

**AUDITOR-CONTROLLER  
COUNTY OF ORANGE**

HALL OF FINANCE AND RECORDS  
12 CIVIC CENTER PLAZA, ROOM 200  
POST OFFICE BOX 567  
SANTA ANA, CALIFORNIA 92702-0567

(714) 834-2450 FAX: (714) 834-2569

[www.ac.ocgov.com](http://www.ac.ocgov.com)



**COUNTY EXECUTIVE OFFICE  
COUNTY OF ORANGE**

ROBERT E. THOMAS HALL OF  
ADMINISTRATION  
333 W. SANTA ANA BLVD.  
SANTA ANA, CALIFORNIA 92701

(714) 834-2345 FAX: (714) 834-3018

[www.oc.ca.gov](http://www.oc.ca.gov)

December 16, 2009

The Citizens of Orange County:

The Comprehensive Annual Financial Report (CAFR) of the County of Orange, State of California (County), for the year ended June 30, 2009, is hereby submitted in accordance with the provisions of Sections 25250 and 25253 of the Government Code of the State of California. The report contains financial statements that have been prepared in conformity with United States generally accepted accounting principles (GAAP) prescribed for governmental entities. Responsibility for both the accuracy of the data, and the completeness and fairness of the presentation, including all disclosures, rests with the County. A comprehensive framework of internal controls has been designed and established to provide reasonable assurance that the enclosed data are accurate in all material respects and are reported in a manner designed to present fairly the financial position and changes in financial position of County funds. Because the cost of internal controls should not outweigh their benefits, the County's comprehensive framework of internal controls has been designed to provide reasonable, rather than absolute assurance that the financial statements will be free from material misstatements.

The CAFR has been audited by the independent certified public accounting firm of Vavrinek, Trine, Day & Co., LLP. The goal of the independent audit was to provide reasonable assurance about whether the basic financial statements of the County for the year ended June 30, 2009, are free of material misstatement. The independent certified public accounting firm has issued an unqualified ("clean") opinion on the County's financial statements as of and for the year ended June 30, 2009. The independent auditor's report is located at the front of the financial section of this report.

This letter of transmittal is designed to complement and should be read in conjunction with Management's Discussion and Analysis (MD&A) that immediately follows the independent auditor's report. MD&A provides a narrative introduction, overview, and an analysis of the basic financial statements.

**PROFILE OF THE GOVERNMENT**

The County, incorporated in 1889 and located in the southern part of the State of California, is one of the major metropolitan areas in the state and nation. The County occupies a land area of 798 square miles with a coastline of 42 miles serving a population of over 3 million. It represents the third most populous county in the state, and ranks sixth in the nation.

The County is a charter county as a result of the March 5, 2002 voter approval of Measure V, which provides for an electoral process to fill mid-term vacancies on the Board of Supervisors. Before Measure V, as a general law county, mid-term vacancies would otherwise be filled by gubernatorial appointment. In November 2008, voters approved Measure J, which added Article III, Section 301 to the Charter of Orange County requiring voter approval for increases in future retirement system benefits of any employee, legislative officer, or elected official of the County of Orange in the Orange County Employees Retirement System or any successor retirement system, with the exception of statutorily-established cost of living adjustments, salary increases, and annual leave or compensatory time cash-outs. In all other respects, the County is like a general law county. The County is governed by a five-member Board of Supervisors (the Board), who each serve four-year terms, and annually elect a Chairman and Vice-Chairman. The supervisors represent districts that are each approximately equal in population. The district

boundaries were revised effective September 14, 2001, incorporating the results of the 2000 census. A County Executive Officer directly oversees 17 County Departments, and elected department heads oversee seven County Departments. The Supervisorial Districts map below shows the boundaries of Orange County and the areas governed by each member of the Board.



The County provides a full range of services countywide, for the unincorporated areas, and contracted through cities. These services are outlined in the following table:

<b>Countywide Services</b>		<b>Unincorporated Area Services</b>	
Affordable Housing (Housing Authority)	Indigent Medical Services	Animal Care & Control	Libraries
Agricultural Commissioner	Jails & Juvenile Facilities	Flood Control	Parks
Airport	Juvenile Justice Commission	Land Use	Water Disposal Collection
Child Protection & Social Services	Landfills & Solid Waste Disposal	Law Enforcement	
Child Support Services	Law Enforcement		
Clerk-Recorder	Local Agency Formation Commission		
Coroner & Forensic Services	Probationary Supervision		
District Attorney	Public Assistance		
Elections & Voter Registration	Public Defender/ Alternate Defense		
Environmental / Regulatory Health	Public & Mental Health		
Flood Control & Transportation	Senior Services		
Grand Jury	Tax Assessment Collection & Appeals		
Harbors, Beaches & Parks	Veterans Services		
Disaster Preparedness	Weights & Measures		

