	47,619	47,411
Total Pledged Revenues		$ 3,815,222	$ 141,927	$ 140,662

7. DISCRETELY PRESENTED COMPONENT UNITS LONG-TERM DEBT (In Thousands)

Discretely presented component units long-term debt as of June 30, 2009 is comprised as follows:

San Diego Convention Center Corporation

Type of Obligation	Interest Rate	Fiscal Year Maturity Date	Original Amount	Balance Outstanding June 30, 2009	Due Within One Year
Compensated Absences				$ 1,214	$ 1,214
Capital Leases			$ 3,942	1,394	863
Note Payable to San Diego Unified Port District, dated 1999	0.00%	2011	10,000	1,500	1,000
Total Long-Term Liabilities				$ 4,108	$ 3,077

Annual requirements to amortize long-term debt as of June 30, 2009, are as follows:

Capital Lease

Fiscal Year	Amount
2010	$ 931
2011	543
Total minimum lease payments	1,474
Less: amount representing interest	(80)
Present value of minimum lease payments	$ 1,394

Note Payable

Fiscal Year	Amount
2010	$ 1,000
2011	500
Total	$ 1,500

San Diego Housing Commission

Type of Obligation	Interest Rate	Fiscal Year Maturity Date	Original Amount	Balance Outstanding June 30, 2009	Due Within One Year
Compensated Absences				$ 1,351	$ 1,351
Note Payable to Chase, dated June 1995	Variable	2012	$ 4,725	3,274	161
Note Payable to State of California (RHCP)	0.0	2014	1,405	1,405	-
Note Payable to State of California (RHCP)	0.0	2015	3,149	3,149	-
Note Payable to US Bank, dated November 2006	Variable	2012	20,550	19,245	241
Total Notes Payable				27,073	402
Total Long-Term Liabilities				$ 28,424	$ 1,753

The interest rate for the Chase obligation as of June 30, 2009 was 3.01%. The variable rate in accordance with the loan agreement is equal to .65 times the sum of the Variable Index Rate plus 3%. The Variable Index Rate is defined as the most recently available monthly weighted average cost of funds for 11th District Savings Institutions published by the Federal Home Loan Bank of San Francisco.

The interest rate for the US Bank obligation as of June 30, 2009 was 7.54%. The variable interest rate in accordance with the loan agreement is 2.25% plus LIBOR.

The Commission entered into an Interest Rate Swap Agreement with US Bank (the Swap Provider) to reduce the impact of changes in interest rate. Under the terms of the Swap Agreement, the Commission has agreed to pay interest to the Swap Provider at a fixed rate of 5.29% plus 2.25% exclusive of any fees, add-ons or other trustee or bank charges, while the Swap Provider has agreed to make the Commission's required monthly mortgage payment. The notional amount of the Swap Agreement is $20,006. The Swap Agreement expires at maturity of the mortgage in 2011.

Pursuant to SFAS No. 133, derivative instruments not meeting the criteria for hedge accounting are recorded at fair value on the statement of net assets with any change in fair value reflected in the statement of activities in the period of change. The Commission recorded a liability for the fair value of the interest rate swap as of June 30, 2009 in the amount of $1,736. During the year ended June 30, 2009, a loss in fair value of $831 has been realized and is included in the statement of activities.

Annual requirements to amortize such long-term debt as of June 30, 2009 to maturity are as follows:

Year Ending June 30	Principal	Interest
2010	$ 402	$ 1,563
2011	416	1,540
2012	21,701	488
2013	-	-
2014	1,405	-
2015-2019	3,149	-
Total	$ 27,073	$ 3,591

8. SHORT-TERM NOTES PAYABLE (In Thousands)

The City issues Tax and Revenue Anticipation Notes (TRANs) in advance of property tax collections, depositing the proceeds into the General Fund. These notes are necessary to meet the cash requirements of the City prior to the receipt of property taxes.

Short-term debt activity for the year ended June 30, 2009, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance
Tax and Revenue Anticipation Notes	$ 116,000	$ 135,000	$ (251,000)	$ -

The $116,000 (FY08) TRANs issue, which was a 13 month note obligation, had an interest rate of 3.90% and was repaid on August 1, 2008.

The $135,000 (FY09) TRANs issue had an average effective interest rate of 2.68% and was repaid on April 30, 2009.

9. JOINT VENTURE and JOINTLY GOVERNED ORGANIZATIONS (In Thousands)

San Diego Medical Services Enterprise, LLC

A joint venture is a legal entity or other organization that results from a contractual arrangement and that is owned, operated, or governed by two or more participants as a separate and specific activity subject to joint control. San Diego Medical Services Enterprise, LLC (SDMSE) is a joint venture that is reported within the General Fund, in accordance with GASB 14.

SDMSE was organized on May 2, 1997 to provide emergency medical services and medical transportation services to the citizens of San Diego. Operations began July 1, 1997 under an initial 5 year agreement that was extended on July 1, 2002 and again on July 1, 2005 for an additional three year period. On July 1, 2008 operations were extended until December 31, 2009 under a separate extension agreement and may be extended an additional six months if necessary. In addition, the City Council has authorized the Mayor to re-negotiate and execute a new five year agreement with SDMSE for ambulance services. The San Diego City Attorney is currently reviewing the proposed extension agreement and related SDMSE agreements to determine whether any changes to these agreements may be appropriate.

The SDMSE partners are the City of San Diego and Rural Metro of San Diego, Inc., a wholly owned subsidiary of Rural Metro Corporation (a publicly traded corporation). The SDMSE governing board of managers is comprised of five members, three of whom are appointed by the City; currently one of the City appointments is vacant.

The maximum funds which the City is required to contribute to the costs of SDMSE operations are limited to an aggregate of $8,450 during the term of the third amended agreement. This aggregate includes a $650 annual subsidy and any other amounts to be paid to the City since 1997 under the original contract, and any losses the City is required to cover under the extended contract, excluding any amount the City contributes for Medicare fee reimbursements. Cumulatively, the City has paid annual subsidies totaling $5,700 as of June 30, 2009. Effective in fiscal year 2006, the City was no longer required to pay the $650 annual subsidy and the Medicare fee reimbursements shall not exceed $250 per fiscal year. Net assets of SDMSE are pro-rated to each partner based on a 50/50 split. In accordance with the operating agreement, profit and loss for each fiscal year is allocated equally to the members, subject to an aggregate limitation on loss to the City of $8,450 (equal to the amount of subsidies discussed above). For the fiscal year ended June 30, 2009, SDMSE reported a net income of $3,185, a member distribution of $3,500, and ending net assets of $3,647.

Under the terms of an operating agreement between Rural/Metro of San Diego, Inc. and SDMSE, Rural/Metro of San Diego, Inc. has made available a line-of-credit in the initial amount of $3,500 bearing an interest rate of 9.5%. SDMSE did not have an outstanding balance, nor did it borrow on the line-of-credit at June 30, 2009.

Complete financial statements can be requested from San Diego Medical Services Enterprise, LLC, 8401 East Indian School Road, Scottsdale, Arizona 85251.

San Diego Workforce Partnership

The City of San Diego and the County of San Diego jointly govern the San Diego Workforce Partnership (Consortium). The Consortium's Board of Directors consists of two members of the City Council, two members from the County Board of Supervisors, and one member of a charitable organization. The purpose of the Consortium is to provide regional employment and training services in order to develop and create job opportunities throughout San Diego County. The Consortium is empowered to make applications for and receive grants from governmental or private sources. The City does not appoint a majority of the Board, is not able to impose its will on the Consortium, and the Consortium is not fiscally dependent on the City. Therefore, it is the City's conclusion that the Consortium is a Governmental Organization with a jointly appointed board and not a component unit of the City. However, in the event the Consortium incurs a liability it cannot financially handle, the City and the County have agreed to share in the payment of those obligations.

Complete financial statements can be requested from San Diego Workforce Partnership, Inc. 3910 University Avenue, Suite 400, San Diego, CA 92105.

San Diego Geographic Information Source (SanGIS)

SanGIS was created in July 1997 as a joint powers agreement between the City of San Diego and the County of San Diego. SanGIS objectives are: to create and maintain a geographic information system; to market and license digital geographic data and software; to provide technical services; and to publish geographical and land-related information.

Complete financial statements can be requested from SanGIS, 5469 Kearny Villa Road, Suite 102, San Diego, CA 92123.

10. LEASE COMMITMENTS (In Thousands)

The City leases various properties and equipment. Leased property having elements of ownership are recorded as capital leases and reported as capital assets in the government-wide financial statements, along with a corresponding capital lease obligation. Leased property that does not have elements of ownership is reported as an operating lease and is expensed when paid.

Operating Leases

The City's operating leases consist primarily of rental property occupied by City departments. The following is a schedule of future minimum rental payments required under operating leases entered into by the City for property that has initial or remaining non-cancelable lease terms in excess of one year as of June 30, 2009:

Year Ended June 30		Amount
2010	$	12,642
2011		12,122
2012		12,332
2013		12,189
2014		7,617
2015-2019		4,818
2020-2024		245
Total	$	61,965

Rent expense as related to operating leases was $12,719 for the year ended June 30, 2009.

Capital Leases

The City has entered into various capital leases for equipment and structures. These capital leases have maturity dates ranging from August 1, 2008 through October 1, 2023, and interest rates ranging from 2.63% to 7.94%. A schedule of future minimum lease payments under capital leases as of June 30, 2009 is provided in Notes 5 and 6. The value of all capital leased assets as of June 30, 2009 for governmental assets is $109,792 net of accumulated depreciation of $58,551, and business-type assets of $1,357, net of accumulated depreciation of $9,684. These amounts are categorized by major asset class in the table below.

		Gross Value		Depreciation		Net Book Value
Governmental						
Equipment	$	134,184	$	(56,708)	$	77,476
Structures & Improvement		4,889		(1,843)		3,046
Construction in Progress		29,270		-		29,270
Total Governmental	$	168,343	$	(58,551)	$	109,792
Business-Type						
Equipment	$	11,041	$	(9,684)	$	1,357
Total Business-Type	$	11,041	$	(9,684)	$	1,357

Lease Revenues

The City has operating leases for certain land, buildings, and facilities with tenants and concessionaires. Leased capital asset carrying values of approximately $76,591, as well as depreciation, are reported in Note 4 and are consolidated with non-leased assets. Minimum annual lease revenues are reported in the following schedule:

Year Ended June 30	Amount
2010	$ 33,813
2011	33,027
2012	32,128
2013	30,975
2014	30,062
2015-2019	138,749
2020-2024	124,203
2025-2029	118,584
2030-2034	110,230
2035-2039	100,732
2040-2044	93,506
2045-2049	66,178
2050-2054	12,334
2055-2059	4,840
2060-2064	1,100
Total	$ 930,461

This amount does not include contingent rentals, which may be received under certain leases of property on the basis of percentage returns. Rental income as related to operating leases was $81,301 for the year ended June 30, 2009, which includes contingent rentals of $46,748.

11. DEFERRED COMPENSATION PLAN (In Thousands)

The City, San Diego Convention Center Corporation (SDCCC), San Diego Data Processing Corporation (SDDPC), and San Diego Housing Commission (SDHC) each offer their employees a deferred compensation plan, created in accordance with Internal Revenue Service Code Section 457, State and Local Government Deferred Compensation Plans. These plans, available to eligible employees, permit them to defer, pre-tax, a portion of their salary until future years. Deferred compensation is not available to employees until termination, retirement, death, disability, or an unforeseeable emergency. All assets and income of the deferred compensation plan are held in trust for the exclusive benefit of plan participants and their beneficiaries. The deferred compensation plans are not considered part of the City of San Diego's financial reporting entity.

12. PENSION PLANS (In Thousands)

The City has a defined benefit pension plan and various defined contribution pension plans covering substantially all of its employees.

DEFINED BENEFIT PLAN

a. **Plan Description**

San Diego City Employees' Retirement System ("SDCERS"), as authorized by Article IX of the City Charter, is a public employee retirement system established in fiscal year 1927 by the City. SDCERS administers independent, qualified, single employer governmental defined benefit plans and trusts for the City, the Port of San Diego (the "Port"), and the San Diego County Regional Airport Authority (the "Airport"). As of July 1, 2007, the assets of the three separate plans and trusts are pooled in the SDCERS Group Trust. These plans are administered by the SDCERS Board (the "Board") to provide retirement, disability, death and survivor benefits for its members. Amendments to the City's benefit provisions require City Council approval as well as a majority vote by members. As of January 1, 2007, benefit increases also require a majority vote of the public. All approved benefit changes are codified in the City's Municipal Code.

The plans cover all eligible employees of the City, the Port, and the Airport. All City employees working half-time or greater and full-time employees of the Port and the Airport are eligible for membership and are required to join SDCERS. The Port and Airport are not component units of the City CAFR per GASB 14; however, the financial statements of SDCERS Pension trust do include the Port and Airport activity and are reported in the trust and agency section of the CAFR. The information disclosed in this note however, relates solely to the City's participation in SDCERS. City employment classes participating in the Plan are elected officers, general and safety (including police, fire and lifeguard members). These classes are represented by various unions depending on the type and nature of work performed, except for elected officials, unclassified and unrepresented employees.

City of San Diego Plan Membership as of June 30, 2009 (actual member count)

	General	Safety	Total by Classification
Active Members	5,825	2,449	8,274
Terminated Members	2,298	528	2,826
Retirees, Disabled and Beneficiaries	4,428	2,943	7,371
Total Members, as of June 30, 2009	12,551	5,920	18,471

Source: SDCERS' CAFR as of June 30, 2009

As a defined benefit Plan, retirement benefits are determined primarily by a member's class, age at retirement, number of years of creditable service, and the member's final compensation based on the highest salary earned over a consecutive one-year period. The Plan provides cost of living adjustments of 2% to retirees, which is factored into the actuarial assumptions. Increases in retirement benefits due to cost of living adjustments do not require voter approval. The Plan requires ten years of service at age 62, or 20 years of service at age 55 for general members (50 for safety members), which could include certain service purchased or service earned at a reciprocating government entity, to vest for a benefit. Typically, retirement benefits are awarded at a rate of 2.5%

of the employee's one-year high annual salary per year of service at age 55 for general members, and 3% for Safety members starting at the age of 50. The actual percentage of final average salary per year served component of the calculation rises as the employee's retirement age increases and depends on the retirement option selected by the employee. General Plan percentage of final average salary per year served is a maximum of 2.8% for general members and 3% for safety members.

On July 28, 2008, the City Council approved R-303977 which presents modified defined contribution and defined benefit Plans for all non-safety City employees hired on or after July 1, 2009 (these changes were subsequently codified into the Municipal Code on June 25, 2009 with Council's approval of O-19874). The new defined benefit Plan includes modified percentages used to determine annual retirement allowance (depending on employees' age at retirement), a pensionable salary calculation used to determine retirement allowances based on a 3-year average, and a maximum annual retiree benefit of 80% of employees' pensionable salary. Additionally, the new defined contribution Plan includes mandatory employee contributions to SPSP (as well as City match) of 1% and the introduction of mandatory employee contribution to a retiree medical trust Plan (as well as City match) of 0.25%. See SDMC Section 24.04 for additional information.

Deferred Retirement Option Program (DROP)

The City also has a Deferred Retirement Option Program (DROP) where participants continue to work for the City and receive a regular paycheck. SDCERS' members electing to participate in DROP must agree to participate in the program for a specific period, up to a maximum of five years. A DROP participant must agree to end employment with the City on or before the end of the selected DROP participation period. A SDCERS member's decision to enter DROP is irrevocable.

Upon entering the program, the DROP participant stops making contributions to SDCERS and stops earning creditable service. Instead, amounts equivalent to the participant's retirement benefit plus earnings and additional contributions are credited to an interest bearing individual account held in the participant's name. On November 21, 2008, the SDCERS Board changed the DROP interest credit rate to 7.75% from 8% to mirror the newly adopted investment return assumption adopted by the Board on September 19, 2008. On February 20, 2009 the Board changed the DROP interest rate again. Effective July 1, 2009, DROP participation interest will be 3.54% and DROP annuity interest will be 5.0%. The DROP benefit is the value of a DROP participant's account at the end of the DROP participation period. Participants select the form of the distribution of the DROP account when they leave employment and begin retirement. The distribution is made as a single lump sum or in 240 equal monthly payments, or as otherwise allowed by applicable provisions of the Internal Revenue Code. Outstanding liabilities for DROP are shown on the Statement of Fiduciary Net Assets in the basic financial statements. During the period of participation, the participant continues to receive most of the employer offered benefits available to regular employees with exception to earning creditable service, as previously discussed.

SDCERS' members who were hired on or after July 1, 2005 are ineligible to participate in the DROP program due to the benefit changes negotiated with the July 1, 2005 Memoranda of Understanding (MOU). However, SDCERS has asserted that due to delays in codification of benefit changes into the Municipal Code, the effective cut off date would instead be February 16, 2007, which is when the Ordinance O-19567 was officially codified in the Municipal Code. As of the issuance of this report, there has been no change in the status of this case [refer to Note 18 for additional information]. Notwithstanding amendments to the municipal code, SDCERS' members who were hired prior to July 1, 2005 are eligible to participate in DROP when they are eligible for a service retirement.

Purchase of Service Credits

Article 4 Division 13 of the City's Municipal Code allows Plan members to purchase years of Creditable Service for use in determining retirement allowances. To purchase Creditable Service, a Member must elect to pay and thereafter pay, in accordance with such election before retirement, into the Retirement Fund an amount, including interest, determined by the Board. No Member will receive Creditable Service under this Division for any service for which payment has not been completed pursuant to this Division before the effective date of the Member's retirement. After review of the purchase of service program, SDCERS' actuary concluded that the service credit pricing structure that was in place prior to November 2003 did not reflect the full cost in the price then charged to SDCERS members. The pricing shortfall of approximately $146,000, which is included in the Unfunded Actuarial Accrued Liability (UAAL), is reported in this note as of the most recent valuation date and in the RSI of these financial statements for the two years prior to the most recent valuation date. On November 13, 2008, a court ruling stated that the Board's decision to amortize the underpaid purchase of service credits, for certain employees who had yet to retire as of November 20, 2007, through the City's existing unfunded actuarial liability is unlawful and contrary to the Municipal Code and City Charter. Judgment was entered in favor of the City on December 12, 2008 which finalized the November 13, 2008 ruling. However, SDCERS submitted an appeal to this ruling which is currently pending. The amount of the potential benefit to the City is not known as of the issuance of this report. Additionally, the service credit pricing structure used after November 2003 does cover the full projected cost to the System when members purchased the service credits.

SDCERS' members who were hired on or after July 1, 2005 are ineligible to participate in the Purchase of Service Credit program due to the benefit changes negotiated with the July 1, 2005 MOU. However, SDCERS has asserted that due to delays in codification of benefit changes into the municipal code, the effective cut off date would instead be February 16, 2007, which is when the Ordinance O-19567 was officially codified in the Municipal Code. As of the issuance of this report, there has been no change in the status of this case [refer to Note 18 for additional information]. Notwithstanding amendments to the municipal code, SDCERS' members who were hired prior to July 1, 2005 are eligible to participate the Purchase of Service Credit Program at the full cost to the participant.

Corbett Settlement Benefits and Retirement Factors

In 1998, a lawsuit was filed by retired employees who alleged that the City's definition of compensation subject to the computation of retirement benefits improperly excluded the value of certain earnings. The City and SDCERS settled in May of 2000, which is known as the Corbett Settlement. This settlement provided for a flat increase of 7% in benefits payable to eligible members who retired prior to July 1, 2000, payable annually. The settlement also provided a 10% benefit increase and allows for two options in calculating the service retirement allowance for employees active at the time of the settlement and who joined the Retirement System before July 1, 2000 and who retired after July 1, 2000.

The options for calculating the service retirement allowance are outlined in the San Diego Municipal Code sections 24.0402 and 24.0403 which can be obtained at City of San Diego City Clerks Office 202 C Street, San Diego, CA 92101 or online at www.sandiego.gov.

On July 1, 2002, the City Council increased the retirement factors used for calculating retirement allowances; this action was related to MP-2 (as discussed later in this note). As a result of the Corbett Settlement and other benefit actions taken by the City Council, the service retirement factors for general members (non-safety and non-legislative) range from 2.0% at age 55 to 2.8% at age 65. The service retirement factors for Safety Members (Fire, Police and Lifeguard) range from 2.2% at age 50 to 3.0% at age 50 depending on the Corbett Settlement option selected. Finally, the City also maintains an Elected Officer's Retirement Plan where members are eligible to receive 3.5% of their final average salary per year of creditable service. Depending on the number of years of service, participants of the Elected Officer's Retirement Plan can retire earlier than the age of 55; however, their retirement allowance is reduced by 2.0% for each year under the age of 55.

Preservation of Benefit Arrangement

On March 19, 2001, the City Council adopted Ordinance O-18930, adding SDMC sections 24.1601 through 24.1608, establishing the Preservation of Benefit (POB) arrangement. The POB arrangement is a qualified governmental excess benefit arrangement (QEBA) under Internal Revenue Code (IRC) section 415(m), which was created by Congress to allow the payment of promised pension benefits that exceed the IRC section 415(b) limits (and therefore cannot be paid from a qualified retirement plan). On October 28, 2008, the IRS issued a private letter ruling to SDCERS approving the qualified status of the QEBA. No additional payments or repayments are required as a result of the Compliance Statement. As provided in SDMC section 24.1606 and required by federal tax law, the POB arrangement is unfunded within the meaning of the federal tax laws. The City may not pre-fund the POB arrangement to cover future liabilities beyond the current year as it can with an IRC section 401(a) pension plan. SDCERS has established procedures to pay for these benefits on a pay-as-you-go basis. As of issuance of this report, actuarial liabilities related to retired member benefits that exceeded §415 limits are included in the RSI for the City's core pension Plan for valuation years up to and including fiscal year 2005. In the fiscal year 2006 actuarial valuation, the estimated actuarial accrued liability related to excess benefits for eligible active members of the system, amounting to approximately $22,800, was removed from the Plan's Actuarial Liabilities (this liability is estimated to be approximately $30,400 in the fiscal year 2007 actuarial valuation). Additionally, the liability for retired members of the POB arrangement, amounting to approximately $6,400, has been excluded from the fiscal year 2007 actuarial valuation. Estimates related to the actuarial liability for benefits that exceed IRS §415 limits were calculated using actuarial assumptions consistent with those used to perform actuarial valuations for the City's core pension Plan and also pursuant to the Compliance Statement, dated December 20, 2007, and Tax Determination Letter provided by the IRS during Voluntary Correction Program discussions.

In Fiscal Year 2009, approximately $1,300 in benefits were paid by the City for the POB arrangement. The number of participants in any given year for the POB arrangement is determined by the number of Plan participants who exceed the current year's IRS §415(b) limitations as calculated by SDCERS' actuary. The maximum annual payment for the calendar year 2009 was $195 and is adjusted downward depending on the age of the participant when benefits began. In fiscal year 2009, the City's ARC was approximately $4,004; however, the City contributed approximately $1,210 to the POB arrangement, and therefore, the remaining $2,794, which represents future liabilities, is included in the City's Net Pension Obligation (NPO). According to the valuation for the fiscal year ended June 30, 2009, the AAL related to the POB arrangement is approximately $7,400, all of which is unfunded. Additionally, financial statements for the Preservation of Benefits arrangement are included in the Trust & Agency section of this report.

b. **Summary of Significant Accounting Policies – Pension**

Basis of Accounting - The pension trust fund uses the economic resources measurement focus and the accrual basis of accounting. Contributions are recognized as additions in the period in which the contributions are due and a formal commitment to provide the contributions has been made. Benefits and refunds are recognized when due and payable in accordance with the Plan.

Method Used to Value Investments - SDCERS investments are stated at fair value. The SDCERS custodial agent provides market values of invested assets with the exception of the fair value of directly owned real estate assets which are provided by the responsible investment manager and independent third party appraisal firms. Investment income is recognized in accordance with GASB 25 and is stated net of investment management fees and related expenses.

c. **Contributions and Reserves - Disclosure Related to Long - Term Contracts and Other Agreements**

Funding Contracts: Union Agreements

The City has historically picked up a portion of the employee's retirement contributions. The fiscal year 2006 MOUs and the changes to current and future employee benefits therein were introduced to the City Council in June 2005, and the changes in benefit eligibility were approved by Council Resolution 300600.

The agreement in the MOUs (agreements with the police union were not reached) was to reduce the amount of individual employees' pension contributions which are paid for by the City, effective fiscal year 2006. The agreements with labor unions resulted in the reduction of City offset of the employee pension contribution by 3% for the Municipal Employees' Association (MEA), the International Association of Fire Fighters Local 145, and the Deputy City Attorney Association (DCAA) and a unilaterally imposed reduction of 3.2% for the San Diego Police Officers Association (POA). In addition, the American Federation of State and County Municipal Employees (AFSCME) Local 127 negotiated a 1.9% salary reduction in lieu of a City "pick up" contribution reduction and a benefit freeze.

The agreements with the bargaining units explicitly indicate that savings to the City must be used to help address its UAAL within the timeframe of the respective contracts. The labor contract with Local 127 states that "By June 30, 2008, if the City has not dedicated a total of $600,000,000 or more to the UAAL reduction, including the amount received by leveraging employee salary reduction and pension contribution monies, the AFSCME salary reduction monies with interest will revert to SDCERS Employee Contribution Rate Reserve for benefit of Local 127 unit members to defray employee pension contributions."

Upon the conclusion of the fiscal year ended June 30, 2008, the City had contributed approximately $143,300 through contributions in excess of the ARC for fiscal years 2006 through 2008, and therefore, was not able to meet the outstanding commitment in its entirety. As such, the City reached agreements with both MEA and Local 127. The MEA settlement required the City to return prior year savings to MEA members of approximately $6,078 and eliminated 2% of the employee pick-up. The Local 127 settlement required the City to return prior year savings to Local 127 members of approximately $4,786 as well as eliminate the 1.9% salary reduction.

Funding Commitments Related to Legal Settlements

The City employer contributions for fiscal years 1996 – 2003 were not based on the full actuarial rates. Instead, employer contributions were less than the full actuarial rates in accordance with agreements between the City and SDCERS, commonly referred to as Manager's Proposal 1 (MP-1) and Manager's Proposal 2 (MP-2). In September 2006, the City entered into a settlement of McGuigan v. City of San Diego (the "McGuigan Settlement") related to the underfunding by the City of the pension system. Under the McGuigan Settlement, the City is obligated to pay into SDCERS $173,000 no later than June 8, 2011. An additional requirement of the McGuigan Settlement is that the City provides SDCERS real property collateral totaling $100,000 (Non-Depreciable Capital Assets – Land). These amounts are to be returned upon the full payment of the settlement. The City provided the real property collateral at the time of the settlement; subsequently, the City provided a cumulative amount of approximately $144,000[1] of additional payments to SDCERS in an attempt to meet the terms of the McGuigan Settlement. This leaves an outstanding obligation resulting from the McGuigan Settlement of approximately $35,722, including interest as of June 30, 2009. The McGuigan Settlement was partially funded through the securitization of future tobacco revenue, transfers of actual tobacco revenue receipts, additional employee "pick up" savings, and City contributions made in addition to the ARC.

d. **Funding Policy and Contribution Rates**

City Charter Article IX Section 143 requires employees and employers to contribute to the retirement Plan. The Charter section, which was amended in fiscal year 2005, stipulates that funding obligations of the City shall be determined by the Board of SDCERS and are not subject to modification by the City. The section also stipulates that under no circumstances may the City and Board enter into any multi-year funding agreements that delay full funding of the retirement Plan. The Charter requires that employer contributions be substantially equal to employee contributions (SDCERS' legal counsel has opined that this requirement applies to the normal cost contribution only). Pursuant to the Charter, City employer contribution rates, adjusted for payment at the beginning of the year, are actuarially determined rates and are expressed as a fixed annual required contribution as well as percentages of annual covered payroll. The entire expense of SDCERS' administration is charged against the earnings and Plan assets of SDCERS.

The following table shows the City's contribution rates (weighted average of each employee group) for fiscal year 2009, based on the valuation ended June 30, 2007, expressed as percentages of active payroll:

	Employer Contribution Rates	
	General Members	Safety Members
Normal Cost*	9.89%	18.41%
Amortization Payment*	13.86%	24.23%
Normal Cost Adjusted for Amortization Payment*	23.75%	42.64%
City Contribution Rates Adjusted for Payment at the Beginning of the Year	22.85%	41.03%

** Rates assume that contributions are made uniformly during the Plan year.*

Normal Cost = The actuarial present value of pension plan benefits allocated to the current year by the actuarial cost method.

Amortization Payment = The portion of the pension plan contribution which is designed to pay interest on and to amortize the unfunded actuarial accrued liability.

Members are required to contribute a percentage of their annual salary to the Plan on a biweekly basis. Rates vary according to entry age. For fiscal year 2009, the City employee contribution rates as a percentage of annual covered payroll averaged 10.06% for general members and 12.69% for safety members. A portion of the employee's share, depending on the employee's member class, is paid by the City (commonly referred to as the Employee Offset). In fiscal year 2009, the amount paid by the City ranges from 1.4% to 5.89% of covered payroll for general members and the rate for safety Plan members ranges from 2.4% to 4.3%. Employee contributions paid by the City, amounting to approximately $20,317 in fiscal year 2009, are made from the City's operating budget. The amount paid on behalf of the employees has been renegotiated through the meet and confer process which ultimately reduced the amount of the employee contribution paid by the City.

[1] This amount includes a contribution in addition to the ARC of approximately $700 in fiscal year 2009.

On September 2, 2008, Council approved O-19781 which amended Chapter 2, Article 4, Division 15 of the San Diego Municipal Code. The intent of the amendment was to eliminate the concept of "Surplus Earnings" (earnings in excess of those earned using the assumed actuarial rate of return) which was the historical term for the funds used to pay for supplemental and contingent benefits. In accordance with these revised SDMC sections, annual distributions of these benefits are paid from Plan assets and take place in priority order. The Plan assets are distributed to various SDCERS system reserves, SDCERS budget, and contingent benefits. The order of distribution and a more detailed discussion of each distribution follows: First, Plan assets are used to credit interest, at a rate determined by the SDCERS Board, which is currently 7.75%, to the Employer and Employee Contribution Reserves and 3.54% to DROP member accounts. Second, Plan assets are used to fund the SDCERS Annual Budget. Third, Plan assets are distributed for supplemental or contingent payments or transfers to reserves. These items include in a priority order: 1) Annual Supplement Benefit Payment ("13th Check") paid to retirees generally equal to approximately $30 (whole dollars) times the number of years of employment. 2) Corbett Settlement Payment paid to retirees who terminated employment prior to July 1, 2000 (Corbett Settlement payments not paid in any one year accrue to the next year and remain an obligation of SDCERS until paid). 3) Crediting interest to the Reserve for Supplemental Cost of Living Adjustment ("COLA").

e. **Funded Status and Funding Progress**

The following table summarizes the Plan's funding status as of the most recent valuation date:

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (b)	UAAL (b - a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b – a)/c)
6/30/2008	$ 4,660,346	$ 5,963,550	$ 1,303,204	78.15%	$ 535,774	243.24%

The actuarial assumptions used for the fiscal year 2008 valuation include an Entry Age Normal actuarial funding method, an Expected Value of Assets smoothing method, a UAL that is amortized over several different periods, a 7.75% earnings assumption, a 4.0% projected salary increase rate with an additional merit component based on member class and years of service, a 2% annual cost-of-living adjustment and a 4% inflation rate. The required schedule of funding progress immediately following the notes to the financial statements presents multiyear trend information about whether the actuarial value of Plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

f. **Annual Pension Cost and Net Pension Obligation**

Annual Pension Costs

Beginning with the valuation dated June 30, 2007, the normal cost (i.e. the actuarial present value of pension Plan benefits allocated to the current year) and the UAAL amortization cost (i.e. the portion of the pension Plan payment designed to amortize the UAAL) were determined using the Entry Age Normal (EAN) actuarial cost method (as opposed to the previously used Projected Unit Credit method), the result of which caused the UAAL used in the determination of the fiscal year 2009 ARC to increase by approximately $252,200. The following are the principal actuarial assumptions used for the fiscal year 2007 valuation (additional assumptions were used regarding a variety of other factors):

a) An 8.0% investment rate of return, net of administrative expenses.**

b) Projected salary increases of at least 4.25% per year.**

c) An assumed annual cost-of-living adjustment that is generally 2% per annum and compounded. In addition, there is a closed group of special safety officers whose annual adjustment is equal to inflation (4.25% per year).

**Both (a) and (b) included an inflation rate of 4.25%.

The actuarial value of assets was determined using a methodology that smoothes the effects of short-term volatility in the market value of investments over a five-year period. In fiscal year 2007, the SDCERS Board approved a different asset smoothing method by marking the actuarial value of assets to market value in the fiscal year 2006 actuarial valuation, the result of which caused the UAAL to decrease by approximately $183,800. The method used by the actuary in fiscal year 2005 was not a commonly used method. The expected actuarial value asset smoothing method commenced with the fiscal year 2007 valuation. Additionally, pursuant to the Gleason Settlement, the UAAL was being amortized over a fixed 30-year closed period for the fiscal years 2006, 2007, and 2008. However, for valuations effective June 30 2007, SDCERS' Board of Administration decided to use a 20-year closed amortization schedule with no negative amortization.

