

MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)

This section of the County's Comprehensive Annual Financial Report (CAFR) provides a narrative overview and analysis of the financial activities of the County for the year ended June 30, 2006. We hope that the information presented here, in conjunction with the Letter of Transmittal, provides a clearer picture of the County's overall financial status. Unless otherwise indicated, all amounts in this section are expressed in thousands of dollars.

FINANCIAL HIGHLIGHTS

- Total net assets increased by \$254,715, or 7% as compared to last year.
- Long-term debt decreased by \$279,368, or 21% during the current fiscal year.
- As of the end of the fiscal year, the County's governmental funds reported combined ending fund balances of \$1,898,401, a decrease of \$50,542, or 3% in comparison with the prior year.
- At June 30, 2006, unreserved fund balance in the General Fund was \$149,617, or 6% of total FY 2005-06 expenditures and transfers of \$2,338,690.
- General Fund revenues and transfers ended the year 2% below budget.
- General Fund expenditures and transfers ended the year 7% below budget.

OVERVIEW OF THE FINANCIAL STATEMENTS

The basic financial statements presented in the County's CAFR have been divided into three different sections:

- Government-wide Financial Statements
- Fund Financial Statements
- Notes to the Basic Financial Statements

<i>Basic Financial Statements</i>			
Government-wide Financial Statements	Fund Financial Statements		
	Governmental Funds	Proprietary Funds	Fiduciary Funds
Statement of Net Assets	Balance Sheet	Statement of Net Assets	Statement of Fiduciary Net Assets
	Statement of Revenues, Expenditures, and Changes in Fund Balances	Statement of Revenues, Expenses, and Changes in Fund Net Assets	
Statement of Activities	Budgetary Comparison Statement	Statement of Cash Flows	Statement of Changes in Fiduciary Net Assets
Notes to the Basic Financial Statements			

The following table summarizes the major features of the basic financial statements:

	Government-wide Financial Statements	Fund Financial Statements		
		Governmental Funds	Proprietary Funds	Fiduciary Funds
Type of Financial Statement	Statement of Net Assets Statement of Activities	Balance Sheet Statement of Revenues, Expenditures, and Changes in Fund Balances	Statement of Net Assets Statement of Revenues, Expenses, and Changes in Fund Net Assets Statement of Cash Flows	Statement of Fiduciary Net Assets Statement of Changes in Fiduciary Net Assets
Scope	Entire entity (except fiduciary funds)	Day-to-day operating activities for basic services	Day-to-day operating activities for business-type services	Resources on behalf of others
Accounting basis and measurement focus	Accrual accounting and economic resources measurement focus	Modified accrual and current financial resources measurement focus	Accrual accounting and economic resources measurement focus	Accrual accounting & economic resources focus
Type of asset and liability information	All assets and liabilities, both financial and capital, short-term and long-term	Current assets and liabilities that come due during the year or soon thereafter	All assets and liabilities, both financial and capital, short-term and long-term	All assets held in a trustee or agency capacity for others
Type of inflow and outflow information	All revenues and expenses during the year, regardless of when cash is received or paid	Revenues for which cash is received during the year or soon thereafter; expenditures when goods or services have been received and the related liability is due and payable	All revenues and expenses during the year, regardless of when cash is received or paid	All additions and deductions during the year, regardless of when cash is received or paid

Government-wide Financial Statements

The government-wide financial statements consist of the following two financial statements: the Statement of Net Assets and the Statement of Activities. Both of these statements were prepared using an accounting method and a measurement focus similar to those used by private-sector companies, the accrual basis of accounting and the economic resources measurement focus. The **Statement of Net Assets** provides information regarding all of the County's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the County is improving or deteriorating. The **Statement of Activities**, on the other hand, provides information on how the government's net assets changed during the most recent fiscal year regardless of the period when the related cash or cash equivalent is received or paid. Therefore, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (for example, uncollected taxes and earned but unused vacation leave).

The Statement of Net Assets and the Statement of Activities distinguish functions of the County that are principally supported by taxes (governmental activities) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (business-type activities). The governmental activities of the County include (1) general government, (2) public protection, (3) public ways and facilities, (4) health and sanitation, (5) public assistance, (6) education, and (7) recreation and cultural services. The business-type activities of the County include airport and waste management.

The government-wide financial statements also provide information regarding the County's component units, entities for which the County (the primary government) is considered to be financially accountable. Blended component units, although legally separate entities, are in substance part of the County's operations, and therefore, data from these component units are combined with data of the primary government. Financial information for the Children and Families Commission of Orange County, a discretely presented component unit, is reported separately from the financial information presented for the primary government itself.

