

CITY OF ESCONDIDO
COMMUNITY DEVELOPMENT COMMISSION

ANNUAL FINANCIAL REPORT

For the Fiscal Year Ended June 30, 2005

| | |
|--------------------|------------------------------------|
| Chairperson | Lori Holt Pfeiler, Mayor |
| Vice Chairperson | Ed Gallo, Mayor Pro-Tempore |
| Member | Sam Abed, Council Member |
| Member | Ron Newman, Council Member |
| Member | Marie Waldron, Council Member |
| Executive Director | Clay Phillips, City Manager |
| Fiscal Officer | Gilbert Rojas, Director of Finance |
| Secretary | Marsha Whalen, City Clerk |

Prepared by
The Department of Finance

CITY OF ESCONDIDO COMMUNITY DEVELOPMENT COMMISSION
ANNUAL FINANCIAL REPORT
June 30, 2005

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Board of Directors
Escondido Community Development Commission
Escondido, California

Independent Auditors' Report

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Escondido Community Development Commission (the Commission), a component unit of the City of Escondido, California, as of and for the year ended June 30, 2005, which collectively comprise the Commission's basic financial statements, as listed in the table of contents. These financial statements are the responsibility of the management of the Commission. Our responsibility is to express opinions on these financial statements based on our audit.

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 of America. 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 examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes 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 provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Commission as of June 30, 2005, and the respective changes in financial position of the Commission for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Commission has changed its method of accounting for long-term loans payable to the City of Escondido that is described further in Note I to the basic financial statements. Also, the City of Escondido has not presented *Management's Discussion and Analysis* that the Governmental Accounting Standards Board has determined necessary to supplement, although not required to be part of, the basic financial statements. The information identified in the accompanying table of contents as *required supplementary information* is not a required part of the basic financial statements, but is supplementary information required by the Governmental Accounting Standards Board. 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.

In accordance with *Government Auditing Standards*, we have also issued a report dated October 12, 2005 on our consideration of the Commission'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

Board of Directors
Escondido Community Development Commission
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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.

Conrad and Associates, L.L.P.

October 12, 2005

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City of Escondido Community Development Commission
Statement of Net Assets
June 30, 2005

| | <u>Governmental Activities</u> |
|---|------------------------------------|
| ASSETS | |
| Current Assets: | |
| Cash and investments | \$ 11,664,533 |
| Cash and investments with fiscal agents | 10,789,757 |
| Taxes receivable | 569,598 |
| Interest receivable | 122,354 |
| Total Current Assets | <u>23,146,242</u> |
| Non-Current Assets: | |
| Loans receivable | 25,733,634 |
| Notes receivable | 279 |
| Due from the Federal Government | 28,467 |
| Loans receivable from the City of Escondido | 2,536,054 |
| Deferred bond issue costs | 228,578 |
| Land held for resale | 1,840,804 |
| Capital assets: | |
| Not being depreciated | 3,155,714 |
| Being depreciated, net | 54,665,068 |
| Total Non-Current Assets | <u>88,188,598</u> |
| Total Assets | <u>111,334,840</u> |
| LIABILITIES | |
| Current Liabilities: | |
| Accounts payable and accrued liabilities | 30,630 |
| Interest payable | 854,427 |
| Total Current Liabilities | <u>885,057</u> |
| Non-Current Liabilities: | |
| Due within one year | 8,321,703 |
| Due in more than one year (including premium of \$197,161) | <u>104,003,061</u> |
| Total Non-Current Liabilities | <u>112,324,764</u> |
| Total Liabilities | <u>113,209,821</u> |
| NET ASSETS | |
| Invested in capital assets, net of related debt | 32,185,782 |
| Restricted for low and moderate housing | 29,328,936 |
| Unrestricted | <u>(63,389,699)</u> |
| Total Net Assets | <u>\$ (1,874,981)</u> |

**City of Escondido Community Development Commission
Statement of Activities
For the Fiscal Year Ended June 30, 2005**

| Functions/Programs | Expenses | Program Revenue Operating Grants and Contributions | Net (Expense) Revenue and Changes in Net Assets Governmental Activities Total |
|---|--------------|--|---|
| Governmental Activities: | | | |
| Community development | \$ 4,460,745 | \$ 148,038 | \$ (4,312,707) |
| ERAF payment | 1,371,088 | | (1,371,088) |
| Pass-through payments | 2,502,874 | | (2,502,874) |
| Interest and fiscal charges | 5,562,412 | | (5,562,412) |
| Total Governmental Activities | \$13,897,119 | \$ 148,038 | (13,749,081) |
| General Revenues: | | | |
| Tax increment | | | 17,858,880 |
| Investment income | | | 692,003 |
| Lease income | | | 41,674 |
| Miscellaneous | | | 349,210 |
| Total General Revenues | | | 18,941,767 |
| Change in Net Assets | | | 5,192,686 |
| NET ASSETS - Beginning of Year, as restated (see note III, H) | | | (7,067,667) |
| NET ASSETS - End of Year | | | \$ (1,874,981) |