<b>Contract Services for Cities</b>	
Animal Care & Control	Libraries
Law Enforcement	Public Works & Engineering

Source: County of Orange Facts and Figures, 2009

In addition to these services, the County is also financially accountable for the reporting of component units. Blended component units, although legally separate entities, are, in substance, part of the County's operations; and therefore, data from these units are combined with data of the County. The County has one component unit, the Children and Families Commission of Orange County, which requires discrete presentation in the government-wide financial statements. The following entities are presented as blended component units in the basic financial statements for the year ended June 30, 2009: the Orange County Flood Control District, Orange County Development Agency, Orange County Housing Authority, Orange County Financing Authority, Orange County Special Financing Authority, Orange County Public Financing Authority, Orange County Public Facilities Corporation, In-Home Supportive Services Public Authority, and certain special districts. Additional information on these entities can be found in Note 1 in the Notes to the Basic Financial Statements.

The County maintains budgetary controls to ensure compliance with legal provisions embodied in the annual appropriated budget approved by the Board. Activities of the General Fund and most of the Special Revenue, Debt Service, Capital Projects and Permanent funds are included in the annual appropriated budget. The level of budgetary control (that level which cannot be exceeded without action by the Board) is at the legal fund-agency unit level, which represents a department or an agency. Budget-to-actual comparisons are provided in this report for each governmental fund for which an appropriated annual budget has been adopted. The Budgetary Comparison Statements for the General Fund and Major Special Revenue Funds are part of the Basic Financial Statements. The Budgetary Comparison Schedules for the nonmajor Governmental Funds and major Debt Service Fund with appropriated annual budgets are presented in the Supplementary Information section for governmental funds. The County also maintains an encumbrance accounting system as one technique of accomplishing budgetary control. Encumbered appropriations do not lapse at year-end; encumbrances outstanding at that time are reported as reservations of fund balances for the following year's budget. Additional information on the budgetary process can be found in Note 1 in the Notes to the Basic Financial Statements.

The County of Orange eGovernment portal at <http://www.ocgov.com> provides extensive information about County government and its services to the citizens of Orange County and others who visit our web pages. During Fiscal Year (FY) 2008-09, over 7 million visits were made to the Orange County web site and those visitors viewed over 22 million pages of information. The County's website includes information about the Board, County job listings, purchasing bid solicitations, County directories, assessment appeals, links to court information and local court rules, voter information, County permits and forms, and financial information. The site also provides several online services, such as ordering birth, death and marriage certificates, performing a fictitious business name search, looking up election results and polling places, and paying property taxes, including the ability to view both live and archived Board meetings, and online public comments to Board agendas. The County continues to improve the website by increasing the citizens' ability to conduct business online with the County.

## FACTORS AFFECTING ECONOMIC CONDITION

### Local Economy

Two indicators of the Orange County economy are: how well the local economy performs relative to surrounding counties, the state and the nation (external indicators), and how well the local economy performs relative to its own historical trends (internal indicators). This section provides various external and internal indicators that describe the current and projected outlook of the Orange County economy.

In terms of the external indicators, Orange County's economy routinely out-performs local surrounding counties, the state and national economies (in annual percentage growth), and, in fact, ranks higher (in absolute dollars) than the economies of the majority of the world's countries. External indicators show a downturn in the local economy.

Orange County's unemployment rate continues to be below that of all surrounding Southern California counties, and the State of California (see Table 1).

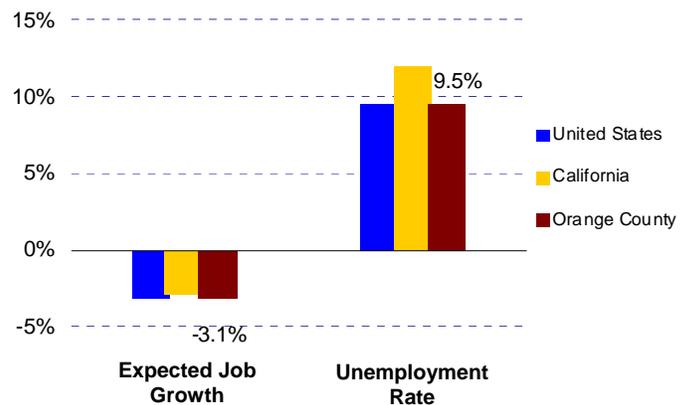
According to Chapman University, Orange County's job growth is expected to decrease by 3.1% in 2009 and result in approximately 45,740 fewer jobs relative to 2008. This compares to decreases of (2.9%) for the State of California and (3.2%) at the national level.