Fund Financial Statements

- **Fund** - a separate accounting entity with a self-balancing set of accounts.
- Focus is on **major funds**.
- Provides information regarding the three major categories of all County funds: **governmental, proprietary, and fiduciary**.

The fund financial statements report on groupings of related funds that are used to maintain control over resources that have been segregated for specific activities or objectives. A fund is a separate accounting entity with a self-balancing set of accounts. Like other state and local governments, the County uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. The focus of governmental and proprietary fund financial statements is on major funds as determined by the criteria set forth in Governmental Accounting Standards Board (GASB) Statement No. 34 "*Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*." All of the County funds can be divided into three major categories of funds: governmental, proprietary, and fiduciary.

Governmental Funds - Governmental funds include most of the County's basic services and are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental funds financial statements are prepared using the modified accrual basis of accounting and current financial resources measurement focus.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Reconciliations are prepared for both the governmental funds' Balance Sheet and the governmental funds' Statement of Revenues, Expenditures, and Changes in Fund Balances to facilitate comparisons between governmental funds and governmental activities. The primary differences between the government-wide and fund financial statements relate to noncurrent assets, such as land and structures and improvements, and noncurrent liabilities, such as bonded debt and amounts owed for

compensated absences and capital lease obligations, which are reported in the government-wide statements but not in the fund financial statements.

In FY 2005-06, an increase of \$183,687 in net assets in the government-wide financial statements was reported, and a decrease of \$50,542 in fund balance was reported in the fund financial statements. Refer to the "Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balances of Governmental Funds to the Statement of Activities" for details on the factors contributing to these differences.

The County maintains several individual governmental funds organized according to their type (General Fund, Special Revenue, Debt Service, Capital Projects and Permanent Funds). Information is presented separately in the governmental funds Balance Sheet and in the Statement of Revenues, Expenditures, and Changes in Fund Balances for the General Fund, which is always a major fund, and all other major funds. Information for nonmajor funds is presented in the aggregate in these statements. Individual fund data for each of the nonmajor governmental funds is presented elsewhere in this report. The County adopts an annual appropriated budget for its governmental funds. Budgetary comparison statements and schedules have been provided for these funds to demonstrate compliance with the budget.

Proprietary Funds - The County maintains two different types of proprietary funds: Enterprise Funds and Internal Service Funds. **Enterprise Funds** are used to report the same functions presented as business-type activities in the government-wide financial statements. The County uses enterprise funds to account for its Airport and Waste Management operations (IWMD). **Internal Service Funds** are used to accumulate and allocate costs internally among the County's various functions such as insurance services, transportation, publishing, and information technology. Because these services predominantly benefit governmental rather than business-type functions, they have been included within governmental activities in the government-wide financial statements.

Proprietary fund financial statements provide the same type of information as the government-wide financial statements, only in more detail. The proprietary fund financial statements provide separate information for the Airport and Waste Management operations, which are both considered to be major funds of the County. Conversely, the Internal Service Funds are combined into a single, aggregated presentation in the proprietary funds financial statements with the individual fund data provided in combining statements, which can be found elsewhere in this report.

Fiduciary Funds - Fiduciary funds include the **Trust** and **Agency** funds and are used to account for assets held on behalf of outside parties, including other governments. Financial information for fiduciary funds is not reported in the government-wide financial statements because the resources of these funds are not available to support the County's programs. The combining statements for fiduciary funds are included elsewhere in this report.

Notes to the Basic Financial Statements

The Notes to the Basic Financial Statements provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. To find a specific note, refer to the Table of Contents.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

As noted earlier, net assets may serve over time as a useful indicator of the County's financial position. At June 30, 2006, the County's combined net assets (governmental and business-type activities) totaled \$4,143,016, an increase of 7% from FY 2004-05.

The largest component of the County's net assets (64%) was **invested in capital assets, less any related outstanding debt** used to acquire those assets. Capital assets include land, structures and improvements, equipment, construction in progress, and infrastructure that are used to provide needed services to the citizens of the County. Since the capital assets themselves cannot

COMPONENTS OF NET ASSETS	
•	Invested in Capital Assets, Net of Related Debt
•	Restricted
•	Unrestricted

be used to liquidate the associated debt, the resources needed to repay the debt must be provided from other sources.

The County's **restricted** net assets total \$1,526,499 which represents 37% of its net assets. This means that these resources are subject to external restrictions on how they may be used. External restrictions include those imposed by grantors, contributors, laws/regulations of other governments, or restrictions imposed by law through constitutional provisions or legislation, including those passed by the County itself.