The following table shows the City's annual pension cost ("APC") and the percentage of APC contributed for the fiscal year ended June 30, 2009 and two preceding years (in thousands):

Fiscal Year Ended June 30	APC	Percentage Contributed	Net Pension Obligation
2007	$ 169,762	99.63%	$ 195,356
2008	145,077	114.82%	173,852
2009	167,529	97.66%	177,767

Net Pension Obligation

Net Pension Obligation (NPO) is the cumulative difference, since the effective date of GASB 27 (fiscal year 1998, with a 10-year look back), between the annual pension cost and the employer's contributions to the Plan. This includes the pension liability at transition (beginning pension liability) and excludes short term differences and unpaid contributions that have been converted to pension-related debt. As of June 30, 2009, the City's NPO is approximately $177,767 and is reported in accordance with GASB 27. See table above.

The change to NPO is derived by first calculating the City's Annual Required Contribution ("ARC"). The ARC is calculated by actuarially determining the cost of pension benefits accrued during the year (normal cost) as well as the annual amount needed to amortize the UAAL (amortization cost) as reported by the actuary, in accordance with the amortization period and method selected. The ARC is then increased by interest accruing on any outstanding NPO (NPO Interest) and then reduced by the amortization of the UAAL that is related to the NPO (ARC Adjustment).

The following shows the calculation for NPO based on the actuarial information provided to the City (in thousands):

ARC [Fiscal Year 2009]	$	165,704
Interest on NPO		13,895
ARC Adjustment		(12,070)
Annual Pension Cost		167,529
Contributions [Fiscal Year 2009]		(163,614)
Change in NPO		3,915
NPO Beginning of Year [July 1, 2008]		173,852
NPO End of Year [June 30, 2009]	$	177,767

Components of the NPO and actions taken to address the Pension Liability

Multiple components have contributed to the City's NPO dating back to fiscal year 1988, including the use of pension assets to pay for costs related to retiree healthcare and employee contribution offset liabilities. Additionally, benefit increases resulting from the Corbett Settlement, which were initially considered contingent, were excluded from the actuarially determined ARC and the City's contributions for the fiscal years 1996-2003 were less than the ARC as a result of MP-1 and MP-2.

As part of the agreements with the labor unions, several benefits were altered or eliminated for all employees hired on or after July 1, 2005, including the Deferred Retirement Option Plan (DROP), the 13th Check, the option to purchase years of service credits ("air-time"), and retiree healthcare benefits; however, the retirement formula generally remains 2.5% at 55 for general members and 3.0% at 50 for safety members.

DEFINED CONTRIBUTION PLANS

a. **Supplemental Pension Savings Plan - City**

Pursuant to the City's withdrawal from the Federal Social Security System effective January 8, 1982, the City established the Supplemental Pension Savings Plan ("SPSP"). Pursuant to the Federal Government's mandate of a Social Security Medicare tax for all employees not covered by Social Security hired on or after April 1, 1986, the City established the Supplemental Pension Savings Plan-Medicare ("SPSP-M"). The SPSP and SPSP-M Plans were merged into a single plan ("SPSP") on November 12, 2004 for administrative simplification, without a change in benefits. Pursuant to the requirements of the Omnibus Budget Reconciliation Act of 1990 ("OBRA-90") requiring employee coverage under a retirement system in lieu of coverage under the Federal Insurance Contributions Act ("FICA") effective July 1, 1991, the City established the Supplemental Pension Savings Plan-Hourly ("SPSP-H"). These supplemental plans are defined contribution plans administered by Wachovia Corporation to provide pension benefits for eligible employees. There are no plan members who belong to an entity other than the City. In a defined contribution plan, benefits depend solely on amounts contributed to the plan plus investment earnings, less investment losses. The City's general retirement members and lifeguard members of the City's safety retirement members participate in the plan. Eligible employees may participate from the date of employment.

The following table details plan participation as of June 30, 2009:

Plan	Participants
SPSP	8,323
SPSP – H	4,355

The SPSP Plan requires that both the employee and the City contribute an amount equal to 3% of the employee's total salary each pay period. Participants in the Plan hired before July 1, 1986 may voluntarily contribute up to an additional 4.5% and participants hired on or after July 1, 1986 may voluntarily contribute up to an additional 3.05% of total salary, with the City matching each. Hourly employees contribute 3.75% on a mandatory basis which is also matched by City contributions.

Under the SPSP Plan, the City's contributions for each employee (and interest allocated to the employee's account) are fully vested after five years of continuous service at a rate of 20% for each year of service. Hourly employees are immediately 100% vested. The unvested portion of City contributions and interest forfeited by employees who leave employment before five years of service are used to reduce the City's cost.

In fiscal year 2009, the City and the covered employees contributed approximately $23,746 and $22,643, respectively. As of June 30, 2009, the fair value of plan assets totaled approximately $489,344. SPSP is considered part of the City of San Diego's financial reporting entity and is reported as a pension and employee savings trust fund.

b. **401(k) Plan - City**

The City established a 401(k) Plan effective July 1, 1985. The 401(k) Plan is a defined contribution plan administered by Wachovia Corporation to provide pension benefits for eligible employees. Employees are eligible to participate from date of employment. Employees make contributions to their 401(k) Plan accounts through payroll deductions, and may also elect to contribute to their 401(k) account through the City's Employees' Flexible Benefits Program.

The employees' 401(k) contributions are based on IRS calendar year limits. Employees contributed approximately $22,246 during the fiscal year ended June 30, 2009. There is no City contribution towards the 401(k) Plan.

As of June 30, 2009, the fair value of plan assets totaled approximately $220,022. The 401(k) Plan is considered part of the City's financial reporting entity and is reported as a pension and employee savings trust fund.

c. **Pension Plan - Centre City Development Corporation (CCDC)**

CCDC has a Money Purchase Pension Plan covering all full-time permanent employees (the "CCDC Plan"). The CCDC Plan is a defined contribution plan under which benefits depend solely on amounts contributed to the plan plus investment earnings. Employees are eligible to participate on the first day of the month following 90 days after their date of employment. During each year, CCDC contributes semi-monthly an amount equal to 8% of the total quarterly compensation for all employees. CCDC's contributions for each employee are fully vested after six years of continuous service. CCDC's total payroll (excluding benefits) in fiscal year 2009 was approximately $3,964. CCDC contributions were calculated using the base salary amount of approximately $3,784. CCDC made the required 8% contribution amounting to approximately $278 (net of forfeitures) for fiscal year 2009.

In addition, CCDC has a Tax Deferred Annuity Plan covering all full-time permanent employees. The CCDC Plan is a defined contribution plan under which benefits depend solely on amounts contributed to the plan by the employer and the employees, plus investment earnings. Employees are eligible to participate on the first day of the month following 90 days after their date of employment. During each plan year, CCDC contributes semi-monthly an amount equal to 16% of the total semi-monthly compensation for eligible employees. CCDC's contributions for each employee are fully vested at time of contribution. The Tax Deferred Annuity Plan includes amounts deposited by employees prior to CCDC becoming a contributor to the CCDC Plan. CCDC made the required 16% contribution amounting to approximately $610 for fiscal year 2009.

The fiduciary responsibilities of CCDC consist of making contributions and remitting deposits collected. The City does not hold these assets in a trustee or agency capacity for CCDC; therefore, these assets are not reported within the City's basic financial statements.

d. **Pension Plan - San Diego Convention Center Corporation (SDCCC)**

SDCCC's Money Purchase Pension Plan (the "SDCCC Plan") became effective January 1, 1986. The SDCCC Plan is a qualified defined contribution plan and as such, benefits depend on amounts contributed to the SDCCC Plan plus investment earnings less allowable plan expenses. The SDCCC Plan covers employees not otherwise entitled to a retirement/pension plan provided through a collective bargaining unit agreement. Employees are eligible at the earlier of the date on which they complete six months of continuous full-time service, or the twelve-month period beginning on the hire date (or any subsequent Plan year) during which they complete 1,000 hours of service.

A plan year is defined as a calendar year. SDCCC's balance for each eligible employee is vested gradually over five years of continuing service with an eligible employee becoming fully vested after five years. Forfeitures and SDCCC Plan expenses are allocated in accordance with Plan provisions. A trustee bank holds the SDCCC Plan assets. The City does not act in a trustee or agency capacity for the SDCCC plan; therefore, these assets are not reported within the City's basic financial statements.

For the year ended June 30, 2009, pension expenditures for the SDCCC Plan amounted to $1,378. SDCCC records pension expenditures during the fiscal year based upon estimated covered compensation.

e. **Pension Plan - San Diego Data Processing Corporation (SDDPC)**

SDDPC administers a Money Purchase Pension Plan (the "SDDPC Plan") covering substantially all employees. The SDDPC Plan is a defined contribution plan, wherein benefits depend solely on amounts contributed to the plan plus investment earnings. Employees are eligible to participate from the date of employment. During each plan year, SDDPC contributes monthly an amount equal to 20% of the total monthly compensation for all employees. SDDPC contributions for each employee are fully vested after four years of continuing service. The City does not act in a trustee or agency capacity for the SDDPC Plan; therefore, these assets are not reported within the City's basic financial statements. In fiscal year 2009, SDDPC made the required 20% contribution, amounting to approximately $4,023.

SDDPC also administers a Tax Sheltered Annuity Plan, a voluntary defined contribution plan covering all employees of SDDPC who are eligible for membership as defined by the plan document. There are no employer contributions to this plan.

f. **Pension Plan - San Diego Housing Commission (SDHC)**

SDHC provides pension benefits for all its full-time employees through a defined contribution plan (the "SDHC Plan"). In a defined contribution plan, benefits depend solely on amounts contributed to the plan plus investment earnings. Employees are eligible to participate on the first day of their employment. SDHC's contributions for each employee (and interest allocated to the employee's account) are fully vested after four years of continuous service. SDHC's contributions for, and interest forfeited by, employees who leave employment before four years of service are used to reduce the SDHC's current-period contribution requirement. SDHC's covered payroll in fiscal year 2009 was approximately $12,166. SDHC made the required 14% contribution, amounting to approximately $1,703 and plan members contributed $67 for fiscal year 2009. The City does not act in a trustee or agency capacity for the SDHC Plan; therefore, these assets are not reported within the City's basic financial statements.

g. **Pension Plan - Southeastern Economic Development Corporation (SEDC)**

SEDC has a 403(b) Tax Sheltered Annuity Plan (Defined Contribution Plan) covering all full-time permanent employees (the "SEDC Plan"). The first six months of the current fiscal year, July 1, 2008 to December 31, 2008, the plan was administered by James Kerr & Associates, Inc with Morgan Stanley Dean Witter as the investment advisor. Under this plan, SEDC contributed a monthly amount equal to 12% of the employees' base salary, or 15% of management employees' base salary. This plan terminated on December 31, 2008. All assets of the plan were transferred to a new 403(b) Tax Sheltered Annuity Plan, effective January 1, 2009. This plan is currently administered by VLP Corporate Services, LLP with Merrill Lynch as the investment advisor. Employees are eligible on their date of employment, and SEDC contributes an amount equal to 12% of all employees' salaries. SEDC's total payroll in fiscal year 2009 was approximately $813 and SEDC made the required 403(b) contribution totaling $96 for fiscal year 2009. SEDC Plan members contributed an additional $14.

13. OTHER POSTEMPLOYMENT BENEFITS (In Thousands)

a. Plan Description

The City provides postemployment healthcare benefits to qualifying general, safety and legislative members, as provided for in San Diego Municipal Code (SDMC) Sections 24.1201 through 24.1204. The Other Postemployment Benefit Plan (the "OPEB Plan") is a single-employer plan, administered by SDCERS, and includes approximately 5,400[1] retirees, 8,900[1] active employees and 600[1] terminated vested members as of June 30, 2009. Postemployment healthcare benefits are primarily for health eligible retirees who were actively employed on or after October 5, 1980 and were otherwise entitled to retirement allowances. Health eligible retirees can obtain health insurance coverage with the plan of their choice, including any City sponsored, union sponsored, or privately secured health plan. In fiscal year 2009, health eligible retirees who were also eligible for Medicare are entitled to receive reimbursement/payment of healthcare premiums, limited to approximately $8.4 per year, in addition to reimbursement/payment for Medicare Part B premiums, limited to approximately $1.2 per year. Health eligible retirees who are not eligible for Medicare are entitled to receive reimbursement/payment of healthcare premiums, limited to approximately $8.9 per year. Reimbursements for health eligible retirees are adjusted annually based upon the projected increase for National Health Expenditures by the Centers for Medicare and Medicaid Services. Annual adjustments may not exceed 10% for any plan year. Non-health eligible employees who retired or terminated prior to October 6, 1980 and who are otherwise eligible for retirement allowances are also eligible for reimbursement/payment of healthcare benefits limited to a total of $1.2 per year. Reimbursements for non-health eligible retirees are not subject to annual adjustments.

As of July 1, 2005, the City's postemployment healthcare benefit plan is closed to new entrants. However, SDCERS has asserted that due to delays in codification of benefit changes into the Municipal Code, the effective cut off date would instead be February 16, 2007, which is when the Ordinance O-19567 was officially codified in the Municipal Code. As of the issuance of this report, there has been no change in the status of this case [refer to Note 18 for additional information].

Effective July 1, 2009, the City has agreed to establish a trust vehicle for a defined contribution plan to fund retiree medical benefits for employees who are excluded from the current plan. This defined contribution plan requires a mandatory employee contribution of 0.25% of gross salary with a corresponding 0.25% match by the City. Legislative and Safety members are ineligible for this plan. Additionally, as part of the agreements with the labor unions, the new definition of "health-eligible retiree" states that employees must have 10 years of service with the City to receive 100% of the retiree health benefit and five years of service to receive 50% of the retiree health benefit.

b. Summary of Significant Accounting Policies

Basis of Accounting - The postemployment healthcare trust funds use the economic resources measurement focus and the accrual basis of accounting. Contributions are recognized as additions in the period in which the contributions are due and a formal commitment to provide the contributions has been made. Benefits and refunds are recognized when due and payable in accordance with the OPEB Plan.

Method Used to Value Investments – CalPERS investments are stated at fair value. Certain construction projects and alternative investments are reported at cost, which approximates market value. Mortgages are valued on the basis of their future principal and interest payments discounted at prevailing interest rates for similar instruments. The fair value of real estate investments, principally rental property subject to long-term net leases, is estimated based on independent appraisals.

[1] Reported as a whole number.

c. Contributions and Reserves

In accordance with SDMC Section 24.1204, postemployment healthcare benefits are to be paid by the City, directly, from any source available to it other than the Pension Plan. Members of the OPEB Plan do not have contribution requirements related to their own coverage; however, retirees are required to pay for the benefits of their beneficiaries (amounts vary based on coverage elections). In fiscal year 2009, the City contributed $25,587 to the Post-Employment Healthcare Benefit Plan, which is administered by SDCERS.

In addition to current retirees and beneficiaries, the OPEB Plan includes active and terminated vested members, and therefore, the City also pre-funds future expenses related to postemployment healthcare benefits through an investment trust administered by CalPERS. The CalPERS Employers Retirement Benefits Trust (CERBT) requires the City to pre-fund in an amount not less than $5 annually. An ARC for the OPEB Plan is calculated by the City's actuary on an annual basis. City management plans to continue funding current year postemployment healthcare benefits from the pay-as-you-go trust established with SDCERS until the City is able to pay the ARC in full. Additionally, City management intends to pre-fund the CERBT with up to $25,000 on an annual basis, which is also outlined in the City's Five Year Financial Outlook. All contributions to the CERBT become trust assets.

The City contributed approximately $23,911 to the CERBT in fiscal year 2009. As of June 30, 2009, the balance in the CERBT was approximately $41,497. This balance is inclusive of all contributions to the plan as well as investment losses and administrative expenses amounting to approximately $12,499 and $45, respectively.

d. Funded Status and Funding Progress

The following table summarizes the OPEB Plan's funding status as of the most recent valuation date:

Schedule of Funded Status

Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as % of Covered Payroll ((b-a)/c)
06/30/09	$ 41,497	$ 1,359,377	$ 1,317,880	3.05%	$ 549,012	240.05%

The schedules presented as required supplementary information following the notes to the financial statements present information regarding the funding status and employer contributions for the current and preceding fiscal years. The Schedule of Funding Progress is intended to present information about whether the actuarial values of plan assets are increasing or decreasing over time relative to the actuarial accrued liabilities for benefits. The Schedule of Employer Contributions is intended to present trend information about the amounts contributed to the OPEB Plan by employers in comparison to the ARC determined in accordance with the parameters of GASB 43. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost for each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years.

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future, and actuarially determined amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future. Actuarial calculations are based on the benefits provided under the terms of the substantive plan in effect at the time of each valuation. Additionally, actuarial calculations reflect a long-term perspective and include methods and assumptions that are designed to reduce short-term volatility of actuarial accrued liabilities and the actuarial value of assets. The following table summarizes the more significant actuarial methods and assumptions used to calculate the ARC for the fiscal year 2009 (actuarial valuation for the fiscal year ended June 30, 2007) as well as for the most current actuarial valuation (ended June 30, 2009):

Description	Method/Assumption
Actuarial Cost Method	Entry Age Normal
Amortization Method	Level Dollar
Remaining Amortization Period	30 years, open
Actuarial Asset Valuation Method	Fair Value
Discount Rate	6.69%*
Inflation Rate	N/A**
Projected Payroll Increases	N/A**
Health Care Cost Trend Rate	10% grading down 0.5% each year to 5%

** Determined as a blended rate based on the City's partial contributions to the Plan.*

*** Postemployment healthcare benefits are not based on inflation or payroll, but rather are determined based on the Health Care Cost Trend Rate.*

Source: Buck Consultants

e. Other Postemployment Benefit Cost and Net OPEB Obligation (NOPEBO)

The following table presents the annual OPEB cost, the percentage of annual OPEB cost contributed during the fiscal year, and the net OPEB obligation at the end of fiscal year 2009 as well as for the preceding fiscal year:

Fiscal Year Ended	Annual OPEB Cost	Percentage Contributed	Net OPEB Obligation
06/30/08	$ 91,346	58.63%	$ 37,793
06/30/09	105,583	46.88%	93,878

As the administrator of the OPEB Plan, the City implemented GASB Statements 43 and 45 in fiscal year 2008 and elected to report a zero net OPEB obligation at the beginning of the transition year. The following table shows the calculation of the City's net OPEB obligation of the OPEB Plan for the fiscal year ended June 30, 2009 (based on the valuation ended June 30, 2007):

ARC [Fiscal Year 2009]	$ 104,475
Interest on NOPEBO	2,548
ARC Adjustment	(1,440)
Annual OPEB Cost	105,583
Contributions [Fiscal Year 2009]	(49,498)
Change in NOPEBO	56,085
NOPEBO Beginning of Year [July 1, 2008]	37,793
NOPEBO End of Year [June 30, 2009]	$ 93,878

14. INTERFUND RECEIVABLES, PAYABLES, AND TRANSFERS (In Thousands)

Interfund Working Capital Advance (WCA) balances are the result of loans between funds that are expected to be repaid in excess of one year. The majority of the advances, approximately $7,359, are advances from the Housing and Urban Development (HUD) Section 108 grant funds to RDA. Interfund WCA balances at June 30, 2009 are as follows:

Contributing Fund (Receivable)	Benefitting Fund (Payable) NonMajor Governmental
NonMajor Governmental	$ 7,959

Interfund receivable and payable balances are the result of loans between funds that are expected to be repaid during the next fiscal year, as well as amounts due for services provided. $5,980 represents amounts owed to SDDPC for data processing services provided to the City but not paid for until July 2009, and $3,604 represents a deficit in the Subdivision Fund which is covered by Development Services. Interfund receivable/payable balances at June 30, 2009 are as follows:

	Benefitting Fund (Payable)						
Contributing Fund (Receivable)	General Fund	NonMajor Governmental	Internal Service	Sewer Utility	Water Utility	Nonmajor Enterprise	Total
General Fund	$ -	$ -	$ 1,500	$ -	$ -	$ -	$ 1,500
Nonmajor Governmental	-	-	26	-	-	-	26
Nonmajor Enterprise	-	3,604	5	-	-	-	3,609
Internal Service	2,095	2,389	281	510	558	147	5,980
Total	$ 2,095	$ 5,993	$ 1,812	$ 510	$ 558	$ 147	$ 11,115

The Sewer Utility Fund has an interfund loan receivable of $3,487, and the Black Mountain Ranch FBA Fund, a capital projects fund, has a corresponding interfund payable of $3,487 for advanced FBA project funding. The Sewer Fund agreed to finance the Carmel Valley Trunk Sewer project to facilitate earlier construction, of which a portion was deemed the responsibility of the Carmel Valley area developers and is intended to be reimbursed in fiscal year 2010 from FBA Fund assessment revenue.

PFFA issued pooled financing bonds, Series 2007 A and B for the purpose of making loans to RDA to be used for financing and refinancing redevelopment activities in the Southcrest, Central Imperial, and Mount Hope Redevelopment Project Areas. The PFFA debt service fund has an interfund loan receivable of $33,460 and the Redevelopment Agency Fund has an aggregate interfund loan payable of $33,460. Since these loans are between governmental funds, the interfund receivable and payable are eliminated through the government-wide conversion.

Interfund transfers result from the transfer of assets without the expectation of repayment. Transfers are most commonly used to (1) move revenues from the fund in which it is legally required to collect them into the fund which is legally required to expend them, including TOT, Storm Drain, and TransNet funds collected in said funds but legally spent within the General Fund, (2) utilize unrestricted revenues collected in the General Fund to finance various programs accounted for in other funds, in accordance with budgetary authorizations, and (3) move tax revenues collected in the special revenue funds to capital projects and debt service funds to pay for the capital projects and debt service needs during the fiscal year.

Interfund transfer balances for the year ended June 30, 2009 are as follows:

	Benefiting Fund							
Contributing Fund	General Fund	Nonmajor Governmental	Sewer Utility	Water Utility	Nonmajor Enterprise	Internal Service	Governmental Capital Asset Transfers	Total
General Fund	$ -	$ 26,031	$ -	$ -	$ 2,196	$ 1,847	$ -	$ 30,074
Nonmajor Governmental	105,059	190,654	1,238	186	421	702	-	298,260
Sewer Utility	-	998	-	33	-	26	2,552	3,609
Water Utility	-	477	-	-	-	99	53	629
Nonmajor Enterprise	2,131	333	-	-	30	33	-	2,527
Internal Service	4,136	171	616	406	246	5	232	5,812
Governmental Capital Asset Transfers	-	-	-	3,257	-	3,174	-	6,431
Total	$ 111,326	$ 218,664	$ 1,854	$ 3,882	$ 2,893	$ 5,886	$ 2,837	$ 347,342

15. RISK MANAGEMENT (In Thousands)

The City is exposed to various risks of loss related to torts, including theft of, damage to, and destruction of assets, errors and omissions, injuries to employees, and natural disasters. The City has established various self-insurance programs and maintains contracts with various insurance companies to manage excessive risks.

The City maintains an excess liability insurance policy in collaboration with a statewide joint powers authority risk pool, the California State Association of Counties-Excess Insurance Authority (CSAC-EIA) for amounts up to $50,000. The City's self-insurance retention amount is $4,000.

The City offers a cafeteria-style flexible benefits plan. For Municipal Employees' Association (MEA) and Local-127 represented employees, this plan requires employees to choose a health plan unless covered elsewhere, and also a life insurance plan. It also gives employees the option of obtaining dental insurance, vision insurance, or catastrophic care insurance. For all other employees, the benefits plan is the same, with the exception that $50 of City-paid life insurance is automatically provided outside of the flexible benefit credit. Employees can place remaining flexible benefit dollars into IRS qualified dental/medical/vision and childcare reimbursement accounts, into their 401(k), and/or take as cash.

The City is self-insured for workers' compensation and long-term disability (LTD). All operating funds of the City participate in both these programs and make payments to the Self Insurance Fund. Each fund contributes an amount equal to a specified rate multiplied by the gross salaries of the fund. These payments are treated as operating expenditures in the contributing funds and operating revenues in the Self Insurance Fund.

Public liability, workers' compensation, and long-term disability estimated liabilities as of June 30, 2009 are determined based on results of independent actuarial evaluations and include amounts for claims incurred but not reported and adjustment expenses. Claims liabilities are calculated considering the effects of inflation, recent claim settlement trends including frequency and amount of payouts, and other economic and social factors. Estimated liabilities for public liability claims have been recorded in the Self Insurance Fund, Sewer Utility Fund, and Water Utility Fund.

A reconciliation of total liability claims, for all three funds, showing current and prior year activity is presented below:

	Public Liability	Workers' Comp & Long-Term Disability	Total
Balance, July 1, 2007	$ 104,244	$ 175,798	$ 280,042
Claims and Changes in Estimates	35,902	17,167	53,069
Claim Payments	(28,043)	(22,381)	(50,424)
Balance, June 30, 2008	112,103	170,584	282,687
Claims and Changes in Estimates	57,357	13,711	71,069
Claim Payments	(25,588)	(21,336)	(46,924)
Balance, June 30, 2009	$ 143,873	$ 162,959	$ 306,832

The City, in collaboration with CSAC-EIA, maintains an “All Risk” policy which includes flood and earthquake coverage for scheduled locations for amounts up to $25,000 per occurrence under the primary policy, with a $25 deductible. Limits include coverage for business interruption losses for designated lease-financed locations. There is no sharing of limits among the City and member counties of the CSAC-EIA pool, unless the City and member are mutually subject to the same loss. Limits and coverage may be adjusted periodically in response to the requirements of bond financed projects, acquisitions, and in response to changes in the insurance marketplace.

Earthquake coverage is provided for designated buildings/structures and certain designated City lease-financed locations in the amount of $60,000, including coverage for business interruption caused by earthquake at certain designated locations. Earthquake coverage is subject to a deductible of 5% of total values per unit per occurrence, subject to a $100 minimum. The City’s earthquake coverage is purchased jointly and shared with the member counties in the CSAC-EIA pool. Due to the potential for geographically concentrated earthquake losses, the CSAC-EIA pool is geographically diverse to minimize any potential sharing of coverage in the case of an individual earthquake occurrence. Depending upon the availability and affordability of such earthquake insurance, the City may elect not to purchase such coverage in the future, or the City may elect to increase the deductible or reduce the coverage from present levels.

The City is a public agency subject to liability for the dishonest and negligent acts or omissions of its officers and employees acting within the scope of their duty (“employee dishonesty” and “faithful performance”). The City participates in the joint purchase of insurance covering employee dishonesty and faithful performance through the CSAC-EIA pool. Coverage is provided in the amount of $10,000 per occurrence, subject to a $25 deductible.

During fiscal year 2009, there were no significant reductions in insurance coverage from the prior year. For each of the past three fiscal years, the settlements have not exceeded insurance coverage.

See Contingencies, Note 18, for additional information.

16. FUND BALANCE / NET ASSETS (DEFICIT) (In Thousands)

Development Services (Enterprise) has a net deficit of approximately ($8,785), due to a drop in workload activity caused by the deteriorating economy. The department reduced their work force by 27 full time equivalents (FTE) in the three months prior to the end of fiscal year 2009, but the adjustment did not correct the structural deficit between revenues and expenditures. A user fee increase was approved by the City Council on October 27, 2009 per Resolution R-305326. Based upon the projected workload decline for the current fiscal year, the Development Services Department has reduced an additional 48 FTEs to correct the revenue/expenditure deficit. Further reductions will be made as required to respond to revenue deficits.

The Self Insurance Fund (Internal Service) has a net deficit of approximately ($164,372), which represents unfunded estimated claims and claim settlements related to Public Liability, Workers' Compensation, and Long-Term Disability. It is anticipated that individual claim settlements will be funded through future user charges, subsequent to the filing of a claim and prior to its settlement. In addition to user charges, in January 2008 the Mayor's office presented a five-year financial outlook to the City Council, including a proposal to fund the Self Insurance Fund. As part of this proposal, during fiscal year 2009, $10,000 was contributed to the Public Liability Fund and $5,000 to the Workers' Compensation Fund. On November 13, 2007, the City Council also approved the formal City Reserve Policy. This policy contains a "Risk Management Reserve Policy" for the self insurance funds. Both the Public Liability and Worker's Compensation funds shall maintain dedicated reserves equal to 50% of the outstanding claims. This is to be achieved no later than fiscal year 2014. However, due to the continued decline in the economy, and a reduction in General Fund revenues, the City may reassess this reserve policy during fiscal year 2010. The Long-Term Disability fund reserve was set to be $12,000 by fiscal year 2012 as recommended in the actuarial valuation report.

Publishing Services (Internal Service) has a net deficit of ($674), due to a decline in work production and outdated pricing for services which are not fully cost recoverable. Publishing Services has restructured their rates to ensure full cost recovery. In Fiscal Year 2009, after the implementation of the revised rates, the net deficit decreased by $76.

17. COMMITMENTS (In Thousands)

As of June 30, 2009, the City's business-type activities contractual commitments are as follows:

Airports	$	1,849
Environmental Services		5,205
Sewer Utility		91,639
Water Utility		92,938
Other		2,051
Total Contractual Commitments	$	193,682

These contractual commitments are to be financed with existing reserves and future service charges. The Sewer and Water Utility Funds intend to finance their contractual commitments with financing proceeds secured by system revenues, in addition to existing reserves and future service charges.

Consent Decree

On April 2, 2001, two environmental groups filed suit against the City alleging that the Municipal System's collection system was deficient as a result of sewer spills from December 1996 to the time of the filing. The complaint sought injunctive relief to prevent illegal discharges, a compliance schedule to upgrade the Municipal System's collection system, and civil penalties of $27.5 per day for each day of violation. The City contested the plaintiffs' claims.

The U.S. Environmental Protection Agency (EPA) and the State also filed suits against the City alleging the same collection system violations, seeking unspecified penalties and injunctive relief for collection system improvements. All three cases were consolidated. On March 16, 2005, the City settled the State lawsuit for $1,200. Of this total, $1,000 funded three supplemental environmental projects to benefit the local environment, and $200 was deposited in the State's Cleanup and Abatement Account.

The EPA, the City, and the environmental groups reached an agreement on additional requirements to reduce sewer spills, which are set forth in a Consent Decree (the "Consent Decree"). The Consent Decree requires increased sewer spill response and tracking, increased root control, replacement or rehabilitation of 250 miles of pipeline, a canyon economic and environmental analysis, pump station and force main upgrades, and entails court supervision of these upgrades at least through June 2013. The estimated average annual cost of this commitment is $117,000 per year in capital projects and $48,700 per year in operational maintenance to the sewer system (based on the projected expenditures for wastewater collections for fiscal year 2009); however, the costs for bidding, constructing and completing the required work will fluctuate depending on variables such as changes in the cost of materials and labor. No civil penalty payment was required, though stipulated penalties ranging from $375 (in whole dollars) to $20,000 (in whole dollars) per occurrence are included for subsequent violations of the Consent Decree. The Consent Decree was approved by the Court on October 9, 2007, settling all remaining issues in the case.

Four sewer rate increases were approved for fiscal year 2007 through fiscal year 2010 to partially fund the obligations of the Consent Decree. However, additional rate increases will be necessary (likely beginning in year 2011) to completely fund the Consent Decree. The City funds the Capital Projects in the Consent Decree through the issuance of notes and bonds which are repaid with sewer system revenues.

Agreement Relative to Modified Permit for the Point Loma Wastewater Treatment

In December 2008, the Environmental Protection Agency (EPA) released its tentative decision to approve the City's request to renew a modified permit for the Point Loma Wastewater Treatment Plant. Point Loma initially received a modified permit (also known as a waiver) in 1995, which was renewed in 2002. The City entered into an agreement with the environmental organizations to support the waiver and the City promised to conduct a study to identify opportunities to maximize recycling wastewater for non-potable and potable uses for an amount not to exceed $2,000,000 (in whole dollars). This request is the City's second renewal. In June 2009, the State of California's Regional Water Quality Control Board concurred with the EPA and concluded the public hearing process by unanimously approving the modified permit. On October 7, 2009 the California Coastal Commission voted 8 to 4 to approve the modified permit with the condition that the City come back in 2 years with the Recycled Water Study. The City is evaluating the specifics of the condition and will return to the California Coastal Commission in February 2010 for further discussion and adoption of findings. During this time, the present modified permit will be administratively continued. Point Loma will continue to operate under the provisions of the modified permit that was adopted in 2002, in full compliance with the Clean Water Act section 301(h), as modified by the Ocean Pollution Reduction Act.

California Department of Public Health Compliance Order

In 1994, the City of San Diego entered into a compliance agreement with the State of California Department of Public Health (DPH) with the approval of City Council, after the DPH Drinking Water Field Operations Branch conducted a sanitary survey of the City's water system. This agreement required the City to correct operational deficiencies and begin necessary capital improvements. The City was notified in January of 1997 that it was not in compliance with this agreement. At that time, the DPH issued a compliance order. The January 1997 Compliance Order was last amended in May of 2007 (Amendment 11), and included additional items that were not in the original Compliance Order. The DPH Compliance Order will remain in effect until the required projects are completed.

Presently, the Water Department is meeting all of the requirements of the DPH Compliance Order, including the ongoing obligation to provide DPH with quarterly progress reports. On February 26, 2007, the City authorized an increase in water rates and charges to continue funding projects mandated in the DPH Compliance Order as well as other Capital Improvement Program projects. In addition, on October 8, 2007, November 17, 2008, and November 17, 2009, the City authorized "pass-through" rate increases to account for the higher cost of water purchased from the San Diego County Water Authority. The 2007 and 2008 pass-through rate increases took effect on January 1, 2008 and January 1, 2009, respectively. The November 2009 pass-through increase is scheduled to take effect on January 1, 2010. All three pass-through rate increases will help preserve the funds previously committed to DPH Compliance Order projects. In conjunction with the November 17, 2008 approval of the January 1, 2009 pass-through rate increase, the City also approved a rate increase to cover the cost of an indirect potable reuse demonstration project. This increase also took effect January 1, 2009 and is anticipated to sunset on July 1, 2010 at which time sufficient revenue is expected to have been generated to offset the costs of the project.