According to Chapman University, inflation, as measured by the Consumer Price Index (CPI), is expected to be comparable for Orange County relative to the U.S. and the State of California in 2009. (see Table 2).

**Table 1 : Unemployment Rate Comparison**

Primary Government Entity	September 2009 Unemployment Rate
United States	9.5%
California	12.0%
Los Angeles County	12.6%
<b>Orange County</b>	<b>9.5%</b>
Riverside County	14.9%
San Bernardino County	13.8%
San Diego County	10.4%

**Unemployment and Expected Job Growth Rates**



Sources: State of California, Employment Development Department  
Economic & Business Review, Chapman University, June 2009

**Table 2: 2009 – Projected Increase of the CPI**

United States	California	Orange County
1.0%	1.1%	1.0%

Orange County's Housing and Urban Development median family income is expected to be \$86,100 (absolute dollars) in 2009, up from \$84,100 (absolute dollars) in 2008. Median family incomes in Orange County continue to exceed all surrounding Southern California counties, the State of California and the nation (see Table 3).

According to DataQuick Information Systems, the median home sales price for new and existing homes in Orange County was \$427,750 (absolute dollars) in August 2009, representing a 2.8% decrease relative to August 2008. This decrease in Orange County is reflected in other Southern California Counties as well. The actual median sales price in Orange County continues to exceed all surrounding counties (see Table 4).

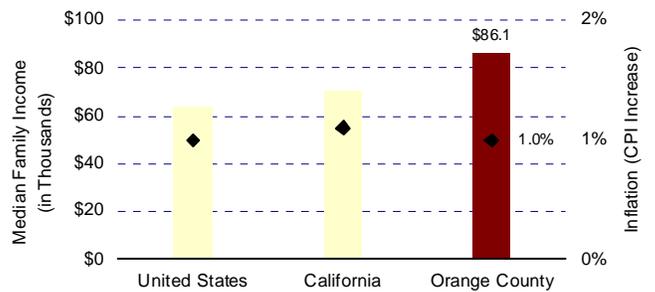
For the future, Chapman University is projecting that while housing values will continue to decline, housing affordability (compared to other parts of the country) will remain low.

In terms of internal trends, current and projected indicators suggest that the Orange County economy will decline throughout 2009. Historical point-in-time unemployment rates in Orange County during the month of August show a steady increase since 2006.

**Table 3: Median Family Income Comparison**

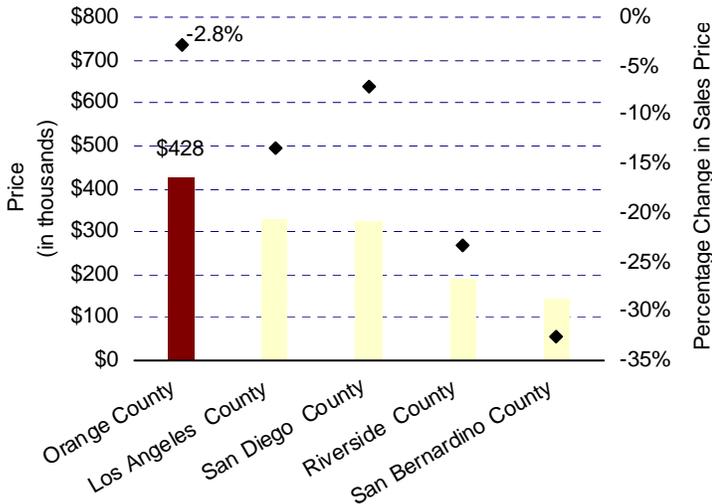
Primary Government Entity	Median Family Income (absolute dollars)
United States	\$64,000
California	\$70,400
Los Angeles County	\$62,100
<b>Orange County</b>	<b>\$86,100</b>
Riverside County	\$64,500
San Diego County	\$74,900

**Comparisons of Inflation and Median Family Income**



Sources: Economic & Business Review, Chapman University, June 2009  
 U.S. Department of Housing and Urban Development, 2009