The final component of net assets is **unrestricted net assets**. Unrestricted net assets are resources that the County may use to meet its ongoing obligations to citizens and creditors. As of June 30, 2006, governmental activities showed a negative amount of \$33,051 in unrestricted net assets. The deficit balance shown for unrestricted net assets was caused primarily by the County's election to settle bankruptcy-related debt according to the Modified Second Amended Plan of Adjustment, and is not a reflection of the County's lack of resources to meet its ongoing obligation to the citizens and creditors. Please refer to Note 10, Long-Term Obligations, for more details of this Plan.

The following table presents condensed financial information derived from the government-wide Statement of Net Assets:

NET ASSETS – Primary Government						
June 30, 2006						
	Governmental		Business-Type		Total	
	Activities		Activities			
	<u>2006</u>	<u>2005</u>	<u>2006</u>	<u>2005</u>	<u>2006</u>	<u>2005</u>
ASSETS						
Current and other assets	\$ 2,832,965	\$ 2,875,262	\$ 660,212	\$ 596,702	\$ 3,493,177	\$ 3,471,964
Capital assets	2,373,933	2,410,746	500,814	507,408	2,874,747	2,918,154
Total Assets	5,206,898	5,286,008	1,161,026	1,104,110	6,367,924	6,390,118
LIABILITIES						
Long-term liabilities	1,393,453	1,649,663	340,154	356,045	1,733,607	2,005,708
Other liabilities	424,653	431,240	66,648	64,869	491,301	496,109
Total Liabilities	1,818,106	2,080,903	406,802	420,914	2,224,908	2,501,817
NET ASSETS						
Invested in capital assets, net of related debt	2,306,178	2,336,881	343,390	335,795	2,649,568	2,672,676
Restricted	1,115,665	913,153	410,834	347,401	1,526,499	1,260,554
Unrestricted	(33,051)	(44,929)	--	--	(33,051)	(44,929)
Total Net Assets	\$ 3,388,792	\$ 3,205,105	\$ 754,224	\$ 683,196	\$ 4,143,016	\$ 3,888,301

As of June 30, 2006, the County's total assets decreased by less than 1%, or \$22,194 during the current fiscal year. Of this amount, current and other assets increased by \$21,213 (1%), while capital assets decreased by \$43,407 (1%). Total liabilities for this year decreased by 11% or \$276,909. Of this amount, long-term liabilities decreased by \$272,101 (14%), while other liabilities decreased by \$4,808 (1%).

The following table provides summarized data of the government-wide Statement of Activities:

CHANGES IN NET ASSETS – Primary Government						
For the Year Ended June 30, 2006						
	Governmental Activities		Business-Type Activities		Total	
	2006	2005	2006	2005	2006	2005
REVENUES						
Program Revenues:						
Charges for Services	\$ 477,360	\$ 470,259	\$ 216,014	\$ 210,103	\$ 693,374	\$ 680,362
Operating Grants and Contributions	1,605,063	1,540,938	22,846	13,968	1,627,909	1,554,906
Capital Grants and Contributions	18,178	66,889	1,720	10,703	19,898	77,592
General Revenues:						
Property Taxes	423,444	387,204	--	--	423,444	387,204
Property Taxes in Lieu of Motor Vehicle License Fees	158,240	141,319	--	--	158,240	141,319
Other Taxes	50,676	48,862	--	--	50,676	48,862
Grants and Contributions not Restricted to Specific Programs	1,881	9,442	--	--	1,881	9,442
State Allocation of Vehicle Motor License Fees	56,873	54,325	--	--	56,873	54,325
Other General Revenues	104,827	79,497	3,016	314	107,843	79,811
Total Revenues	2,896,542	2,798,735	243,596	235,088	3,140,138	3,033,823
EXPENSES						
General Government	227,536	171,771	--	--	227,536	171,771
Public Protection	972,996	947,698	--	--	972,996	947,698
Public Ways and Facilities	105,342	77,928	--	--	105,342	77,928
Health and Sanitation	467,640	455,059	--	--	467,640	455,059
Public Assistance	773,109	740,987	--	--	773,109	740,987
Education	40,452	30,641	--	--	40,452	30,641
Recreation and Cultural Services	72,535	73,530	--	--	72,535	73,530
Interest on Long-Term Debt	64,680	81,841	--	--	64,680	81,841
Airport	--	--	84,362	79,882	84,362	79,882
Waste Management	--	--	76,771	87,533	76,771	87,533
Total Expenses	2,724,290	2,579,455	161,133	167,415	2,885,423	2,746,870
Excess before Transfers	172,252	219,280	82,463	67,673	254,715	286,953
Transfers	11,435	14,579	(11,435)	(14,579)	--	--
Increase in Net Assets	183,687	233,859	71,028	53,094	254,715	286,953
Net Assets - Beginning of the Year	3,205,105	2,971,246	683,196	630,102	3,888,301	3,601,348
Net Assets - End of the Year	\$ 3,388,792	\$ 3,205,105	\$ 754,224	\$ 683,196	\$ 4,143,016	\$ 3,888,301