**City of Escondido Community Development Commission
Balance Sheet
Governmental Funds
June 30, 2005**

| | Special Revenue | Debt Service | Nonmajor | |
|---|--|--|-----------------------------|-----------------------------|
| | Low and Moderate Income Housing | Community Development Commission | Capital Projects Fund | Total |
| ASSETS: | | | | |
| Cash and investments | \$ 3,529,754 | \$ 8,095,811 | \$ 38,968 | \$ 11,664,533 |
| Cash with fiscal agents | | 10,789,757 | | 10,789,757 |
| Taxes receivable | 132,249 | 437,349 | | 569,598 |
| Interest receivable | 47,731 | 74,138 | 485 | 122,354 |
| Loans receivable | 25,733,634 | | | 25,733,634 |
| Notes receivable | 279 | | | 279 |
| Due from Federal Government | 28,467 | | | 28,467 |
| Loans receivable from the City of Escondido | 2,066,066 | | 469,988 | 2,536,054 |
| Land held for resale | 1,840,804 | | | 1,840,804 |
| Total Assets | <u>\$ 33,378,984</u> | <u>\$ 19,397,055</u> | <u>\$ 509,441</u> | <u>\$ 53,285,480</u> |
| LIABILITIES AND FUND BALANCES | | | | |
| Liabilities: | | | | |
| Accounts payable and accrued liabilities | \$ 30,630 | \$ | \$ | \$ 30,630 |
| Total Liabilities | <u>30,630</u> | <u></u> | <u></u> | <u>30,630</u> |
| Fund Balances: | | | | |
| Reserved for non-current loans, advances and notes receivable | 27,799,700 | | 469,988 | 28,269,688 |
| Reserved for low and moderate income housing | 3,707,850 | | | 3,707,850 |
| Reserved for debt service | | 19,397,055 | | 19,397,055 |
| Reserved for capital projects | | | 4,796 | 4,796 |
| Reserved for land held for resale | 1,840,804 | | | 1,840,804 |
| Unreserved; designated for future projects | | | 34,657 | 34,657 |
| Total Fund Balances | <u>33,348,354</u> | <u>19,397,055</u> | <u>509,441</u> | <u>53,254,850</u> |
| Total Liabilities and Fund Balances | <u>\$ 33,378,984</u> | <u>\$ 19,397,055</u> | <u>\$ 509,441</u> | |

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 | 57,820,782 |
| Long-term debt, including bonds payable, amortization, interest, and accretion, are not due and payable in the current period and therefore are not reported in the funds | (112,950,613) |
| NET ASSETS OF GOVERNMENTAL ACTIVITIES | <u>\$ (1,874,981)</u> |

City of Escondido Community Development Commission
Statement of Revenues, Expenditures, and Changes in Fund Balances
Governmental Funds
For the Fiscal Year Ended June 30, 2005

| | Special Revenue | Debt Service | Nonmajor | |
|--|--|--|-----------------------------|---------------------|
| | Low and Moderate Income Housing | Community Development Commission | Capital Projects Fund | Total |
| Revenues: | | | | |
| Tax increment | \$ 3,571,776 | \$ 14,287,104 | \$ | \$ 17,858,880 |
| Investment income | 458,782 | 232,035 | 1,187 | 692,004 |
| Lease income | 41,674 | | | 41,674 |
| Intergovernmental | 148,038 | | | 148,038 |
| Miscellaneous | 349,210 | | | 349,210 |
| Total Revenues | <u>4,569,480</u> | <u>14,519,139</u> | <u>1,187</u> | <u>19,089,806</u> |
| Expenditures: | | | | |
| Community development | 1,499,384 | 26,805 | | 1,526,189 |
| ERAF payment | | 1,371,088 | | 1,371,088 |
| Pass-through payments | | 2,502,874 | | 2,502,874 |
| Capital projects | | | 99,996 | 99,996 |
| Debt service: | | | | |
| Principal | | 9,034,275 | | 9,034,275 |
| Interest and fiscal charges | | 2,869,808 | | 2,869,808 |
| Total Expenditures | <u>1,499,384</u> | <u>15,804,850</u> | <u>99,996</u> | <u>17,404,230</u> |
| Excess (Deficiency) of Revenues over Expenditures | <u>3,070,096</u> | <u>(1,285,711)</u> | <u>(98,809)</u> | <u>1,685,576</u> |
| Other Financing Sources (Uses): | | | | |
| Transfers in | 382,893 | 1,668,956 | | 2,051,849 |
| Transfers out | (1,668,956) | (382,893) | | (2,051,849) |
| Issuance of long-term liabilities | | 1,371,088 | | 1,371,088 |
| Total Other Financing Sources (Uses) | <u>(1,286,063)</u> | <u>2,657,151</u> | | <u>1,371,088</u> |
| Net Change in Fund Balance | 1,784,033 | 1,371,440 | (98,809) | 3,056,664 |
| FUND BALANCE - Beginning of Year as restated (see note H) | <u>31,564,321</u> | <u>18,025,615</u> | <u>608,250</u> | <u>50,198,186</u> |
| FUND BALANCE - End of Year | <u>\$33,348,354</u> | <u>\$19,397,055</u> | <u>\$ 509,441</u> | <u>\$53,254,850</u> |

Amounts reported for governmental activities in the statement of net assets are different because:

| | |
|--|---------------------|
| Net change in fund balances - total governmental funds | \$ 3,056,664 |
| 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 depreciation exceeded capital outlays in the current period. | (2,815,606) |
| The issuance of long-term debt provides current financial resources of governmental funds while the repayment of principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net assets. Also governmental funds report the effect of issuance costs, premiums, discounts, and similar items when debt is first issued, whereas these amounts are all deferred and amortized or accreted in the Statement of Activities. This amount is the net effect of those differences. | 4,951,628 |
| CHANGE IN NET ASSETS OF GOVERNMENTAL ACTIVITIES | <u>\$ 5,192,686</u> |

CITY OF ESCONDIDO COMMUNITY DEVELOPMENT COMMISSION
Notes to Financial Statements
Year Ended June 30, 2005

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The following is a summary of the significant accounting policies of the City of Escondido Community Development Commission (Commission):

A. Reporting Entity - City of Escondido Community Development Commission

The Commission was established in 1984 and currently involves Civic Center development including a community theater, park and convention facilities. Other activities include providing housing financial assistance to increase and improve the community's supply of low and moderate-income housing. The original redevelopment plan is dated December 19, 1984 and has a life of 45 years.