The DPH has authority to impose civil penalties if the City fails to meet Compliance Order deadlines, although DPH has not imposed such penalties to date. Violation of the DPH Compliance Order may be subject to judicial action, including civil penalties specified in the California Health and Safety Code, Section 116725. Section 116725 penalties for violating a schedule of compliance for a primary drinking water standard can go as high as $25,000 (in whole dollars) per day for each violation. For violations of other standards, such as turbidity, the penalties can reach $5,000 (in whole dollars) per day. There are a number of additional enforcement tools prescribed by law, including mandatory water conservation, litigation and service connection moratoriums.

The costs for bidding, constructing and completing the required work will fluctuate depending on variables such as changes in the cost of materials and labor. As of June 2009, the Water Department's DPH Compliance Order project and DPH related project costs approximate:

Total Projects	FY09 Actuals	FY10 - FY11	FY12 - FY19	TOTAL
DPH & EPA Requirements	$ 126,355	$ 131,212	$ 216,279	$ 473,846
DPH Related Projects	19,150	98,633	296,286	414,069

These commitments are to be financed with existing net assets, present and future revenues, and financing proceeds secured by system revenues.

Convention Center Dewatering

The City is responsible for the disposition and monitoring of the quality of groundwater from the parking structure at the San Diego Convention Center located adjacent to San Diego Bay. The Convention Center includes a subterranean parking garage, which is subject to infiltration of groundwater, much of which originates from the bay. This groundwater must be continually pumped from the parking structure to prevent it from being inundated. Approximately 500,000 gallons of groundwater is pumped daily from the parking structure. Until March 26, 2008, this water was discharged into San Diego Bay. The City held a National Pollutant Discharge Elimination System (NPDES) permit for the discharge, issued by the Regional Water Quality Control Board (RWQCB). Monthly groundwater discharge sample results have not met the standards dictated by the NPDES permit since the end of calendar year 2005. This triggered the implementation of work to cease effluent violations within 27 months (from the end of March 2008), pursuant to an order of the RWQCB.

To achieve compliance with groundwater discharge requirements, the City retained an engineering consultant in fiscal year 2006 to review all previous work and develop the most cost-effective engineering solution to achieve compliance. The consultant's final report was received in August 2007. This report determined that the most cost effective method to comply with the RWQCB Order in the near term was to divert the discharge from the bay to the sewer system.

The City of San Diego established the diversion to the sewer effective March 26, 2008 in compliance with the RWQCB Order. The City requested permission from the EPA to make diversion of the groundwater into the sewer system permanent. The EPA granted the City's request on December 3, 2009. The City is now requesting concurrence from the State Water Resources Control Board ("SWRCB"), which must also approve the permanent diversion as a condition of funding it received from the EPA and passed through to the City.

18. CONTINGENCIES (In Thousands)

FEDERAL AND STATE GRANTS

The City recognizes as revenue grant monies received as reimbursement for costs incurred in certain Federal and State programs it administers. Although the City's Federal grant programs are audited in accordance with the requirements of the Federal Single Audit Act of 1984, the Single Audit Act Amendments of 1996 and the related U.S. Office of Management and Budget Circular A-133, these programs may be subject to financial and compliance audits by the reimbursing agencies. The amount, if any, of expenditures which may be disallowed by the granting agencies cannot be determined at this time. The Single Audit for fiscal year 2008 was completed by Macias Gini & O'Connell LLP. The Single Audit for fiscal year 2009 is in process.

The Office of the Inspector General (OIG) audited the City's Community Development Block Grant (CDBG) program, specifically CDBG loans to RDA, and on December 30, 2008, OIG issued its audit report to HUD, Office of Community Planning and Development (OPD). In addition to other findings, OIG determined that the City failed to execute loan agreements and repayment schedules for the CDBG loans issued to RDA that include a principal balance of $63,000 and an accumulated interest of approximately $76,000 totaling $139,202 in loans outstanding. The OIG audit report recommended that HUD require the City to execute written interagency agreements and loan agreements with RDA for these outstanding loan amounts. The City is currently in discussions with HUD on the audit findings and any actions HUD may require of the City, including the possible repayment by the City of certain CDBG funds and that HUD could forgive a portion of the accumulated interest so that repayment of the loans would not adversely impact RDA project areas. Depending on the outcome of the City's negotiations with HUD, repayment of the loans by RDA could impact RDA's liquidity. These loans are reported as a component of loans payable and accrued interest payable to the City in the long-term liabilities footnote of the Redevelopment Agency Financial Statements with an "unscheduled" maturity date. These loans do not appear in the City's CAFR as they represent interfund loans between two governmental funds in which repayment is not expected in a reasonable amount of time. Therefore, these loans are reported as interfund transfers in the fund level statements, and then eliminated as interfund activity in the government wide statements per GASB 34.

CONTINUING DISCLOSURE OBLIGATIONS

The City, in connection with all bond offerings since the effective date (July 1995) of the continuing disclosure requirements of SEC Rule 15c2-12, has contractually obligated itself to provide annual financial information, including audited financial statements, within certain specified time periods (generally nine months) after the end of each fiscal year. During fiscal year 2009, the City has met its contractual obligations to provide to the national repositories the audited financial statement for the fiscal year ended 2008 and certain annual financial information and operating data for fiscal year ended 2008 on a timely basis. Previously, the City failed to file required annual reports and the audited financial statements by the filing dates for the fiscal years ended 2003 through 2007. Each required annual report and the audited financial statements were subsequently filed. As of fiscal year 2009, there are no annual reports pending to be filed.

SEC ACTIONS

In November 2006, the Securities and Exchange Commission (SEC) entered an Order sanctioning the City of San Diego for committing securities fraud by failing to disclose, in 2002 and 2003, material information about its pension and retiree health care obligations in connection with disclosures relating to the sale of its municipal bonds. To settle the action, the City agreed to cease and desist from future securities fraud violations and to retain an independent consultant for three years to foster compliance with its disclosure obligations under the federal securities laws. The SEC's investigation with respect to the City's misleading disclosures may be ongoing as to individuals and other entities that may have violated the federal securities laws.

The SEC Order sanctioning the City of San Diego for committing securities fraud is available at: www.sec.gov

Changes to the City Charter to enhance the independence of both the City Auditor and the Audit Committee were approved with the passage of Proposition C (Prop C) in the June 3, 2008 election. These amendments included a restructured Audit Committee consisting of two Councilmembers, one being chair, and three public members. The public members must have at least ten years of professional auditing or accounting experience, and are appointed by the City Council.

INDEPENDENT CONSULTANT'S REPORTS

The Independent Consultant required by the SEC Order has several specific mandates. Among these are annual reviews, for a three year period, of the City's policies, procedures and internal controls regarding financial disclosures. The Independent Consultant is also required to make recommendations concerning the City's policies, procedures and internal controls and to assess the City's adoption and implementation of these recommendations

On April 24, 2009 the Independent Consultant issued his second annual report to the City of San Diego which was presented to the City Council on July 20, 2009. This report described his review and assessment of the City's policies, procedures and internal controls regarding the City's financial and other disclosures; the hiring of internal personnel and external experts for disclosure functions and; training programs focused on compliance and disclosure obligations. His complete report and recommendations is available at: www.sandiego.gov (included with the July 20, 2009 Audit Committee materials.)

On September 30, 2009 the Mayor sent a response to the Independent Consultant's second annual report to the Securities and Exchange Commission. This response is available at: www.sandiego.gov.

STATUS OF INTERNAL CONTROLS OVER FINANCIAL REPORTING

The plan to improve the City's internal controls over financial reporting includes the implementation of an enterprise resource planning (ERP) system during fiscal year 2010 to improve the way the City manages finances and the processes and internal controls involved in the City's accounting and human resources functions. As of June 30, 2009, setup work for the internal controls module called Governance, Risk and Compliance (GRC) has been completed within our ERP system. The GRC system for monitoring and testing access and process controls was activated with the new ERP system on July 1, 2009. The City has an 18 month internal controls plan in place that addresses the remediation of internal control weaknesses over financial reporting through more robust process documentation, further access and process control development within GRC, internal control testing, and employee training.

LITIGATION AND REGULATORY ACTIONS

The City is a defendant in lawsuits pertaining to material matters, including claims asserted which are incidental to performing routine governmental and other functions. This litigation includes but is not limited to: actions commenced and claims asserted against the City arising out of alleged torts; alleged breaches of contracts; alleged violations of law; and condemnation proceedings. The City has received approximately 2,300 notices of claims in fiscal year 2009.

The estimate of the liability for unsettled claims has been reported in the Government-wide Statement of Net Assets and the proprietary funds financial statements. The liability was estimated by categorizing the various claims and supplemented by information provided by the City Attorney with respect to certain large individual claims and proceedings. The recorded liability is the City's best estimate based on available information.

Significant individual lawsuits are described below.

SDCERS v. City of San Diego

In 1996 and 2002, SDCERS, the City, and various labor unions entered into agreements wherein the City's contribution to the pension system was less than the actuarially required contribution, while also increasing pension benefits. SDCERS has filed a complaint claiming the benefits are legal and should continue to be paid by the City. The City Attorney filed a cross-complaint alleging the benefits were not legal; however, that case was dismissed in January 2007. SDCERS filed a compulsory cross-complaint against the City, seeking damages in an amount equivalent to what the City should have contributed to the pension system in the absence of the funding relief granted by earlier management agreements MP-1 and MP-2. The City does not currently have an estimate of the range, if any, potential loss in the event of an adverse ruling.

City v. SDCERS

On October 15, 2007, the City filed a lawsuit concerning the effective date of certain benefit changes arising from the 2005 MOU entered into between the City and four of its collective bargaining units. The City contends the effective date of the benefit changes is July 1, 2005; however, the defendants contend the effective date is February 16, 2007 when the Municipal Code change was codified by O-19567. In the event of an adverse ruling, the liability facing the City is estimated to be in the range of $0 - $5,000.

Ernest Abbit, etc. v. City of San Diego

Residents of the De Anza Mobilehome Park filed a lawsuit alleging violations of the California Mobilehome Residency laws for management abuses and individual tort claims. In the event of an adverse ruling, the liability facing the City is estimated to be in the range of $0 - $19,000.

Joseph Aglio, etc v. City of San Diego

This complaint was filed by the firm Tatro & Zamoyski, representing a separate class of residents of the De Anza Mobilehome Park that were previously excluded from the Ernest Abbit case above due to settlements entered into with the City or because they were evicted. The claims are identical to the Ernest Abbit case. In the event of an adverse ruling, the liability facing the City is estimated to be in the range of $0 - $16,000.

Colony Hills Homeowners Association, Wayne Akeson, et al. v. City of San Diego

On August 6, 2006, a lawsuit arose following a water main break which caused flooding along a private street in the Colony Hills Homeowners Association in La Jolla. Claimants allege the water main failure caused soil subsidence, hillside failure, road failure and diminished property values of forty homes. In the event of an adverse ruling, the liability facing the City is estimated to be in the range of $0 - $45,000.

Janet Wood v. City of San Diego

This case against the City claims that women and unmarried retirees receive less benefits than others. In the event of an adverse ruling, the liability facing the City is estimated to be in the range of $0 - $2,000.

Frazier, Patricia, et al v. City of San Diego

This is an action by former City employees who are now defendants to a civil action by the SEC. Plaintiffs seek a declaratory judgment in the form of an order from the courts for the City to defend and indemnify Plaintiffs. In the event of an adverse ruling, the liability facing the City is estimated to be in the range of $0 - $3,000.

San Diego Police Tow operators v. City of San Diego

This case was brought by the towing companies under contract with the City, and alleges that the City is charging them "franchise fees" that exceed the amount permitted to be charged under the California Vehicle Code. In the event of an adverse ruling, the liability facing the City is estimated to be in the range of $0 - $14,000.

California Restaurant Management System Inc. v. City of San Diego

The California Restaurant Management System filed a class action lawsuit seeking refunds of sewer collection fees paid by "Food Service Establishments" as defined by the City's wastewater department. The Plaintiff alleges that the City failed to properly calculate the proportional impact of Food Service Establishments' use of the sewer system in determining sewer rates from 1994-2004. In the event of an adverse ruling, the liability facing the City is estimated to be in the range of $0 - $5,000.

Richard S. Pearson v. Mission and PB Drive, LLP and City of San Diego

Mission and PB Drive, LLP (MPB) is currently building a mixed-use, residential-commercial development on property which shares a common border with Pearson's residential property in Pacific Beach. The City owns a six foot drainage easement along the common border of the Pearson and MPB properties. MPB sued Pearson for trespass and nuisance. Pearson then filed a cross-complaint against MPB for nuisance, trespass and to quiet title to easement/declaratory relief/prescriptive easement. Pearson then amended his cross-complaint to bring the City into the lawsuit claiming nuisance, breach of contract, implied contractual indemnity, invasion of privacy and quiet title to easement/declaratory relief/prescriptive easement. In the event of an adverse ruling, the liability facing the City is estimated to be in the range of $0 - $2,500.

Betty Jones v. City of San Diego

This case concerns an allegation of personal injury due to a trip and fall in a City park. In the event of an adverse ruling, the liability facing the City is estimated to be in the range of $0 - $2,000.

Grande North at Santa Fe Place Home Owner's Association v. BOSA Development; City of San Diego

This case alleges property damage from hydrogen sulfide gas escaping from sewer lines. The damage includes the venting and plumbing throughout the multiple unit high rise condominium project. In the event of an adverse ruling, the liability facing the City is estimated to be in the range of $0 - $10,000.

Significant regulatory actions are described below (Other regulatory actions are described in Note 17 Commitments).

POLLUTION REMEDIATION OBLIGATIONS

In November 2006, GASB issued Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*, which addresses accounting and financial reporting standards for pollution (including contamination) remediation obligations, which are obligations to address the current or potential detrimental effects of existing pollution by participating in pollution remediation activities such as site assessments and clean ups. This Statement is effective for this fiscal year ended June 30, 2009.

Significant Pollution Remediation Events are discussed below:

California Regional Water Quality Board Administrative Proceeding

This matter involves a tentative cleanup and abatement order by the Regional Water Quality Control Board (RWQCB) which when made effective will require remediation of polluted bay sediments near historic shipyards on San Diego Bay. The City has been named as a "Discharger" in the tentative order along with other entities which include shipyard operators, the local electric utility SDG&E, and the U.S. Navy. The basis for the City being named is pollution flowing from its storm water conveyance system into the bay and Chollas Creek, which empties into the bay at the site. The discharges causing the polluted sediment are alleged to have occurred from 1915 to present. The order was originally issued in 2005 and was stayed by the Board in 2006; the stay was lifted in April 2008 after the RWQCB staff revised and reissued the tentative order. The proceeding was then stayed again in June 2008 while the parties pursued mediation. The Board has extended the mediation stay several times, at this time indefinitely, as the parties continue to actively pursue a settlement in confidential mediation. It is anticipated that a mediated settlement will be presented for public consideration and adoption by the RWQCB in late 2009 or early 2010, and that the RWQCB staff and Dischargers will be in accord with this possible settlement proposal. It is uncertain whether intervening environmental groups will subscribe to a proposed settlement and a contested hearing before the RWQCB and litigation remain possible results. The total cost of the cleanup is estimated to be between $900 and $122,000 (industrial shipbuilders urge the low end, environmental groups urge cleanup levels that would cost at the high end) – but those are the far ends of the spectrum and the cost of the actual total cleanup will likely be in the $40,000 to $80,000 range, subject to post-remedial monitoring, plus an additional $6,000 to $9,000 in site investigation, assessment costs, and RWQCB oversight costs. The order will include post-remedial monitoring requirements which, depending on monitoring results and trends, may lead to further cleanup orders. The parties will address allocation of all of these costs in mediation; however there exist many variables which make accurate estimation of the City's likely share of the total costs impossible at this time. Issues of allocation among the parties will be determined using principles established in the federal Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA), as interpreted in existing case law. CERCLA principles will be the basis of discussion in further mediation, and absent a settlement on allocation, those principles will be at issue in litigation. In this case there are a myriad of factual inputs relative to the CERCLA principles of allocation. Disputes over those facts and the weight they should be given, the number of Discharger parties, the confidential nature of the mediation, and the exposure to the possibility of litigation all preclude the City from publishing more a specific projected outcome in this matter at this time.

California Regional Water Quality Board (Board) Administrative Civil Liability Complaint

This matter involves a sewage spill into Lake Hodges in August 2007. The allegation from the Board is that the City violated the Clean Water Act and its NPDES permit. The penalty approved by the Board's staff, on 11/18/09, is $620 with an additional amount also due Santa Fe Irrigation for $60 as a result of the same spill. The $620 liability has been accrued in the Water Utility fund level financial statements.

County Department of Environmental Health (DEH) Unauthorized Release Cases

The City owns Underground Storage Tank Systems (UST) at various locations, including but not limited to: Airports, Fleet Division, and Fire and Rescue Divisions. The City has been named as a responsible party by the DEH in 23 cases located at 11 UST sites. The nature of the pollution involves soil and groundwater contamination by the UST's. The City has been able to utilize the State's UST Cleanup Fund to obtain reimbursement for a vast majority of the site assessment and mitigation costs. An estimate of the City's Pollution Liability has been calculated using a variety of methods and assumptions including but not limited to: soil borings; monitoring wells; lateral and vertical extent of impacts being defined; treatment; attenuation monitoring; and, soil and vapor sampling. The liability for each site ranges from $0 to $1,000, all but two estimates are under $300. Given that the vast majority of all costs are paid out of the State's UST Cleanup Fund, and the majority of the estimates are of relatively small amounts, the estimates are expensed when incurred throughout the year in the responsible fund and no liability is accrued in the financial statements.

19. THIRD PARTY DEBT (In Thousands)

The City has authorized the issuance of certain conduit revenue private activity bonds, in its name, to provide tax exempt status because it believes a substantial public benefit will be achieved through the use of the proceeds. Aside from the fact that these bonds have been issued in the City's name, the City has no legal obligation to make payment on these bonds and has not pledged any City assets as a guarantee to the bondholders. The following describes the outstanding third party debt:

Mortgage and Revenue Bonds

Single family mortgage revenue bonds have been issued to provide funds to purchase mortgage loans secured by first trust deeds on newly constructed and existing single-family residences. The purpose of this program is to provide low interest rate home mortgage loans to persons of low or moderate income who are unable to qualify for conventional mortgages at market rates. Multi-family housing revenue bonds are issued to provide construction and permanent financing to developers of multi-family residential rental projects located in the City to be partially occupied by persons of low income.

As of June 30, 2009, the status of all third party bonds issued is as follows (in thousands):

	Original Amount	Balance June 30, 2009
Mortgage Revenue	$ 15,700	$ 7,320

These bonds do not constitute an indebtedness of the City. The bonds are payable solely from payments made on and secured by a pledge of the acquired mortgage loans, certain funds and other monies held for the benefit of the bondholders pursuant to the bond indentures, property liens and other loans. In reliance upon the opinion of bond counsel, City officials have determined that these bonds are not payable from any revenues or assets of the City, and neither the full faith nor credit of the taxing authority of the City, the state, or any political subdivision thereof is obligated to the payment of principal or interest on the bonds. In essence, the City is acting as a conduit for the private property owners/bondholders in collecting and forwarding the funds. Accordingly, no liability has been recorded in the City's government-wide statement of net assets.

20. CLOSURE AND POST CLOSURE CARE COST (In Thousands)

State and federal laws and regulations require that the City of San Diego place a final cover on its Miramar Landfill site when it stops accepting waste and to perform certain maintenance and monitoring functions at the site for thirty years after closure. Although closure and post closure care costs will be paid only near or after the date that the landfill stops accepting waste, the City reports a portion of these closure and post closure care costs as an operating expense in each period based on landfill capacity used as of each financial statement date.

The $19,336 reported as landfill closure and post closure care liability at June 30, 2009 represents the cumulative amount reported to date based on the use of 76% of the estimated capacity of the landfill. The remaining life of the landfill is approximately eight years, based on the estimated closing date of 2017.

The City will recognize the remaining estimated cost of closure and post closure care of $6,112 as the remaining estimated capacity is filled. These amounts are based on what it would cost to perform all closure and post-closure care at June 30, 2009. Actual costs may be higher due to inflation, changes in technology, or changes in regulations.

The City is required by state and federal laws and regulations to make annual contributions to finance closure and post-closure care. The City is in compliance with these requirements and at June 30, 2009, cash or equity in pooled cash and investments of $37,983 was held for this purpose. This is reported as restricted assets on the statement of net assets in the Environmental Services Fund. The City expects that future inflation costs will be paid from interest earnings on these annual contributions. However, if interest earnings are inadequate or additional post-closure care requirements are determined (due to changes in technology or applicable laws or regulations, for example), these costs may need to be paid by charges to future landfill users or from other sources.

21. OPERATING AGREEMENTS (In Thousands)

San Diego Data Processing Corporation and Automated Regional Justice Information System

SDDPC has a yearly information technology services contract agreement with a joint powers agency known as the Automated Regional Justice Information System ("ARJIS") whose main purpose is to pursue development of computerized law enforcement systems in the region.

Under the agreement, SDDPC provides information technology services to ARJIS at rates which, on an annual basis, are equivalent to those charged to other governmental agency clients. Included in SDDPC's services revenue is approximately $3,689 related to ARJIS for the year ended June 30, 2009.

City of San Diego and Padres L.P.

On February 1, 2000, the City entered into a Joint Use and Management Agreement (Agreement) with the San Diego Padres baseball team (Padres) governing the rights and duties of the City and Padres with respect to the use and operation of the new Petco Park Ballpark Facility (Facility). The Facility was completed and operational in April 2004 and the City and Padres jointly own the facility. The Padres have a 30% divided interest based upon the original Facility cost estimate of $267,500 (or $80,250), and the City owns 70%, which is capitalized on the City's books. The City and the Padres have agreed upon the schedule of items and components that constitute the Padres' divided ownership, and the value of that divided ownership may vary from (but does not exceed) 30% due to the calculation of cost overruns for the Facility. Following termination of any occupancy agreement for the Facility, the Padres' ownership interest will automatically transfer to the City. Under the terms of the Agreement, the Padres are responsible for Facility operation and management, including maintenance, repairs and security required to preserve its condition. The City is responsible for paying certain expenses associated with the operation and maintenance of the Facility, up to a maximum of $3,500 per year, subject to certain inflationary adjustments.

For information pertaining to the operating agreement with San Diego Medical Services Enterprises, LLC please refer to Note 9, Joint Ventures and Jointly Governed Organizations.

22. SUBSEQUENT EVENTS (In Thousands)

On July 1, 2009, the City issued the fiscal year 2009-2010 Tax and Revenue Anticipation Notes in the amount of $125,000 to meet the annual general fund cash flow needs of the City. The fiscal year 2008-2009 Tax Revenue Anticipation Note was repaid on April 1, 2009.

On July 24, 2009, the State Legislature passed Assembly Bill (AB) 26 4x, which requires redevelopment agencies statewide to deposit a total of $2.05 billion of property tax increment in county “Supplemental” Educational Revenue Augmentation Funds (SERAF) to be distributed to meet the State’s Proposition 98 obligations to schools. The SERAF revenue shift of $2.05 billion will be made over two years, $1.7 billion in fiscal year 2010 and $350 million in fiscal year 2011. The SERAF would then be paid to school districts and the county offices of education which have students residing in redevelopment project areas, or residing in affordable housing projects financially assisted by a redevelopment agency, thereby relieving the State of payments to those schools. RDA’s share of this revenue shift is approximately $55,649 in fiscal year 2010 and $11,457 in fiscal year 2011. Payments are to be made by May 10 of each respective fiscal year. RDA intends to fund these payments with a combination of tax increment to be collected in fiscal year 2010 and 2011 and carryover funds from the current year.

On July 28, 2009 the State passed its 2009-2010 budget. This budget and related legislation contained provisions requiring California cities, counties, and special districts to lend property tax revenues to the State. The State is not required to repay the borrowed amounts until June 30, 2013. For the City, the borrowed amount totals $35,815. As part of the State budget actions, local agencies were provided the opportunity to receive the monies being borrowed by the State up front through a securitization program offered by the California Statewide Communities Development Authority (“CSCDA”), a joint powers authority. The City elected to participate in the program offered by CSCDA, and on October 19, 2009 the City Council approved Resolution R-305333, authorizing the applicable participation documents. The securitization was executed on November 19, 2009, and payments to the City will be made in two equal installments on January 15, 2010 and May 3, 2010. Under the program, there is no impact to the City’s Fiscal Year 2009-2010 budget.

On July 30, 2009, RDA issued $13,930 of Subordinate Tax Allocation Bonds for the purpose of repaying certain outstanding obligations and to finance redevelopment activities relating to the North Park Redevelopment Project area. The Series 2009A bonds are payable solely from and secured by a pledge of tax revenues and are subordinate to the prior liens of the outstanding North Park Redevelopment Project Tax Allocation Bonds, Series 2000, Series 2003A and Series 2003B. The bond issuance is structured as term bonds and has an interest rate that ranges from 6.0% to 7.0%, with a final maturity date of November 1, 2039.

On September 11, 2009 the City Council approved the *“Improper Influence of Outside Professionals and Obstruction of the City Auditor”* Ordinance #19895. This ordinance makes it unlawful for any elected official, officer or employee of the City, or anyone acting under their direction, to take any action to coerce or fraudulently influence, manipulate or mislead the City Auditor or any member of his or her staff in the conduct of an audit with the specific intent of obstructing such audit or rendering any report materially misleading. Municipal Code Section 22.0711 has been updated with this new ordinance language and can be accessed at sandiego.gov.

On September 25, 2009, the Related Companies (Plaintiffs) filed a lawsuit against RDA, the City, and CCDC, contending they breached a negotiating agreement entered into with Plaintiffs. Plaintiffs claim a development agreement acceptable to Plaintiffs wrongfully failed to be executed by RDA, the City, and CCDC under the pretext that CCDC’s president had a financial interest in Plaintiffs’ sister company while CCDC’s president resided in Florida. Plaintiffs claim they lost millions of dollars in pre-development investment expenditures as a result of the breach of the negotiating agreement. No estimate of the amount or range of potential loss may be made at this time.

The California Redevelopment Association (CRA) is the lead petitioner on a lawsuit to invalidate AB 26 4x, similar to last year's successful lawsuit challenging the constitutionality of AB 1389. The CRA filed the lawsuit on October 20, 2009. The lawsuit asserts that the transfer of property tax increment to the SERAF is not permitted under Article XVI, Section 16 of the California Constitution. The complaint also asserts impairment of contract and gift of public funds arguments. While the State made adjustments in AB 26 4x to address the constitutional issues raised by the Superior Court over last year's lawsuit challenging AB 1389, the Agency, along with the CRA and other California redevelopment agencies, believe that the SERAF remains unconstitutional.

On November 30, 2009, RDA terminated its Disposition and Development Agreement (DDA) with CentrePoint LLC for the development of a mixed-use development project within the Crossroads Project Area. Pursuant to the DDA, RDA's contribution was in the form of a developer loan of $5,245 to be repaid from the Crossroads Low and Moderate Income Housing Fund to subsidize 47 affordable units. The loan amount was later reduced to $4,969 pursuant to the third implementation agreement with CentrePoint LLC. Termination of the agreement will result in recognition of revenue for the loan payable balance of $4,969 and removal of the long term liability in the government-wide financial statements.

On December 9, 2009, the RDA Board approved the principal terms of a settlement agreement with San Diego State University Foundation (Foundation) on a complaint for specific performance alleging that the RDA breeched an agreement requiring them to sell certain property to the plaintiff. The settlement provides that the RDA contractual obligation of $1,715 and accrued interest of $1,613 payable to the Foundation will be reduced to the sum of $750. Additionally, RDA will transfer fee title of the property to the Foundation by Grant Deed.

Required Supplementary Information (Unaudited)
June 30, 2009

PENSION TRUST FUNDS

Schedule of Funding Progress

The following table shows the funding progress of the City's pention trust funds for the last three fiscal years (in thousands):

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (b)	UAAL (b - a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b – a)/c)
6/30/2006	$ 3,981,932	$ 4,982,700	$ 1,000,768	79.92%	$ 534,103	187.37%
6/30/2007 *	4,413,411	5,597,653	1,184,242	78.84%	512,440	231.10%
6/30/2008	4,660,346	5,963,550	1,303,204	78.15%	535,774	243.24%

Source: Cheiron, Inc.

* The actuarial accrued liability was calculated using the Entry Age Normal (EAN) method beginning in fiscal year 2007. Prior to fiscal year 2007, the Projected Unit Credit (PUC) method was used.

OPEB TRUST FUND

Schedule of Funding Progress
The following table shows the funding progress of the City's OPEB trust fund for the last two fiscal years (in thousands):

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (b)	UAAL (b - a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b – a)/c)
6/30/2008	$ 29,637	$ 1,235,707	$ 1,206,070	2.40%	$ 556,857	216.59%
6/30/2009	41,497	1,359,377	1,317,880	3.05%	549,012	240.05%

Schedule of Contributions from Employer and Other Contributing Entities
The following table shows contributions to the City's OPEB trust fund for the last two fiscal years (in thousands):

Fiscal Year	Annual Required Contribution	Actual Contribution	Percentage Contributed
6/30/2008	$ 91,645	$ 53,553	58.44%
6/30/2009	104,475	49,498	47.38%

Source: Buck Consultants

REQUIRED SUPPLEMENTARY INFORMATION - GENERAL FUND

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GENERAL FUND

The general fund is the chief operating fund of the City. It is used to account for all financial resources except those required to be accounted for in another fund.

General fund revenues are derived from such sources as: Taxes; Licenses and Permits; Fines, Forfeitures, and Penalties; Use of Money and Property; Aid from Other Governmental Agencies; Charges for Current Services; and Other Revenue.

Current expenditures and encumbrances are classified by the functions of: General Government and Support; Public Safety–Police; Public Safety–Fire and Life Safety and Homeland Security; Parks, Recreation, Culture and Leisure; Transportation; Sanitation and Health; Neighborhood Services; and Debt Service Principal and Interest. Appropriations are made from the fund annually.

GENERAL FUND
SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE
BUDGET AND ACTUAL (BUDGETARY BASIS)
YEAR ENDED JUNE 30, 2009
(In Thousands)

	Original Budget	Final Budget	Actual Amounts	Variance with Final Budget Positive (Negative)
REVENUES				
Property Tax	$ 411,142	$ 396,620	$ 398,743	$ 2,123
Sales Tax	230,196	223,618	212,918	(10,700)
Transient Occupancy Tax	90,629	82,189	73,765	(8,424)
Other Local Taxes	78,537	76,977	72,432	(4,545)
Licenses and Permits	32,687	32,240	31,249	(991)
Fines, Forfeitures and Penalties	34,215	34,216	32,467	(1,749)
Revenue from Use of Money and Property	54,019	52,351	42,252	(10,099)
Revenue from Federal Agencies	15,724	15,701	4,268	(11,433)
Revenue from Other Agencies	9,283	8,423	8,915	492
Charges for Current Services	135,582	131,016	133,117	2,101
Other Revenue	29,334	26,858	5,296	(21,562)
TOTAL REVENUES	1,121,348	1,080,209	1,015,422	(64,787)
EXPENDITURES				
Current:				
General Government and Support	279,818	269,270	249,134	20,136
Public Safety - Police	406,503	398,601	391,774	6,827
Public Safety - Fire and Life Safety and Homeland Security	186,752	197,166	196,329	837
Parks, Recreation, Culture and Leisure	125,464	123,904	120,573	3,331
Transportation	83,016	78,455	75,562	2,893
Sanitation and Health	100,903	90,630	81,462	9,168
Neighborhood Services	22,183	21,621	19,416	2,205
Debt Service:				
Principal Retirement	-	818	818	-
Interest	2,979	3,173	3,106	67
TOTAL EXPENDITURES	1,207,618	1,183,638	1,138,174	45,464
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	(86,270)	(103,429)	(122,752)	(19,323)
OTHER FINANCING SOURCES (USES)				
Transfers from Proprietary Funds	2,746	2,746	6,267	3,521
Transfers from Other Funds	69,347	71,334	105,059	33,725
Transfers to Proprietary Funds	(6,150)	(4,043)	(4,043)	-
Transfers to Other Funds	(24,688)	(26,031)	(26,031)	-
Net Loss from Joint Venture	-	-	(157)	(157)
TOTAL OTHER FINANCING SOURCES (USES)	41,255	44,006	81,095	37,089
NET CHANGE IN FUND BALANCE	(45,015)	(59,423)	(41,657)	17,766
Fund Balance Undesignated at July 1, 2008	75,339	75,339	75,339	-
Reserved for Encumbrances at July 1, 2008	43,853	43,853	43,853	-
Reserved for Minority Interest in Joint Venture at July 1, 2008	-	-	1,981	1,981
Reserved for Minority Interest in Joint Venture at June 30, 2009	-	-	(1,824)	(1,824)
Designated for Subsequent Years' Expenditures at July 1, 2008	862	862	862	-
Designated for Subsequent Years' Expenditures at June 30, 2009	-	-	(207)	(207)
FUND BALANCE UNDESIGNATED AT JUNE 30, 2009	$ 75,039	$ 60,631	$ 78,347	$ 17,716

The accompanying note is an integral part of the Required Supplementary Information

Note to Required Supplementary Information
Year Ended June 30, 2009

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

a. Budgetary Data

On or before the first meeting in May of each year, the City Manager submits to the City Council a proposed operating and capital improvements budget for the fiscal year commencing July 1. This budget includes annual budgets for the following funds:

- **General Fund**
- **Special Revenue Funds:**
  - City of San Diego:
    - -Acquisition, Improvement and Operation
    - -Environmental Growth Funds:
      - -Two-Thirds Requirement
      - -One-Third Requirement
    - -Police Decentralization
    - -Public Transportation
    - -Qualcomm Stadium Operations
    - -Special Gas Tax Street Improvement
    - -Street Division Operations
    - -Transient Occupancy Tax
    - -Underground Surcharge
    - -Zoological Exhibits
    - -Other Special Revenue
  - Centre City Development Corporation
  - Southeastern Economic Development Corporation
- **Debt Service Funds:**
  - City of San Diego:
    - -Public Safety Communications Project
  - San Diego Open Space Park Facilities District #1
- **Capital Projects Funds:**
  - City of San Diego:
    - -TransNet

Public hearings are then conducted to obtain citizen comments on the proposed budget. During the month of July the budget is legally adopted through passage of an appropriation ordinance by the City Council. Budgets are prepared on the modified accrual basis of accounting except that (1) encumbrances outstanding at year-end are considered expenditures and (2) the increase/decrease in reserve for advances and deposits to other funds and agencies are considered as additions/deductions of expenditures. The City budget is prepared excluding unrealized gains or losses resulting from the change in fair value of investments, proceeds from capital leases, and net income from joint venture.