**Comparison of Median Home Sales Price and Price Changes Among Counties**



Source: DataQuick Information Systems, October 2009

**Table 4: Median Home Sales Price Comparison – Southern California Counties – August 2009**

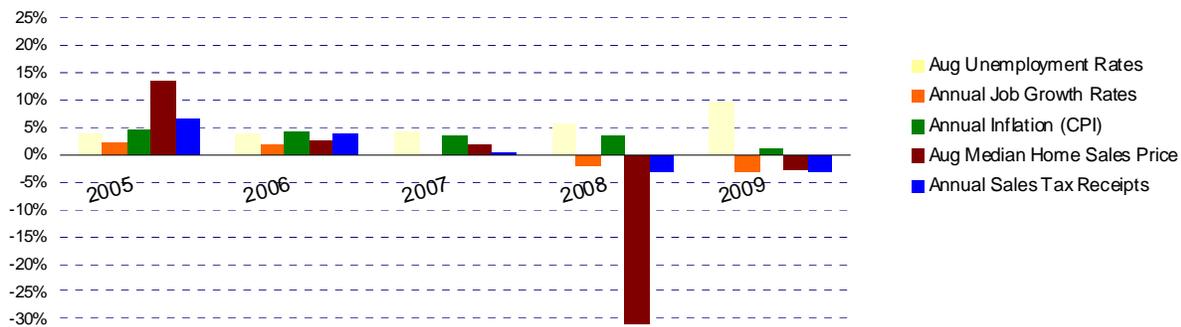
Primary Government Entity	Median Home Sales Price Change Increase/(Decrease)	Median Home Sales Price (absolute dollars)
Los Angeles County	(13.3%)	\$329,500
<b>Orange County</b>	<b>(2.8%)</b>	<b>\$427,750</b>
Riverside County	(23.2%)	\$190,000
San Bernardino County	(32.6%)	\$145,000
San Diego County	(7.1%)	\$325,000

Table 5 shows various internal indicators reflecting the slowing of Orange County's economy. First, job growth has decreased since 2005. Second, year-to-year home sales prices have continued to decrease for several years. Third, changes in taxable sales in Orange County have continually declined since 2005.

**Table 5: Orange County Historical Data**

Historical Indicators	2005	2006	2007	2008	2009
Aug Unemployment Rates	3.8%	3.6%	4.2%	5.8%	9.6%
Annual Job Growth	2.3%	1.9%	(0.2%)	(2.0%)	(3.1%)
Annual CPI Inflation	4.5%	4.3%	3.3%	3.5%	1.0%
Aug Median Home Sales Price increase	13.6%	2.6%	1.9%	(31.5%)	(2.8%)
Annual Change in Sales Tax Receipts	6.5%	3.9%	0.2%	(3.0%)	(3.1%)

**Orange County Historical Data Comparison**  
(Shown as a year-to-year percentage increase/decrease)



Sources: State of California, Employment Development Department  
Economic & Business Review, Chapman University, June 2009  
DataQuick Information Systems, September 2009  
Auditor-Controller, County of Orange

In summary, economic growth in Orange County continues to show signs of slowing down. Projected trends suggest a continuing pattern.

### Long-Term Financial Planning

Strategic Plan: In March 1997, the Board initiated a financial planning process that is a key component of the County's commitment to fiscal responsibility, accountability and efficiency. The plan includes projections of County general purpose revenues, departmental projections of operating costs, revenues and capital needs for current programs and services and anticipated caseload changes. New programs, services and capital projects are identified and prioritized on a countywide basis with financial impacts identified over the plan period. The plan covers a five-year period and includes a ten-year analysis of operating costs in cases where new programs and facilities are recommended to ensure the ability to pay for long-term operational costs.

The Board adopted the 2009 Strategic Financial Plan (SFP) on December 15, 2009. The 2009 SFP is the foundation in planning for continued financial stability and will be augmented by the monitoring and establishment of budgetary controls, via the FY 2009-10 quarterly budget reporting process and the adoption of the FY 2010-11 Budget. The five-year SFP projections indicate that General Purpose Revenue growth will continue to remain relatively flat in the first year of the plan and will grow at a much slower rate than predicted in prior years SFPs, including 2008. The continued flux in the economy, coupled with continued wariness of consumer confidence will continue to impact recovery at least into the next fiscal year and possibly into FY 2011-12. As such, operations cannot be maintained at past levels, and the Departments and the County Executive Office will collaboratively monitor programs and financial operations on an ongoing basis to ensure that the County continues to provide outstanding, cost-effective regional public services.

In order to address identified budget issues and prepare for the continued uncertainty of the general and local economy, the following represent some of the actions taken or identified as options for early planning. Early action is critical to ensure baseline services are met and that the County continues to experience financial stability.

- The 2009 SFP reflects a 6% reduction in FY 2010-11 Net County Cost limits.
- Action was taken in the FY 2009-10 First Quarter Budget Report to apply year-end Fund Balance Available toward projected current year General Fund revenue shortfalls in order to balance the budget.
- Actions to delete vacant positions and a hard hiring freeze were implemented.
- Departments continue to monitor the State budget for additional impact and take action when quantifiable.
- Capital project and information technology projects were identified for elimination or deferral.
- Equipment and capital asset purchases are being deferred where appropriate.