The Commission is an integral part of the reporting entity of the City of Escondido (City). The funds of the Commission have been blended within the financial statements of the City because the City Council of the City of Escondido is the governing board of the Commission and exercises control over the operations of the Commission. Only the funds of the Commission are included herein, therefore, these financial statements do not purport to represent the financial position or results of operations of the City of Escondido, California.

B. Government-wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net assets and the statement of changes in net assets) report information on all of the activities of the Commission. For the most part, the effect of the interfund activity has been removed from these statements.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. 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.

Separate financial statements are provided for governmental funds. Major individual governmental funds are reported as separate columns in the fund financial statements.

CITY OF ESCONDIDO COMMUNITY DEVELOPMENT COMMISSION
Notes to Financial Statements (Continued)
Year Ended June 30, 2005

C. Measurement Focus, Basis of Accounting, and Financial Statement Presentation

1. Basis of accounting

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting wherein revenues are recorded when they are both earned and realized, regardless of the timing of the related cash flows.

Governmental fund statements are reported using the modified accrual basis of accounting wherein revenues are recognized as soon as they are both measurable and available as a resource to finance operations of the current year. Expenditures are recorded when incurred except that interest on long-term debt is recorded as an expenditure on its due date.

The financial statements have been prepared in accordance with generally accepted accounting principles and necessarily include amounts based on estimates and assumptions by Management. Actual results could differ from those amounts.

2. Tax increment revenue

The Commission has no power to levy and collect taxes, and any legislative property tax de-emphasis might necessarily reduce the amount of tax revenues that would otherwise be available to pay the principal of, and interest on loans from the City of Escondido ("City"). Broadened property tax exemptions could have a similar effect. Conversely, any increase in the tax rate or assessed valuation, or any reduction or elimination of present exemptions would necessarily increase the amount of tax revenues that would be available to pay principal and interest on tax allocation bonds or loans from the City.

3. Description of funds

The Commission reports the following major governmental funds:

The Low and Moderate Income Housing Special Revenue Fund is used to account for the 20% portion of the Commission's tax increment revenue that is required to be set aside for low and moderate income housing and related expenditures, and to account for other specific revenue sources that are legally restricted to account for the specific revenue sources that are legally restricted to expenditures for specified purposes.

CITY OF ESCONDIDO COMMUNITY DEVELOPMENT COMMISSION
Notes to Financial Statements (Continued)
Year Ended June 30, 2005

C. Measurement Focus, Basis of Accounting, and Financial Statement Presentation,
(Continued)

The Debt Service Fund is used to account for the payment of interest and principal on long-term debt, and the accumulation of resources thereof.

Additionally, the Commission reports the following nonmajor fund types:

The Capital Projects Fund is used to account for the financial resources used in developing the project areas as well as the capital expenditures incurred in sustaining Commission activities.

D. Assets, Liabilities, and Net Assets or Equity

1. Cash and investments

Investments are reported in the accompanying balance sheet at fair value, except for certain certificates of deposit and investment contracts that are reported at cost because they are not transferable and they have terms that are not affected by changes in market interest rates. Changes in fair value that occur during a fiscal year are recognized as investment income reported for that fiscal year. Investment income includes interest earnings, changes in fair value, and any gains or losses realized upon the liquidation, maturity, or sale of investments.

The Commission's cash and investments held by fiscal agents are pledged to the payment or security of certain long-term debt issuances. The California Government Code provides that these monies, in the absence of specific statutory provisions governing the issuance of bonds, may be invested in accordance with the ordinance, resolutions or indentures specifying the types of investments its trustees or fiscal agents may make.

CITY OF ESCONDIDO COMMUNITY DEVELOPMENT COMMISSION
Notes to Financial Statements (Continued)
Year Ended June 30, 2005

D. Assets, Liabilities, and Net Assets or Equity. (Continued)

1. Cash and investments, (Continued)

Cash and investments, except for cash and investments with fiscal agents, are pooled with other City of Escondido funds for investment purposes, with interest being allocated quarterly to all funds legally requiring allocation and to other various funds at the direction of management based on average month-end pooled funds cash and investment balances. Interest income for cash and investments excluded from pooled cash is credited directly to the related fund. Investment policies applicable to the Commission's funds are those of the City of Escondido and are included in the notes to the City's basic financial statements.

2. Land held for resale

Land acquired by the Commission and held for resale is recorded at cost unless market value is determined to be below cost.

II. STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY

A. Budgetary Data

The Commission adopts an annual budget prepared on the modified accrual basis for the Special Revenue and Debt Service Funds. The Executive Director is required to prepare and submit to the Commission Board of Directors the annual budget of the Commission and administer it after adoption. Any revisions that alter the total appropriations of the fund must be approved by the Board of Directors. Prior year appropriations lapse unless they are encumbered at year-end or re-appropriated through the formal budget process.