The legal level of budgetary control for the City's general fund is exercised at the salaries and wages and non-personnel expenditures level. Budgetary control for the other budgeted funds, including those of certain component units, is maintained at the total fund appropriation level. All amendments to the adopted budget require City Council approval except as delegated in the Annual Appropriation Ordinance.

Reported budget figures are as originally adopted or subsequently amended plus prior year continuing appropriations. Such budget amendments during the year, including those related to supplemental appropriations, did not cause these reported budget amounts to be significantly different than the originally adopted budget amounts. Appropriations lapse at year-end to the extent that they have not been expended or encumbered, except for those of a capital nature, which continue to subsequent years.

The following is a reconciliation of the net change in fund balance prepared on a GAAP basis to that prepared on the budgetary basis for the year ended June 30, 2009 (in thousands):

	General Fund
Net Change in Fund Balances - GAAP Basis	$ (10,389)
Add (Deduct):	
Encumbrances Outstanding, June 30, 2009	(32,071)
Reserved for Advances, June 30, 2009	-
Designated for Unrealized Gains, June 30, 2009	(1,943)
Reserved for Advances, June 30, 2008	9
Designated for Unrealized Gains, June 30, 2008	2,737
Net Change in Fund Balances - Budgetary Basis	$ (41,657)

b. <u>Encumbrances</u>

Encumbrance accounting, under which purchase orders, contracts and other commitments for the expenditure of funds are recorded in order to reserve that portion of the applicable appropriation, is employed as an extension of formal budgetary control in the budgeted governmental funds.

Encumbrances outstanding at year-end are reported as reservations of fund balances, since the commitments will be honored through subsequent years' continuing appropriations. Encumbrances do not constitute expenditures or liabilities for GAAP reporting purposes.

SUPPLEMENTARY INFORMATION

City of San Diego
Pledged-Revenue Coverage - Water Bonds (Unaudited)
Last Ten Fiscal Years (In Thousands)

Fiscal Year Ended June 30	Total System Revenues	Total Maintenance and Operation Costs (Excludes Depreciation)	Net System Revenues [1]	Less: Interest Earnings on Reserve Fund - Senior Obligations	Adjusted Net System Revenues [2]
2000	$ 255,736	$ 213,358	$ 42,378	$ -	$ 42,378
2001	255,974	214,056	41,918	(54)	41,864
2002	261,333	222,104	39,229	(3,444)	35,785
2003	256,968	226,058	30,910	(1,305)	29,605
2004	267,649	232,193	35,456	(1,296)	34,160
2005	294,904	234,392	60,512	(1,262)	59,250
2006	303,453	242,180	61,273	(1,228)	60,045
2007	336,599	255,486	81,113	(1,346)	79,767
2008	350,770	258,813	91,957	(1,481)	90,476
2009	364,413	263,280	101,133	(2,668)	98,465

[1] Net System Revenues is defined as "System Revenues" less "Maintenance and Operation Costs" of the Water System for the fiscal year.

[2] Adjusted Net System Revenues is the "Net System Revenues" less "an amount equal to earnings from investments in any Reserve Fund or Reserve Account" for the fiscal year.

[3] All Obligations include Senior, Subordinate and State Revolving Fund (SRF) Loans.

Source: Comprehensive Annual Financial Reports

Table 13

Senior Debt Service						All Obligations [3]	
Principal	Interest	Total	Less: Senior Interest Earnings	Adjusted Debt Service	Adjusted Debt Service Coverage	Total Debt Service	Aggregate Debt Service Coverage
$ -	$ 18,730	$ 18,730	$ -	$ 18,730	2.26	$ 18,730	2.26
-	18,730	18,730	(54)	18,676	2.24	18,730	2.24
6,780	18,594	25,374	(3,444)	21,930	1.63	25,510	1.54
7,055	16,308	23,363	(1,305)	22,058	1.34	27,002	1.14
7,345	14,010	21,355	(1,296)	20,059	1.70	34,861	1.02
7,645	13,710	21,355	(1,262)	20,093	2.95	34,861	1.74
7,965	13,390	21,355	(1,228)	20,127	2.98	35,549	1.72
8,305	13,046	21,351	(1,346)	20,005	3.99	40,759	1.99
8,675	12,679	21,354	(1,481)	19,873	4.55	43,082	2.13
9,065	12,289	21,354	(2,668)	18,686	5.27	49,600	2.04

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APPENDIX B

SUMMARY OF PRINCIPAL LEGAL DOCUMENTS

This Appendix B contains only a brief summary of certain of the terms of the Installment Purchase Agreement, the Indenture, and the Assignment Agreement relating to the Series 2010A Bonds and a full review should be made of the entire Official Statement, including the cover page and the Appendices. References to, and summaries of, provisions of the documents referred to herein do not purport to be complete and such references are qualified in their entirety by reference to the complete provisions. All statements contained in this Appendix B are qualified in their entirety by reference to the entire Official Statement and the complete provisions of the documents referenced.

INDENTURE

The Indenture sets forth certain terms of the Bonds, the nature and extent of the security for the Bonds, the rights of the Owners of the Bonds, rights, duties and immunities of the Trustee, and the rights and obligations of the Authority. Certain provisions of the Indenture are summarized below. Other provisions are summarized in the body of this Official Statement under the captions, "DESCRIPTION OF THE SERIES 2010A BONDS" and "SECURITY AND SOURCES OF PAYMENT FOR THE SERIES 2010A BONDS." Capitalized terms used in connection with the Indenture but not defined below have the meanings ascribed thereto in the body of this Official Statement.

Selected Definitions.

Additional Bonds

The term "Additional Bonds" means those Bonds authorized and issued under the Indenture on a parity with the 2009A Bonds, in accordance with Indenture.

Acquisition Fund

The term "Acquisition Fund" means the fund by that name established under the Indenture.

Beneficial Owners

The term "Beneficial Owners" means those individuals, partnerships, corporations, or other entities for whom the Participants have caused the Depository to hold Book-Entry Bonds.

Board

The term "Board" means the Board of Commissioners of the Authority.

Bond or Bonds

The term "Bond" or "Bonds" means any of the bonds issued under the Indenture by the Authority, including any Additional Bonds.

Bond Counsel

The term "Bond Counsel" means a firm of attorneys that are nationally recognized as experts in the laws governing and relating to municipal finance.

Book-Entry Bonds

The term "Book-Entry Bonds" means Bonds executed and delivered under the book-entry system described in the Indenture.

Business Day

The term "Business Day" means a day of the year other than Saturday or Sunday, or a day on which banking institutions located in California are required or authorized to remain closed, or on which the New York Stock Exchange is closed. If the date for making any payment or the last date for performance of any act or the exercising of any right, as provided in the Indenture, shall not be a Business Day, such payment may be made or act performed or right exercised on the next succeeding Business Day, with the same force and effect as if done on the nominal date provided in the Indenture, and, unless otherwise specifically provided in the Indenture, no interest shall accrue for the period from and after such nominal date.

Certificate of the City

The term "Certificate of the City" means an instrument in writing signed by the Chief Financial Officer, the Chief Operating Officer, or any of their respective designees.

Charter

The term "Charter" means the Charter of the City as it now exists or may be amended, and any new or successor Charter.

Closing Date

The term "Closing Date" means any date upon which a Series of Bonds is purchased.

Code

The term "Code" means the Internal Revenue Code of 1986, as amended, and the regulations thereunder, and any successor laws or regulations.

Components

The term "Components" means components of the Project for which the City makes Installment Payments or Subordinated Installment Payments pursuant to any Supplement.

Comptroller

The term "Comptroller" means the Comptroller of the City.

Corporate Trust Office of the Trustee

The term "Corporate Trust Office of the Trustee" means the corporate trust office of the Trustee at the address set forth in the Indenture or such other or additional offices as may be specified to the Authority by the Trustee in writing.

Costs of Issuance

The term "Costs of Issuance" means all items of expense directly or indirectly payable by or reimbursable to the City, the Corporation, or the Authority relating to the issuance, sale, and delivery of any Bonds under the Indenture, including, but not limited to, costs of preparation and reproduction of documents; fees and expenses of the Feasibility Consultant; fees and expenses of the Authority (including its counsel); expenses of City, Authority, and Corporation staff; fees of the City's Financial Advisor; initial fees, expenses, and charges of the Trustee (including its counsel); Rating Agency fees; Underwriters' discount; legal fees and charges of Bond Counsel, Disclosure Counsel, Underwriters' counsel, and the City Attorney; and any other cost, charge, or fee in connection with the issuance and delivery of the Bonds.

Costs of Issuance Account

The term "Costs of Issuance Account" means, with respect to the 2010A Bonds, the account by that name established under the Second Supplemental Indenture for the payment of Costs of Issuance with respect to the 2010A Bonds.

Depository

The term "Depository" means the securities depository acting as Depository pursuant to the Indenture.

DTC

The term "DTC" means The Depository Trust Company, New York, New York, and its successors.

Event of Default

The term "Event of Default" shall have the meaning set forth in the Indenture or the Installment Purchase Agreement, as applicable.

Federal Securities

The term "Federal Securities" means the following securities:

1. United States Treasury Bills, bonds, and notes for which the full faith and credit of the United States are pledged for payment of principal and interest;

2. Direct senior obligations issued by the following agencies of the United States Government: the Federal Farm Credit Bank System, the Federal Home Loan Bank System, the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation, and the Tennessee Valley Authority;

3. Mortgage Backed Securities (except stripped mortgage securities) issued by the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation, and the Government National Mortgage Association; and

4. United States Treasury Obligations, State and Local Government Series.

First Supplemental Indenture

The term "First Supplemental Indenture" means the First Supplemental Indenture, dated as of June 1, 2009, by and between the Authority and the Trustee.

Fiscal Year

The term "Fiscal Year" means the fiscal year of the Authority, which, as of the date of the Indenture, is the period from July 1 to and including the following June 30.

Fitch

The term "Fitch" means Fitch Ratings and its successors and, if such company shall for any reason no longer perform the functions of a securities rating agency, "Fitch" shall be deemed to refer to any nationally recognized securities rating agency designated by the Authority and the City.

Indenture

The term "Indenture" means the Original Indenture, as supplemented and amended by the First Supplemental Indenture and the Second Supplemental Indenture.

Information Services

Information Services being Financial Information, Inc.'s "Daily Called Bond Service," 30 Montgomery Street, 10th Floor, Jersey City, New Jersey 07302, Attention: Editor; Moody's "Municipal and Government," 99 Church Street, 8th Floor, New York, New York 10007, Attention: Municipal News Reports; and Xcitek's "Called Bond Service," 5 Hanover Square, New York, New York 10004, Attention: Bond Redemption Group; provided, however, in accordance with then current guidelines of the Securities and Exchange Commission, Information Services shall mean such other organizations providing information with respect to called bonds as the Authority may designate in writing to the Trustee.

Interest Account

The term "Interest Account" means the account by that name established under the Indenture.

Interest Payment Date

The term "Interest Payment Date" means August 1, 2009, and each February 1 and August 1 thereafter until the Bonds are paid or redeemed in full.

Letter of Representations

The term "Letter of Representations" means the letter of the Authority delivered to and accepted by the Depository on or prior to the delivery of any Book-Entry Bonds setting forth the basis on which the Depository serves as depository for such Book-Entry Bonds, as originally executed or as it may be supplemented or revised or replaced by a letter to a substitute Depository.

Moody's

The term "Moody's" means Moody's Investors Service, a corporation organized and existing under the laws of the State of Delaware, and its successors, and if such corporation shall for any reason no longer perform the functions of a securities rating agency, "Moody's" shall be deemed to refer to any other nationally recognized securities rating agency designated by the Authority and the City.

Nominee

The term "Nominee" means the nominee of the Depository, which may be the Depository, as determined from time to time pursuant to the Indenture.

Original Indenture

The term "Original Indenture" means the Indenture, dated as of January 1, 2009, by and between the Authority and the Trustee.

Outstanding

The term "Outstanding," when used as of any particular time with reference to Bonds, means (subject to the provisions of the Indenture) all Bonds theretofore or thereupon executed by the Authority and authenticated and delivered by the Trustee pursuant to the terms of the Indenture, except:

1. Bonds theretofore cancelled by the Trustee or surrendered to the Trustee for cancellation;

2. Bonds paid or deemed to have been paid within the meaning of the Indenture;

3. Bonds beneficially owned by the City or the Authority; and

4. Bonds in lieu of or in substitution for which other Bonds shall have been executed by the Authority and authenticated and delivered pursuant to the terms of the Indenture.

Owner

The term "Owner" means any Person who shall be the registered owner of any Outstanding Bond, as shown on the registration books required to be maintained by the Trustee pursuant to the Indenture.

Parity Installment Payments

The term "Parity Installment Payments" means Installment Payments that are Parity Obligations scheduled to be paid by the City under and pursuant to any Supplement that has been assigned to the Trustee (as assignee of the Authority) to secure such Parity Obligations.

Participants

The term "Participants" means those broker-dealers, banks, and other financial institutions from time to time for which the Depository holds Book-Entry Bonds as securities depository.

Payment Fund

The term "Payment Fund" means the fund by that name established under the Indenture.

Permitted Investments

The term "Permitted Investments" means any of the following to the extent then permitted by law and the Indenture:

1. Federal Securities;

2. Obligations of any state, territory, or commonwealth of the United States of America or any political subdivision thereof or any agency or department of the foregoing; provided that at the time of their purchase such obligations are rated "AAA" by two Rating Agencies;

3. Bonds, notes, debentures, or other evidences of indebtedness issued or guaranteed by any corporation which are, at the time of purchase, rated by each Rating Agency in their respective highest short-term rating categories or, if the term of such indebtedness is longer than three years, rated "AAA" by two Rating Agencies;

4. Taxable commercial paper or tax-exempt commercial paper with a maturity of not more than 270 days, rated "A1/P1/F1" by two Rating Agencies;

5. Deposit accounts or certificates of deposit, whether negotiable or non-negotiable, issued by a state or national bank (including the Trustee) or a state or federal savings and loan association or a state-licensed branch of a foreign bank; provided, however, that such certificates of deposit or deposit accounts shall be either (a) continuously and fully insured by the Federal Deposit Insurance Corporation; or (b) have maturities of not more than 365 days (including certificates of deposit) and are issued by any state or national bank or a state or federal savings and loan association, the short-term obligations of which are rated in the highest short term letter and numerical rating category by two Rating Agencies;

6. Bills of exchange or time drafts drawn on and accepted by a commercial bank, otherwise known as bankers acceptances, which bank has short-term obligations outstanding which are rated by two

Rating Agencies in their respective highest short-term rating categories, and which bankers acceptances mature not later than 180 days from the date of purchase;

7. Any repurchase agreement with any bank or trust company organized under the laws of any state of the United States or any national banking association (including the Trustee), or a state-licensed branch of a foreign bank, having a minimum permanent capital of one hundred million dollars ($100,000,000) and with short-term debt rated by two Rating Agencies in their respective three highest short-term rating categories or any government bond dealer reporting to, trading with, and recognized as a primary dealer by, the Federal Reserve Bank of New York, which agreement is secured by any one or more of the securities and obligations described in clause (1) of this definition, which shall have a market value (valued at least weekly) not less than 102% of the principal amount of such investment and shall be lodged with the Trustee, the Treasurer, or other fiduciary, as custodian for the Trustee, by the bank, trust company, national banking association, or bond dealer executing such repurchase agreement. The entity executing each such repurchase agreement required to be so secured shall furnish the Trustee with an undertaking satisfactory to it that the aggregate market value of all such obligations securing each such repurchase agreement (as valued at least weekly) will be an amount equal to 102% the principal amount of such repurchase agreement and the Trustee shall be entitled to rely on each such undertaking;

8. Any cash sweep or similar account arrangement of or available to the Trustee, the investments of which are limited to investments described in clauses (1), (2) and (7) of this definition and any money market fund, the entire investments of which are limited to investments described in clauses (1), (2) and (7) of this definition and which money market fund is rated in their respective highest rating categories by two Rating Agencies;

9. Any guaranteed investment contract, including forward delivery agreements ("FDAs") and forward purchase agreements ("FPAs"), with a financial institution or insurance company which has at the date of execution thereof an outstanding issue of unsecured, uninsured and unguaranteed debt obligations or a claims-paying ability rated within the two highest rating categories of two or more Rating Agencies. Only Permitted Investments described in clause (1) above and having maturities equal to or less than 30 years from their date of delivery will be considered eligible for any collateralization/delivery purposes for guaranteed investment contracts, FDAs or FPAs;

10. Certificates, notes, warrants, bonds, or other evidence of indebtedness of the State or of any political subdivision or public agency thereof which are rated in the highest short-term rating category or within one of the three highest long-term rating categories of two Rating Agencies (excluding securities that do not have a fixed par value and/or whose terms do not promise a fixed dollar amount at maturity or call date);

11. For amounts less than $10,000, interest-bearing demand or time deposits (including certificates of deposit) in a nationally or state-chartered bank, or a state or federal savings and loan association in the State, fully insured by the Federal Deposit Insurance Corporation, including the Trustee or any affiliate thereof;

12. Investments in taxable money market funds or portfolios restricted to obligations with an average maturity of one year or less and which funds or portfolios are rated in either of the two highest rating categories by two Rating Agencies or have or are portfolios guaranteed as to payment of principal and interest by the full faith and credit of the United States of America;

13. Investments in the City's pooled investment fund;

14. Investments in the Local Agency Investment Fund created pursuant to Section 16429.1 of the Government Code of the State;

15. Shares of beneficial interest in diversified management companies investing exclusively in securities and obligations described in clauses (1) through (12) of this definition and which companies are rated in their respective highest rating categories by two Rating Agencies or have an investment advisor registered with the Securities and Exchange Commission with not less than five years' experience investing in such securities and obligations and with assets under management in excess of five hundred million dollars ($500,000,000); and

16. Shares in a California common law trust established pursuant to Title 1, Division 7, Chapter 5 of the Government Code of the State, which consists exclusively of investments permitted by Section 53601 of Title 5, Division 2, Chapter 4 of the Government Code of the State, as it may be amended.

Person

The term "Person" means any legal entity or natural person, as the context may require.

Pre-Refunded Municipals

The term "Pre-Refunded Municipals" means any bonds or other obligations of any state of the United States of America or of any agency, instrumentality, or local governmental unit of any such state which are not callable at the option of the obligor prior to maturity or as to which irrevocable instructions have been given by the obligor to call on the date specified in the notice.

Principal Account

The term "Principal Account" means the account of that name established under the Indenture.

Principal Payment Date

The term "Principal Payment Date" means, (i) with respect to the 2009A Bonds, each August 1, commencing August 1, 2009, through and including August 1, 2038, (ii) with respect to the 2009B Bonds, each August 1, commencing August 1, 2010, through and including August 1, 2039, and (iii) with respect to the 2010A Bonds, each August 1, commencing August 1, 2022, through and including August 1, 2028.

Project

The term "Project" means the acquisition, construction, installation, and improvements to the Water System described in Exhibit A to the Installment Purchase Agreement and as modified with respect to Components in conformance with the Installment Purchase Agreement.

Project Costs

The term "Project Costs" means the costs of the Project disbursed from time to time by the Comptroller from the Acquisition Fund pursuant to the Indenture.

Purchase Price

The term "Purchase Price" means the principal amount plus interest thereon owed by the City under the terms of the Installment Purchase Agreement as provided in the Indenture thereof and as specified in a Supplement.

Rating Agency

The term "Rating Agency" means Fitch, Moody's, or S&P.

Rebate Fund

The term "Rebate Fund" means the fund by that name created under the Indenture and any other accounts thereunder.

Record Date

The term "Record Date" means the fifteenth day of the calendar month immediately preceding an Interest Payment Date, whether or not such day is a Business Day.

Redemption Account

The term "Redemption Account" means the account by that name established under the Indenture.

Refunded Components

The term "Refunded Components" means, with respect to the 2010A Bonds, the Components originally financed with the proceeds of the Refunded 1998 Certificates that are being refunded with the proceeds of sale of the 2010A Bonds.

Refunded 1998 Certificates

The term "Refunded 1998 Certificates" means those maturities of the 1998 Certificates being prepaid with a portion of the proceeds of the 2010A Bonds.

Requisition

The term "Requisition" means a requisition form, by which the City shall withdraw moneys from the Acquisition Fund or the Costs of Issuance Account.

Reserve Fund

The term "Reserve Fund" means the fund by that name established under the Indenture, in which the Reserve Requirement shall be held and invested.

Reserve Requirement

The term "Reserve Requirement" means, as of any date of calculation, the least of (i) ten percent (10%) of the proceeds (within the meaning of section 148 of the Code) of the Bonds; (ii) 125% of average annual debt service on the then-Outstanding Bonds; or (iii) the Maximum Annual Debt Service for that and any subsequent year. Upon early redemption of any of the Bonds, the Authority, at the request of the City, may request the Trustee to recalculate and reduce any Reserve Requirement, whereupon any excess in the Reserve Fund over and above such Reserve Requirement shall be transferred to the Payment Fund.

Revenues

The term "Revenues" means all Installment Payments received by or due to be paid to the Corporation pursuant to all Supplements executed and delivered by the City and the Corporation to secure the payment of principal of and interest on Bonds issued under the Indenture and the interest or profits from the investment of money in any account or fund (other than the Rebate Fund) pursuant to the Indenture.

S&P

The term "S&P" means Standard & Poor's Ratings Group, a division of The McGraw-Hill Companies, Inc., a corporation organized and existing under the laws of the State of New York, and its successors, and if such corporation shall for any reason no longer perform the functions of a securities rating agency, "S&P" shall be deemed to refer to any other nationally recognized securities rating agency designated by the Authority and the City.

Second Supplement

The term "Second Supplement" means the Second Supplemental Indenture, dated as of June 1, 2010, by and the Authority and the Trustee.

Securities Depository

The term "Securities Depository" means The Depository Trust Company, 55 Water Street, 50th Floor, New York, N.Y. 10041-0099 Attn. Call Notification Department, Fax (212) 855-7232, or, in accordance with then-current guidelines of the Securities and Exchange Commission, such other securities depositories, or no such depositories, as the Authority may indicate in a Written Request of the Authority delivered to the Trustee.

State

The term "State" means the State of California.

Subordinated Installment Payments

The term "Subordinated Installment Payments" means Installment Payments that are Subordinated Obligations (as defined in the Installment Purchase Agreement) scheduled to be paid by the City under and pursuant to any Supplement that has been assigned to the Trustee (as assignee of the Authority) to secure any Subordinated Bonds or Notes.

Supplement

The term "Supplement" means a supplement to the Installment Purchase Agreement providing for the payment of specific Installment Payments as the Purchase Price for Components of the Project, executed and delivered by the City and the Corporation.

Supplemental Indenture

The term "Supplemental Indenture" means any indenture supplemental to or amendatory of the Indenture duly executed and delivered by the Authority and the Trustee as authorized under the Indenture.

Surety Bond

The term "Surety Bond" means a reserve surety bond, insurance policy, letter of credit, or other similar instrument rated "Aa3" or "AA-" or better by at least two Rating Agencies at the time of purchase or issuance and providing, by its terms, a stated amount as a credit towards or in satisfaction of all or part of the Reserve Requirement, which Surety Bond shall be held by the Trustee in trust pursuant to the Indenture. A Surety Bond shall constitute and qualify as a "Reserve Fund Credit Facility," as such term is defined in the Installment Purchase Agreement.

Tax Certificate

The term "Tax Certificate" means the Tax Exemption Certificate delivered with respect to Tax-Exempt Bonds on their Closing Date.

Tax-Exempt Bonds

The term "Tax-Exempt Bonds" means those Bonds that, by their terms, bear interest that is excluded from gross income for federal income tax purposes, pursuant to the Code.

Treasurer

The term "Treasurer" means the Office of the City Treasurer of the City of San Diego.

Trustee

The term "Trustee" means Wells Fargo Bank, National Association, a national banking association existing under and by virtue of the laws of the United States, or any other bank or trust company that may at any time be substituted in its place as provided in the Indenture.

Underwriters

The term "Underwriters" means, with respect to the 2010A Bonds, collectively, Morgan Stanley & Co. Incorporated, E. J. De La Rosa & Co., Inc., and RBC Capital Markets Corporation.

Water System

The term "Water System" means any and all facilities, properties, improvements, and works at any time owned, controlled, or operated by the City as part of the public utility system of the City for water purposes, for the development, obtaining, conservation, production, storage, treatment, transmission, furnishing, and distribution of water and its other commodities or byproducts for public and private use (whether located within or outside the City), and any related or incidental operations designated by the City as part of the Water System, including reclaimed and re-purified water.

Written Request of the Authority

The term "Written Request of the Authority" means an instrument in writing signed by the Chair, the Vice Chair, or the Secretary of the Authority, or by any other officer or Commissioner of the Board duly authorized by the Authority for that purpose.

Written Request of the City

The term "Written Request of the City" means an instrument in writing signed by the Chief Operating Officer, the Chief Financial Officer or any of their respective designees, or by any other official of the applicable administrative departments of the City duly authorized by the City for that purpose.

2009A Bonds

The term "2009A Bonds" means the Public Facilities Financing Authority of the City of San Diego Water Revenue Bonds, Series 2009A (Payable Solely From Installment Payments Secured by Net System Revenues of the Water Utility Fund) issued in the aggregate principal amount of $157,190,000.

2009A Installment Payments

The term "2009A Installment Payments" means those Installment Payments scheduled to be paid by the City under the 2009A Supplement.

2009A Supplement

The term "2009A Supplement" means the 2009A Supplement to the Installment Purchase Agreement, by and between the City and the Corporation, dated as of January 1, 2009.

2009B Bonds

The term "2009B Bonds" means the Public Facilities Financing Authority of the City of San Diego Water Revenue Bonds, Series 2010A (Payable Solely From Installment Payments Secured by Net System Revenues of the Water Utility Fund) issued in the aggregate principal amount of $328,060,000.

<u>2010A Bonds</u>

The term "2010A Bonds" means the Public Facilities Financing Authority of the City of San Diego Water Revenue Bonds, Refunding Series 2010A (Payable Solely from Installment Payments Secured by Net System Revenues of the Water Utility Fund), issued under the Indenture in the original aggregate principal amount of $123,075,000.

<u>2010A Closing Date</u>

The term "2010A Closing Date" means June 30, 2010, the date of initial delivery of the 2010A Bonds.

<u>2010A Installment Payments</u>

The term "2010A Installment Payments" means those Installment Payments scheduled to be paid by the City under the 2010A Supplement.

<u>2010A Reserve Account</u>

The term "2010A Reserve Account" means the account established within the Reserve Fund in which the 2010A Reserve Requirement shall be held and invested.

<u>2010A Reserve Requirement</u>

The term "2010A Reserve Requirement" means, initially, the amount of $10,034,005.46.

<u>2010A Supplement</u>

The term "2010A Supplement" means the 2010A Supplement to Amended and Restated Master Installment Purchase Agreement, dated as of June 1, 2010, by and between the City and the Corporation.

Establishment of Funds; Deposit and Application

Establishment of Funds and Accounts.

(a) Pursuant to the Second Supplement, the Trustee shall establish the Costs of Issuance Account for the 2010A Bonds.

(b) Pursuant to the Original Indenture, the Trustee has established the Payment Fund, including the Interest Account, the Principal Account, and the Redemption Account.

(c) Pursuant to the Original Indenture, the Trustee has established the Reserve Fund, and, within the Reserve Fund, pursuant to the Second Supplement, the Trustee shall establish the 2010A Reserve Account, in order to facilitate compliance by the City with the Tax Certificate and the Installment Purchase Agreement. On the 2010A Closing Date, the Trustee shall deposit the 2010A Reserve Requirement into the 2010A Reserve Account.

Use of Moneys in Costs of Issuance Account for the 2010A Bonds. The Trustee shall disburse moneys from the Costs of Issuance Account for the 2010A Bonds to pay Costs of Issuance with respect to the 2010A Bonds. Such disbursements shall be made from time to time upon receipt of Requisitions of the City on behalf of the Authority substantially in the form attached as Exhibit B to the Second Supplemental Indenture. On the day that is the 181st day following the 2010A Closing Date, the Trustee shall transfer any then-remaining but uncommitted amount on deposit in the Costs of Issuance Account for the 2010A Bonds to the Interest Account within the Payment Fund, to be applied as a credit towards the next interest payment on the 2010A Bonds.

Reserve Fund.

(a) The Reserve Fund is a separate fund held in trust by the Trustee. On the 1010A Closing Date, the Trustee shall receive for deposit an amount equal to the 2010A Reserve Requirement. An amount equal to the Reserve Requirement shall be maintained in or credited to the Reserve Fund at all times, subject to the provisions of the Indenture, and any deficiency therein shall be replenished from the first available Revenues pursuant to the Indenture.

(b) Moneys in or available from the Reserve Fund shall be used solely for the purpose of paying the principal of and interest on the Bonds, including the redemption price of the Bonds coming due and payable by operation of mandatory sinking fund redemption pursuant to the Indenture, in the event that the moneys in the Payment Fund are insufficient therefor. If and during such time as a Surety Bond is in effect, not less than two Business Days prior to each Interest Payment Date, the Trustee shall ascertain the necessity for a draw upon the Surety Bond and, if a draw is necessary, shall provide notice thereof to the provider of the Surety Bond in accordance with the terms of the Surety Bond at least two Business Days prior to each Interest Payment Date. In the event that the amount on deposit in the Payment Fund on any date is insufficient to enable the Trustee to pay in full the aggregate amount of principal of and interest on the Bonds coming due and payable, including the redemption price of the Bonds coming due and payable by operation of mandatory sinking fund redemption pursuant to the Indenture, the Trustee shall withdraw the amount of such insufficiency from the Reserve Fund or make a draw upon the Surety Bond in the amount of such insufficiency and transfer such amount to the Payment Fund.

(c) In the event that the amount on deposit in the Reserve Fund exceeds the Reserve Requirement on the fifteenth (15th) calendar day of the month preceding any Interest Payment Date, the amount of such excess shall be withdrawn therefrom by the Trustee and transferred to (a) the Rebate Fund, to the extent required under the Indenture, or (b) the Payment Fund.

(d) The Authority may replace all or a portion of the Reserve Requirement, if originally funded with cash, with one or more Surety Bonds. Upon deposit of any Surety Bond with the Trustee, the Trustee shall transfer to the Acquisition Fund from amounts in the Reserve Fund an amount equal to the principal of the Surety Bond, which principal shall comprise the Reserve Requirement under the Indenture, or make other transfers in accordance with a Written Direction of the City.

In any case where the Reserve Fund is funded with a combination of cash and a Surety Bond, the Trustee shall deplete all cash balances before drawing on the Surety Bond. With regard to replenishment, any available moneys provided by the City shall be used first to reinstate the Surety Bond and second, to replenish the cash in the Reserve Fund in accordance with subsection (e) of this section in the Indenture. In the event the Surety Bond is drawn upon, the City shall make payment of interest on amounts advanced under the Surety Bond after making any payments pursuant to the Indenture.

In the event the Surety Bond is scheduled to lapse or expire, the Trustee shall draw upon such Surety Bond prior to its lapsing or expiring in the full amount of such Surety Bond, make deposits from available Revenues to the Reserve Fund to increase the amount on deposit therein to the Reserve Requirement or substitute such Surety Bond with a Surety Bond that satisfies the requirements of the Indenture.

The Authority acknowledges that the rating on any Surety Bond obtained or provided under the Indenture may change after the date such Surety Bond is purchased or issued. Within twelve (12) months after the date that the Authority obtains actual knowledge that any Surety Bond is no longer rated at least "Aa3" or "AA-" by any Rating Agency, the Authority shall either (i) deposit into the Reserve Fund money in an amount equal to the stated or principal amount of such Surety Bond or (ii) obtain a substitute Surety Bond that satisfies the provisions of the Indenture.