Santa Ana River Mainstem Project: The Santa Ana River Mainstem Project (SARP) was initiated in 1964, in partial response to a resolution of the United States House Committee on Public Works adopted May 8, 1964. A survey report was completed by the Orange County Flood Control District in 1975. The report was reviewed and submitted to Congress in September 1978. In September 1980, the United States Corps of Engineers completed the General Design Memorandum for the SARP. Construction for the SARP was authorized by the Water Resources Development Act of 1986. Construction for the SARP was initiated in 1989, and completion is scheduled for 2015.

The SARP is designed to provide flood protection to the growing urban communities in Orange, Riverside and San Bernardino Counties. The proposed improvements to the system cover 75 miles, from the headwater of the Santa Ana River east of the city of San Bernardino to the mouth of the river at the Pacific Ocean between the cities of Newport Beach and Huntington Beach. The project will increase levels of flood protection to more than 3.35 million people within the three county areas. The project includes seven independent features: Seven Oaks Dam, Mill Creek Levee, San Timoteo Creek, Oak Street Drain, Prado Dam, Santiago Creek and the Lower Santa Ana River. More information on the SARP is available in Note 15, Construction and Other Significant Commitments. To learn more about the SARP, visit the Orange County Flood Control Division's website at <http://www.ocflood.com>.

Trial Court Facilities: On September 30, 2002, Governor Gray Davis signed the Trial Court Facilities Act of 2002 (SB 1732). This landmark legislation shifts governance of California's more than 450 courthouse facilities from the counties to the State. The bill took effect on January 1, 2003, and required the transfer of all court facilities before June 30, 2007. In April 2008, AB 1491 extended the deadline to December 31, 2009, for the transfer of court facilities to the State. The State Administrative Office of Courts (State AOC) is under direction to continue to work on transfers, and to prepare the transfer agreements, pending legislative approval. The County formed a transition task force and negotiating team to develop a plan to identify the impacts and the steps necessary to ensure a smooth and timely transition. Some important issues were bonded indebtedness, calculation of county facilities payments for each court facility, seismic ratings of court buildings, County space allocation, parking space allocation, approved capital projects, former Federal modular court facility, and transfer/financing of the proposed new South Justice Center. All of the important issues have been resolved by the County through negotiations and dispute resolution processes.

On December 12, 2006, the Board approved a "Letter of Intent" between the Superior Court of California, County of Orange, and State AOC relating to the Funding and Expansion of the South Justice Center in Laguna Niguel, California and directed County staff to work with the Superior Court of California and the State AOC to develop the Transaction Documents. On November 12, 2008, the Superior Court advised the County that the project will be officially declared "on hold." In the course of negotiations related to the transfer of all of the court facilities, the County, the State AOC, and the Superior Court determined that the former court facility located at 30143 Crown Valley Parkway, Laguna Niguel, California, commonly referred to as the "South Justice Center" will not transfer and will remain the property and responsibility of the County. The County agreed to transfer the Civil Complex Center (CXC) or former Federal modular county facility in exchange for the South Justice Center, Laguna Niguel court facility.

The August 2005 refunding of the 1996 Recovery Certificates of Participation allowed the County to unencumber (release) all court properties from this particular refunding debt. The Betty Lou Lamoreaux Justice Center continues

to be encumbered by the Orange County Public Financing Authority, Juvenile Justice Center Facility Lease Revenue Refunding Bonds, Series 2002 and is the only remaining court facility with bonded indebtedness.

On July 28, 2009, the Board approved an agreement with the AOC to transfer the Harbor Court facility. On October 20, 2009, the Board approved an agreement with the AOC to transfer the Irvine Lease and Laguna Hills leased court facilities in South County. On November 10, 2009, the Board approved an agreement with the AOC to transfer the North County Trial Court facilities located in Fullerton and the West Justice Center Trial Court facilities located in Westminster. On November 24, 2009, the Board approved an agreement with the AOC to transfer the Lamoreaux Court facilities located in Orange. On December 8, 2009, the Board approved an agreement with the AOC to transfer the Central Court, the CXC and the Community Court facilities located in Santa Ana. These actions will complete the Court Transfer process required by State legislation.

OC Dana Point Harbor Revitalization Plan: On October 9, 2009, the Coastal Commission approved the Dana Point Harbor Revitalization Plan, which includes long awaited revitalization improvements in Dana Point Harbor. The next steps for the Harbor Revitalization Plan involve various phases for projects on both the waterside and landside. The County will prepare specific projects for coastal development permits within each specific planning area as appropriate. All of these projects will be based on the policies contained within the new Local Coastal Program approved by the Coastal Commission.

