

FINANCE DEPARTMENT

23 Russell Boulevard – Davis, California 95616
Accounts Payable & Payroll – 530/757-5615 – FAX: 530/758-0204
Utilities, Business Licenses & Citations: 530/757-5651 – TDD 530/757-5666



December 6, 2005

Honorable Mayor and City Council
City of Davis
Davis, California

The Comprehensive Annual Financial Report (CAFR) of the city of Davis for the Fiscal Year ended June 30, 2005 is hereby submitted. This report was prepared by the Finance Department and responsibility for both the accuracy of the presented data and the completeness and fairness of its presentation, including all disclosures, rests with the city. We believe the data, as presented, is accurate in all material aspects; that it is presented in a manner designed to fairly set forth the financial position and results of operations of the city as measured by the financial activity of its various funds; and that all disclosures necessary to enable the reader to gain the maximum understanding of the city's financial affairs have been included.

This CAFR is organized in three sections: introductory, financial, and statistical. The Introductory section includes this transmittal letter, a list of the principal officials of the city of Davis, an organization chart of the city government and a community profile designed to acquaint the reader with the city. The Financial section includes management discussion and analysis, the city's basic financial statements, required supplemental information and the combining financial statements for non-major funds, as well as the independent auditor's report on these financial statements. The Statistical section includes selected financial information on the city government and economic and demographic information on the community, generally presented in a multi-year comparative format. The section is intended to give the reader a broader perspective on the city's financial affairs than is provided in the other sections of the report.

The city is required to undergo an annual single audit in conformity with the provisions of the Single Audit Act Amendments of 1996 and the U. S. Office of Management and Budget Circular A-133, *Audits of State and Local Governments and Non-Profit Organizations*. The city's Single Audit for Fiscal Year 2004-2005 will be completed shortly and a separate Single Audit Report will be prepared. As soon as it has been completed a copy of that Report may be obtained by contacting the city Finance Department.

This report includes all funds of the city of Davis. The city provides services to its citizens in the areas of public safety; community planning and development; water, waste water and sanitation utilities; transportation, recreation, cultural and social assistance. In addition, the City Council of the city of Davis has financial accountability and responsibility for the following legally separate entities: Redevelopment Agency of the City of Davis, City of Davis Public

Facilities Financing Authority and Community Facilities District 1991-2 (Mace Ranch).
Financial information on these entities has, therefore, been included in this report.

Included as a part of this letter are several attachments which provide important information regarding the operations, economic environment and financial position of the City. The attachments are:

Attachment A	Governmental Structure, Local Economic Condition and Outlook
Attachment B	Highlights and Accomplishments
Attachment C	Financial Information
Attachment D	Other Information

The preparation of the Comprehensive Annual Financial Report was made possible by the dedicated service of the entire Finance Department staff. Each member of the Department has our appreciation for the contributions made in the preparation of this report.

Respectfully submitted,



Paul Navazio
Finance Director

ATTACHMENT A

GOVERNMENTAL STRUCTURE, LOCAL ECONOMIC CONDITION AND OUTLOOK

The City of Davis is a general law city and employs the Council Manager form of government. The City Council is comprised of five council members. One of these serves as the Mayor and another as the Mayor Pro tem. Council members are elected for a four-year term on a citywide basis (called "at large"). The member elected with the greatest number of votes serves as Mayor Pro tem for the first two years of the term and Mayor for the last two years of the term. The City Council acts as the legislative and policy-making body. Council appoints the City Manager and awards the contract for City Attorney services. The City Manager is the chief administrator and is responsible for implementing the policies and priorities of the City Council.

The City of Davis is a university and residential community internationally known for its commitment to implementing progressive and innovative programs. Located just 13 miles west of the state capital in Sacramento, the center of State government operations, and home to the University of California, Davis, the city has an economy that has traditionally mirrored employment trends in these two institutions.