CITY OF ESCONDIDO COMMUNITY DEVELOPMENT COMMISSION
Notes to Financial Statements (Continued)
Year Ended June 30, 2005

II. STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY, (Continued)

B. Excess of Expenditures over Appropriations

The following funds had an excess of expenditures over appropriations:

| <u>Fund</u> | <u>Final Budget</u> | <u>Actual</u> | <u>Excess over Appropriations</u> |
|-------------------|-------------------------|---------------|---------------------------------------|
| Debt Service Fund | \$ 14,961,500 | \$ 15,804,850 | \$ 843,350 |

These expenditures were funded either by the revenues in excess of the estimated revenues or by the available fund balance.

III. DETAILED NOTES ON ALL FUNDS

A. Cash and Investments

Cash and investments as of June 30, 2005 are classified in the accompanying financial statements as follows:

| | |
|--|---------------------|
| Statement of net assets: | |
| Cash and investments | \$11,664,533 |
| Cash and investments with fiscal agent | <u>10,789,757</u> |
| Total cash and investments | <u>\$22,454,290</u> |

Cash and investments as of June 30, 2005 consisted of the following:

| | |
|--------------------------------|---------------------|
| Equity in City investment pool | \$11,664,533 |
| Investments | <u>10,789,757</u> |
| Total cash and investments | <u>\$22,454,290</u> |

CITY OF ESCONDIDO COMMUNITY DEVELOPMENT COMMISSION
Notes to Financial Statements (Continued)
Year Ended June 30, 2005

A. Cash and Investments, (Continued)

Equity in the Cash and Investment Pool of the City of Escondido

The Commission has no separate bank accounts or investments other than in Equity investments held by bond trustee and the Commission's equity in the cash and investment pool managed by the City of Escondido. The Commission is a voluntary participant in that pool. This pool is governed by and under the regulatory oversight of the Investment Policy adopted by the City Council of the City of Escondido. The Commission has not adopted an investment policy separate from that of the City of Escondido. The fair value of the Commission's investment in this pool is reported in the accompanying financial statements at amounts based upon the Commission's pro-rata share of the fair value calculated by the City for the entire City portfolio. The balance available for withdrawal is based on the accounting records maintained by the City, which are recorded on an original cost basis.

Investments Authorized by Debt Agreements

Investment of debt proceeds held by bond trustee are governed by provisions of the debt agreements, rather than the general provisions of the California Government Code or the Commission's investment policy. The table below identifies the investment types that are authorized for investments held by bond trustee. The table also identifies certain provisions of these debt agreements that address interest rate risk and concentration of credit risk.

| <u>Authorized Investment Type</u> | <u>Maximum Maturity</u> | <u>Maximum Percentage Allowed</u> | <u>Maximum Investment in One Issuer</u> |
|---------------------------------------|-----------------------------|---|---|
| U.S. Treasury Obligations | None | None | None |
| U.S. Commission Securities | None | None | None |
| Banker's Acceptances | 360 days | None | None |
| Commercial Paper | 180 days | None | None |
| Money Market Mutual Funds | N/A | None | None |
| Investment Contracts | 30 years | None | None |
| Repurchase Agreements | None | None | None |
| State and Municipal Obligations | None | None | None |
| State and Pooled Investment Fund | None | None | None |

CITY OF ESCONDIDO COMMUNITY DEVELOPMENT COMMISSION
Notes to Financial Statements (Continued)
Year Ended June 30, 2005

A. Cash and Investments, (Continued)

Disclosures Relating to Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. One of the ways that the Commission manages exposure to interest rate risk is by purchasing a combination of shorter term and longer term investments and by timing cash flows from maturities so that a portion of the portfolio is maturing or coming close to maturity evenly over time as necessary to provide the cash flow and liquidity needed for operations.

Information about the Commission's exposure to interest rate risk as a result of its equity in the cash and investment pool of the City of Escondido is provided by disclosures in the notes to the basic financial statements of the City of Escondido that shows the distribution of the City's investments by maturity.

Information about the sensitivity of the fair values of the Commission's investments held by bond trustee to market interest rate fluctuations is provided by the following table that shows the distribution of these investments by maturity:

| <u>Investment Type</u> | <u>Remaining Maturity (in Months)</u> | | | |
|---------------------------|---------------------------------------|------------------------|-------------------------------|-------------------------------|
| | <u>18 Months Or Less</u> | <u>18 to 42 Months</u> | <u>42-66 Months</u> | <u>More Than 66 Months</u> |
| Held by bond trustee: | | | | |
| Money market funds | \$ 921,463 | \$ 921,463 | \$ | \$ |
| Federal Agency Securities | <u>9,868,294</u> | <u>9,868,294</u> | <u> </u> | <u> </u> |
| Total | <u>\$10,789,757</u> | <u>\$10,789,757</u> | <u>\$ </u> | <u>\$ </u> |

CITY OF ESCONDIDO COMMUNITY DEVELOPMENT COMMISSION
Notes to Financial Statements (Continued)
Year Ended June 30, 2005

A. Cash and Investments, (Continued)

Disclosures Relating to 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. Presented below is the minimum rating required by (where applicable) the California Government Code, the Commission's investment policy, or debt agreements, and the actual rating as of year end for each investment type.