The total revitalization cost is estimated at \$168,000, including waterside improvements of \$85,000 and landside improvements of \$83,000. Waterside improvements would be funded by the State Department of Boat and Waterways (DBW) loan of up to \$60,000. The landside improvements would be funded by bond proceeds up to \$55,000; the balance needed to complete the financing of the improvements will be accumulated from the OC Dana Point Harbor cash flow (i.e., pay-as-you-go). Bond proceeds are projected to be received in FY 2011-12. OC Dana Point Harbor and County Executive Office Public Finance staff is expected to present the initial financial plan to the Public Facilities Advisory Committee and the Board.

### **Relevant Financial Policies**

To achieve the goal of providing outstanding, cost-effective regional public services, the County of Orange applies sound management practices and policies that enhance the quality of life of its citizens. Such financial management practices have been identified by the Government Finance Officers Association of the United States and Canada (GFOA) and recognized by Fitch Ratings as best practices that promote financial soundness, efficiency in government and solvency in public finance. The following table summarizes the County's financial management practices. For additional information regarding the County's financial management practices, visit the CEO Finance and Budget website at <http://www.ocgov.com/finance/financereports.asp>.

<b>Relevant Financial Policies</b>	
<b>Department Business Plans</b>	Each County Department prepares a biennial Business Plan. Business Plans communicate the value the department brings to the community and outcome indicators that measure performance. A business plan sets forth long-term goals, operational and budget challenges, strategies for overcoming challenges and progress towards achieving those goals during the coming year.
<b>Multi-year Strategic Financial Plan</b>	The County's Strategic Financial Plan is based on a five-year financial forecast and includes a 10-year analysis of operating costs in cases where new programs and facilities are recommended to ensure the ability to pay for long-term operational costs. Department Business Plans are a key element of the Strategic Financial Plan process.
<b>Five-Year Capital Improvement Plan</b>	The County's five-year Capital Improvement Plan (CIP) is a long-term list of significant projects funded by the General Fund in the Capital Projects budget. It also includes the five-year capital program for non-General Fund agencies. The CIP aids the County in its assessment of the best use of funds available in order to establish and prioritize its capital asset goals, while maintaining long-term financial stability.
<b>Quarterly Budget Report</b>	The County Executive Office issues quarterly budget reports that provide the Board, County departments, members of the public, and other interested parties with an overview of the current status of budgeted revenues and expenditures, total budgeted positions and various departmental issues requiring adjustments to the County's budget.
<b>Annual Budget Policies and Guidelines</b>	The Annual Budget reflects the County's disciplined approach to fiscal management and is consistent with the County's Strategic Financial Planning process. Department budgets are consistent with the priorities and operations plans contained in the Strategic Financial Plan and the approved departmental business plans. Departments use these planning processes, along with outcome indicators, to evaluate programs and redirect existing resources as needed for greater efficiency to reduce costs and minimize the need for additional resources.
<b>Fund Balance Reserve Policy</b>	The County General Fund currently contains formal reserves, appropriations for contingencies, appropriated reserve-type funds, and reserves held by others. The purpose of these reserves is to protect community programs and services from temporary revenue shortfalls and provide for unpredicted, sudden and unavoidable one-time expenditures.

<b>Relevant Financial Policies (Continued)</b>	
<b>Contingency Planning Policy</b>	<p>The County General Fund maintains a Reserve for Contingencies. The target amount for this reserve is 10% of ongoing annual general purpose revenues (excludes fund balance available and one-time amounts and transfers). For FY 2008-09, the target amount for the reserve was \$61,300. The current balance is \$61,300.</p> <p>In addition to the Reserve for Contingencies, the County budgets an annual Appropriation for Contingencies of no less than \$5,000 in the General Fund, which may be used for significant unanticipated emergencies, catastrophes, one-time expenditures and opportunities.</p>
<b>Debt Disclosure Practices</b>	The County presents a set of disclosures in the County's adopted Budget document and the CAFR.
<b>Pay-as-you-go Capital Funding</b>	The County's long-term practice has been to use pay-as-you-go funding for capital projects whenever possible. The use of systematic long range financial planning assists in making fiscal decisions such as debt vs. pay-as-you-go capital project financing. The Strategic Financial Plan forecasts sources of the County's revenue and operating expenses and incorporates a list of previously identified and prioritized projects that will benefit the citizens of the County. The financial planning for capital projects considers the County's limited funding sources, the capital and operating costs, useful life of projects, and good business practices.
<b>Credit and Debt Management Policy</b>	The County's long-term practice has been to rapidly repay debt when practicable. The County's Credit and Debt Management Policy states that one of its most important goals and objectives is to continue efficient debt reduction strategies through refunding, defeasance, or purchase and cancellation of bankruptcy related debt to lower the financial burden on the General Fund.
<b>Public Financing Advisory Committee</b>	The Public Financing Advisory Committee (PFAC) is responsible for the review, approval, modification or denial of debt financing proposals. No debt financing proposal is considered by the Board unless recommended in writing by the PFAC. The PFAC membership consists of the following: five public voting members, each representing a district, and three Ex-Officio County government members (the County Executive Officer (non-voting), the elected Treasurer-Tax Collector, and the elected Auditor-Controller).
<b>Audit Oversight Committee</b>	The Audit Oversight Committee (AOC) oversees the quality of financial reporting activities, results of operations, internal controls, and planned and long-term commitments. The AOC also oversees and monitors County compliance with pertinent laws and regulations and applicable ethical standards, as well as conflicts of interest and fraud policies. The AOC membership consists of five Ex-Officio members: the Chairman and Vice-Chairman of the Board, the elected Auditor-Controller, the County Executive Officer, the elected Treasurer-Tax Collector (non-voting), and one public member from the private sector appointed by the Board.