(e) In the event that the amount on deposit in the Reserve Fund at any time falls below the Reserve Requirement or in the event of a draw on the Surety Bond deposited therein, the Trustee shall promptly notify the City and the Authority of such fact and the Trustee shall promptly (A)(i) withdraw the amount of such insufficiency from available Revenues on deposit in the Payment Fund, and (ii) transfer such amount to the Reserve Fund or (B)(i) withdraw an amount necessary to repay such drawing on the Surety Bond and related expenses. Repayment of draws, expenses and accrued interest (collectively, "Policy Costs") shall commence in the first month following each draw, and each such monthly payment shall be in an amount at least equal to 1/12 of the aggregate of Policy Costs related to such draw. No deposit need be made in the Reserve Fund so long as the balance therein, taken together with amounts available under any Surety Bond, at least equals the Reserve Requirement. Upon receipt of written notice from the Trustee of a shortfall in the Reserve Fund, the City shall promptly transfer to the Trustee from Net System Revenues an amount sufficient to restore the balance on deposit in or credited to the Reserve Fund to the Reserve Requirement and to repay any amounts then due to the provider of the Surety Bond, if any.

Revenues

Pledge of Revenues.

(a) All Revenues and amounts on deposit in the funds and accounts established under the Indenture (other than amounts on deposit in the Rebate Fund created pursuant to the Indenture) are irrevocably pledged to the payment of the interest on and principal of the Bonds but only as provided in the Indenture, and the Revenues shall not be used for any other purpose while any of the Bonds remain Outstanding; provided, that out of the Revenues there may be allocated such sums for such purposes as are expressly permitted by the Indenture.

(b) To secure the pledge of the Revenues contained in this subheading, the Authority transfers, conveys and assigns to the Trustee, for the benefit of the Owners, all of the Authority's rights under the 2009A Supplement and, in connection with any Additional Bonds issued under the Indenture, the Authority's rights under the Supplement(s) executed by the City and the Corporation to secure payment of principal of and interest on such Additional Bonds, including the right to receive Installment Payments from the City, the right to receive any proceeds of insurance maintained thereunder or any condemnation award rendered with respect to the Refunded Components and the right to exercise any remedies provided therein in the event of a default by the City thereunder. The Trustee accepts said assignment for the benefit of the Owners subject to the provisions of the Indenture.

(c) The Trustee shall be entitled to and shall receive all of the 2009A Installment Payments and, in connection with any Additional Bonds issued under the Indenture, the Installment Payments made by the City pursuant to the Supplement(s) executed by the City and the Corporation to secure payment of principal of and interest on such Additional Bonds, and any 2009A Installment Payments and additional Installment Payments collected or received by the Authority shall be deemed to be held, and to have been collected or received, by the Authority as agent of the Trustee and shall forthwith be paid by the Authority to the Trustee.

Receipt and Deposit of Revenues in the Payment Fund. To carry out and effectuate the pledge contained in the Indenture, the Authority agrees and covenants that all Revenues when and as received shall be received in trust under the Indenture for the benefit of the Owners and shall be deposited when and as received in the Payment Fund. All Revenues shall be accounted for through and held in trust in the Payment Fund, and the Authority shall have no beneficial right or interest in any of the Revenues except only as provided in the Indenture. All Revenues, whether received by the Authority in trust or deposited with the Trustee as provided in the Indenture, shall nevertheless be allocated, applied and disbursed solely to the purposes and uses set forth in the Indenture, and shall be accounted for separately and apart from all other accounts, funds, money, or other assets of the Authority.

Maintenance of Accounts for Use of Money in the Payment Fund.

(a) All money in the Payment Fund shall be deposited by the Trustee in the following respective special accounts within the Payment Fund in the following order of priority:

(i) Interest Account,

(ii) Principal Account, and

(iii) Redemption Account.

All money in each of such Accounts shall be held in trust by the Trustee and shall be applied, used and withdrawn only for the purposes authorized in the Indenture.

(b) On or before each Interest Payment Date, the Trustee shall transfer from the Payment Fund and deposit in the Interest Account that amount of money that, together with any money contained in the Interest Account, equals the aggregate amount of interest becoming due and payable on all Outstanding Bonds on such Interest Payment Date. No deposit need be made in the Interest Account if the amount contained in the Interest Account equals at least the aggregate amount of interest becoming due and payable on all Outstanding Bonds on such Interest Payment Date. All money in the Interest Account shall be used and withdrawn by the Trustee solely for the purpose of paying the interest on the Bonds as it shall become due and payable (including accrued interest on any Bonds redeemed prior to maturity).

(c) On or before each Principal Payment Date, the Trustee shall transfer from the Payment Fund and deposit in the Principal Account that amount of money that, together with any money contained in the Principal Account, equals the aggregate principal becoming due and payable on all Outstanding Bonds. No deposit need be made in the Principal Account if the amount contained therein is at least equal to the aggregate amount of principal become due and payable on all Outstanding Bonds. All money in the Principal Account shall be used and withdrawn by the Trustee solely for the purpose of paying the principal of the Bonds as it shall become due and payable.

(d) All money in the Redemption Account shall be held in trust by the Trustee and shall be applied, used, and withdrawn either to redeem the Bonds pursuant to the Indenture. Any moneys that, pursuant to the Installment Purchase Agreement and the related provisions of any Supplements, are to be used to redeem Bonds shall be deposited by the Trustee in the Redemption Account. The Trustee shall, on the scheduled redemption date, withdraw from the Redemption Account and pay to the Owners entitled thereto an amount equal to the redemption price of the Bonds to be redeemed on such date.

(e) Any delinquent Installment Payments pledged to the Bonds shall be applied first to the Interest Account for the immediate payment of interest payments past due and then to the Principal Account for immediate payment of principal payments past due on any Bond. Any remaining money representing delinquent Installment Payments pledged to Bonds shall be deposited in the Payment Fund to be applied in the manner provided therein.

Investment of Moneys in Funds and Accounts. Moneys in the Acquisition Fund shall be accounted for by the Comptroller and invested by the Treasurer in any legally permitted investment, including but not limited to the pooled investment fund of the City. In the absence of a Written Request of the City, the Trustee may invest moneys in the funds and accounts held by the Trustee in Permitted

Investments described in clause (8) of the definition thereof. The obligations in which moneys in the said funds and accounts are invested shall mature prior to the date on which such moneys are estimated to be required to be paid out under the Indenture. For purposes of determining the amount of deposit in any fund or account, all investments credited to such fund or account shall be valued at the lesser of market value or the cost thereof. The Trustee shall semiannually, on or before January 15 and July 15 of each year, and at such times as the Authority shall deem appropriate, value the investments in the funds and accounts under the Indenture on the basis of the lesser of market value or the cost thereof. Except as otherwise provided in the Indenture, Permitted Investments representing an investment of moneys attributable to any fund or account under the Indenture and all investment profits or losses thereon shall be deemed at all times to be a part of said fund or account.

Additional Bonds

Execution and Delivery of Additional Bonds. In addition to the 2009A Bonds, the Trustee shall, upon Written Request of the Authority, by a supplement to the Indenture, establish one or more other series of Bonds secured by the pledge made under the Indenture equally and ratably with any Bonds previously issued and delivered, in such principal amount as shall be determined by the Authority, but only upon compliance with the provisions of the Indenture, the requirements of the Installment Purchase Agreement applicable to the incurrence of Parity or Subordinated Obligations, as applicable, and any additional requirements set forth in the applicable Supplemental Indenture, which are made conditions precedent to the execution and delivery of Additional Bonds:

(a) No Event of Default shall have occurred and be then continuing;

(b) The Supplemental Indenture providing for the execution and delivery of such Additional Bonds shall specify the purposes for which such Additional Bonds are then proposed to be delivered, which shall be one or more of the following: (i) to provide moneys needed to provide for Project Costs by depositing into the Acquisition Fund the proceeds of such Additional Bonds to be so applied; (ii) to provide for the payment or redemption of Bonds then Outstanding under the Indenture, by depositing with the Trustee moneys and/or investments required for such purpose under the defeasance provisions set forth in the Indenture; or (iii) to provide moneys needed to refund or refinance all or part of any other current or future obligations of the City with respect to the funding of the Water System. Such Supplemental Indenture may, but shall not be required to, provide for the payment of expenses incidental to such purposes, including the Costs of Issuance of such Additional Bonds, capitalized interest with respect thereto for any period authorized under the Code (in the case of Tax-Exempt Bonds) and, in the case of any Additional Bonds intended to provide for the payment or redemption of existing Bonds, or other Obligations of the City, expenses incident to calling, redeeming, paying, or otherwise discharging the Obligations to be paid with the proceeds of the Additional Bonds;

(c) The Authority shall deliver or cause to be delivered to the Trustee, from the proceeds of such Additional Bonds or from any other lawfully available source of moneys, an amount (or a Surety Bond in an amount) sufficient to increase the balance in the Reserve Fund to the Reserve Fund Requirement for all Bonds and Additional Bonds to be then Outstanding;

(d) The Additional Bonds shall be payable as to principal on August 1 and as to interest on February 1 and August 1 of each year during their term, except that the first interest payment due with respect thereto may be for a period of not longer than twelve (12) months;

(e) Fixed serial maturities or mandatory sinking account payments, or any combination thereof, shall be established in amounts sufficient to provide for the retirement of all of the Additional Bonds of such Series on or before their respective maturity dates;

(f) The aggregate principal amount of Bonds and Additional Bonds executed and delivered under the Indenture shall not exceed any limitation imposed by law or by any Supplemental Indenture; and

(g) The Trustee shall be the Trustee for the Additional Bonds.

Nothing in the Indenture shall limit in any way the power and authority of the Authority to incur other obligations payable from other lawful sources.

Proceedings for Execution and Delivery of Additional Bonds. Whenever the Authority shall determine to file its Written Request with the Trustee for the execution and delivery of Additional Bonds, the Authority shall authorize the execution and delivery of a Supplemental Indenture, specifying the aggregate principal amount and describing the forms of Bonds and providing the terms, conditions, distinctive designation, denominations, date, maturity date or dates, interest rate or rates (or the manner of determining same), Interest Payments and payment dates, redemption provisions and place or places of payment of principal or redemption price, if any, and interest represented by such Additional Bonds not inconsistent with the terms of the Indenture.

Before any series of Additional Bonds may be executed and delivered by the Trustee, the Authority shall file the following documents with the Trustee:

(a) An executed copy of the applicable Supplemental Indenture;

(b) A statement of the Authority to the effect that the requirements of the Indenture have been met;

(c) In the case of a Series of Additional Bonds delivered for the purpose described in the Indenture, irrevocable instructions to the Trustee to give notice as provided in the Indenture of redemption of all Bonds to be redeemed in connection therewith; and

(d) An opinion or opinions of Bond Counsel, to the effect that the execution and delivery of the Additional Bonds, the supplement to the Indenture and related supplements or amendments have been duly authorized by the Authority and meet the requirements of the Indenture; and that the execution and delivery of such Additional Bonds will not, in and of themselves, cause the interest on the Tax-Exempt Bonds to become included within the gross income for purposes of federal income taxation.

Covenants of Authority

Punctual Payment and Performance. The Authority shall punctually pay the interest and the principal to become due on every Bond issued under the Indenture in strict conformity with the terms of the Indenture and of the Bonds, and shall faithfully observe and perform all the agreements and covenants contained therein.

Rebate Fund.

(a) The Trustee shall maintain such accounts within the Rebate Fund as it is instructed by the Authority as shall be necessary in order to comply with the applicable Tax Certificate (which is incorporated in the Indenture by reference). The Trustee shall deposit moneys in the Rebate Fund made available by the Authority and/or the City pursuant to a Written Request of the City. All money at any time deposited in the Rebate Fund shall be governed by the Indenture and the Tax Certificate and shall be held by the Trustee in trust, to the extent required to satisfy the amount required to be rebated to the United States under the Code, and none of the City, the Corporation, Authority, the Trustee, or the Owners shall have any rights in or claims to such money. The Trustee shall make information regarding the investments under the Indenture available to the City, shall invest the Rebate Fund in Permitted Investments pursuant to a Written Request of the City that is in conformity with the restrictions set forth in the Tax Certificate and shall deposit income from such Permitted Investments immediately upon receipt thereof into the Rebate Fund. The Trustee agrees to comply with all Written Requests of the City given in accordance with the Tax Certificate.

(b) The City and the Authority shall make or cause to be made the rebate computations respecting all Outstanding Bonds in accordance with the Tax Certificate, as required by the Code, and shall provide to the Trustee written evidence that the computation of the rebate requirement has been made along with a letter from an independent certified public accountant or arbitrage consultant verifying the accuracy of such calculations. Upon a Written Request of the City, the Trustee shall make deposits into the Rebate Fund from deposits by the City so that the balance of the amount on deposit shall be equal to the rebate requirement. The Trustee shall have no obligation to rebate any amounts required to be rebated pursuant to the Indenture, other than from moneys held in the Rebate Fund or from other moneys provided to it by the City on behalf of itself or the Authority.

(c) Not later than sixty (60) days after the end of the fifth Bond Year as defined in the Tax Certificate and every five (5) years thereafter, the Trustee, upon receipt of a Written Request of the City, shall pay to the United States part or all of the amounts in the Rebate Fund, as so directed. Each payment shall be accompanied by a statement summarizing the determination of the amount to be paid to the United States, as provided by the City. In addition, if the City so directs, then the Trustee shall deposit moneys into or transfer moneys out of the Rebate Fund from or into such accounts or funds as directed by the Written Request of the City. Any amounts remaining in the Rebate Fund following the final payment of the rebate requirement shall be paid to the City. Money, including investment earnings, shall not be transferred from the Rebate Fund except as provided in the Indenture.

(d) Notwithstanding any other provision the Indenture, the obligation to remit the rebate requirement to the United States and to comply with all other requirements of the Indenture and the Tax Certificate shall survive the defeasance or payment in full of the Tax-Exempt Bonds.

(e) The Authority shall not use or permit any proceeds of the Tax-Exempt Bonds or any funds of the Authority, directly or indirectly, to acquire any securities or obligations, and shall not take or permit to be taken any other action or actions, that would cause any Tax-Exempt Bonds to be an "arbitrage bond" within the meaning of the Code or "federally guaranteed" within the meaning of Section 149(b) of the Code and any applicable regulations promulgated from time to time thereunder and under Section 103(c) of the Code. The Authority shall observe and not violate the requirements of Section 148 of the Code and any such applicable regulations. The Authority shall comply with all requirements of Sections 148 and 149(b) of the Code to the extent applicable to the Tax-Exempt Bonds.

(f) The Authority specifically covenants to comply with the provisions and procedures of the Tax Certificate.

(g) The Authority shall not use or permit the use of any proceeds of the Bonds or any funds of the Authority, directly or indirectly, in any manner, and shall not take or omit to take any action that would cause any Tax-Exempt Bonds to be treated as an obligation not described in Section 103(a) of the Code.

(h) Notwithstanding any provisions of the Indenture, if the Authority and the City shall provide to the Trustee an opinion of Bond Counsel to the effect that any specified action required under the Indenture is no longer required or that some further or different action is required to maintain the exclusion from gross income for federal income tax purposes of interest with respect to the Tax-Exempt Bonds, the Trustee, the Authority and the City may conclusively rely on such opinion in complying with the requirements of the Indenture and the covenants under the Indenture shall be deemed to be modified to that extent.

Accounting Records and Reports. The Authority shall keep or cause to be kept proper books of record and accounts in which complete and correct entries shall be made of all transactions relating to the receipts, disbursements, allocation and application of the Revenues, and such books shall be available for inspection by the Trustee, at reasonable hours and under reasonable conditions. Not more than 270 days after the close of each Fiscal Year, the Authority shall furnish or cause to be furnished to the Trustee financial statements that include the Water Utility Fund for the preceding Fiscal Year, prepared in accordance with generally accepted accounting principles, together with a report of an Independent Certified Public Accountant thereon. For purposes of the Indenture, "financial statement" shall mean audited financial statements, if available, or unaudited financial statements, if audited financial statements are not available and unaudited financial statements are available. The Authority shall also keep or cause to be kept such other information as is required under the Tax Certificate.

The City's Budgets. The Authority shall supply to the Trustee, as soon as practicable after the beginning of each Fiscal Year following the effectiveness of the applicable City ordinance but in no event later than six months from the date of effectiveness of such ordinance, a Certificate of the City certifying that the City has made adequate provision in its annual budget for such Fiscal Year for the payment of all Parity Installment Payments, Subordinated Installment Payments, and all other Obligations due under the Installment Purchase Agreement in such Fiscal Year. If the amounts so budgeted are not adequate for the payment of all Parity Installment Payments, Subordinated Installment Payments, and all other Obligations due under the Installment Purchase Agreement in such Fiscal Year, the Authority shall take such action as may be necessary and within its power to request such annual budget to be amended, corrected, or augmented by the City so as to include therein the amounts required to be paid by the City from Net System Revenues in such Fiscal Year, and shall notify the Trustee of the proceedings then taken or proposed to be by the Authority.

Continuing Disclosure. The City has undertaken all responsibility for compliance with continuing disclosure requirements, and accordingly the Authority shall have no liability to the Owners of the Bonds or any other person with respect to Securities and Exchange Commission Rule 15c2-12, and the City shall comply with and carry out all of the provisions of each continuing disclosure certificate, each dated the date of the execution and delivery of each Series of Bonds. See the caption in this Official Statement "CONTINUING DISCLOSURE." Notwithstanding any other provision the Indenture, failure of the City to comply with a Continuing Disclosure Certificate shall not be considered an Event of Default under the Indenture or under the Installment Purchase Agreement; provided, that the Trustee may and, at the request of any participating underwriter or the Owners of at least twenty-five percent (25%) in aggregate principal amount of the Outstanding Bonds of any series, shall, or any Owner or Beneficial Owner of any of the Bonds may, take such actions as may be necessary and appropriate, including seeking mandate or specific performance by court order, to cause the City to comply with its obligations under the related Continuing Disclosure Certificate.

Amendment of Indenture

Amendment of Indenture.

(a) The Indenture and the rights and obligations of the Authority and of the all Owners of the Bonds may be amended at any time by a Supplemental Indenture, which shall become binding when the written consents of the Owners of 51% in aggregate principal amount of the Bonds then Outstanding, exclusive of Bonds disqualified as provided in the Indenture, are filed with the Trustee. No such amendment shall (i) permit the creation by the Authority of any pledge of the Revenues as provided in the Indenture superior to or on a parity with the pledge created for the benefit of any Bond without the written consent of the Owner thereof; (ii) modify any rights or obligations of the Trustee without its prior written assent thereto; or (iii) modify provisions respecting the time or amount of payments on any Bond, without the written consent of the Owner thereof.

(b) The Indenture and the rights and obligations of the Authority and of the Owners may also be amended at any time by a Supplemental Indenture, which shall become binding without the consent of any Owners of Bonds for any one or more of the following purposes:

(i) to make such provisions for the purpose of curing any ambiguity or of correcting, curing or supplementing any defective provision contained in the Indenture in regard to questions arising under the Indenture that the Authority may deem desirable or necessary and not inconsistent herewith and that shall not adversely affect the interests of the Owners; or

(ii) to make any other change or addition thereto that shall not materially adversely affect the interests of the Owners, or to surrender any right or power reserved in the Indenture to or conferred in the Indenture on the Authority; provided, however, that the Owners shall be given prompt notice of any such amendment and shall receive a copy of the final executed Supplemental Indenture making such changes.

Disqualified Bonds. Bonds owned or held by or for the account of the Authority or the City shall not be deemed Outstanding for the purpose of any consent or other action or any calculation of Outstanding Bonds provided in the Indenture, and shall not be entitled to consent to or take any other action provided therein.

Endorsement or Replacement of Bonds After Amendment. After the effective date of any action taken as described above, the Authority may determine that the Bonds may bear a notation by endorsement in form approved by the Authority as to such action, and in that case upon demand of the Owner of any Outstanding Bond and presentation of its Bond for such purpose at the Corporate Trust Office of the Trustee, a suitable notation as to such action shall be made on such Bond. If the Authority shall determine that a Bond shall bear such a notation by endorsement pursuant to the Indenture, a new Bond so modified shall be prepared and executed, and upon demand of the Owner of any Outstanding Bond, such new Bond shall be exchanged at the Corporate Trust Office of the Trustee without cost to such Owner upon surrender of such Bond.

Amendment by Mutual Consent. The provisions of the Indenture shall not prevent any Owner from accepting any amendment as to the particular Bonds owned by him, provided that due notation thereof is made on such Bonds.

Events of Default and Remedies of Holders

Events of Default and Acceleration of Maturities.

(a) The following events shall constitute events of default under the Indenture:

(i) failure in the due and punctual payment of the interest on the Bonds when and as the same shall become due and payable;

(ii) failure in the due and punctual payment of the principal of the Bonds when and as the same shall become due and payable, whether at maturity as therein expressed or by proceedings for redemption;

(iii) failure by the Authority in the performance of any of the other agreements or covenants required in the Indenture to be performed by the Authority, as set forth in the Indenture, and such default shall have continued for a period of 30 days after the Authority and the City shall have been given notice in writing of such default by the Trustee or to the Authority, the City and the Trustee by Owners of 25% or more of the aggregate principal amount of the Bonds then Outstanding; or

(iv) if any event of default shall have occurred and be continuing under Section 8.01 of the Installment Purchase Agreement; or

(v) if the Authority shall file a petition or answer seeking arrangement or reorganization under the federal bankruptcy laws or any other applicable law of the United States of America or any state therein, or if under the provisions of any other law for the relief or aid of debtors any court of competent jurisdiction shall assume custody or control of the Authority or of the whole or any substantial part of its property.

(b) If one or more Events of Default shall occur, then and in each and every such case during the continuance of such Event of Default, the Trustee may by notice in writing to the Authority and the City, declare the principal of all Bonds then Outstanding and the interest accrued thereon to be due and payable immediately. Upon any such declaration, the same shall become due and payable, anything contained in the Indenture or in the Bonds to the contrary notwithstanding. These provisions are subject to the condition that if at any time after the entire principal amount of the unpaid Bonds and the accrued interest thereon shall have been so declared due and payable and before any judgment or decree for the payment of the moneys due shall have been obtained or entered, there shall be deposited with the Trustee a sum sufficient to pay the unpaid principal amount of the Bonds due prior to such declaration and the accrued interest thereon, with interest on such overdue installments at the rate or rates applicable thereto in accordance with their terms, and the reasonable fees and expenses of the Trustee, and any and all other defaults known to the Trustee (other than in the payment the entire principal amount of the unpaid Bonds and the accrued interest thereon due and payable solely by reason of such declaration) shall have been made good or cured to the satisfaction of the Trustee or provision deemed by the Trustee to be adequate shall have been made therefor, then and in every such case the Trustee, by written notice to the City and the Authority, may rescind and annul such declaration and its consequences; but no such rescission and annulment shall extend to or shall affect any subsequent default or shall impair or exhaust any right or power consequent thereon.

Proceedings by Trustee. Upon the occurrence and continuance of any Event of Default, the Trustee in its discretion may, and at the written request of Owners of 51% or more in aggregate principal amount of Bonds Outstanding shall (but only to the extent indemnified to its satisfaction from fees and expenses, including attorneys' fees), do the following:

(a) by mandamus, or other suit, action, or proceeding at law or in equity, enforce all rights of the Owners and require the Authority to enforce all rights of the Owners of the Bonds, including the right to require the Authority to receive and collect Revenues and to enforce its rights under the Installment Purchase Agreement and to require the Authority to carry out any other covenant or agreement with Owners of Bonds and to perform its duties under the Indenture;

(b) bring suit upon the Bonds;

(c) by action or suit in equity enjoin any acts or things that may be unlawful or in violation of the rights of the Owners; and

(d) as a matter of right, have receivers appointed for the Revenues and the issues, earnings, income, products and profits thereof, pending such proceedings, with such powers as the court making such appointment shall confer.

Effect of Discontinuance or Abandonment. In case any proceeding taken by the Trustee on account of any default or Event of Default shall have been discontinued or abandoned for any reason, or shall have been determined adversely to the Trustee, then and in every such case, the Authority, the Trustee, and the Owners shall be restored to their former positions and rights under the Indenture, respectively, and all rights, remedies and powers of the Trustee shall continue as though no such proceeding had been taken.

Rights of Owners.

(a) Anything in the Indenture to the contrary notwithstanding and subject to the limitations and restrictions as to the rights of the Owners in the Indenture, upon the occurrence and continuance of any Event of Default or the Owners of 51% or more in aggregate principal amount of the Bonds then Outstanding shall have the right upon providing the Trustee security and indemnity reasonably satisfactory to it against the costs, expenses, and liabilities to be incurred therein or thereby, by an instrument in writing executed and delivered to the Trustee, to direct the method and place of conducting all remedial proceedings to be taken by the Trustee under the Indenture.

(b) The Trustee may refuse to follow any direction that conflicts with law or the Indenture or that the Trustee determines is prejudicial to rights of other Owners or would subject the Trustee to personal liability.

Restrictions on Owners' Actions.

(a) In addition to the other restrictions on the rights of Owners to request action upon the occurrence of an Event of Default and to enforce remedies set forth in the Indenture, no Owner of any of the Bonds shall have any right to institute any suit, action, or proceeding in equity or at law for the enforcement of any trust under the Indenture, or any other remedy under the Indenture or on said Bonds, unless:

(i) such Owner previously shall have given to the Trustee written notice of an Event of Default as provided in the Indenture; and

(ii) the Owners of 51% or more in aggregate principal amount of the Bonds then Outstanding shall have made written request of the Trustee to institute any such suit, action, proceeding, or other remedy, after the right to exercise such powers or rights of action, as the case may be, shall have accrued, and shall have afforded the Trustee a reasonable opportunity either to proceed to exercise the powers granted in the Indenture, or to institute such action, suit or proceeding in its or their name; and

(iii) there shall have been offered to the Trustee security and indemnity satisfactory to it against the costs, expenses, and liabilities to be incurred therein or thereby; and

(iv) the Trustee shall not have complied with such request within a reasonable time.

(b) Such notification, request and offer of indemnity are declared in every such case, at the option of the Trustee, to be conditions precedent to the execution of the trusts of the Indenture or for any other remedy under the Indenture. It is understood and intended, subject to the Indenture, that no one or more Owners of the Bonds shall have any right in any manner whatever by his or their action to affect, disturb or prejudice the security of the Indenture, or to enforce any right under the Indenture or under the Bonds, except in the manner therein provided, and that all proceedings at law or in equity shall be instituted, and maintained in the manner therein provided, and for the equal benefit of all Owners of Outstanding Bonds.

Power of Trustee to Enforce. All rights of action under the Indenture or under any of the Bonds secured by the Indenture that are enforceable by the Trustee may be enforced by it without the possession of any of the Bonds, or the production thereof at the trial or other proceedings relative thereto. Any such suit, action, or proceedings instituted by the Trustee shall be brought in its own name, as Trustee, for the equal and ratable benefit of the Owners of the Bonds, subject to the provisions of the Indenture.

Remedies Not Exclusive. No remedy in the Indenture conferred upon or reserved to the Trustee or to the Owners of the Bonds is intended to be exclusive of any other remedy or remedies, and each and every such remedy shall be cumulative, and shall be in addition to every other remedy given under the Indenture or now or hereafter existing at law or in equity or by statute.

Waiver of Events of Default; Effect of Waiver.

(a) The Trustee shall waive any Event of Default under the Indenture and its consequences and rescind any declaration of acceleration, upon the written request of the Owners of 67% or more of the Outstanding Bonds. If any Event of Default shall have been waived as provided in the Indenture, the Trustee shall promptly give written notice of such waiver to the Authority and shall give notice thereof by first class mail, postage prepaid to all Owners of Outstanding Bonds if such Owners had previously been given notices of such Event of Default. No such waiver, rescission and annulment shall extend to or affect any subsequent Event of Default, or impair any right or remedy consequent thereon.

(b) No delay or omission of the Trustee or any Owner of the Bonds to exercise any right or power accruing upon any default or Event of Default shall impair any such right or power or shall be construed to be a waiver of any such default or Event of Default or an acquiescence therein. Every power and remedy given by the Indenture to the Trustee or the Owners of the Bonds, respectively, may be exercised from time to time and as often as may be deemed expedient.

Application of Moneys.

(a) Any moneys received by the Trustee pursuant to the Indenture, together with any moneys that upon the occurrence of an Event of Default are held by the Trustee in any of the funds and accounts under the Indenture (other than the Rebate Fund and other than moneys held for Bonds not presented for payment) shall, after payment of all fees and expenses of the Trustee, and the fees and expenses of its counsel, be applied as follows:

(i) Unless the principal of all of the Outstanding Bonds shall be due and payable:

First – To the payment of the Owners of all installments of interest then due on the Bonds, in the order of the maturity of the installments of such interest and, if the amount available shall not be sufficient to pay in full any particular installment, then to the payment ratably, according to the amounts due on such installment, to the Owners, without any discrimination or privilege;

Second – To the payment of the Owners of the unpaid principal of any of the Bonds that shall have become due (other than Bonds matured or called for redemption for the payment of which moneys are held pursuant to the provisions of the Indenture), in the order of their due dates and, if the amount available shall not be sufficient to pay in full the principal of and premium, if any, on such Bonds due on any particular date, then to the payment ratably, according to the amount due on such date, to the Owners without any discrimination; and

Third – To be held for the payment to the Owners as the same shall become due of the principal of and interest on the Bonds, that may thereafter become due either at maturity or upon call for redemption prior to maturity and, if the amount available shall not be sufficient to pay in full such principal and premium, if any, due on any particular date, together with interest then due and owing thereon, payment shall be made in accordance with the Indenture.

(ii) If the principal of all of the Outstanding Bonds shall be due and payable, to the payment of the principal and interest then due and unpaid upon the Outstanding Bonds without preference or priority of any of principal, or interest over the others or of any installment of interest, or of any Outstanding Bond over any other Outstanding Bond, ratably, according to the amounts due respectively for principal and interest, to the Owners without any discrimination or preference except as to any difference in the respective amounts of interest specified in the Outstanding Bonds.

(b) Whenever moneys are to be applied pursuant to the provisions of the Indenture, such moneys shall be applied at such times, and from time to time, as the Trustee shall determine, having due regard to the amount of such moneys available for application and the likelihood of additional moneys becoming available for such application in the future. The Trustee shall give, by mailing by first-class mail as it may deem appropriate, such notice of the deposit with it of any such moneys.

Defeasance

If the Authority shall pay or cause to be paid to the Owners of all Outstanding Bonds the interest thereon and the principal thereof and the premiums, if any, thereon at the times and in the manner stipulated therein, then the Owners of such Bonds shall cease to be entitled to the pledge of the Revenues as provided in the Indenture, and all agreements, covenants and other obligations of the Authority to the Owners of such Bonds shall cease, terminate and become void and be discharged and satisfied. In such event, the Trustee shall execute and deliver to the Authority all such instruments as may be necessary or desirable to evidence such discharge and satisfaction, and the Trustee shall pay over or deliver to the Authority all money or securities or other property held by it pursuant to the Indenture that are not required for the payment of the interest on and principal of and redemption premiums, if any, on such Bonds.

Subject to the provisions of the above paragraph, when any of the Bonds shall have been paid and if, at the time of such payment, the Authority shall have kept, performed and observed all the covenants and promises in such Bonds and in the Indenture required or contemplated to be kept, performed and observed by the Authority or on its part on or prior to that time, then the Indenture shall be considered to have been discharged in respect of such Bonds and such Bonds shall cease to be entitled to the lien of the Indenture and such lien and all agreements, covenants, and other obligations of the Authority therein shall cease, terminate, and become void and be discharged and satisfied as to such Bonds.

Notwithstanding the satisfaction and discharge of the Indenture or the discharge of the Indenture in respect of any Bonds, those provisions of the Indenture relating to the maturity of the Bonds, interest payments and dates thereof, exchange and transfer of Bonds, replacement of mutilated, destroyed, lost, or stolen Bonds, the safekeeping and cancellation of Bonds, nonpresentment of Bonds, and the duties of the Trustee in connection with all of the foregoing, remain in effect and shall be binding upon the Trustee and the Owners of the Bonds and the Trustee shall continue to be obligated to hold in trust any moneys or investments then held by the Trustee for the payment of the principal of, redemption premium, if any, and interest on the Bonds, to pay to the Owners of Bonds the funds so held by the Trustee as and when such payment becomes due. Notwithstanding the satisfaction and discharge of the Indenture or the discharge thereof in respect of any Bonds, those provisions of the Indenture relating to the compensation of the Trustee shall remain in effect and shall be binding upon the Trustee and the Authority.

