STANDARD & POOR'S

RatingsDirect®

June 15, 2009

Summary:

San Diego, California; Note

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Credit Profile		
US$55.795 mil 2009-10 TRANs ser B dtd 07/01/2009 due 01/29/2010		
Short Term Rating	SP-1	New
US$49.605 mil 2009-10 TRANs ser C dtd 07/01/2009 due 04/30/2010		
Short Term Rating	SP-1	New
US$18.6 mil 2009-10 TRANs ser A dtd 07/01/2009 due 12/31/2009		
Short Term Rating	SP-1	New

Rationale

Standard & Poor's Ratings Services has assigned its 'SP-1' short-term rating to each of San Diego, Calif.'s series 2009-2010 series A ($18.6 million), series B ($55.8 million), and series C ($49.6 million) tax and revenue anticipation notes (TRANs).

The ratings reflect our opinion of:

- The city's underlying credit characteristics (underlying rating: A/Positive) and its proactive measures to adjust expenditures to balance its budget in fiscal 2009 as revenue has declined;
- Adequate projected TRANs debt service coverage by total net available ending cash fund balances, including general fund and policy fund cash, at each of the maturity dates. This somewhat mitigates inadequate coverage from projected pledged net general fund cash balances alone; and
- Strong projected TRANs debt service coverage by cash balances when including existing alternate liquidity in the city's enterprise funds.

Although cash balances (including policy fund cash and alternate liquidity from San Diego's enterprise funds) support what we consider a strong capacity to pay, these funds are not part of the pledged revenue as per the resolution. Furthermore, city officials indicate permanent transfers of policy fund cash, although legally available for TRANs repayment, would require council action, as would any transfers from the enterprise funds.

According to the resolution, on and after the set-aside dates, the city comptroller will deposit into the note repayment fund taxes, income, revenue, cash receipts, and other money chargeable to the general fund, attributable to fiscal 2010, and lawfully available for payment. If this does not repay the notes, they are payable from any other lawfully available funds.

- The series 2009-10A TRANs are secured by the first unrestricted revenues chargeable to the city's general fund to be received on and after Dec. 10, 2009, and mature Dec. 31.
- The series 2009-10B TRANs are secured by the first unrestricted general fund revenues received on and after Jan. 1, 2010, and mature Jan. 29.
- The series 2009-10C TRANS are secured by the first unrestricted general fund revenues received on and after April 1, 2010 and mature April 30.

Although the legal pledge refers to first money to the general fund, according to our short-term debt criteria, Standard & Poor's calculates debt service coverage by measuring debt service due against available cash balances at month's end, after paying out normal operating expenditures and not including proceeds from additional note borrowings.

San Diego's projected net general fund cash balances at the Dec. 31, 2009, Jan. 29, 2010, and April 30, 2010, maturity dates do not include a potential $60 million of lost revenue from state cuts, which we believe are likely in fiscal 2010 given California's budget situation. In fiscal 2010, with the state's proposition 1A borrowing, San Diego estimates about $36 million of annual property taxes could be affected, as well as another $24 million of gas tax revenue for the general fund. The city has identified another $15.5 million of Proposition 42 funds that the state could cut, but officials have indicated that these are not included in the general fund or policy fund cash flows and would not impair projected coverage levels. The timing of a state take-away of cash receipts is unknown. Stressing the ending general fund cash balances at each of the maturity dates by the total annual $60 million of potential lost revenue in fiscal 2010, in our view, these stressed coverage levels could fall to negative 2.8x, negative 0.22x, and 0.25x for series A, B, and C, respectively, at each maturity date, depending on the timing of the lost revenue.

San Diego has also included policy fund cash in its cash flows that it indicates were originally funded with general fund money and are unrestricted and lawfully available for TRANs repayment. These policy funds primarily include public liability reserve and self-insurance funds, internal service funds, and a capital improvement reserve funded with general fund contributions. Even if the state borrowed the entire $36 million of San Diego's property tax revenue and took the entire $24 million of the gas tax revenue in December 2009 or January 2010, combined ending general fund and policy fund cash balances projected by the city for each of the Dec. 31, 2009, and Jan. 29, 2010, maturity dates would, in our view, cover series A or B TRANS by an adequate 1.4x or 1.3x, respectively. Should the state intercept the full annual estimated amount of property tax and gas tax revenue in April 2010, series C coverage at the April 30, 2009, the maturity date would still be good, in our view, at 1.8x. The city has identified savings and we understand intends to lower disbursements to mitigate proposition 1A borrowing or any state take-away of gas tax revenue in fiscal 2010 which, if the council adopts, would, in our view, likely boost overall cash levels and coverage. Council reduced expenditures to offset declining revenues throughout fiscal 2009.

San Diego also has identified sources of alternative liquidity in its sewer, water, and environmental services enterprise funds. As of May 1, 2009, the combined cash in these three funds totaled $617 million, but the city is unable to project actual cash balances on the respective series' maturity dates. Using alternate liquidity available as of May 1, 2009, total coverage at each of the maturity dates for series A, B, and C rises, in our view, significantly to 29.9x, 10.7x, and 12.5x, respectively.

San Diego's fiscal 2008 unreserved general fund balance totaled $79 million, or a good 7.5% of expenditures, in our opinion. Due to a slowing economy and a drop in sales taxes and transient occupancy taxes, the city adjusted its budget downward in fiscal 2009 by $37 million to balance it; it expects a stable ending reserve. In its fiscal 2010 budget, San Diego expects an $80 million ending budgetary general fund reserve, or what we view as a good 7% of budget, which is in line with the city's targeted levels. However, budgeted estimates do not include any potential state takeaways or borrowing.

Related Research

USPF Criteria: "Short-Term Debt," June 15, 2007

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