<b>Relevant Financial Policies (Continued)</b>	
<b>Treasury Oversight Committee</b>	The Treasury Oversight Committee (TOC) is responsible for reviewing and monitoring the annual Investment Policy Statement (IPS) prepared by the Treasurer. The TOC membership consists of the following: the elected Auditor-Controller, the County Executive Officer, the elected County Superintendent of Schools, one special district representative member, and one member from the public sector appointed by the Board.
<b>24/7 Fraud Hotline</b>	The Fraud Hotline is part of an ongoing fraud detection and prevention effort. The Fraud Hotline is intended for use by County employees, the general public, or vendors for reporting suspected waste, fraud, violations of County policy or misuse of County resources by vendors, contractors or County employees.

Investment Strategies in Uncertain Financial Markets

The Treasurer’s Investment Pools have weathered the turbulent financial markets well. Over the last year, the Treasurer maintained his strategy of a heavy concentration in United States government agencies effectively guaranteed by the Federal government. The Treasurer combined a strategic focus to keep the Pools’ investments safe with maintenance of liquidity in excess of the participants’ cash needs.

Credit and Debt Management Policy Strategies in Uncertain Financial Markets

The crisis in the financial markets in 2008 resulted in major bank failures, massive federal intervention in the form of financial support and guarantees to the banking, auto, and insurance industries. Ratings downgrades occurred for a variety of public and private entities. However, the County of Orange has not experienced any downgrades nor is the County on credit watch by any of the rating agencies. The direct impact on the County’s debt portfolio has been limited to periods of higher interest costs on variable rate debt issues, and lower interest earnings on some debt service reserve accounts due to termination of downgraded Guaranteed Investment Contract providers. The County’s own ratings were not affected. In June 2009, the County received the best available short-term ratings (MIG 1 by Moody’s, and SP-1+ by S&P) for its 2009-10 Tax and Revenue Anticipation Note of \$150,000 and had its long-term issuer rating confirmed.

**Major Initiatives**

Water Quality: The County of Orange, Orange County Flood Control District (District), and 34 cities operate water quality programs pursuant to the National Pollutant Discharge Elimination System program, a section of the federal Clean Water Act. Permits are issued by two Regional Water Quality Control Boards covering Orange County for five-year terms. The County is the principal permittee under both permits. The most recent permits issued in 2002 imposed stricter, more detailed, requirements than previous municipal stormwater permits. The permittees are required to review new development plans and inspect projects to ensure the inclusion of appropriate water quality protection measures (termed best management practices or BMPs), monitor the water quality in streams, flood control channels, harbors, bays, and beaches, and report their activities and monitoring results to the Regional Water Quality Control Boards. The permits require collaborative water quality planning initiatives in all eleven major watersheds in the County and direct the permittees to cooperate in appropriate water quality management programs across the region and within each watershed. The County, District, and cities must also determine and implement BMPs for public projects, commercial and industrial activities, construction sites, municipal operations, and maintenance activities and educate the public on common activities that prevent pollution. Permits are expected to be reissued with revised requirements during 2009.

Because of the importance of beach recreation to Orange County’s economy and quality of life, the County, District, and cities are investing heavily in runoff reduction and treatment programs. At the same time, the County is leading a regional coalition to review and update the water quality standards that are used to determine whether beaches and streams are unsafe because of pollution.