Any Outstanding Bonds shall prior to the maturity date or redemption date thereof be deemed to have been paid for purposes of the Indenture if: (i) in case any of such Bonds are to be redeemed on any date prior to their maturity date, the Authority shall have given to the Trustee in form satisfactory to it irrevocable instructions to mail, on a date in accordance with the provisions of the Indenture, notice of redemption of such Bonds on said redemption date, said notice to be given in accordance with the Indenture; (ii) there shall have been deposited with the Trustee either (A) money in an amount that shall be sufficient; or (B) Federal Securities of which are not subject to redemption prior to maturity except by the holder thereof (including any such Permitted Investments issued or held in book-entry form on the books of the Department of the Treasury of the United States of America) and/or Pre-Refunded Municipals, the interest on and principal of which when due, and without any reinvestment thereof, will provide money that, together with the money, if any, deposited with the Trustee at the same time, shall, as verified by an independent certified public accountant or other independent financial consultant acceptable to the Trustee, be sufficient, to pay when due the interest to become due on such Bonds on and prior to the maturity date or redemption date thereof, as the case may be, and the principal of and interest on such Bonds; and; (iii) in the event such Bonds are not by their terms subject to redemption within the next succeeding 60 days, the Authority shall have given the Trustee in form satisfactory to it irrevocable instructions to mail as soon as practicable, a notice to the Owners of such Bonds and to the Securities Depositories and the Information Services that the deposit required by clause (ii) above has been made with the Trustee and that such Bonds are deemed to have been paid in accordance with the Indenture and stating the maturity date or redemption date upon which money is to be available for the payment of the principal of and interest on such Bonds.

INSTALLMENT PURCHASE AGREEMENT

The Installment Purchase Agreement sets forth certain terms and conditions of the purchase of the Project by the City. The term "Installment Purchase Agreement" means the Master Installment Purchase Agreement, dated as of August 1, 1998, as supplemented and amended by a 1998 Supplement to Master Installment Purchase Agreement, dated as of August 1, 1998, a 2002 Supplement to Master Installment Purchase Agreement, dated as of October 1, 2002, an Amended and Restated Master Installment Purchase Agreement, dated as of January 1, 2009, a 2009A Supplement to Amended and Restated Master Installment Purchase Agreement, dated as of January 1, 2009, a 2009B Supplement to Amended and Restated Master Installment Purchase Agreement, dated as of June 1, 2009, and the 2010A Supplement, each by and between the City and the Corporation, as such Agreement may from time to time be further amended or supplemented by all Supplements executed pursuant to the provisions thereof. Certain definitions under and provisions of the Installment Purchase Agreement are given and summarized below. Other provisions are summarized in the Official Statement under the caption "SECURITY FOR THE SERIES 2010A BONDS."

Selected Definitions.

<u>Accountant's Report</u>

The term "Accountant's Report" means a report signed by an Independent Certified Public Accountant.

Adjusted Debt Service

The term "Adjusted Debt Service" means, for any Fiscal Year, Debt Service on Parity Obligations for such Fiscal Year, minus an amount equal to earnings from investments in any Reserve Fund securing Parity Obligations for such Fiscal Year.

Adjusted Net System Revenues

The term "Adjusted Net System Revenues" means, for any Fiscal Year, the Net System Revenues for such Fiscal Year, minus an amount equal to earnings from investments in any Reserve Fund securing Parity Obligations for such Fiscal Year.

Authorizing Ordinance

The term "Authorizing Ordinance" means the ordinance pursuant to which the Installment Purchase Agreement was authorized and any additional ordinance or official authorizing act of the council of the City approving execution and delivery of any Supplement to the Installment Purchase Agreement or any Issuing Instrument.

Balloon Indebtedness

The term "Balloon Indebtedness" means, with respect to any Series of Obligations twenty-five percent (25%) or more of the principal of which matures on the same date or within a 12-month period (with sinking fund payments on Term Obligations deemed to be payments of matured principal), that portion of such Series of Obligations which matures on such date or within such 12-month period; provided, however, that to constitute Balloon Indebtedness the amount of indebtedness maturing on a single date or over a 12-month period must equal or exceed 150% of the amount of such Series of Obligations which matures during any preceding 12-month period. For purposes of this definition, the principal amount maturing on any date shall be reduced by the amount of such indebtedness which is required, by the documents governing such indebtedness, to be amortized by prepayment or redemption prior to its stated maturity date.

Capacity Charge

The term "Capacity Charge" means a charge imposed upon a person, firm, corporation, or other entity incident to the granting of a permit for a new water connection or due to an increase in water usage by the addition of any type of dwelling, commercial or industrial unit, which charge is based upon an increase in water consumption as measured by equivalent dwelling units, and the proceeds of which are used to construct, improve and expand the Water System to accommodate the additional business of such added dwellings or commercial or industrial units.

Consultant

The term "Consultant" means the consultant, consulting firm, engineer, architect, engineering firm, architectural firm, accountant, or accounting firm retained by the City to perform acts or carry out the duties provided for such consultant in the Installment Purchase Agreement. Such consultant, consulting firm, engineer, architect, engineering firm, or architectural firm shall be nationally recognized within its profession for work of the character required. Such accountants or accounting firm shall be independent certified public accountants licensed to practice in the State.

Credit Provider

The term "Credit Provider" means any municipal bond insurance company, bank, or other financial institution or organization which is performing in all material respects its obligations under any Credit Support Instrument for some or all of the Parity Obligations.

Credit Provider Reimbursement Obligations

The term "Credit Provider Reimbursement Obligations" means obligations of the City to repay, from Net System Revenues, amounts advanced by a Credit Provider as credit support or liquidity for Parity Obligations, which obligations shall constitute Parity Obligations or Subordinated Obligations, as designated by the City.

Credit Support Instrument

The term "Credit Support Instrument" means a policy of insurance, a letter of credit, a standby purchase agreement, revolving credit agreement or other credit arrangement pursuant to which a Credit Provider provides credit support or liquidity with respect to the payment of interest, principal, or the purchase price of any Parity Obligations.

Debt Service

With regard to the issuance of Parity Obligations, the term "Debt Service" means, for any Fiscal Year, the sum of (a) the interest payable during such Fiscal Year on all Outstanding Parity Obligations, assuming that all Outstanding Serial Parity Obligations are retired as scheduled and that all Outstanding Term Parity Obligations are redeemed or paid from sinking fund payments as scheduled (except to the extent that such interest is to be paid from the proceeds of sale of any Parity Obligations), (b) that portion of the principal amount of all Outstanding Serial Parity Obligations maturing on the next succeeding principal payment date which falls in such Fiscal Year (excluding Serial Obligations which at the time of issuance are intended to be paid from the sale of a corresponding amount of Parity Obligations), (c) that portion of the principal amount of all Outstanding Term Parity Obligations required to be redeemed or paid on any redemption date which falls in such Fiscal Year (together with the redemption premiums, if any, thereon); provided that, (1) as to any Balloon Indebtedness, Tender Indebtedness, and Variable Rate Indebtedness, interest thereon shall be calculated as provided in the definition of Maximum Annual Debt Service and principal shall be deemed due at the nominal maturity dates thereof; (2) the amount on deposit in a debt service reserve fund on any date of calculation of Debt Service shall be deducted from the amount of principal due at the final maturity of the Parity Obligations for which such debt service reserve fund was established and in each preceding year until such amount is exhausted; and (3) the amount of payments on account of Parity Obligations which are redeemed, retired, or repaid on the basis of the accreted value due on the scheduled redemption, retirement, or repayment date shall be deemed principal payments, and interest that is compounded and paid as part of the accreted value shall be deemed payable on the scheduled redemption, retirement, or repayment date, but not before.

With regard to the issuance of Subordinated Obligations, the term "Debt Service" means, for any Fiscal Year, the sum of (a) the interest payable during such Fiscal Year on all Outstanding Obligations, assuming that all Outstanding Serial Obligations are retired as scheduled and that all Outstanding Term Obligations are redeemed or paid from sinking fund payments as scheduled (except to the extent that such interest is to be paid from the proceeds of sale of any Obligations), (b) that portion of the principal amount of all Outstanding Serial Obligations maturing on the next succeeding principal payment date which falls in such Fiscal Year (excluding Serial Obligations which at the time of issuance are intended to be paid from the sale of a corresponding amount of other Obligations) (c) that portion of the principal amount of all Outstanding Term Obligations required to be redeemed or paid on any redemption date which falls in such Fiscal Year (together with the redemption premiums, if any, thereon) provided that, (1) as to any Balloon Indebtedness, Tender Indebtedness, and Variable Rate Indebtedness, interest thereon shall be calculated as provided in the definition of Maximum Annual Debt Service and principal shall be deemed due at the nominal maturity dates thereof; (2) the amount on deposit in a Reserve Fund on any date of calculation of Debt Service shall be deducted from the amount of principal due at the final maturity of the Obligations for which such Reserve Fund was established and in each preceding year, until such amount is exhausted; and (3) the amount of payments on account of Obligations which are redeemed, retired, or repaid on the basis of the accreted value due on the scheduled redemption, retirement, or repayment date shall be deemed principal payments, and interest that is compounded and paid as part of the accreted value thereof shall be deemed payable on the scheduled redemption, retirement, or repayment date, but not before.

Default Rate

The term "Default Rate" means the Maximum Rate.

Defaulted Obligations

The term "Defaulted Obligations" means Obligations in respect of which an Event of Default has occurred and is continuing.

Engineer's Report

The term "Engineer's Report" means a report signed by an Independent Engineer.

Fiscal Year

The term "Fiscal Year" means the period beginning on July 1 of each year and ending on the next succeeding June 30, or any other twelve-month period selected and designated as the official Fiscal Year of the City.

Independent Certified Public Accountant

The term "Independent Certified Public Accountant" means any firm of certified public accountants appointed by the City, and each of whom is independent pursuant to the Statement on Auditing Standards No. 1 of the American Institute of Certified Public Accountants.

Independent Engineer

The term "Independent Engineer" means any registered engineer or firm of registered engineers of national reputation generally recognized to be well qualified in engineering matters relating to water systems, appointed and paid by but not under the control of the City.

Installment Payment Date

The term "Installment Payment Date" means any date on which an Installment Payment is due as specified in the Installment Purchase Agreement or determined pursuant to a Supplement.

Installment Payments

The term "Installment Payments" means the Installment Payments scheduled to be paid by the City under and pursuant to the Installment Purchase Agreement and any Supplement.

Installment Payment Obligations

The term "Installment Payment Obligations" means Obligations consisting of or which are supported in whole by Installment Payments.

Issuing Instrument

The term "Issuing Instrument" means any indenture, trust agreement, loan agreement, lease, installment purchase agreement, or the Installment Purchase Agreement, including any Supplement or other instrument under which Obligations are issued or created.

Law

The term "Law" means the Charter and all applicable laws of the State.

Maintenance and Operation Costs of the Water System

The term "Maintenance and Operation Costs of the Water System" means (a) any Qualified Take or Pay Obligation, and (b) the reasonable and necessary costs spent or incurred by the City for maintaining and operating the Water System, calculated in accordance with generally accepted accounting principles, including, without limitation, the costs of the purchase, delivery or storage of water, the reasonable expenses of maintenance and repair and other expenses necessary to maintain and preserve the Water System in good repair and working order, and including administrative costs of the City attributable to the Water System, including the Project and the Installment Purchase Agreement, salaries and wages of employees of the Water System, payments to such employees' retirement systems (to the extent paid from System Revenues), overhead, taxes (if any), fees of auditors, accountants, attorneys, or engineers and insurance premiums, and including all other reasonable and necessary costs of the City or charges required to be paid by it to comply with the terms of the Obligations, including the Installment Purchase Agreement, including any amounts required to be deposited in the Rebate Fund pursuant to a Tax Certificate, and fees and expenses payable to any Credit Provider (other than in repayment of a Credit Provider Reimbursement Obligation), but excluding in all cases (1) depreciation, replacement and obsolescence charges or reserves therefor, (2) amortization of intangibles or other bookkeeping entries of a similar nature, (3) costs of capital additions, replacements, betterments, extensions or improvements to the Water System which under generally accepted accounting principles are chargeable to a capital account or to a reserve for depreciation, (4) charges for the payment of principal of and interest on any general obligation bond issued for Water System purposes, and (5) charges for the payment of principal of and interest on any debt service on account of any Obligation on a parity with or subordinate to the Installment Payments.

Maximum Annual Debt Service

The term "Maximum Annual Debt Service" means,

(A) with respect to Parity Obligations then Outstanding, the maximum amount of principal and interest becoming due on the Parity Obligations in the then-current or any future Fiscal Year, calculated by the City or by an Independent Certified Public Accountant in accordance with the Installment Purchase Agreement and provided to the Trustee. For purposes of calculating Maximum Annual Debt Service, the following assumptions shall be used to calculate the principal and interest becoming due in any Fiscal Year:

(i) in determining the principal amount due in each Fiscal Year, payments shall (except to the extent a different subsection of this definition applies for purposes of determining principal maturities or amortization) be assumed to be made in accordance with any amortization schedule established for such debt, including the amount of any Parity Obligations which or have the characteristics of commercial paper and which not intended at the time of issuance to be retired from the sale of a corresponding amount of Parity Obligations, and including any scheduled mandatory redemption or prepayment of Parity Obligations on the basis of accreted value due upon such redemption or prepayment, and for such purpose, the redemption payment or prepayment shall be deemed a principal payment; provided, however, that with respect to Parity Obligations which are or have the characteristics of commercial paper and which are intended at the time of issuance to be retired from the sale of a corresponding amount of other Obligations, which other Obligations would not constitute Balloon Indebtedness, each maturity thereof shall be treated as if it were to be amortized in substantially equal installments of principal and interest over a term of 30 years, commencing in the year of such stated maturity; in determining the interest due in each Fiscal Year, interest payable at a fixed rate shall (except to the extent paragraph (A)(ii) or (iii) of this definition applies) be assumed to be made at such fixed rate and on the required payment dates;

(ii) if all or any portion or portions of an Outstanding Series of Parity Obligations constitute Balloon Indebtedness or if all or any portion or portions of a Series of Parity Obligations or such payments then proposed to be issued would constitute Balloon Indebtedness, then, for purposes of determining Maximum Annual Debt Service, each maturity which constitutes Balloon Indebtedness shall be treated as if it were to be amortized in substantially equal annual installments of principal and interest over a term of 30 years, commencing in the year the stated maturity of such Balloon Indebtedness occurs, the interest rate used for such computation shall be determined as provided in paragraph (A)(iv) or (v) below, as appropriate, and all payments of principal and interest becoming due prior to the year of the stated maturity of the Balloon Indebtedness shall be treated as described in paragraph (A)(i) above;

(iii) if any Outstanding Series of Parity Obligations constitutes Tender Indebtedness or if Parity Obligations proposed to be issued would constitute Tender Indebtedness, then for purposes of determining Maximum Annual Debt Service, Tender Indebtedness shall be treated as if the principal amount of such Parity Obligations were to be amortized in accordance with the amortization schedule set forth in the Supplement or Issuing Instrument for such Tender Indebtedness or in the standby purchase or liquidity facility established with respect to such Tender Indebtedness, or if no such amortization schedule is set forth, then such Tender Indebtedness shall be deemed to be amortized in substantially equal annual installments of principal and interest over a term of 30 years commencing in the year in which such Series is first subject to tender, the interest rate used for such computation shall be determined as provided in paragraph (A)(iv) or (v) below, as appropriate;

(iv) if any Outstanding Series of Parity Obligations constitutes Variable Rate Indebtedness, the interest rate on such Obligations shall be assumed to be 110% of the daily average interest rate on such Parity Obligations during the 12 months ending with the month preceding the date of calculation, or such shorter period that such Parity Obligations shall have been Outstanding;

(v) if Parity Obligations proposed to be issued will be Variable Rate Indebtedness, then such Parity Obligations shall be assumed to bear interest at 80% of the average Revenue Bond Index during the calendar quarter preceding the calendar quarter in which the calculation is made, or if that index is no longer published, another similar index selected by the City, or if the City fails to select a replacement index, an interest rate equal to 80% of the yield for outstanding United States Treasury bonds having an equivalent maturity, or if there are no such Treasury bonds having such maturities, 100% of the lowest prevailing prime rate of any of the five largest commercial banks in the United States ranked by assets; and

(vi) if moneys or Permitted Investments have been deposited by the City into a separate fund or account or are otherwise held by the City or by a fiduciary to be used to pay principal of and/or interest on specified Parity Obligations, then the principal and/or interest to be paid from such moneys, Permitted Investments, or from the earnings thereon shall be disregarded and not included in calculating Maximum Annual Debt Service.

(B) with regard to all Obligations then Outstanding, the maximum amount of principal and interest becoming due on the Obligations in the then-current or any future Fiscal Year, calculated by the City or by an Independent Certified Public Accountant in accordance with this subsection and provided to the Trustee. For purposes of calculating Maximum Annual Debt Service, the following assumptions shall be used to calculate the principal and interest becoming due in any Fiscal Year:

(i) in determining the principal amount due in each Fiscal Year, payments shall (except to the extent a different subsection of this definition applies for purposes of determining principal maturities or amortization) be assumed to be made in accordance with any amortization schedule established for such debt, including the amount of any Obligations which are or have the characteristics of commercial paper and which are not intended at the time of issuance to be retired from the sale of a corresponding amount of Obligations, and including any scheduled mandatory redemption or prepayment of Obligations on the basis of accreted value due upon such redemption or prepayment, and for such purpose, the redemption payment or prepayment shall be deemed a principal payment; provided, however, that with respect to Obligations which are or have the characteristics of commercial paper and which are intended at the time of issuance to be retired from the proceeds of sale of a corresponding amount of other Obligations, and which would not constitute Balloon Indebtedness, each maturity thereof shall be treated as if it were to be amortized in substantially equal installments of principal and interest over a term of 30 years, commencing in the year of such stated maturity; in determining the interest due in each Fiscal Year, interest payable at a fixed rate shall (except to the extent paragraph (B)(ii) or (iii) of this definition applies) be assumed to be made at such fixed rate and on the required payment dates;

(ii) if all or any portion or portions of an Outstanding Series of Obligations constitute Balloon Indebtedness or if all or any portion or portions of a Series of Obligations or such payments then proposed to be issued would constitute Balloon Indebtedness, then, for purposes of determining Maximum Annual Debt Service, each maturity which constitutes Balloon Indebtedness shall be treated as if it were to be amortized in substantially equal annual installments of principal and interest over a term of 30 years, commencing in the year the stated maturity of such Balloon Indebtedness occurs, the interest rate used for such computation shall be determined as provided in paragraph (B)(iv) or (v) below, as appropriate, and all payments of principal and interest becoming due prior to the year of the stated maturity of the Balloon Indebtedness shall be treated as described in paragraph (B)(i) above;

(iii) if any Outstanding Series of Obligations constitutes Tender Indebtedness or if Obligations proposed to be issued would constitute Tender Indebtedness, then for purposes of determining Maximum Annual Debt Service, Tender Indebtedness shall be treated as if the principal amount of such Obligations were to be amortized in accordance with the amortization schedule set forth in the Supplement or Issuing Instrument for such Tender Indebtedness or in the standby purchase or liquidity facility established with respect to such Tender Indebtedness, or if no such amortization schedule is set forth, then such Tender Indebtedness shall be deemed to be amortized in substantially equal annual installments of principal and interest over a term of 30 years, commencing in the year in which such Obligations are first subject to tender, the interest rate used for such computation shall be determined as provided in paragraph (B)(iv) or (v) below, as appropriate;

(iv) if any Outstanding Series of Obligations constitute Variable Rate Indebtedness, the interest rate on such Series of Obligations shall be assumed to be 110% of the daily average interest rate on such Series of Obligations during the 12 months ending with the month preceding the date of calculation, or such shorter period that such Series of Obligations shall have been Outstanding;

(v) if Obligations proposed to be issued will be Variable Rate Indebtedness, then such Obligations shall be assumed to bear interest at 80% of the average Revenue Bond Index during the calendar quarter preceding the calendar quarter in which the calculation is made, or if that index is no longer published, another similar index selected by the City, or if the City fails to select a replacement index, an interest rate equal to 80% of the yield for outstanding United States Treasury bonds having an equivalent maturity, or if there are no such Treasury bonds having such maturities, 100% of the lowest prevailing prime rate of any of the five largest commercial banks in the United States ranked by assets; and

(vi) if moneys or Permitted Investments have been deposited by the City into a separate fund or account or are otherwise held by the City or by a fiduciary to be used to pay principal and/or interest on specified Obligations, then the principal and/or interest to be paid from such moneys, Permitted Investments or from the earnings thereon shall be disregarded and not included in calculating Maximum Annual Debt Service.

Maximum Rate

The term "Maximum Rate" means, on any day, the maximum interest rate allowed by law.

Net Proceeds

The term "Net Proceeds" means, when used with respect to any insurance, self-insurance, or condemnation award, the proceeds from such award that are remaining after payment of all expenses (including attorneys' fees) incurred in the collection of such proceeds.

Net System Revenues

The term "Net System Revenues" means, for any Fiscal Year, the System Revenues for such Fiscal Year, less the Maintenance and Operation Costs of the Water System for such Fiscal Year.

Obligations

The term "Obligations" means (a) obligations of the City for money borrowed (such as bonds, notes or other evidences of indebtedness) or as installment purchase payments under any contract (including Installment Payments), or as lease payments under any financing lease (determined to be such in accordance with generally accepted accounting principles), the principal of and interest on which are payable from Net System Revenues; (b) obligations to replenish any debt service reserve funds with respect to such obligations of the City; (c) obligations secured by or payable from any of such obligations of the City; and (d) obligations of the City payable from Net System Revenues under (1) any contract providing for payments based on levels of, or changes in, interest rates, currency exchange rates, stock or other indices, (2) any contract to exchange cash flows or a series of payments, or (3) any contract to hedge payment, currency, rate spread or similar exposure, including but not limited to interest rate cap agreements.

Outstanding

The term "Outstanding," when used as of any particular time with respect to Obligations, means all Obligations theretofore or thereupon executed, authenticated and delivered by the City or any trustee or other fiduciary, *except* (a) Obligations theretofore cancelled or surrendered for cancellation; (b) Obligations paid or deemed to be paid within the meaning of any defeasance provisions thereof; (c) Obligations owned by the City; and (d) Obligations in lieu of or in substitution for which other Obligations have been executed and delivered.

Owner

The term "Owner" means any person who shall be the registered owner of any certificate or other evidence of a right to receive Installment Payments directly or as security for payment of an Outstanding Obligation.

Parity Installment Obligation

The term "Parity Installment Obligation" means Obligations consisting of or payable from Installment Payments which are not subordinated in right of payment to other Installment Payments.

Parity Obligations

The term "Parity Obligations" means (a) Parity Installment Obligations, (b) Obligations, the principal of and interest on which are payable on a parity with Parity Installment Obligations, and (c) Reserve Fund Obligations.

Payment Fund

The term "Payment Fund" means the fund designated in the Issuing Instrument as the fund into which Installment Payments are to be deposited for the purposes of paying principal of or interest on related Obligations.

Permitted Investments

The term "Permitted Investments" means investments which, pursuant to an Issuing Instrument, are permissible for the investment of funds received from the sale of Obligations pursuant to the Issuing Document or from other funds held pursuant to the Issuing Document.

Purchase Price

The term "Purchase Price" means the principal amount, plus interest thereon, owed by the City to the Corporation under the terms of the Installment Purchase Agreement for the purchase of Project Components, as specified in the Installment Purchase Agreement or in a Supplement.

Qualified Take or Pay Obligation

The term "Qualified Take or Pay Obligation" means the obligation of the City to make use of any facility, property, or services, or some portion of the capacity thereof, or to pay therefor from System Revenues, or both, whether or not such facilities, properties, or services are ever made available to the City for use, and there is provided to the City a certificate of the City or of an Independent Engineer to the effect that the incurrence of such obligation will not adversely affect the ability of the City to comply with the provisions of the Installment Purchase Agreement.

Rate Stabilization Fund

The term "Rate Stabilization Fund" means the fund by that name established pursuant to the Installment Purchase Agreement.

Rebate Requirement

The term "Rebate Requirement" shall have the meaning specified in any Tax Certificate.

Reserve Fund

The term "Reserve Fund" shall refer to the fund by that name established under an Issuing Instrument or Supplement.

Reserve Fund Obligations

The term "Reserve Fund Obligations" means the obligations of the City to pay amounts advanced under any Reserve Fund Credit Facility entered into in accordance with the provisions of the related Issuing Instrument or Supplement, which obligations shall constitute Parity Obligations or Subordinated Obligations, as designated by the City.

Reserve Fund Credit Facility

The term "Reserve Fund Credit Facility" means a letter of credit, line of credit, surety bond, insurance policy or similar facility deposited in the Reserve Fund established under an Issuing Instrument in lieu of or in partial substitution for cash or securities on deposit therein.

Reserve Requirement

The term "Reserve Requirement" shall have the meaning given to such term in any Issuing Instrument or Supplement.

Revenue Bond Index

The term "Revenue Bond Index" means the Revenue Bond Index by that name published from time to time in *The Bond Buyer*.

Secondary Purchase Fund

The term "Secondary Purchase Fund" means any fund by that name established pursuant to the Installment Purchase Agreement.

Serial Obligations

The term "Serial Obligations" means Obligations for which no sinking fund payments are provided.

Serial Parity Obligations

The term "Serial Parity Obligations" means Serial Obligations which are Parity Installment Payments or are payable on a parity with Parity Installment Obligations.

Series

The term "Series" means Obligations issued at the same time or sharing some other common term or characteristic and designated as a separate Series.

Subordinated Credit Provider

The term "Subordinated Credit Provider" means any municipal bond insurance company, bank, or other financial institution or organization which is performing in all respects its obligations under any Subordinated Credit Support Instrument for some or all of the Subordinated Obligations.

Subordinated Credit Provider Reimbursement Obligations

The term "Subordinated Credit Provider Reimbursement Obligations" means obligations of the City to repay, from Net System Revenues, amounts advanced by a Subordinated Credit Provider as credit support or liquidity for Subordinated Obligations, which obligations shall constitute Subordinated Obligations.

Subordinated Credit Support Instrument

The term "Subordinated Credit Support Instrument" means a policy of insurance, a letter of credit, a standby purchase agreement, revolving credit agreement, or other credit arrangement pursuant to which a Subordinated Credit Provider provides credit support or liquidity with respect to the payment of interest, principal, or the purchase price of any Subordinated Obligations.

Subordinated Obligations

The term "Subordinated Obligations" means any Obligations, the payment of which is subordinated in right of payment to Parity Obligations.

System Revenues

The term "System Revenues" means all income, rents, rates, fees, charges, and other moneys derived from the ownership or operation of the Water System, including, without limiting the generality of the foregoing:

(a) all income, rents, rates, fees, charges, or other moneys derived by the City from the water services or facilities, and commodities or byproducts, including hydroelectric power, sold, furnished, or supplied through the facilities of or in the conduct or operation of the business of the Water System, and including, without limitation, investment earnings on the operating reserves to the extent that the use of such earnings is limited to the Water System by or pursuant to law, and earnings on any Reserve Fund for Obligations, but only to the extent that such earnings may be utilized under the Issuing Instrument for the payment of debt service for such Obligations;

(b) standby charges and Capacity Charges [*] derived from the services and facilities sold or supplied through the Water System;

(c) the proceeds derived by the City directly or indirectly from the lease of a part of the Water System;

(d) any amount received from the levy or collection of taxes which are solely available and are earmarked for the support of the operation of the Water System;

(e) amounts received under contracts or agreements with governmental or private entities and designated for capital costs for the Water System [*]; and

(f) grants for maintenance and operations received from the United States of America or from the State; provided, however, that System Revenues shall not include: (1) in all cases, customers' deposits or any other deposits or advances subject to refund until such deposits or advances have become the property of the City; and (2) the proceeds of borrowings; but

(g) notwithstanding the foregoing, there shall be deducted from System Revenues any amounts transferred into a Rate Stabilization Fund as contemplated by the Installment Purchase Agreement, and any amounts transferred from current System Revenues to the Secondary Purchase Fund as contemplated by the Installment Purchase Agreement, and there shall be added to System Revenues any amounts transferred out of such Rate Stabilization Fund or the Secondary Purchase Fund to pay Maintenance and Operation Costs of the Water System.

Tax-Exempt Installment Payment Obligations

The term "Tax-Exempt Installment Payment Obligations" means Installment Payment Obligations, the interest component of which is excluded from gross income pursuant to Section 103 of the Code.

Tender Indebtedness

The term "Tender Indebtedness" means any Obligations or portions of Obligations, a feature of which is an option, on the part of the holders thereof, or an obligation, under the terms of such Obligations, to tender all or a portion of such Obligations to the City, a Trustee or other fiduciary or agent for payment or purchase and requiring that such Obligations or portions of Obligations or that such rights to payments or portions of payments be purchased if properly presented. Tender Indebtedness may consist of either Parity Obligations or Subordinated Obligations.

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[*] These items of System Revenue may not be used to pay Maintenance and Operation Costs of the Water System.

Term Parity Obligations

The term “Term Parity Obligations” means Term Obligations which are Parity Installment Obligations or are payable on a parity with Parity Installment Obligations.

Term Obligations

The term “Term Obligations” means Obligations which are payable on or before their specified maturity dates from sinking fund payments established for that purpose and calculated to retire such Obligations on or before their specified maturity dates.

Variable Rate Indebtedness

The term “Variable Rate Indebtedness” means any portion of indebtedness evidenced by Obligations, the interest rate for which is subject to adjustment periodically through a remarketing process or according to a stated published index for similar obligations in the municipal markets. Variable Rate Indebtedness may consist of either Parity Obligations or Subordinated Obligations.

Water Service

The term “Water Service” means the collection, conservation, production, storage, treatment, transmission, furnishing, and distribution services made available or provided by the Water System.

Water Utility Fund

The term “Water Utility Fund” means the fund by that name established under the Charter.

1998 Project

The term “1998 Project” means the Components of the Project initially financed under the Installment Purchase Agreement.

Installment Payments

Purchase Price.

(a) The City will pay the Purchase Price for any Components being purchased as provided in a Supplement. The Purchase Price to be paid by the City to the Corporation pursuant to any Supplement, solely from Net System Revenues and from no other sources, is the sum of the principal amount of the City’s obligations under such Supplement plus the interest to accrue on the unpaid balance of such principal amount from the effective date thereof over the term thereof, subject to prepayment as provided therein.

(b) The principal amount of the Installment Payments to be made by the City under a Supplement shall be paid at least three Business Days prior to the date such Installment Payments are payable as specified in such Supplement or at such other earlier time or times and in the manner or manners as specified in such Supplement. In the event the principal amount of an Installment Payment is not paid by the date the same is due and payable as specified in such Supplement, the same shall bear interest at the Default Rate, commencing on the day the same as due, to, but not including, the payment date.

(c) The interest to accrue on the unpaid balance of such principal amount shall be paid at least three Business Days prior to the date such interest is payable as specified in a Supplement or at such other earlier time or times as specified in such Supplement, and shall be paid by the City as and constitute interest paid on the principal amount of the City’s obligations thereunder. Interest shall be payable in an amount not exceeding the Maximum Rate at the time of incurring such obligation, at such intervals and according to such interest rate formulas as shall be specified in a Supplement or by reference to any Issuing Instrument to which such Supplement relates, and shall be payable with such frequency as shall be specified therein. In the event that interest is not paid by the date such interest is payable, to the extent permitted by applicable law, such interest shall thereafter bear interest at the Default Rate, commencing on the day the same is due, to, but not including, the payment date.

Installment Payments; Reserve Fund Payments.

(a) The City shall, subject to any rights of prepayment provided for in a Supplement, pay to the Corporation, solely from Net System Revenues and from no other sources, the Purchase Price in Installment Payments over a period not to exceed the maximum period permitted by law, all as specified in a Supplement.

(b) In the event that a Trustee notifies the City that the amount on deposit in a Reserve Fund or Reserve Account is less than the Reserve Requirement, the City shall deposit or cause to be deposited, solely from Net System Revenues in accordance with the Installment Purchase Agreement, in such Reserve Fund or Reserve Account such amounts on a monthly basis as are necessary to increase the amount on deposit therein to the Reserve Requirement in the ensuing twelve months.

(c) The obligation of the City to make the Installment Payments solely from Net System Revenues is absolute and unconditional, and until such time as the Purchase Price shall have been paid in full (or provision for the payment thereof shall have been made pursuant to the Installment Purchase Agreement), the City will not discontinue or suspend any Installment Payments required to be made by it under the Installment Purchase Agreement when due, whether or not the Project or any part thereof is operating or operable or has been completed, or its use is suspended, interfered with, reduced or curtailed or terminated in whole or in part, and such Installment Payments shall not be subject to reduction whether by offset or otherwise and shall not be conditioned upon the performance or nonperformance by any party of any agreement for any cause whatsoever.

System Revenues

Commitment of the Net System Revenues.

(a) All Parity Obligations, including Parity Installment Payment Obligations, shall be secured by a first priority lien on and pledge of Net System Revenues. The City grants such first priority lien on and pledge of Net System Revenues to secure Parity Obligations. All Parity Obligations shall be of equal rank with each other without preference, priority, or distinction of any Parity Obligations over any other Parity Obligations.

(b) All Subordinated Obligations shall be secured by a second priority lien on and pledge of Net System Revenues that is junior and subordinate to the lien on and pledge of Net System Revenues securing Parity Obligations. The City grants such second priority lien on and pledge of Net System Revenues to secure Subordinated Obligations. All Subordinated Obligations shall be of equal rank with each other without preference, priority, or distinction of any Subordinated Obligations over any other Subordinated Obligations.

(c) The City represents and states that it has not granted any lien or charge on any of the Net System Revenues except as provided in the Installment Purchase Agreement; provided, however, that out of Net System Revenues there may be apportioned such sums for such purposes as are expressly permitted by the Installment Purchase Agreement.

(d) Nothing contained in the Installment Purchase Agreement shall affect the ability of the City to grant liens on and pledges of the Net System Revenues that are subordinate to the liens on and pledges of Net System Revenues for the benefit of Parity Obligations and Subordinated Obligations contained therein.