| <u>Investment Type</u> | | <u>Minimum Legal Rating</u> | <u>Exempt From Disclosure</u> | <u>Rating as of Year End</u> | | |
|---------------------------|---------------------|-------------------------------------|---------------------------------------|------------------------------|-----------------------------|-----------------------------|
| | | | | <u>AAA</u> | <u>A-</u> | <u>Not Rated</u> |
| Held by bond trustee: | | | | | | |
| Money market funds | \$ 921,463 | A | \$ | \$ | \$ | \$ 921,463 |
| Federal Agency Securities | <u>9,868,294</u> | N/A | <u> </u> | <u>9,868,294</u> | <u> </u> | <u> </u> |
| Total | <u>\$10,789,757</u> | | <u>\$</u> | <u>\$9,868,294</u> | <u>\$</u> | <u>\$ 921,463</u> |

Concentration of Credit Risk

Investments in any one issuer (other than U.S. Treasury securities, mutual funds, and investment pools) that represent 5% or more of total investments for the entire entity (or for each separate major fund or for nonmajor funds in the aggregate) are as follows.

\$9,868,294 of the investments held by bond trustee reported in the Commission's Debt Service Fund are held in the form of federal agency securities issued by the Federal Home Loan Mortgage Corporation and Federal Home Loan Bank and mature between July 15, 2005 and August 5, 2005.

CITY OF ESCONDIDO COMMUNITY DEVELOPMENT COMMISSION
Notes to Financial Statements (Continued)
Year Ended June 30, 2005

A. Cash and Investments, (Continued)

Custodial Credit Risk

The Commission does not have significant certificates of deposit or demand accounts held by bond trustee that are subject to disclosable custodial credit risk (as defined by GASB Statement No.40). The Commission does not have direct investments in securities subject to disclosable custodial credit risk (as defined by GASB Statement No. 40).

For the investments held by bond trustee, the bond trustee selects the investment under the terms of the applicable trust agreement, acquires the investment, and holds the investment on behalf of the reporting government.

B. Loan Receivables

The Commission has entered into agreement with the City of Escondido and various other parties to establish low and moderate income housing loans. At June 30, 2005 the outstanding loans receivable totaled \$2,536,054 and \$25,733,634, respectively.

C. Interfund Transfers

| | Transfers In: | | |
|------------------------------------|---|---------------------|--------------------|
| | Special Revenue Low and Moderate Income Housing | <u>Debt service</u> | <u>Totals</u> |
| Transfers out: | | | |
| Special Revenue: | | | |
| Low and Moderate Income Housing | \$ | \$1,668,956 | \$1,668,956 |
| Debt Service Fund | <u>382,893</u> | <u> </u> | <u>382,893</u> |
| | <u>\$382,893</u> | <u>\$1,668,956</u> | <u>\$2,051,849</u> |

Interfund transfers were primarily used to move receipts to the Debt Service Fund from the Low and Moderate Income Housing Fund for Mobilehome sales during the year.

CITY OF ESCONDIDO COMMUNITY DEVELOPMENT COMMISSION
Notes to Financial Statements (Continued)
Year Ended June 30, 2005

D. Capital Assets

Changes in capital assets during the year ended June 30, 2005 were as follows:

| | <u>Balance at July 1, 2004</u> | <u>Increases</u> | <u>Decreases</u> | <u>Balance at June 30, 2005</u> |
|---|------------------------------------|-----------------------|------------------|-------------------------------------|
| Governmental activities: | | | | |
| Capital assets, | | | | |
| Not being depreciated: | | | | |
| Land | \$ 3,155,714 | \$ | \$ | \$ 3,155,714 |
| Capital assets, being depreciated: | | | | |
| Land improvements | 139,295 | | | 139,295 |
| Buildings and improvements | 82,080,470 | | | 82,080,470 |
| Machinery and equipment | 276,473 | | | 276,473 |
| Total capital assets, being depreciated | <u>82,496,238</u> | | | <u>82,496,238</u> |
| Less accumulated depreciation for: | | | | |
| Land improvements | (85,899) | (27,859) | | (113,758) |
| Buildings and improvements | (24,752,343) | (2,736,016) | | (27,488,359) |
| Machinery and equipment | (177,322) | (51,731) | | (229,053) |
| Total accumulated depreciation | <u>(25,015,564)</u> | <u>(2,815,606)</u> | | <u>(27,831,170)</u> |
| Total capital assets, being depreciated, net | <u>57,480,674</u> | <u>(2,815,606)</u> | | <u>54,665,068</u> |
| Governmental activities capital assets, net | <u>\$ 60,636,388</u> | <u>\$ (2,815,606)</u> | <u>\$</u> | <u>\$ 57,820,782</u> |

Depreciation of \$2,815,606 was charged to community development.

CITY OF ESCONDIDO COMMUNITY DEVELOPMENT COMMISSION
Notes to Financial Statements (Continued)
Year Ended June 30, 2005