UC Davis represents, by far, the largest employer in the Davis area with 29,000 academic, staff and student employees on the campus. The university has approximately 30,000 students enrolled; however, University officials expect a significant surge in student demand in the next several years and preliminary projections foresee 31,000 students enrolled by the year 2010. A number of building and infrastructure projects have been undertaken on the campus to prepare for this growth. Joint efforts between university and city officials in land use and infrastructure planning have received greater emphasis to ensure that the campus and the community can accommodate the expanding student population.

UC Davis has been estimated to contribute \$2.7 billion to the regional economy. Besides its impact as an academic institution, the university is an acknowledged international leader in agricultural, biological, biotechnological and environmental science and has increased its efforts at strengthening ties with industry. Mutually beneficial university-private relationships are encouraged and UC Davis is becoming an increasingly valuable "drawing card" for economic development efforts in the community and the region.

The entire Sacramento region enjoyed the economic boom of the late 1990s. However, the slowing national, state, and regional economies create cause for significant concern. Despite such concern, the Sacramento region is expected to remain one of the fastest growing areas in California. Sacramento has seen higher percentage gains in population, employment, income, and retail sales than any other region in the State over the last several years. The region has emerged as a center for high-tech manufacturing and research & development firms. Back-office operations for large San Francisco Bay area firms have also begun moving into the Sacramento region with its lower cost land and relative earthquake safety as advantages. While

the duration and depth of the current economic downturn is unknown, the Sacramento region will likely fare better than other major metropolitan areas of the state.

Closer to home, the prospect of significant State budget problems is one of the City's primary concerns at this time. Cities and counties throughout the state remain unsure about the funding for the "VLF backfill". State general fund money has, for the past few years, kept local agencies whole in the face of the state's reduction of vehicle license fees. This backfill is worth more than \$2 million to the City's General Fund, and would necessitate significant City service reductions if it is lost to the State.

Although development activity in the City began the anticipated decline in 2001-2002, the city of Davis issued permits for about 87,580 square feet of new commercial and industrial construction during 2004-2005, down about 56,420 square feet from the prior year. Highlights of this development activity include new office and industrial buildings in Mace Ranch, Midtown Business Park, Sutter Hospital and the northwest triangle. These developments will contribute incremental property tax, sales tax, and business license tax revenues to the City's General Fund in the coming years.

Residential development has begun its expected decline. Over 400 new single family units were built in each of the three years ending in fiscal year 1999-2000. In fiscal year 2000-2001 that number dropped to 264, then in 2001-02 to 119, in 2002-03 to 66, in 2003-04 to 72 and in 2004-05 to 59, not from lack of demand, but rather supply constraints. As of November 2005, approximately 74 single-family lots remain in currently approved subdivisions. The City's recently adopted General Plan update decreased the amount of single family residential development from the prior plan. Development capacity for limited additional multi-family development remains within the plan, and discussions are underway with the University about ways to accommodate projected growth in student population.

ATTACHMENT B

HIGHLIGHTS AND ACCOMPLISHMENTS

Public Safety Radio Tower

The City replaced an antiquated and inadequate radio system with a new digital 800MHz radio system serving all city departments including Fire, Police, Parks & Community Services and Public Works.

Senior Center Expansion

The City of Davis Parks and Community Services Department officially opened the Phase III Expansion to the Davis Senior Center this past year. The Phase III Expansion project not only created additional programming space to accommodate the future needs of senior services in the city, but it also served as the new home for the Alternative/Inclusive Recreation programs, which serves disabled teens and adults. The addition of 2,750 square feet includes a medium sized multipurpose room, residential kitchen, fireside lounge, and office/conference room space.

Historic City Hall

The city of Davis and Davis Redevelopment Agency developed architectural plans and constructed shell improvements to the approximately 11000 square foot building at 226 F Street. The building had previously been used by the Police Department including a jail cell. The improvements included gutting most interior walls, structural upgrades, reroofing, plumbing and painting of the building. The improved shell was turned over to a private party to construct interior improvements to transform property to a restaurant.

Wastewater Plan Reclamation II

Work has begun on assessment of existing plant systems, evaluating alternative wastewater disposal and reuse options. This analysis is necessitated by the City's pending State discharge permit.

Water Main Replacement

The city undertook a rehabilitation project to replace existing deteriorating water mains and reduce extraordinary maintenance costs due to water main breaks. This will also improve the system reliability.