Allocation of System Revenues.

(a) In order to carry out and effectuate the commitment and pledge contained in the Installment Purchase Agreement, the City agrees and covenants that all System Revenues shall be received by the City in trust and shall be deposited when and as received in the Water Utility Fund, which fund the City agrees and covenants to maintain so long as any Installment Payment Obligations remain unpaid, and all moneys in the Water Utility Fund shall be so held in trust and applied and used solely as provided in the Installment Purchase Agreement. The City shall pay from the Water Utility Fund: (1) directly or as otherwise required all Maintenance and Operation Costs of the Water System; and (2) to the Trustee, for deposit in the Payment Fund for Parity Obligations, including Reserve Fund Obligations that are Parity Obligations, the amounts specified in any Issuing Instrument, as payments due on account of Parity Obligations (including any Credit Provider Reimbursement Obligations that are Parity Obligations). In the event there are insufficient Net System Revenues to make all of the payments contemplated by clause (2) of the immediately preceding sentence, then said payments should be made as nearly as practicable, pro rata, based upon the respective unpaid principal amounts of said Parity Obligations.

(b) After the payments contemplated by subsection (a) above have been made, and in any event not less frequently than January 15 and July 15 of each year, any remaining Net System Revenues shall be used to make up any deficiency in the Reserve Funds for Parity Obligations. Notwithstanding the use of a Reserve Fund Credit Facility in lieu of depositing funds in the related Reserve Fund for Parity Obligations, in the event of any draw on the related Reserve Fund Credit Facility, there shall be deemed a deficiency in such Reserve Fund for Parity Obligations until the amount of the Reserve Fund Credit Facility is restored to its pre-draw amount. In the event there are insufficient Net System Revenues to make up all deficiencies in all Reserve Funds for Parity Obligations, such payments into the Reserve Funds shall be made as nearly as practicable pro rata based on the respective unpaid principal amount of all Parity Obligations. Any amounts thereafter remaining in the Water Utility Fund may from time to time be used to pay the amounts specified in any Issuing Instrument as payments due on account of Subordinated Obligations (including any Reserve Fund Obligations for Subordinated Obligations, any Credit Provider Reimbursement Obligations that are Subordinated Obligations and any Subordinated Credit Provider Reimbursement Obligations), provided the following conditions are met:

(i) all Maintenance and Operation Costs of the Water System are being and have been paid and are then current; and

(ii) all deposits and payments contemplated by clause (2) of paragraph (a) above shall have been made in full and no deficiency in any Reserve Fund for Parity Obligations shall exist, and there shall have been paid, or segregated within the Water Utility Fund, the amounts payable during the current month pursuant to clause (2) of paragraph (a) above.

After deposits contemplated above have been made, any amounts thereafter remaining in the Water Utility Fund may be used for any lawful purpose of the Water System.

Additional Obligations.

(a) The City may not create any Obligations, the payments of which are senior or prior in right to the payment by the City of Parity Obligations.

(b) Without regard to paragraph (c) below, the City may at any time enter into or create an obligation or commitment which is a Reserve Fund Obligation, provided that the Obligation to which the Reserve Fund Obligation relates is permitted to be entered into under the terms of the Installment Purchase Agreement.

(c) After the initial issuance of Parity Obligations under the Installment Purchase Agreement, the City reserved the right, at any time and from time to time, to issue or create any other Parity Obligations, provided that:

(i) there shall not have occurred and be continuing an Event of Default under the terms of the Installment Purchase Agreement, any Issuing Instrument or any Credit Support Instrument; and

(ii) the City obtains or provides a certificate or certificates, prepared by the City or at the City's option by a Consultant, showing that:

(A) the Net System Revenues as shown by the books of the City for any 12-consecutive-month period within the 18 consecutive months ending immediately prior to the incurring of such additional Parity Obligations shall have amounted to or exceeded the greater of (i) at least 1.20 times the Maximum Annual Debt Service on all Parity Obligations to be Outstanding immediately after the issuance of the proposed Parity Obligations or (ii) at least 1.00 times the Maximum Annual Debt Service on all Obligations to be Outstanding immediately after the issuance of the proposed Parity Obligations. For purposes of preparing the certificate or certificates described above, the City or its Consultant may rely upon audited financial statements, or, if audited financial statements for the period are not available, financial statements prepared by the City that have not been subject to audit by an Independent Certified Public Accountant; or

(B) the estimated Net System Revenues for the five Fiscal Years following the earlier of (i) the end of the period during which interest on those Parity Obligations is to be capitalized or, if no interest is to be capitalized, the Fiscal Year in which the Parity Obligations are issued, or (ii) the date on which substantially all new Components to be financed with such Parity Obligations are expected to commence operations, will be at least equal to 1.20 times the Maximum Annual Debt Service for all Parity Obligations which will be Outstanding immediately after the issuance of the proposed Parity Obligations.

(d) For purposes of the computations to be made as described in paragraph (c)(ii)(B) above, the determination of Net System Revenues:

(i) may take into account any increases in rates and charges which relate to the Water System and which have been approved by the City Council, and shall take into account any reduction in such rates and charges which have been approved by the City Council, which will, for purposes of the test described in paragraph (c)(ii)(B) above, be effective during a Fiscal Year ending within the five-Fiscal Year period for which such estimate is being made; and

(ii) may take into account an allowance for any estimated increase in such Net System Revenues from any revenue-producing additions or improvements to or extensions of the Water System to be made with the proceeds of such additional indebtedness or with the proceeds of Parity Obligations previously issued, all in an amount equal to the estimated additional average annual Net System Revenues to be derived from such additions, improvements and extensions during the five-Fiscal Year period contemplated by paragraph (c)(ii)(B) above, all as shown by such certificate of the City or its Consultant, as applicable; and

(iii) for the period contemplated by paragraph (c)(ii)(B), Maintenance and Operation Costs of the Water System shall initially be deemed to be equal to such costs for the 12 consecutive months immediately prior to incurring such other Parity Obligations for the first Fiscal Year of the five-Fiscal Year period, but adjusted if deemed necessary by the City or its Consultant, as applicable, for any increased Maintenance and Operations Costs of the Water System which are, in the judgment of the City or such Consultant, as applicable, essential to maintaining and operating the Water System and which will occur during any Fiscal Year ending within the period contemplated by paragraph (c)(ii)(B) above.

(e) The certificate or certificates described above in paragraph (c)(ii)(B) shall not be required if the Parity Obligations being issued are for the purpose of (1) issuing the Parity Obligations initially issued under the Installment Purchase Agreement or (2) refunding (A) any then Outstanding Parity Obligations if at the time of the issuance of such Parity Obligations a certificate of an Authorized City Representative shall be delivered showing that the sum of Adjusted Debt Service on all Parity Obligations Outstanding for all remaining Fiscal Years after the issuance of the refunding Parity Obligations will not exceed the sum of Adjusted Debt Service on all Parity Obligations Outstanding for all remaining Fiscal Years prior to the issuance of such refunding Parity Obligations; or (B) then Outstanding Balloon Indebtedness, Tender Indebtedness or Variable Rate Indebtedness, but only to the extent that the principal amount of such indebtedness has been put, tendered to or otherwise purchased pursuant to a standby purchase or other liquidity facility relating to such indebtedness.

(f) Without regard to paragraph (c) above, if (A) no Event of Default has occurred and is continuing and (B) no event of default or termination event attributable to an act of or failure to act by the City under any Credit Support Instrument has occurred and is continuing, the City may issue or incur Subordinated Obligations, and such Subordinated Obligations shall be paid in accordance with the provisions of the Installment Purchase Agreement, provided that:

(i) City obtains or provides a certificate or certificates, prepared by the City or at the City's option by a Consultant, showing that:

(1) the Net System Revenues as shown by the books of the City for any 12-consecutive-month period within the 18 consecutive months ending immediately prior to the incurring of such additional Subordinated Obligations shall have amounted to at least 1.00 times the Maximum Annual Debt Service on all Obligations to be Outstanding immediately after the issuance of the proposed Subordinated Obligations; or

(2) the estimated Net System Revenues for the five Fiscal Years following the earlier of (i) the end of the period during which interest on those Subordinated Obligations is to be capitalized or, if no interest is to be capitalized, the Fiscal Year in which the Subordinated Obligations are issued; or (ii) the date on which substantially all new facilities financed with such Subordinated Obligations are expected to commence operations, will be at least equal to 1.00 times the Maximum Annual Debt Service on all Obligations to be Outstanding immediately after the issuance of the proposed Subordinated Obligations.

(ii) For purposes of preparing the certificate or certificates described in clause (1) of paragraph (f)(i) above, the City and its Consultant(s) may rely upon audited financial statements or, if audited financial statements for the period are not available, financial statements prepared by the City that have not been subject to audit by an Independent Certified Public Accountant.

(iii) For purposes of the computations to be made as described in clause (2) of paragraph (f)(i) above, the determination of Net System Revenues:

(1) may take into account any increases in rates and charges which relate to the Water System and which have been approved by the City Council and shall take into account any reduction in such rates and charges which have been approved by the City Council, which will, for purposes of the test described in clause (2) of paragraph (f)(i) above, be effective during any Fiscal Year ending within the five-Fiscal Year period for which such estimate is made; and

(2) may take into account an allowance for any estimated increase in such Net System Revenues from any revenue-producing additions or improvements to or extensions of the Water System to be made with the proceeds of such additional indebtedness, with the proceeds of Obligations previously issued or with cash contributions made or to be made by the City, all in an amount equal to the estimated additional average annual Net System Revenues to be derived from such additions, improvements and extensions during the five-Fiscal Year period contemplated by clause (2) of paragraph (f)(i) above, all as shown by such certificate of the City or its Consultant, as applicable; and

(3) for the period contemplated by clause (2) of paragraph (f)(i) above, shall initially include Maintenance and Operation Costs of the Water System in an amount equal to such costs for any 12-consecutive month period within the 24 consecutive months ending immediately prior to incurring such Subordinated Obligations for the first Fiscal Year of the five-Fiscal Year period, but adjusted if deemed necessary by the City or its Consultant, as applicable, for any increased Maintenance and Operations Costs of the Water System which are, in the judgment of the City or its Consultant, as applicable, essential to maintaining and operating the Water System and which will occur during any Fiscal Year ending within the period contemplated by clause (2) of paragraph (f)(i) above.

(iv) The certificate or certificates described above in paragraph (f)(i) above shall not be required if the Subordinated Obligations being issued are for the purpose of refunding (i) then-Outstanding Parity Obligations or Subordinated Obligations if at the time of the issuance of such Subordinated Obligations a certificate of an Authorized City Representative shall be delivered showing that the sum of Debt Service for all remaining Fiscal Years on all Parity Obligations and Subordinated Obligations Outstanding after the issuance of the refunding Subordinated Obligations will not exceed the sum of Debt Service for all remaining Fiscal Years on all Parity Obligations and Subordinated Obligations Outstanding prior to the issuance of such refunding Subordinated Obligations; or (ii) then-Outstanding Balloon Indebtedness, Tender Indebtedness or Variable Rate Indebtedness, but only to the extent that the principal amount of such indebtedness has been put, tendered to or otherwise purchased by a standby purchase agreement or other liquidity facility relating to such indebtedness.

Covenants of the City

Compliance With Installment Purchase Agreement and Ancillary Agreements.

(a) The City will punctually pay Parity Obligations in strict conformity with the terms of the Installment Purchase Agreement and thereof; and will faithfully observe and perform all the agreements, conditions, covenants and terms contained in the Installment Purchase Agreement required to be observed and performed by it, and will not terminate the Installment Purchase Agreement for any cause including, without limiting the generality of the foregoing, any acts or circumstances that may constitute failure of consideration, destruction of or damage to the Project, commercial frustration of purpose, any change in the tax or other laws of the United States of America or of the State or any political subdivision of either or any failure of the Corporation to observe or perform any agreement, condition, covenant or term contained in the Installment Purchase Agreement required to be observed and performed by it, whether express or implied, or any duty, liability or obligation arising out of or connected therewith or the insolvency, or deemed insolvency, or bankruptcy or liquidation of the Corporation or any force majeure, including acts of God, tempest, storm, earthquake, war, rebellion, riot, civil disorder, acts of public enemies, blockade or embargo, strikes, industrial disputes, lock outs, lack of transportation facilities, fire, explosion, or acts or regulations of governmental authorities.

(b) The City will faithfully observe and perform all the agreements, conditions, covenants and terms contained in the Installment Purchase Agreement, including Supplements, and any Issuing Instrument or Credit Support Instrument relating to Parity Obligations required to be observed and performed by it, and it is expressly understood and agreed by and between the parties to the Installment Purchase Agreement that each of the agreements, conditions, covenants and terms contained therein is an essential and material term of the purchase of and payment for each Component by the City pursuant to, and in accordance with, and as authorized under the Law.

(c) The City will faithfully observe and perform all of the agreements and covenants of the City contained in each Authorizing Ordinance and will not permit the same to be amended or modified so as to adversely affect the Owners of Installment Payment Obligations.

(d) The City shall be unconditionally and irrevocably obligated, so long as any Installment Payment Obligations remain Outstanding and unpaid, to take all lawful action necessary or required to continue to entitle the City to collect and deposit such System Revenues in the Water Utility Fund for use as provided in the Installment Purchase Agreement; provided, however, that such obligation does not, in any way, limit the City's ability to undertake any and all legal actions, including any appeals, in the defense of a federal court order dictating a water system configuration other than that approved and adopted by the City.

Against Encumbrances. The City will not make any pledge of or place any lien on the Net System Revenues except as otherwise provided or permitted in the Installment Purchase Agreement.

Debt Service Reserve Fund. The City will maintain or cause to be maintained each Reserve Fund at the applicable Reserve Requirement. In the event the amount in any such fund or account falls below the applicable Reserve Requirement, the City will replenish such fund or account up to the applicable Reserve Requirement pursuant to the Installment Purchase Agreement.

Against Sale or Other Disposition of Property.

(a) The City will not sell, lease or otherwise dispose of the Water System or any part thereof essential to the proper operation of the Water System or to the maintenance of the System Revenues, except as provided in the Installment Purchase Agreement. Further, the City will not, except as otherwise provided in the Installment Purchase Agreement, enter into any agreement or lease that impairs the operation of the Water System or any part thereof necessary to secure adequate Net System Revenues for the payment of the Parity Obligations or that would otherwise impair the rights of the Corporation with respect to the System Revenues or the operation of the Water System.

(b) The City may dispose of any of the works, plant properties, facilities, or other parts of the Water System, or any real or personal property comprising a part of the Water System, only upon the approval of the City Council and consistent with one or more of the following:

(i) the City in its discretion may carry out such a disposition if the facilities or property being disposed of are not material to the operation of the Water System, or shall have become unserviceable, inadequate, obsolete, or unfit to be used in the operation of the Water

System or are no longer necessary, material or useful to the operation of the Water System, and if such disposition will not materially reduce the Net System Revenues and if the proceeds of such disposition are deposited in the Water Utility Fund;

(ii) the City in its discretion may carry out such a disposition if the City receives from the acquiring party an amount equal to the fair market value of the portion of the Water System disposed of. As used in this clause (ii), "fair market value" means the most probable price that the portion being disposed of should bring in a competitive and open market under all conditions requisite to a fair sale, the willing buyer and willing seller each acting prudently and knowledgeably, and assuming that the price is not affected by coercion or undue stimulus. The proceeds of the disposition shall be used (A) first, promptly to redeem, or irrevocably set aside for the redemption of, Parity Obligations, and second, promptly to redeem, or irrevocably set aside for the redemption of, Subordinated Obligations, and/or (B) to provide for a part of the cost of additions to and betterments and extensions of the Water System; provided, however, that before any such disposition under this clause (2), the City must obtain (i) a certificate of an Independent Engineer to the effect that upon such disposition and the use of the proceeds of the disposition as proposed by the City, the remaining portion of the Water System will retain its operational integrity and the estimated Net System Revenues for the five Fiscal Years following the Fiscal Year in which the disposition is to occur will be equal to or exceed the greater of (i) at least 1.20 times the Adjusted Debt Service on all Outstanding Parity Obligations during the five Fiscal Years following the Fiscal Year in which the disposition is to occur, or (ii) at least 1.00 times the Adjusted Debt Service on all Outstanding Obligations during the first five Fiscal Years following the Fiscal Year in which the disposition is to occur, taking into account (aa) the reduction in revenue resulting from the disposition, (bb) the use of any proceeds of the disposition for the redemption of Parity Obligations and/or Subordinated Obligations, (cc) the Independent Engineer's estimate of revenue from customers anticipated to be served by any additions to and betterments and extensions of the Water System financed in part by the proceeds of the disposition, and (dd) any other adjustment permitted in the preparation of a certificate under Section 5.03(c)(2)(B) of the Installment Purchase Agreement, and (ii) confirmation from the Rating Agencies to the effect that the rating then in effect on any Outstanding Parity Obligations will not be reduced or withdrawn upon such disposition.

(c) The City will operate the Water System in an efficient and economic manner, *provided* that the City may remove from service on a temporary or permanent basis such part or parts of the Water System as the City shall determine, so long as (1) Net System Revenues are at least equal to the greater of (i) 100% of all Obligations payable in the then-current Fiscal Year or (ii) 120% of Adjusted Debt Service for the then-current Fiscal Year, after giving effect to any defeasance of Parity Obligations and/or Subordinated Obligations occurring incident to such removal, and for each Fiscal Year thereafter to and including the Fiscal Year during which the last Installment Payment is due, after giving effect to such defeasance, as evidenced by (i) an Engineer's Report on file with the City, or (ii) a Certificate of the City, (2) the value of the parts of the Water System to be so removed is less than 5% of the total Water System Plant assets, each as shown on the most recent audited financial statements that include the Water Utility Fund, and (3) the City shall have filed with each Trustee an opinion of Bond Counsel to the effect that the removal of such part or parts of the Water System will not adversely affect the exclusion from-gross income for federal income tax purposes of the interest on Tax-Exempt Installment Payment Obligations.

Prompt Acquisition and Construction. The City shall take all necessary and appropriate steps to construct, acquire and install the Project, as agent of the Corporation, with all practicable dispatch and in an expeditious manner and in conformity with law so as to complete the same as soon as possible.

Maintenance and Operation of the Water System; Budgets. The City shall maintain and preserve the Water System in good repair and working order at all times and shall operate the Water

System in an efficient and economical manner and will pay all Maintenance and Operation Costs of the Water System as they become due and payable. The City shall adopt and make available to the Corporation, on or before the effective date of the Installment Purchase Agreement, a budget approved by the City Council of the City setting forth the estimated Maintenance and Operation Costs of the Water System for the period from such date until the close of the then-current Fiscal Year. On or before August 1 of each Fiscal Year, the City shall adopt, and on or before the day that is 120 days after the beginning of the Fiscal Year, make available to the Corporation a budget approved by the City Council of the City setting forth the estimated Maintenance and Operation Costs of the Water System for such Fiscal Year. Any budget may be amended at any time during any Fiscal Year and such amended budget shall be filed by the City with the Corporation.

Amount of Rates and Charges; Rate Stabilization Fund; Other Funds.

(a) The City shall fix, prescribe and collect rates and charges for the Water Service which will be at least sufficient to yield the greater of (1) Net System Revenues sufficient to pay during each Fiscal Year all Obligations payable in such Fiscal Year or (2) Adjusted Net System Revenues during each Fiscal Year equal to 120% of the Adjusted Debt Service for such Fiscal Year. The City may make adjustments from time to time in such rates and charges and may make such classification thereof as it deems necessary, but shall not reduce the rates and charges then in effect unless the Net System Revenues from such reduced rates and charges will at all times be sufficient to meet the requirements of these provisions.

(b) The City may establish, as a fund within the Water Utility Fund, a fund denominated the "Rate Stabilization Fund." From time to time, the City may deposit into the Rate Stabilization Fund, from current System Revenues, such amounts as the City shall determine and the amount of available current System Revenues shall be reduced by the amount so transferred. Amounts may be transferred from the Rate Stabilization Fund solely and exclusively to pay Maintenance and Operation Costs of the Water System, and any amounts so transferred shall be deemed System Revenues when so transferred. All interest or other earnings upon amounts in the Rate Stabilization Fund may be withdrawn therefrom and accounted for as System Revenues.

(c) The City may establish, as a fund within the Water Utility Fund, a fund denominated the "Secondary Purchase Fund." From time to time, the City may deposit in the Secondary Purchase Fund, from any lawful source, which may or may not consist of current System Revenues, such amounts as the City shall determine, and the amount of available System Revenues shall be reduced by the amount so transferred, but only to the extent that amounts so transferred consist of then-current System Revenues. Amounts may be transferred from the Secondary Purchase Fund solely and exclusively to pay Maintenance and Operation Costs of the Water System, and any amounts so transferred shall be deemed System Revenues when so transferred. All interest or other earnings upon amounts in the Secondary Purchase Fund may be withdrawn therefrom and accounted for as System Revenues.

Payment of Claims. The City will pay and discharge any and all lawful claims for labor, materials or supplies which, if unpaid, might become a lien on the System Revenues or any part thereof or on any funds in the hands of the City or the Trustee might impair the security of the Installment Payments, but the City shall not be required to pay such claims if the validity thereof shall be contested in good faith.

Compliance with Contracts. The City will comply with, keep, observe and perform all agreements, conditions, covenants and terms, express or implied, required to be performed by it contained in all contracts for the use of the Water System and all other contracts affecting or involving the Water System to the extent that the City is a party thereto.

Insurance.

(a) The City will procure and maintain or cause to be procured and maintained insurance on the Water System with responsible insurers, in such amounts and against such risks (including accident to or destruction of the Water System) as are usually covered in connection with water systems similar to the Water System, or it will self-insure or participate in an insurance pool or pools with reserves adequate, in the reasonable judgment of the City, to protect the Water System against loss. In the event of any damage to or destruction of the Water System caused by the perils covered by such insurance or self insurance, the Net Proceeds thereof shall be applied to the reconstruction, repair or replacement of the damaged or destroyed portion of the Water System. The City shall begin such reconstruction, repair or replacement promptly after such damage or destruction shall occur, and shall continue and properly complete such reconstruction, repair or replacement as expeditiously as possible, and shall pay out of such Net Proceeds all costs and expenses in connection with such reconstruction, repair or replacement so that the same shall be completed and the Water System shall be free and clear of all claims and liens unless the City determines that such property or facility is not necessary to the efficient or proper operation of the Water System and therefore determines not to reconstruct, repair or replace such project or facility. If such Net Proceeds exceed the costs of such reconstruction, repair or replacement, then the excess Net Proceeds shall be deposited in the Water Utility Fund and be available for other proper uses of funds deposited in the Water Utility Fund.

(b) The City will procure and maintain such other insurance which it shall deem advisable or necessary to protect its interests and the interests of the Corporation, which insurance shall afford protection in such amounts and against such risks as are usually covered in connection with water systems similar to the Water System; provided that any such insurance may be maintained under a self-insurance program so long as such self-insurance is maintained in the amounts and in the manner usually maintained in connection with water systems similar to the Water System.

(c) All policies of insurance required to be maintained under the Installment Purchase Agreement shall, to extent reasonably obtainable, provide that the Corporation and each Trustee shall be given 30 days' written notice of any intended cancellation thereof or reduction of coverage provided thereby. The City shall certify to the Corporation and each Trustee annually on or before August 31 that it is in compliance with the insurance requirements under the Indenture.

Accounting Records; Financial Statements and Other Reports.

(a) The City will keep appropriate accounting records in which complete and correct entries shall be made of all transactions relating to the Water System, which records shall be available for inspection by the Corporation and the Trustee at reasonable hours and under reasonable conditions.

(b) The City will prepare and file with the Corporation annually (commencing with the Fiscal Year ending June 30, 1998), within 270 days of the close of each Fiscal Year, financial statements that include the Water Utility Fund for the preceding Fiscal Year prepared in accordance with generally accepted accounting principles, together with an Accountant's Report thereon.

(c) The City will furnish a copy of the financial statements referred to in paragraph (b) above to any Owner of the Certificates requesting a copy thereof, which may be in electronic form.

Payment of Taxes and Compliance with Governmental Regulations. The City shall pay and discharge all taxes, assessments and other governmental charges which may be lawfully imposed upon the Water System or any part thereof or upon the System Revenues when the same shall become due, except that the City may contest in good faith any taxes, assessments and other governmental charges so long as the City shall have budgeted for the amount being contested and, if appropriate, such amount shall have been included as a Maintenance and Operation Costs of the Water System. The City shall duly observe and conform with all valid regulations and requirements of any governmental authority relative to the operation of the Water System or any part thereof, but the City shall not be required to comply with any regulations or requirements so long as the validity or application thereof shall be contested by the City in good faith.

Collection of Rates and Charges; No Free Service. The City shall have in effect at all times rules and regulations for the payment of bills for Water Service. Such regulations may provide that where the City furnishes water to the property receiving Water Service, the Water Service charges shall be collected together with the water rates upon the same bill providing for a due date and a delinquency date for each bill. In each case where such bill remains unpaid in whole or in part after it becomes delinquent, the City may disconnect such premises from the Water System, and such premises shall not thereafter be reconnected to the Water System except in accordance with City operating rules and regulations governing such situations of delinquency. To the extent permitted by law, the City shall not permit any part of the Water System or any facility thereof to be used or taken advantage of free of charge by any authority, firm or person, or by any public agency (including the United States of America, the State and any city, county, district, political subdivision, public authority or agency thereof).

Eminent Domain Proceeds. If all or any part of the Water System shall be taken by eminent domain proceedings, then subject to the provisions of any Authorizing Ordinance, the Net Proceeds thereof shall be applied to the replacement of the property or facilities so taken, unless the City determines that such property or facility is not necessary to the efficient or proper operation of the Water System and therefore determines not to replace such property or facilities. Any Net Proceeds of such award not applied to replacement or remaining after such work has been completed shall be deposited in the Water Utility Fund and be available for other proper uses of funds deposited in the Water Utility Fund.

Tax Covenants. There shall be included in each Supplement relating to Tax-Exempt Installment Payment Obligations such covenants as are deemed necessary or appropriate by Bond Counsel for the purpose of assuring that interest on such Installment Payment Obligations shall be excluded from gross income under section 103 of the Code.

Subcontracting. Nothing contained in the Installment Purchase Agreement to the contrary shall prevent the City from delegating the power to be an operator of some or all of the Water System, even though the City continues to retain ownership of the Water System and its operations, and no such subcontracting arrangement shall relieve the City of any of its obligations under the Indenture. Prior to the effective date of any such delegation, the City shall deliver to the Trustee an opinion of Bond Counsel to the effect that the proposed delegation will not have an adverse effect on the exclusion from gross income for federal income tax purposes of the interest component of Tax-Exempt Installment Payment Obligations.

Prepayments of Installment Payments

Prepayment of Installment Payments. Provisions may be made in any Supplement for the prepayment of Installment Payments, in whole or in part, in such multiples and in such order of maturity and from funds of any source, and with such prepayment premiums and other terms as are specified in the Supplement. Said Supplement shall also provide for any notices to be given relating to such prepayment.

Events of Default and Remedies of the Corporation

Events of Default and Acceleration of Maturities. If one or more of the following Events of Default shall happen, that is to say:

(a) if default shall be made in the due and punctual payment of or on account of any Parity Obligation as the same shall become due and payable;

(b) if default shall be made by the City in the performance of any of the agreements or covenants required in the Installment Purchase Agreement to be performed by it (other than as specified in subsection (a) above), and such default shall have continued for a period of 60 days after the City shall have been given notice in writing of such default by the Corporation or any Trustee;

(c) if any Event of Default specified in any Supplement, Authorizing Ordinance or Issuing Instrument shall have occurred and be continuing; or

(d) if the City shall file a petition or answer seeking arrangement or reorganization under the federal bankruptcy laws or any other applicable law of the United States of America or any state therein, or if a court of competent jurisdiction shall approve a petition filed with the consent of the City seeking arrangement or reorganization under the federal bankruptcy laws or any other applicable law of the United States of America or any state therein, or if under the provisions of any other law for the relief or aid of debtors any court of competent jurisdiction shall assume custody or control of the City or of the whole or any substantial part of its property;

then, and in each and every such case during the continuance of such Event of Default, the Corporation shall upon the written request of the Owners of 25% or more of the aggregate principal amount of all Series of Parity Installment Obligations Outstanding, voting collectively as a single class, by notice in writing to the City, declare the entire unpaid principal amount thereof and the accrued interest thereon to be due and payable immediately, and upon any such declaration the same shall become immediately due and payable, anything contained in the Installment Purchase Agreement to the contrary notwithstanding; provided, that with respect to a Series of Parity Installment Obligations that is credit enhanced by a Credit Support Instrument, acceleration shall not be effective unless the declaration is consented to by the related Credit Provider. The foregoing provisions, however, are subject to the condition that if at any time after the entire principal amount of all Parity Installment Obligations and the accrued interest thereon shall have been so declared due and payable and before any judgment or decree for the payment of the moneys due shall have been obtained or entered, the City shall deposit with the Corporation a sum sufficient to pay the unpaid principal amount of all such Parity Installment Obligations and the unpaid payments of any other Parity Obligations referred to in clause (a) above due prior to such declaration and the accrued interest thereon, with interest on such overdue installments at the rate or rates applicable thereto in accordance with their terms, and the reasonable expenses of the Corporation, and any and all other defaults known to the Corporation (other than in the payment of the entire principal amount of the unpaid Parity Installment Obligations and the accrued interest thereon due and payable solely by reason of such declaration) shall have been made good or cured to the satisfaction of the Corporation or provision deemed by the Corporation to be adequate shall have been made therefor, then and in every such case the Corporation, by written notice to the City, may rescind and annul such declaration and its consequences; but no such rescission and annulment shall extend to or shall affect any subsequent default or shall impair or exhaust any right or power consequent thereon.

The Owners of Subordinated Obligations may enforce the provisions of the Installment Purchase Agreement for their benefit by appropriate legal proceedings. The payment of Subordinated Obligations will be subordinated in right of payment to payment of the Parity Obligations (except for any payment in respect of Subordinated Obligations from the Reserve Fund securing such Subordinated Obligations). Upon the occurrence and during the continuance of any Event of Default, Owners of Parity Obligations will be entitled to receive payment thereof in full before the Owners of Subordinated Obligations are entitled to receive payment thereof (except for any payment in respect of Subordinated Obligations from the Reserve Fund securing such Subordinated Obligations) and the Owners of the Subordinated

Obligations will become subrogated to the rights of the Owners of Parity Obligations to receive payments with respect thereto.

Application of Net System Revenues Upon Acceleration. All Net System Revenues received after the date of the declaration of acceleration by the Corporation as provided in the Installment Purchase Agreement shall be applied in the following order:

(a) First, to the payment of the costs and expenses of the Corporation and the Trustee, if any, in carrying out the provisions of the Installment Purchase Agreement, including reasonable compensation to its accountants and counsel;

(b) Second, to the payment of the entire principal amount of the unpaid Parity Installment Obligations and the unpaid principal amount of all other Parity Obligations and the accrued interest thereon, with interest on the overdue installments at the rate or rates of interest applicable thereto in accordance with their respective terms. In the event there are insufficient Net System Revenues to pay the entire principal amount of and accrued interest on all Parity Obligations, then accrued interest shall first be paid and any remaining amount shall be paid on account of principal, and in the event there are insufficient Net System Revenues to fully pay either interest or principal in accordance with the foregoing, then payment shall be prorated within a priority based upon the total amounts due in that priority; and

(c) Third, to the payment of the entire principal amount of the unpaid Subordinated Obligations and the accrued interest thereon, with interest on the overdue installments at the rate or rates of interest applicable thereto in accordance with their respective terms. In the event there are insufficient Net System Revenues to pay the entire principal amount of and accrued interest on all Subordinated Obligations, then accrued interest shall first be paid and any remaining amount shall be paid on account of principal, and in the event there are insufficient Net System Revenues to fully pay either interest or principal in accordance with the foregoing, then payment shall be prorated within a priority based upon the total amounts due in that priority.

Discharge of Installment Payment Obligations

Discharge of Installment Payment Obligations. If the City shall pay or cause to be paid or there shall otherwise be paid to the Owners all Outstanding Installment Payment Obligations of a Series, the principal thereof and the interest and redemption premiums, if any, thereon or if all such Outstanding Installment Payment Obligations shall be deemed to have been paid at the times and in the manner stipulated in the applicable Issuing Instrument, then, as to any such Series, all agreements, covenants and other obligations of the City under the Indenture shall thereupon cease, terminate and become void and be discharged and satisfied, except for the obligation of the City to pay or cause to be paid all sums due under the Installment Purchase Agreement.

Miscellaneous

Liability of City Limited to System Revenues.

(a) Notwithstanding anything contained in the Installment Purchase Agreement, the City shall not be required to advance any moneys derived from any source of income other than the Net System Revenues and the other funds provided in the Installment Purchase Agreement for the payment of the Installment Payments or for the performance of any other agreements or covenants required to be performed by it contained in the Installment Purchase Agreement. The City may, however, but in no event shall be obligated to, advance moneys for any such purpose so long as such moneys are derived from a source legally available for such purpose and may be legally used by the City for such purpose.

(b) The obligation of the City to make the Installment Payments is a special obligation of the City payable solely from such Net System Revenues and other funds provided for in the Installment Purchase Agreement, and does not constitute a debt of the City or of the State or of any political subdivision thereof within the meaning of any constitutional or statutory debt limitation or restriction.