E. Long-Term Liabilities

The following is a summary of changes in long-term liabilities for the year ended June 30, 2005:

| | Balance at July 1, 2004 as restated | Additions | Deletions | Balance at June 30, 2005 | Due Within One Year | Due Beyond One Year |
|------------------------------|---|---------------------|-----------------------|-----------------------------|------------------------|------------------------|
| Tax Allocation Bonds: | | | | | | |
| January 1992 | \$ 2,591,074 | \$ 169,129 | | \$ 2,760,203 | | \$ 2,760,203 |
| March 1993 | 10,930,000 | | (1,605,000) | 9,325,000 | 1,685,000 | 7,640,000 |
| Lease Revenue Bonds: | | | | | | |
| COP May 1995 | 66,984,136 | 2,601,597 | (4,305,000) | 65,280,733 | 4,400,000 | 60,880,733 |
| March 1999 | 2,335,000 | | (1,025,000) | 1,310,000 | 65,000 | 1,245,000 |
| December 2001 | 18,335,000 | | (2,025,000) | 16,310,000 | 2,090,000 | 14,220,000 |
| Loans Payable | 15,785,523 | 1,371,088 | (74,275) | 17,082,336 | 81,703 | 17,000,633 |
| Employee Benefits Payable | 40,377 | 18,954 | | 59,331 | | 59,331 |
| Total | \$ 117,001,110 | \$ 4,160,768 | \$ (9,034,275) | \$ 112,127,603 | \$ 8,321,703 | 103,805,900 |
| Add bond premium | | | | | | 197,161 |
| Total | | | | | | \$ 104,003,061 |

Long-term liabilities consisted of the following at June 30, 2005:

Tax Allocation Bonds

In January 1992, the Escondido Joint Powers Financing Authority issued \$35,986,152 Revenue Bonds Series 1992 for the purpose of making a loan to the Commission. In December 2001, the Commission issued \$22,420,000 Revenue Bonds to advance refund \$23,585,000 of the bonds. The remaining bonds consist of capital appreciation bonds in the initial amounts of \$612,259 and \$568,893 due on September 1, 2012 and September 1, 2013, respectively, in the accreted amounts of \$2,240,000 each. The outstanding balance at June 30, 2005 includes \$1,579,051 of accreted value of the capital appreciation bonds.

\$ 2,760,203

CITY OF ESCONDIDO COMMUNITY DEVELOPMENT COMMISSION
Notes to Financial Statements (Continued)
Year Ended June 30, 2005

E. Long-Term Liabilities (Continued)

In March 1993, the Escondido Joint Powers Financing Authority issued \$24,790,000 Revenue Bonds Series 1993A for the purpose of making a loan (advance) to the Commission. Principal is due annually in amounts ranging from \$1,050,000 to \$2,055,000 on September 1 of each year through the year 2009. Interest is payable semiannually on March 1 and September 1 of each year commencing September 1, 1993 at rates ranging from 3.00% to 5.20%. The reserves are fully funded.

9,325,000

\$12,085,203

Lease Revenue Bonds

In May 1995, the Commission issued \$51,385,757 of Certificates of Participation (COPs) Lease Revenue Bonds to advance refund \$41,000,000 of the 1992 COPs which provided financing for the Civic Center Construction project. The 1995 refunding COPs bear interest rates between 5.50% and 6.65% and were issued under a trust agreement dated May 1, 1995 with the First Interstate Bank of California as trustee. The refunding COPs mature between September 1, 2003 through September 2018 in amounts ranging from \$2,140,730 to \$5,136,800. Bonds maturing on or after September 1, 2005, are subject to optional redemption in any amount at the discretion of the Commission, on any date on or after September 1, 2003 at redemption prices ranging from 100% to 102% of principal. Additionally, \$12,195,000 term bonds are due September 1, 2018 and are subject to mandatory redemption from a sinking fund account in amounts ranging from \$850,000 to \$1,845,000. Interest is payable semiannually on March 1 and September 1 of each year commencing on March 1, 1996, at rates ranging from 5.6% to 6.0%.

Capital appreciation bonds in the initial amount of \$26,970,757 are due annually in accreted maturity amounts ranging from \$2,605,000 to \$7,010,000 on September 1 of each year through the year 2018 commencing in 2003. The outstanding balance at June 30, 2005, includes \$21,704,976 of accreted value of the capital appreciation bonds. The reserve was fully funded.

\$65,280,733

CITY OF ESCONDIDO COMMUNITY DEVELOPMENT COMMISSION
Notes to Financial Statements (Continued)
Year Ended June 30, 2005

E. Long-Term Liabilities (Continued)

In March 1999, the Commission issued \$6,625,000 in Lease Revenue Bonds which bear interest rates between 3.63% and 4.7% to advance refund \$6,160,000 of outstanding 1991 Mobile Home Parks Project Certificates of Participation (COPS). The \$6,625,000 1999 Lease Revenue Bonds are due in annual installments through 2021 of \$155,000 to \$215,000. In addition term bonds of \$1,885,000 at 5.0% mature on March 1, 2021. The Bonds maturing on or after March 1, 2015 will be subject to redemption at the option of the Commission from any available funds as a whole or in part on any date on or after March 1, 2009, at redemption prices ranging from 100% to 102%. The term bonds maturing March 21 are subject to mandatory redemption from a sinking fund account in amounts ranging from \$235,000 to \$310,000. The reserve was fully funded. 1,310,000

In December 2001, the Commission issued \$22,420,000 of Lease Revenue Bonds to refund \$22,005,000 of the 1992 Certificates of Participation which were issued to refund certain certificates of participation originally issued by the City of Escondido in 1986 to finance a portion of the construction of the City Hall. The Bonds are due in annual installments from 2002 through 2011, with interest rates ranging from 3.00% to 4.25% and annual installments of \$1,970,000 to \$2,580,000. 16,310,000

Total Lease Revenue Bonds \$82,900,733

CITY OF ESCONDIDO COMMUNITY DEVELOPMENT COMMISSION
Notes to Financial Statements (Continued)
Year Ended June 30, 2005

E. Long-Term Liabilities (Continued)

Loans payable

The Commission and the City have entered into a cooperative agreement to loan the Commission monies for general operation and authorized development activities. The agreement specifies that the loan will be reimbursed to the City from whatever revenues the Commission possesses, or is entitled to, including future tax increment funds. Interest was accrued at 6.78% per annum through February 1989, on funds the Commission expended for authorized purposes. Subsequent to February 1989, the interest accrued to the City was one percent plus the average annual AA Municipal General Obligation Bond rate for a twenty-year bond. Accrued interest on the loan from the City of Escondido amounting to \$20,633,392 is not reflected in the accompanying financial statements, as payment is contingent upon the availability of tax increment.