Labor Agreements: Multi-year labor agreements that include pension reform, no general salary increases and reductions in overtime costs have been approved with the Orange County Employees Association (OCEA) and several other bargaining units. These agreements are for three years through June of 2012. The Orange County Managers Association (OCMA) agreed to an extension of their contract through January of 2011 and the Orange County Attorneys Association (OCAA) agreed to an extension of their contract to June 2011. These groups represent over 15,000 of the County's 17,480 employees.

The pension reform provides new and existing employees the option of selecting a new retirement benefit formula (1.62% of pay times years of service at age 65) which would significantly reduce retirement benefit costs for employees and the County. Employees selecting the new plan would be eligible for a new Defined Contribution Plan with a County match of contributions up to a maximum of 2% of pay.

Overtime cost reductions of as much as 30% are estimated under the new OCEA agreement because overtime will be paid based on "hours worked" in excess of FLSA standards (generally after 40 hours worked in a week) compared to the prior agreement which provided overtime pay after 40 hours inclusive of paid time off hours.

The agreement with OCMA extended a prior three year agreement by one year and eliminated a previously negotiated salary increase. The OCMA agreement will save the County an estimated \$12,000 compared to the prior agreement that it replaced. The extension agreement with OCAA defers a general salary increase for one year and saves an estimated \$2,900, with the possible deferral for one additional year. It is anticipated that OCMA and OCAA will also agree to the pension reform as described above before the planned implementation of January 2010.

County of Orange Retiree Medical Plan: On April 6, 1993, the Board approved the County of Orange Retiree Medical Plan (the Retiree Medical Plan) to become effective August 1, 1993. Historically, the County funded the Retiree Medical Plan on a "pay-as-you-go" basis and had not established a long term financing plan. Based on actuarial valuation of the plan as of June 30, 2005, the County's Unfunded Actuarial Accrued Liability (UAAL) for this Other Postemployment Benefits (OPEB) plan was \$1,418,692 (unaudited).

Following the Board's approval of agreements with labor groups in 2006 and 2007 for the restructuring of the Retiree Medical Plan, the County's total UAAL for the June 2007 valuation of the restructured plan was approximately \$408,322 (unaudited), a decrease of over one billion dollars from the June 30, 2005, valuation. The County is paying the full amount of its Annual Required Contribution (ARC) for its OPEB obligation. The County is one of the few large government entities that has significantly reduced its OPEB obligation, and is paying its full ARC.

Refer to Note 19, Postemployment Health Care Benefits, for further details on the Retiree Medical Plan.

## **AWARDS AND ACKNOWLEDGEMENTS**

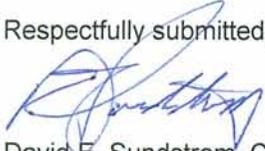
GFOA Awards: The GFOA awarded a Certificate of Achievement for Excellence in Financial Reporting to the County of Orange for its CAFR for the year ended June 30, 2008. This represents the County's 14<sup>th</sup> consecutive award. The Certificate of Achievement is the highest form of recognition for excellence in state and local government financial reporting.

In order to be awarded a Certificate of Achievement, a government unit must publish an easily readable and efficiently organized CAFR, whose contents conform to program standards. Such a CAFR 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 our current report continues to meet the Certificate of Achievement Program's requirements and we are submitting it to the GFOA to determine its eligibility for another certificate.

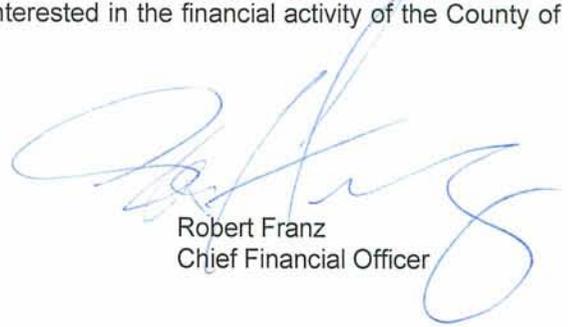
In addition, the County issued its sixth consecutive Popular Annual Financial Report (PAFR) titled the "OC Citizens' Report" for the year ended June 30, 2008. The County received the GFOA Award for Outstanding Achievement in Popular Annual Financial Reporting for this PAFR. The award is a prestigious national award recognizing conformance with the highest standards for preparation of state and local government popular reports. In order to be awarded, a government must publish a PAFR that reflects the program standards of creativity, presentation, understandability and reader appeal.

Acknowledgments: We would like to express our sincere appreciation to County staff and the staff of the certified public accounting firm of Vavrinek, Trine, Day & Co., LLP. We hope this report will be of interest and use to those in county government, other governmental agencies, and the public interested in the financial activity of the County of Orange.

Respectfully submitted,



David E. Sundstrom, CPA  
Auditor-Controller



Robert Franz  
Chief Financial Officer