Amendments.

(a) The Installment Purchase Agreement may be amended with respect to a Series of Installment Payment Obligations in writing as may be mutually agreed by the City and the Corporation, with the written consent of any Credit Provider for any Installment Payment Obligations or, as to Installment Obligations for which there is no Credit Support Instrument, the Owners of a majority in aggregate principal amount of such Series of Installment Payment Obligations then Outstanding, provided that no such amendment shall (1) extend the payment date of any Installment Payment, or reduce the amount of any Installment Payment without the prior written consent of the Owner of each Obligation so affected; or (2) reduce the percentage of Installment Payment Obligations the consent of the Owners of which is required for the execution of any amendment of the Installment Purchase Agreement without the prior written consent of each of the Owners so affected.

(b) The Installment Purchase Agreement and the rights and obligations of the City and the Corporation thereunder may also be amended for supplemented at any time by an amendment or supplement to the Installment Purchase Agreement that shall not adversely affect the interests of the Owners of the Installment Payment Obligations and that shall become binding upon execution by the City and the Corporation, without the written consents of any Owner of Installment Payment Obligations or any Credit Provider, but only to the extent permitted by law and only upon receipt of an unqualified opinion of Bond Counsel to the effect that such amendment or supplement is permitted by the provisions of the Installment Purchase Agreement and is not inconsistent with the Installment Purchase Agreement and does not adversely affect the exclusion of the interest portion of the Installment Payments received by the Owners from gross income for federal income tax purposes, and only for any one or more of the following purposes:

(1) to add to the covenants and agreements of the Corporation or the City contained in the Installment Purchase Agreement other covenants and agreements thereafter to be observed or to surrender any right or power in the Installment Purchase Agreement reserved to or conferred upon the Corporation or the City;

(2) to cure, correct or supplement any ambiguous or defective provision contained in the Installment Purchase Agreement or in regard to questions arising under the Installment Purchase Agreement, as the Corporation or the City may deem necessary or desirable;

(3) to make other amendments or modifications that shall not materially adversely affect the interests of the Owners of the Installment Payment Obligations;

(4) to provide for the issuance of Parity Installment Payment Obligations; and

(5) to provide for the issuance of Subordinated Obligations.

Net Contract. The Installment Purchase Agreement shall be deemed and construed to be a net contract, and the City shall pay absolutely net during the term thereof the Installment Payments arid all other payments required under the Indenture, free of any deductions and without abatement, diminution or setoff whatsoever.

2010A SUPPLEMENT

The 2010A Supplement to Amended and Restated Master Installment Purchase Agreement (the "2010A Supplement"), sets forth certain terms and conditions of the purchase of the Refunded Components of the Project by the City. Certain definitions and provisions of the 2010A Supplement are given and summarized below.

Selected Definitions.

Interest Portion

The term "Interest Portion" means the interest portion of 2010A Installment Payments specified in the 2010A Supplement.

Principal Portion

The term "Principal Portion" means the principal portion of 2010A Installment Payments specified in the 2010A Supplement.

Refunded Components

The term "Refunded Components" means the Components of the Project specified in Exhibit A attached to the 2010A Supplement and by reference made a part thereof, which Components comprise a portion of the original 1998 Project, for which Components the City will be making 2010A Installment Payments.

2010A Installment Payment Date

The term "2010A Installment Payment Date" means the 15^{th} day of the calendar month immediately preceding each Interest Payment Date for the 2010A Bonds.

2010A Installment Payments

The term "2010A Installment Payments" means the Installment Payments specified in the 2010A Supplement that are to pay the Purchase Price of the Refunded Components in accordance with the terms of the 2010A Supplement.

General. Pursuant to the 2010A Supplement, the City agrees to purchase the Refunded Components from the Corporation, and to pay the 2010A Installment Payments therefor. See the caption, "SECURITY AND SOURCES OF PAYMENT FOR THE SERIES 2010A BONDS – Pledge of Revenues; Installment Payments" in this Official Statement.

Additional Covenants relating to Tax Exemption.

(a) The City shall not directly or indirectly use or permit the use of any proceeds of the 2010A Bonds or any other funds of the City or of the Refunded Components or take or omit to take any action that would cause the 2010A Bonds to be "private activity bonds" within the meaning of Section 141 of the Code, or obligations that are "federally guaranteed" within the meaning of Section 149(b) of the Code.

(b) The City covenants that it will not take any action, or fail to take any action, if any such action or failure to take action would adversely affect the exclusion from gross income of the interest on the 2010A Bonds under Section 103 of the Code. The City shall not directly or indirectly use or permit the use of any proceeds of the 2010A Bonds or any other funds of the City, or take or omit to take any action, that would cause the 2010A Bonds to be "arbitrage bonds" within the meaning of Section 148(a) of the Code. To that end, the City shall comply with all requirements of Section 148 of the Code to the extent applicable to the 2010A Bonds. If, at any time, the City is of the opinion that for purposes of this section it is necessary to restrict or limit the yield on the investment of any moneys held by the Trustee under the Indenture or otherwise, then the City shall so instruct the Trustee in writing, and shall cause the Trustee to take such action as may be necessary in accordance with such instructions.

(c) Without limiting the generality of the foregoing, the City agrees that there shall be paid from time to time all amounts required to be rebated to the United States of America pursuant to Section 148(f) of the Code and any Treasury Regulations promulgated thereunder as may be applicable to the 2010A Bonds from time to time. This covenant shall survive payment in full or defeasance of the 2010A Bonds. The City specifically covenants to pay or cause to be paid to the United States of America at the times and in the amounts determined under this Section the rebate requirement, as described in the Tax Certificate, and to otherwise comply with the provisions of the Tax Certificate executed by the City and the Authority in connection with the execution and delivery of the 2010A Bonds.

(d) Notwithstanding any above provision, if the City provides to the Trustee an opinion of Bond Counsel to the effect that any action required under this section is no longer required, or to the effect that some further action is required, to maintain the exclusion from gross income of the interest on the 2010A Bonds pursuant to Section 103 of the Code, then the City may rely conclusively on such opinion in complying with the provisions in the Installment Purchase Agreement, and the covenants thereunder shall be deemed to be modified to that extent.

Continuing Disclosure. The City covenants and agrees in the 2010A Supplement that it will comply with and carry out all of the provisions of the Continuing Disclosure Certificate to be executed and delivered by the City in connection with the issuance of the 2010A Bonds. Notwithstanding any other provision of the 2010A Supplement, failure of the City to comply with the Continuing Disclosure Certificate shall not be considered a default of any kind under the 2010A Supplement; provided, however, that the Trustee may (and, at the request of any participating underwriter or the Owners of at least twenty-five percent (25%) in aggregate principal amount of the Outstanding 2010A Bonds, shall), or any Owner or Beneficial Owner may, take such actions as may be necessary and appropriate, including seeking mandate or specific performance by court order, to cause the City to comply with its obligations under such Continuing Disclosure Certificate. For purposes of this paragraph, "Beneficial Owner" means any person that has or shares the power, directly or indirectly, to make investment decisions concerning ownership of any 2010A Bond (including, any persons holding any 2010A Bond through nominees, depositories, or other intermediaries).

ASSIGNMENT AGREEMENT

The Assignment Agreement provides for the granting, sale, assignment, and transfer by the Corporation to the Authority, for the benefit of the Owners of the 2010A Bonds, all of the Corporation's right, title, and interest in and to the 2010A Supplement, including, without limitation, its right to receive the 2010A Installment Payments to be paid by the City under and pursuant to the 2010A Supplement. The Authority accepts such assignment for the benefit of the Owners of the 2010A Bonds, subject to the terms and provisions of the Indenture.

APPENDIX C

FORM OF BOND COUNSEL OPINION

[Closing Date]

Board of Commissioners
Public Facilities Financing Authority
of the City of San Diego
San Diego, California

$123,075,000
Public Facilities Financing Authority of the City of San Diego
Water Revenue Bonds, Refunding Series 2010A
(Payable Solely From Installment Payments
Secured by Net System Revenues of the Water Utility Fund)
(Final Opinion)

Ladies and Gentlemen:

We have acted as Bond Counsel to the Public Facilities Financing Authority of the City of San Diego (the "Authority") in connection with the issuance by the Authority of $123,075,000 aggregate principal amount of the Public Facilities Financing Authority of the City of San Diego Water Revenue Bonds, Refunding Series 2010A (Payable Solely From Installment Payments Secured by Net System Revenues of the Water Utility Fund) (the "Bonds"), pursuant to Article 11 (commencing with Section 53580) of Chapter 3 of Part 1 of Division 2 of Title 5 of the California Government Code and the Indenture, dated as of January 1, 2009, as amended and supplemented by the First Supplemental Indenture, dated as of June 1, 2009, and by the Second Supplemental Indenture, dated as of June 1, 2010 (collectively, the "Indenture"), each by and between the Authority and Wells Fargo Bank, National Association, as Trustee (the "Trustee"). Capitalized terms not otherwise defined herein shall have the meanings ascribed to them in the Indenture and in the Amended and Restated Master Installment Purchase Agreement, dated as of January 1, 2009 (the "Master Installment Purchase Agreement"), as supplemented prior to the date hereof and as supplemented by the 2010A Supplement to Amended and Restated Master Installment Purchase Agreement, dated as of June 1, 2010 (the "2010A Supplement"), each by and between the City and the San Diego Facilities and Equipment Leasing Corporation (the "Corporation"), as applicable.

In such connection, we have reviewed the Indenture, the Master Installment Purchase Agreement, the 2010A Supplement, the Assignment Agreement, dated as of June 1, 2010 (the "Assignment Agreement"), by and between the Authority and the Trustee, the Tax Certificate of the City and the Authority, dated the date hereof (the "Tax Certificate"), opinions of the City Attorney, certifications of the City, the Authority, the Corporation, and others, and such other documents, opinions, and matters to the extent we deemed necessary to render the opinions set forth herein.

The opinions expressed herein are expressed only on and as of the date hereof and are based on an analysis of existing laws, regulations, rulings, and judicial decisions and cover certain matters not directly addressed by such authorities. Such opinions may be affected by actions taken or omitted or events occurring after the date hereof. Changes to existing law may occur hereafter and could have retroactive effect. We have not undertaken to determine, or to inform any person, whether any such actions are taken or omitted or events do occur. Our engagement with respect to the Bonds has concluded with their issuance, and we disclaim any obligation to update this opinion. We have assumed the genuineness of all documents and signatures presented to us (whether as originals or copies) and the due and legal execution and delivery thereof by, and validity against, all parties thereto. We have not undertaken to verify independently, and have assumed, the accuracy of the factual matters represented, warranted, or certified in the documents, and of the legal conclusions contained in the opinions referred to in the second paragraph hereof.

Furthermore, we have assumed compliance with all covenants and agreements contained in the Indenture, the Master Installment Purchase Agreement, the 2010A Supplement, the Assignment Agreement, and the Tax Certificate, including (without limitation) covenants and agreements compliance with which is necessary to ensure that future actions, omissions, or events will not cause interest on the Bonds to be included in gross income for federal income tax purposes. In addition, we call attention to the fact that the rights and obligations under the Bonds, the Indenture, the Master Installment Purchase Agreement, the 2010A Supplement, the Assignment Agreement, and the Tax Certificate and their enforceability may be subject to bankruptcy, insolvency, reorganization, arrangement, fraudulent conveyance, moratorium, and other similar laws relating to or affecting creditors' rights, to the application of equitable principles, to the exercise of judicial discretion in appropriate cases, and to the limitations on legal remedies against cities, joint powers authorities, and nonprofit public benefit corporations in the State of California. We express no opinion with respect to any indemnification, contribution, penalty, choice of law, choice of forum, choice of venue, severability, or waiver provisions contained in the documents mentioned in the previous sentence.

We undertake no responsibility for the accuracy, completeness, or fairness of the Official Statement or other offering material relating to the Bonds and express no opinion with respect thereto. We express no opinion regarding the perfection or priority of the lien on the 2010A Installment Payments or the Net System Revenues.

Based on and subject to the foregoing, and in reliance thereon, as of the date hereof, we are of the following opinions:

1. The 2010A Supplement has been duly executed and delivered by the City and the obligation of the City to pay the 2010A Installment Payments under the 2010A Supplement constitutes a valid and binding limited obligation of the City. The Master Installment Purchase Agreement, as supplemented by the 2010A Supplement, creates a valid pledge, to secure the payment of the 2010A Installment Payments, of the Net System Revenues.

2. The Second Supplemental Indenture has been duly executed and delivered by, and constitutes a valid and binding limited obligation of, the Authority. The Indenture creates a valid pledge, to secure the payment of the principal of and interest on the Bonds, of the 2010A Installment Payments. The Bonds constitute the valid and binding limited obligations of the Authority.

3. Interest on the Bonds is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986, as amended (the "Code"), and is exempt from State of California personal income taxes. Interest on the Bonds is not a specific preference item for purposes of the federal individual or corporate alternative minimum taxes, although we observe that such interest is included in adjusted current earnings in calculating federal corporate alternative minimum taxable income.

Except as stated in paragraph 3 above, we express no opinion as to federal or State of California tax consequences of the ownership of the Bonds. We also express no opinion regarding any other tax consequences with respect to the acquisition, ownership, or disposition of, or the accrual or receipt of interest on, the Bonds.

Respectfully submitted,

APPENDIX D

FORM OF CONTINUING DISCLOSURE CERTIFICATE

This Continuing Disclosure Certificate, dated as of June 1, 2010 (the "Disclosure Certificate"), is executed and delivered by the City of San Diego (the "City") in connection with the issuance by the Public Facilities Financing Authority of the City of San Diego (the "Authority") of $123,075,000 Public Facilities Financing Authority of the City of San Diego Water Revenue Bonds, Refunding Series 2010A (Payable Solely From Installment Payments Secured by Net System Revenues of the Water Utility Fund) (the "2010A Bonds"). The 2010A Bonds are being issued pursuant to that certain Indenture, dated as of January 1, 2009, as amended and supplemented by the First Supplemental Indenture, dated as of June 1, 2009, and by the Second Supplemental Indenture, dated as of June 1, 2010 (collectively, the "Indenture"), each by and between the Authority and Wells Fargo Bank, National Association, as trustee. The proceeds of the 2010A Bonds are being used to (i) prepay all of the outstanding 1998 Certificates and (ii) pay costs of issuance with respect to the 2010A Bonds. In connection therewith, the City, as an "obligated person" with respect to the 2010A Bonds (within the meaning of the Rule, as defined herein), covenants and agrees as follows:

Section 1. Purpose of the Disclosure Certificate. This Disclosure Certificate is being executed and delivered by the City for the benefit of the holders and beneficial owners of the 2010A Bonds and in order to assist the Participating Underwriter in complying with the Rule.

Section 2. Definitions. In addition to the definitions set forth in the Indenture, which apply to any capitalized term used in this Disclosure Certificate unless otherwise defined in this Section, the following capitalized terms shall have the following meanings:

"Annual Report" shall mean any Annual Report provided by the City pursuant to, and as described in, Sections 3 and 4 of this Disclosure Certificate.

"Dissemination Agent" shall mean the City, acting in its capacity as Dissemination Agent hereunder, or any successor Dissemination Agent designated in writing by the City and which has filed with the City and the then-current Dissemination Agent a written acceptance of such designation.

"Listed Events" shall mean any of the events listed in Section 5(a) of this Disclosure Certificate.

"MSRB" shall mean the Municipal Securities Rulemaking Board established pursuant to Section 15B(b)(1) of the Securities Exchange Act of 1934, as amended.

"Official Statement" shall mean the Official Statement, dated June 16, 2010, relating to the 2010A Bonds.

"Participating Underwriter" shall mean any of the original Underwriters of the 2010A Bonds required to comply with the Rule in connection with offering of the 2010A Bonds.

"Rule" shall mean Rule 15c2-12(b)(5) adopted by the SEC under the Securities Exchange Act of 1934, as the same may be amended from time to time.

"SEC" shall mean the Securities and Exchange Commission.

Section 3. Provision of Annual Reports.

(a) The City shall, or upon written direction shall cause the Dissemination Agent to, not later than 270 days after the end of the City's Fiscal Year (which currently ends June 30), commencing with the report for the 2010 Fiscal Year (each, a "Filing Date"), provide to the MSRB an Annual Report that is consistent with the requirements of Section 4 of this Disclosure Certificate for so long as the 2010A Bonds remain Outstanding. The Annual Report must be submitted in an electronic format as prescribed by the MSRB, accompanied by such identifying information as is prescribed by the MSRB. Not later than fifteen (15) Business Days prior to each Filing Date, the City shall provide the Annual Report to the Dissemination Agent (if other than the City). The Annual Report may be submitted as a single document or as separate documents comprising a package, and may include by reference other information as provided in Section 4 of this Disclosure Certificate; provided that the audited financial statements of the City may be submitted separately from the balance of the Annual Report, and later than the Filing Date for the filing of the Annual Report if not available by such Filing Date. If the City's Fiscal Year changes, it shall give notice of such change in the same manner as for a Listed Event under Section 5(c) hereof. The City shall provide a written certification with each Annual Report furnished to the Dissemination Agent to the effect that such Annual Report constitutes the Annual Report required to be furnished by it hereunder. The Dissemination Agent may conclusively rely upon such certification of the City and shall have no duty or obligation to review such Annual Report.

(b) If the City is unable to provide to the MSRB an Annual Report by the date required in subsection (a), the City shall send a notice to the MSRB in substantially the form attached as Exhibit A. Such notice must be submitted in an electronic format as prescribed by the MSRB, accompanied by such identifying information as is prescribed by the MSRB.

(c) The Dissemination Agent shall:

(i) file the Annual Report with the MSRB; and

(ii) if the Dissemination Agent is other than the City, and such information is available to it, file a report with the City certifying that the Annual Report has been provided to the MSRB pursuant to this Disclosure Certificate, and stating the date the Annual Report was so provided.

Section 4. Content of Annual Reports. The City's Annual Report shall contain or incorporate by reference the following:

(a) The audited financial statements for the most recently completed Fiscal Year prepared in accordance with generally accepted accounting principles as promulgated to apply to governmental entities from time to time by the Governmental Accounting Standards Board. If the City's audited financial statements are not available by the time the Annual Report is required to be filed pursuant to Section 3(a), the Annual Report shall contain unaudited financial statements in a format similar to the financial statements contained in the final Official Statement, if any, and the audited financial statements shall be filed in the same manner as the Annual Report when they become available.

(b) Financial information and operating data with respect to the City, as such information and data relate to the City's Public Utilities Department and the Water Utility Fund, for the most recently completed Fiscal Year of the type included in the Official Statement, in the following categories (to the extent not included in the City's audited financial statements):

(i) An update of the information contained in Table 1 (entitled "Historical Number of Retail Connections to Water System") of the Official Statement for the most recently completed Fiscal Year;

(ii) An update of the information contained in Table 2 (entitled "Major Non-Governmental Retail Customers and Top Governmental Customers") of the Official Statement for the most recently completed Fiscal Year;

(iii) An update of the information contained in Table 6 (entitled "Projected Water Supply Sources") of the Official Statement for the most recently completed Fiscal Year;

(iv) An update of the information contained in Table 7 (entitled "Summary of Projected CIP Projects") of the Official Statement as of the end of the most recently completed Fiscal Year;

(v) An update of the information contained in Table 8 (entitled "Five-Year Water Service Charge History for Single Family Residential, Multi-Family, Commercial, Industrial, Irrigation, and Temporary Construction") of the Official Statement for the most recently completed Fiscal Year;

(vi) An update of the information contained in Table 11 (entitled "Recent Rate History for Water Capacity Charges") of the Official Statement for the most recently completed Fiscal Year;

(vii) An update of the information contained in Table 12 (entitled "Water Utility Fund Historical Capacity Charge Revenues") of the Official Statement for the most recently completed Fiscal Year;

(viii) An update of the information contained in Table 13 (entitled "Water Customer Accounts Receivable and Shut-Offs by Fiscal Year") of the Official Statement for the most recently completed Fiscal Year;

(ix) An update of the information contained in Table 14 (entitled "Historical Sources of Water Sales Revenues") of the Official Statement for the most recently completed Fiscal Year;

(x) An update of the information contained in Table 15 (entitled "Statements of Revenues, Expenses, and Changes in Fund Net Assets") of the Official Statement for the most recently completed Fiscal Year;

(xi) An update of the information contained in Table 16 (entitled "Calculation of Historic Debt Service Coverage") of the Official Statement for the most recently completed Fiscal Year;

(xii) An update of the information contained in Table 17 (entitled "Water Utility Cash and Cash Equivalents (Including Reserves)") of the Official Statement for the most recently completed Fiscal Year;

(xiii) An update of the information contained in Table 22 (entitled "City of San Diego Pooled Investment Fund") of the Official Statement as of the most recently completed Fiscal Year;

(xiv) An update of the information contained in Table 23 (entitled "City of San Diego Schedule of Funding Progress") of the Official Statement for the most recently completed Fiscal Year;

(xv) An update of the information contained in Table 24 (entitled "City of San Diego and Water Utility Fund Pension Contribution") of the Official Statement for the most recently completed Fiscal Year;

(xvi) An update of the information contained in Table 25 (entitled "Water System Retiree Health Contribution") of the Official Statement for the most recently completed Fiscal Year; and

(xvii) An update of the information contained in the Official Statement under the heading "WATER SYSTEM FINANCIAL OPERATIONS – Labor Relations" for the most recently completed Fiscal Year.

Any or all of the items listed above may be included by specific reference to other documents, including official statements of debt issues of the City or related public entities, that are available to the public on the MSRB's Internet web site or filed with the SEC. If the document included by reference is a final official statement, it must be available from the MSRB. The City shall clearly identify each such other document so included by reference.

Section 5. Reporting of Significant Events.

(a) Pursuant to the provisions of this Section 5, the City shall give, or cause to be given, notice of the occurrence of any of the following events with respect to the 2010A Bonds, if material:

(i) Principal and interest payment delinquencies.

(ii) Non-payment related defaults.

(iii) Unscheduled draws on debt service reserves reflecting financial difficulties.

(iv) Unscheduled draws on credit enhancements reflecting financial difficulties.

(v) Substitution of credit or liquidity providers, or their failure to perform.

(vi) Adverse tax opinions or events affecting the tax-exempt status of the 2010A Bonds.

(vii) Modifications to rights of the owners of the 2010A Bonds.

(viii) Contingent or unscheduled 2010A Bond calls.

(ix) Defeasances.

(x) Release, substitution, or sale of property securing repayment of the 2010A Bonds.

(xi) Rating changes.

(b) Whenever the City obtains knowledge of the occurrence of a Listed Event, the City shall as soon as possible determine if such event would be material under applicable federal securities law.

(c) If the City determines that knowledge of the occurrence of a Listed Event would be material under applicable federal securities law, the City shall promptly file a notice of such occurrence with the MSRB. Such notice must be submitted in an electronic format as prescribed by the MSRB, accompanied by such identifying information as is prescribed by the MSRB. Notwithstanding the foregoing, notice of Listed Events described in subsections (a) (viii) and (ix) need not be given under this subsection any earlier than the notice (if any) of the underlying event is given to holders of affected 2010A Bonds pursuant to the Indenture.

(d) If the Dissemination Agent has been instructed by the City to report the occurrence of a Listed Event, the Trustee shall file a notice of such occurrence with the MSRB with a copy to the City. Such notice must be submitted in an electronic format as prescribed by the MSRB, accompanied by such identifying information as is prescribed by the MSRB. Notwithstanding the foregoing, notice of Listed Events described in subsections (a) (viii) and (ix) need not be given under this subsection any earlier than the notice (if any) of the underlying event is given to the holders of affected 2010A Bonds pursuant to the Indenture.

Section 6. Termination of Reporting Obligation. The City's obligations under this Disclosure Certificate shall terminate upon the legal defeasance, prior redemption, or payment in full of all of the 2010A Bonds. If such termination occurs prior to the final maturity of the 2010A Bonds, the City shall give notice of such termination in the same manner as for a Listed Event under Section 5(c).

Section 7. Dissemination Agent. The City may, from time to time, appoint or engage a Dissemination Agent to assist it in carrying out its obligations under this Disclosure Certificate, and may discharge any such Dissemination Agent, with or without appointing a successor Dissemination Agent. The initial Dissemination Agent shall be the City. The Dissemination Agent may resign as Dissemination Agent by providing thirty (30) days written notice to the City. The Dissemination Agent shall not be responsible for the content of any report or notice prepared by the City. The Dissemination Agent shall have no duty to prepare any information report nor shall the Dissemination Agent be responsible for filing any report not provided to it by the City in a timely manner and in a form suitable for filing.

Section 8. Amendment; Waiver. Notwithstanding any other provision of this Disclosure Certificate, the City may amend this Disclosure Certificate and any provision of this Disclosure Certificate may be waived (provided no amendment that modifies or increases its duties or obligations of the Dissemination Agent shall be effective without the consent of the Dissemination Agent), provided that the following conditions are satisfied:

(a) if the amendment or waiver relates to the provisions of Sections 3(a), 4, or 5(a), it may only be made in connection with a change in circumstances that arises from a change in legal requirements, change in law, or change in the identity, nature, or status of an obligated person with respect to the 2010A Bonds, or type of business conducted;

(b) the undertakings herein, as proposed to be amended or waived, would, in the opinion of nationally recognized bond counsel, have complied with the requirements of the Rule at the time of the primary offering of the 2010A Bonds, after taking into account any amendments or interpretations of the Rule, as well as any change in circumstances; and

(c) the proposed amendment or waiver either (i) is approved by holders of the 2010A Bonds in the manner provided in the Indenture for amendments to the Indenture with the consent of holders, or

(ii) does not, in the opinion of nationally recognized bond counsel, materially impair the interests of the holders or beneficial owners of the 2010A Bonds.

If the annual financial information or operating data to be provided in the Annual Report is amended pursuant to the provisions hereof, the first annual financial information filed pursuant hereto containing the amended operating data or financial information shall explain, in narrative form, the reasons for the amendment and the impact of the change in the type of operating data or financial information being provided.

If an amendment is made to the undertaking specifying the accounting principles to be followed in preparing financial statements, the annual financial information for the year in which the change is made shall present a comparison between the financial statements or information prepared on the basis of the new accounting principles and those prepared on the basis of the former accounting principles. The comparison shall include a qualitative discussion of the differences in the accounting principles and the impact of the change in the accounting principles on the presentation of the financial information, in order to provide information to investors to enable them to evaluate the ability of the City to meet its obligations. To the extent reasonably feasible, the comparison shall be quantitative. A notice of the change in the accounting principles shall be sent to the MSRB in the same manner as for a Listed Event under Section 5(c).

Section 9. Additional Information. Nothing in this Disclosure Certificate shall be deemed to prevent the City from disseminating any other information, using the means of dissemination set forth in this Disclosure Certificate or any other means of communication, or including any other information in any Annual Report or notice of occurrence of a Listed Event, in addition to that which is required by this Disclosure Certificate. If the City chooses to include any information in any Annual Report or notice of occurrence of a Listed Event in addition to that which is specifically required by this Disclosure Certificate, the City shall have no obligation under this Disclosure Certificate to update such information or include it in any future Annual Report or notice of the occurrence of a Listed Event.

Section 10. Default. In the event of a failure of the City to comply with any provision of this Disclosure Certificate, any Participating Underwriter or any holder or beneficial owner of the 2010A Bonds may take such actions as may be necessary and appropriate, including seeking mandate or specific performance by court order, to cause the City to comply with its obligations under this Disclosure Certificate. A default under this Disclosure Certificate shall not be deemed an Event of Default under the Indenture, and the sole remedy under this Disclosure Certificate in the event of any failure of the City to comply with this Disclosure Certificate shall be an action to compel performance.

Section 11. Duties, Immunities and Liabilities of Dissemination Agent. The Dissemination Agent shall have only such duties as are specifically set forth in this Disclosure Certificate, and the City agrees to indemnify and save the Dissemination Agent, its officers, directors, employees, and agents harmless against any loss, expense, and liabilities that it may incur arising out of or in the exercise or performance of its powers and duties hereunder, including the costs and expenses (including attorneys fees) of defending against any claim of liability, but excluding liabilities due to the Dissemination Agent's negligence or willful misconduct. The Dissemination Agent shall be paid compensation by the City for its services provided hereunder in accordance with its schedule of fees as amended from time to time and shall be reimbursed for all expenses, legal fees, and advances made or incurred by the Dissemination Agent in the performance of its duties hereunder. The Dissemination Agent shall have no duty or obligation to review any information provided to it hereunder and shall not be deemed to be acting in any fiduciary capacity for the City, the Authority, the owners of the 2010A Bonds, or any other party. Other than in the case of negligence, gross negligence, or willful misconduct of the Dissemination Agent, the Dissemination Agent shall not have any liability to the owners of the 2010A Bonds or any other party for any monetary damages or financial liability of any kind whatsoever related to or arising from any breach of any obligation of the Dissemination Agent. The obligations of the City under this Section shall survive resignation or removal of the Dissemination Agent and payment of the 2010A Bonds.

Section 12. Beneficiaries. This Disclosure Certificate shall inure solely to the benefit of the City, the Dissemination Agent, each Participating Underwriter, and holders and beneficial owners from time to time of the 2010A Bonds, and shall create no rights in any other person or entity.

THE CITY OF SAN DIEGO

By:_______________________________

Attest:

____
City Clerk

APPROVED AS TO FORM:

JAN I. GOLDSMITH, City Attorney

By: __________________________
Name: ________________________
Deputy City Attorney

EXHIBIT A

NOTICE TO MSRB OF FAILURE TO FILE ANNUAL REPORT

Name of Obligor:	The City of San Diego
Name of Issue:	Public Facilities Financing Authority of the City of San Diego Water Revenue Bonds, Refunding Series 2010A (Payable Solely From Installment Payments Secured by Net System Revenues of the Water Utility Fund)
Date of Issuance:	[Closing Date]

NOTICE IS HEREBY GIVEN that the City of San Diego (the "City") has not provided an Annual Report with respect to the above-named Bonds as required by Section 3 of the Continuing Disclosure Certificate, dated as of June 1, 2010, executed and delivered by the City. The City anticipates that the Annual Report will be filed by ___________.

Dated: ____________________

THE CITY OF SAN DIEGO

By:________________________________

APPENDIX E

INFORMATION REGARDING THE BOOK-ENTRY ONLY SYSTEM

The following description of DTC and its book-entry system has been provided by DTC and has not been verified for accuracy or completeness by the City or the Authority, and neither the City nor the Authority shall have any liability with respect thereto. Neither the City nor the Authority shall have any responsibility or liability for any aspects of the records maintained by DTC relating to or payments made on account of beneficial ownership, or for maintaining, supervising, or reviewing any records maintained by DTC relating to beneficial ownership, of interests in the 2010A Bonds.

DTC will act as securities depository for the 2010A Bonds. The 2010A Bonds will be issued as fully-registered securities registered in the name of Cede & Co. (DTC's partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered certificate will be issued for the 2010A Bonds in the aggregate principal amount of such issue, and will be deposited with DTC.

DTC, the world's largest securities depository, is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of the New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 3.5 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments (from over 100 countries) that DTC's participants ("Direct Participants") deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants' accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation ("DTCC"). DTCC is the holding company for DTC, National Securities Clearing Corporation, and Fixed Income Clearing Corporation, all of which are registered clearing agencies. DTCC is owned by the users of its regulated subsidiaries. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). DTC has Standard & Poor's highest rating: AAA. The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtcc.com and www.dtc.org.

Purchases of the 2010A Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the 2010A Bonds on DTC's records. The ownership interest of each actual purchaser of each Security ("Beneficial Owner") is in turn to be recorded on the Direct and Indirect Participants' records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the 2010A Bonds are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in 2010A Bonds, except in the event that use of the book-entry system for the 2010A Bonds is discontinued.

To facilitate subsequent transfers, all 2010A Bonds deposited by Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of 2010A Bonds with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the 2010A Bonds; DTC's records reflect only the identity of the Direct Participants to whose accounts such 2010A Bonds are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time. Beneficial Owners of 2010A Bonds may wish to take certain steps to augment the transmission to them of notices of significant events with respect to the 2010A Bonds, such as redemptions, tenders, defaults, and proposed amendments to the 2010A Bond documents. For example, Beneficial Owners of 2010A Bonds may wish to ascertain that the nominee holding the 2010A Bonds for their benefit has agreed to obtain and transmit notices to Beneficial Owners. In the alternative, Beneficial Owners may wish to provide their names and addresses to the registrar and request that copies of notices be provided directly to them.

Redemption notices shall be sent to DTC. If less than all of the 2010A Bonds within an issue are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such issue to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to 2010A Bonds unless authorized by a Direct Participant in accordance with DTC's MMI Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the City as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts 2010A Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Redemption proceeds, distributions, and dividend payments on the 2010A Bonds will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the City or the Trustee, on payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC, the Trustee, or the City, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of redemption proceeds, distributions, and dividend payments to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the City or the Trustee, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

DTC may discontinue providing its services as depository with respect to the 2010A Bonds at any time by giving reasonable notice to the City or the Trustee. Under such circumstances, in the event that a successor depository is not obtained, 2010A Bond certificates are required to be printed and delivered.

The City may decide to discontinue use of the system of book-entry-only transfers through DTC (or a successor securities depository). In that event, Security certificates will be printed and delivered to DTC.

The information in this section concerning DTC and DTC's book-entry system has been obtained from sources that the City believes to be reliable, but the City takes no responsibility for the accuracy thereof.