\$13,934,365

In 2002 and 2004, the Commission of the City of Escondido received loans from the California Housing Finance Agency. The proceeds of the loan are to be used to finance the acquisition of Washington Plaza Apartments and Trinity Apartments, respectively. The term of the loans are ten years with an annual interest rate of 3%. Payment is deferred for the term of the loans.

2,650,000

The Commission entered into a Disposition and Development Agreement on July 22, 1992 with Arroyo Energy Limited Partnership, a California limited partnership (Developer). The Agreement was entered into for the purpose of developing an ice arena and health club facility within the redevelopment area. Under the terms of the Agreement, the Commission would pay \$1,000,000 to the Developer, attributable to the site of the development (net of the site's pro rata share of any existing pass-through agreements and the required low and moderate income housing deposits). The interest rate on the loan is 10%, and the annual payment of interest and principal is \$131,500 commencing 1995 and ending 2009.

497,971

Total Loans Payable

\$17,082,336

CITY OF ESCONDIDO COMMUNITY DEVELOPMENT COMMISSION
Notes to Financial Statements (Continued)
Year Ended June 30, 2005

F. Debt to Maturity Schedule

The annual requirements to amortize the tax allocation bonds and the lease revenue bonds, including accreted values, are as follows: (in thousands)

| Year Ending June 30 | Tax Allocation Bonds | | Lease Revenue Bonds | |
|------------------------|-------------------------|-----------------|------------------------|------------------|
| | Principal | Interest | Principal | Interest |
| | 2006 | \$ 1,685 | \$ 433 | \$ 6,555 |
| 2007 | 1,770 | 346 | 6,735 | 1,906 |
| 2008 | 1,860 | 255 | 7,010 | 1,720 |
| 2009 | 1,955 | 157 | 7,305 | 1,521 |
| 2010 | 2,055 | 53 | 7,610 | 1,301 |
| 2011-15 | 1,181 | 3,299 | 36,510 | 3,492 |
| 2016-20 | | | 36,180 | 949 |
| 2021 | | | 115 | 6 |
| Total | <u>\$ 10,506</u> | <u>\$ 4,543</u> | <u>\$ 108,020</u> | <u>\$ 12,939</u> |

G. Prior Year Defeasance of Long-Term Debt

In prior years, the Commission defeased certain certificates of participation and tax allocation bonds by placing the proceeds of refunding the debt issues in an irrevocable trust to provide for all future debt service payments on the old debt issues. Accordingly, the trust account assets and the liability for the defeased debt issues are not included in the Commission's financial statements. As of June 30, 2005, \$31,915,000 of bonds outstanding are considered defeased.

CITY OF ESCONDIDO COMMUNITY DEVELOPMENT COMMISSION
Notes to Financial Statements (Continued)
June 30, 2005

H. Restatement of Fund Balance

The basic fund statements reflect the following certain prior period adjustment to beginning fund balance:

| | <u>CDC Debt Service Fund</u> | <u>Government-wide Statement</u> |
|---|----------------------------------|--------------------------------------|
| Fund balance, July 1, 2004 as previously reported | \$5,462,338 | \$(8,334,831) |
| Adjustment to exclude advances from the City of Escondido from fund liabilities | 12,563,277 | |
| Adjustment to properly record prior year's accretion to long-term debt | _____ | <u>1,267,164</u> |
| Fund balance, July 1, 2004 as restated | <u>\$18,025,615</u> | <u>\$(7,067,667)</u> |

I. Change in Method of Accounting

In fiscal year 2004-2005, the Commission has changed its method of accounting for long-term loan's payable to the City of Escondido. In prior years, such loans were recorded as advances from the City of Escondido and were included in both the fund financial statements and the government-wide financial statements. Beginning fiscal year 2004-2005, such loans are recorded as long-term liabilities only in the government-wide financial statements. The effect of this change in method of accounting on beginning fund balance is disclosed in footnote H.

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Required Supplementary Information

**City of Escondido Community Development Commission
 Low and Moderate Income Housing Special Revenue Fund
 Budgetary Comparison Schedule
 For the Fiscal Year Ended June 30, 2005**