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ATTACHMENT C

FINANCIAL INFORMATION

The city's accounting records are organized and operated on the basis of funds. A fund is defined as a fiscal and accounting entity with a self-balancing set of accounts and fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities.

Management of the city is responsible for establishing and maintaining an internal control structure designed to ensure that the assets of the city are protected from loss, theft or misuse and to ensure that adequate accounting data are compiled to allow for the preparation of financial statements in conformity with generally accepted accounting principles. The internal control structure is designed to provide reasonable, but not absolute, assurance that these objectives are met. The concept of reasonable assurance recognizes that: (1) the cost of a control should not exceed the benefits likely to be derived; and (2) the valuation of costs and benefits requires estimates and judgments by management.

In addition, the city maintains budgetary controls. The objective of these controls is to ensure compliance with legal provisions embodied in the annual appropriated budget approved by the City Council. All operating, special revenue, debt service and capital improvement activities of the city are included in the annual appropriated budget. The legal level of budgetary control (that is, the level at which actual expenditures may not legally exceed the appropriated amount) is at the fund level. The city also maintains an encumbrance accounting system as one technique in accomplishing budgetary control. Open encumbrances at June 30, 2005 are reported as reservations of fund balance in the city's governmental funds. Management considers such encumbrances as a use of budgetary authority and they are reflected as equivalent to an expenditure in the accompanying budget and actual schedules. In conformance with generally accepted accounting principles, encumbrances are otherwise not included in the accompanying operating statements.

We believe that the statements and schedules included in the Financial Section of this report demonstrate that the city is meeting its responsibility for sound financial management.

CASH MANAGEMENT

The city pools all cash funds not held by fiscal agents in order to maximize investment opportunities and increase flexibility. Investment earnings are credited back to all funds contributing to the pool monthly, based on the fund's cash balance as a percentage of the pool. Investment responsibility is located organizationally within the Finance Department, but internal control is rigorously maintained to provide accountability and to protect the city's cash assets. Investments are conservatively managed with the three primary objectives of safety of principal, liquidity to meet disbursement requirements, and investment yield pursued in that order.

During the 2004-05 Fiscal Year, a portion of the city's pooled cash was invested in the Local Agency Investment Fund, an investment pool for local agencies operated by the State of California Treasurer's Office. Investments were also placed in federally sponsored agency notes where opportunities presented themselves to enhance investment yield while maintaining safety and liquidity. Total investment earnings for all funds held in the city treasury totaled \$2,526,366, a return of 2.669%. Our return exceeds the average effective yield of the Local Agency Investment Fund of .149%

At the June 30, 2005 close of the city's fiscal year, \$91,061,646 was accounted for in the city's treasury with investments valued based on fair value (rather than the actual amount invested). During Fiscal Year 1997-98, the city adopted the requirements of Governmental Accounting Standards Board Statement 31, which calls for the recognition in the city's accounts of the unrealized net market value gain or loss on investments held by the city and its fiscal agents.

RISK MANAGEMENT

The Yolo County Public Agency Risk Management Insurance Authority (YCPARMIA) JPA handles the city's risk management. The deductible for liability is \$5,000 and for workers comp is \$1,000. This limits the city's risk to an insignificant amount.

ATTACHMENT D

OTHER INFORMATION

INDEPENDENT AUDIT

The city's financial statements were audited by the independent accounting firm of Maze & Associates Accountancy Corporation. Their unqualified opinion is presented at the front of the financial section. We wish to express our appreciation to the staff of Maze & Associates for their assistance during the audit process.

AWARDS

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the city of Davis for its comprehensive annual financial report for the fiscal year ended June 30, 2004. This was the seventh consecutive year that the government has achieved this prestigious award. In order to be awarded a Certificate of Achievement, a government must publish an easily readable and efficiently organized comprehensive annual financial report. This report must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe that our current comprehensive annual financial report, which implements GASB Statement 34, continues to meet the Certificate of Achievement Program's requirements and we are submitting it to the GFOA and CSMFO to determine its eligibility for another certificate.