| | Budgeted Amounts | | Actual | Variance |
|---|---------------------|---------------------|---------------------|---------------------|
| | Original | Final | | Over (Under) |
| Revenues: | | | | |
| Tax increment | \$ 3,100,000 | \$ 3,100,000 | \$ 3,571,776 | \$ 471,776 |
| Investment income | 370,000 | 370,000 | 458,782 | 88,782 |
| Lease income | 119,290 | 119,290 | 41,674 | (77,616) |
| Intergovernmental | 1,007,545 | 1,007,545 | 148,038 | (859,507) |
| Miscellaneous | 4,800 | 4,800 | 349,210 | 344,410 |
| Total Revenues | <u>4,601,635</u> | <u>4,601,635</u> | <u>4,569,480</u> | <u>(32,155)</u> |
| Expenditures: | | | | |
| Community development: | | | | |
| Low and moderate housing | 976,120 | 986,090 | 942,754 | 43,336 |
| Mobile home management | 162,975 | 164,475 | 57,575 | 106,900 |
| Home | 134,280 | 135,780 | 134,305 | 1,475 |
| Rental subsidy | 400,000 | 400,000 | 364,750 | 35,250 |
| Total Expenditures - | <u>1,673,375</u> | <u>1,686,345</u> | <u>1,499,384</u> | <u>186,961</u> |
| Excess of Revenues over Expenditures | <u>2,928,260</u> | <u>2,915,290</u> | <u>3,070,096</u> | <u>154,806</u> |
| Other Financing (Uses): | | | | |
| Sale of property | 65,000 | 65,000 | | (65,000) |
| Transfers in | | | 382,893 | 382,893 |
| Transfers out | (662,160) | (918,336) | (1,668,956) | (750,620) |
| Total Other Financing (Uses) | <u>(597,160)</u> | <u>(853,336)</u> | <u>(1,286,063)</u> | <u>(432,727)</u> |
| Net Change in Fund Balance | 2,331,100 | 2,061,954 | 1,784,033 | (277,921) |
| FUND BALANCE - Beginning of Year | <u>31,564,321</u> | <u>31,564,321</u> | <u>31,564,321</u> | |
| FUND BALANCE - End of Year | <u>\$33,895,421</u> | <u>\$33,626,275</u> | <u>\$33,348,354</u> | <u>\$ (277,921)</u> |

CITY OF ESCONDIDO COMMUNITY DEVELOPMENT COMMISSION
Notes to Required Supplementary Information
June 30, 2005

A. Budgetary Data

The Commission adopts an annual budget prepared on the modified accrual basis for the Special Revenue and Debt Service Funds. The Finance Director is required to prepare and submit to the Commission Board of Directors the annual budget of the Commission and administer it after adoption. Any revisions that alter the total appropriations of the fund must be approved by the Board of Directors. Prior year appropriations lapse unless they are encumbered at year-end or re-appropriated through the formal budget process.

Supplementary Information

**City of Escondido Community Development Commission
Community Development Commission Debt Service Fund
Budgetary Comparison Schedule
For the Fiscal Year Ended June 30, 2005**

| | <u>Final Budget Amount</u> | <u>Actual</u> | <u>Variance Over (Under)</u> |
|---|------------------------------------|----------------------|--------------------------------------|
| Revenues: | | | |
| Tax increment | \$ 12,622,830 | \$ 14,287,104 | \$ 1,664,274 |
| Investment income | 240,000 | 232,035 | (7,965) |
| Total Revenues | <u>12,862,830</u> | <u>14,519,139</u> | <u>1,656,309</u> |
| Expenditures: | | | |
| Community development | 26,715 | 26,805 | (90) |
| ERAF payment | 1,371,000 | 1,371,088 | (88) |
| Pass-through payments | 2,361,965 | 2,502,874 | (140,909) |
| Debt service: | | | |
| Principal | 8,335,000 | 9,034,275 | (699,275) |
| Interest and fiscal charges | 2,866,820 | 2,869,808 | (2,988) |
| Total Expenditures | <u>14,961,500</u> | <u>15,804,850</u> | <u>(843,350)</u> |
| (Deficiency) of Revenues over Expenditures | <u>(2,098,670)</u> | <u>(1,285,711)</u> | <u>812,959</u> |
| Other Financing Sources: | | | |
| Transfers in | 662,160 | 1,668,956 | 1,006,796 |
| Transfers out | | (382,893) | (382,893) |
| Issuance of long-term liabilities | | 1,371,088 | 1,371,088 |
| Total Other Financing Sources | <u>662,160</u> | <u>2,657,151</u> | <u>1,994,991</u> |
| Net Change in Fund Balance | (1,436,510) | 1,371,440 | 2,807,950 |
| FUND BALANCE - Beginning of Year, as restated | <u>18,025,615</u> | <u>18,025,615</u> | |
| FUND BALANCE - End of Year | <u>\$ 16,589,105</u> | <u>\$ 19,397,055</u> | <u>\$ 2,807,950</u> |

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Compliance Section

Board of Directors
Escondido Community Development Commission
Escondido, California

**Report on Internal Control over Financial Reporting and on Compliance and Other
Matters Based on an Audit of Financial Statements Performed In Accordance
With *Government Auditing Standards***

We have audited the financial statements of the Escondido Community Development Commission (the Commission), a component unit of the City of Escondido, California, as of and for the year ended June 30, 2005 and have issued our report thereon dated October 12, 2005. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Commission's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance

As part of obtaining reasonable assurance about whether the financial statements of the Commission are free of material misstatements, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. Such provisions included those provisions of laws and regulations identified in the *Guidelines for Compliance Audits of California Redevelopment Agencies*, issued by the State Controller and as interpreted in the *Suggested Auditing Procedures for Accomplishing Compliance Audits of California Redevelopment Agencies*, issued by the Governmental Accounting and Auditing Committee of the California Society of Certified Public Accountants. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Board of Directors
Escondido Community Development Commission
Escondido, California
Page Two

This report is intended solely for the information of management and the State Controller and is not intended to be and should not be used by anyone other than those specified parties.

Conrad and Associates, L.P.

October 12, 2005