As of June 30, 2006, the County's net assets increased by 7%, or \$254,715 during the current fiscal year. Revenues for the year totaled \$3,140,138, an increase of \$106,315 from the previous year and expenses totaled \$2,885,423, an increase of \$138,553.

Governmental Activities

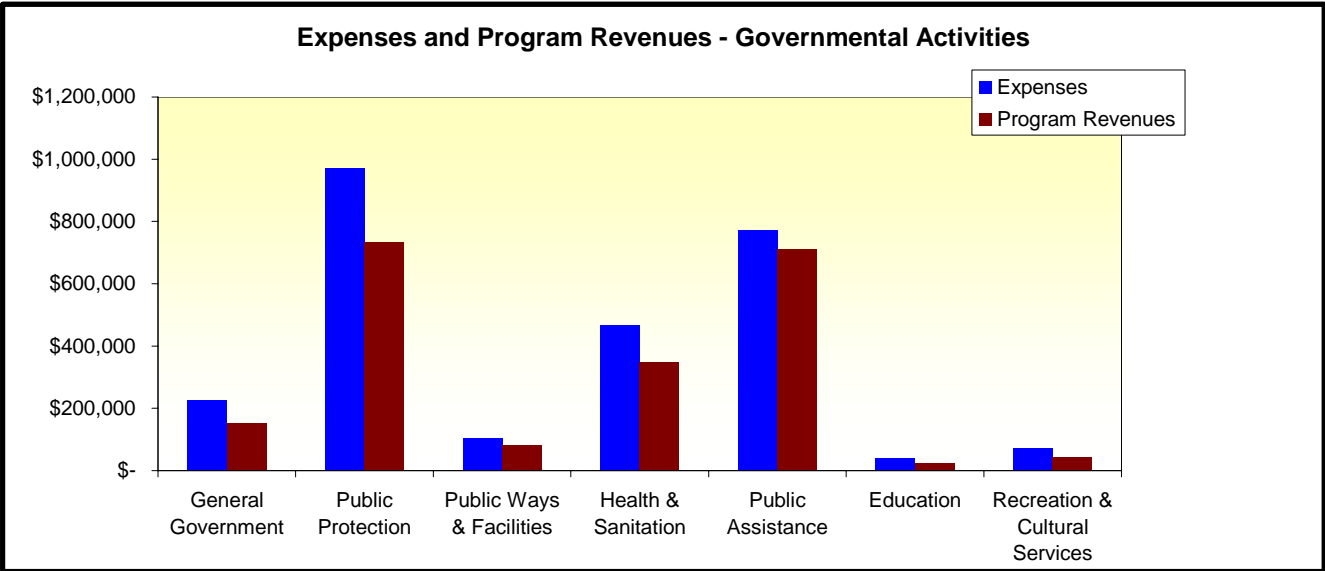
The County's governmental activities rely on several sources of revenue to finance ongoing operations. Operating Grants and Contributions comprised the largest revenue source for the County followed by Charges for Services. Operating Grants and Contributions are monies received from parties outside the County and are generally restricted to one or more specific programs such as the State and Federal revenues for public assistance and for health care. In the governmental funds, expenditure-driven grants are recognized as revenue when the qualifying expenditures have been incurred and all other grant requirements have been met. As expenditures increase, revenues increase proportionately. Charges for Services are revenues that arise from charges to customers or applicants who purchase, use, or directly benefit from the goods, services, or privileges provided. Examples of the types of services that fall under this category include engineering services provided to cities under contract, park and recreation fees, and law enforcement services provided to governmental agencies under contract.

At the end of FY 2005-06 total revenues for the governmental activities, including transfers from the business-type activities were \$2,907,977, an increase of \$94,663 from the previous year. Expenses totaled \$2,724,290, an increase of \$144,835 from the prior year. While revenues and expenses increased from the prior year, revenues still exceeded the expenses. Governmental activities increased the County's net assets by \$183,687, accounting for 72% of the total growth in the net assets of the County. In addition to the effects of expenditure-driven grants, key elements of the increase are as follows:

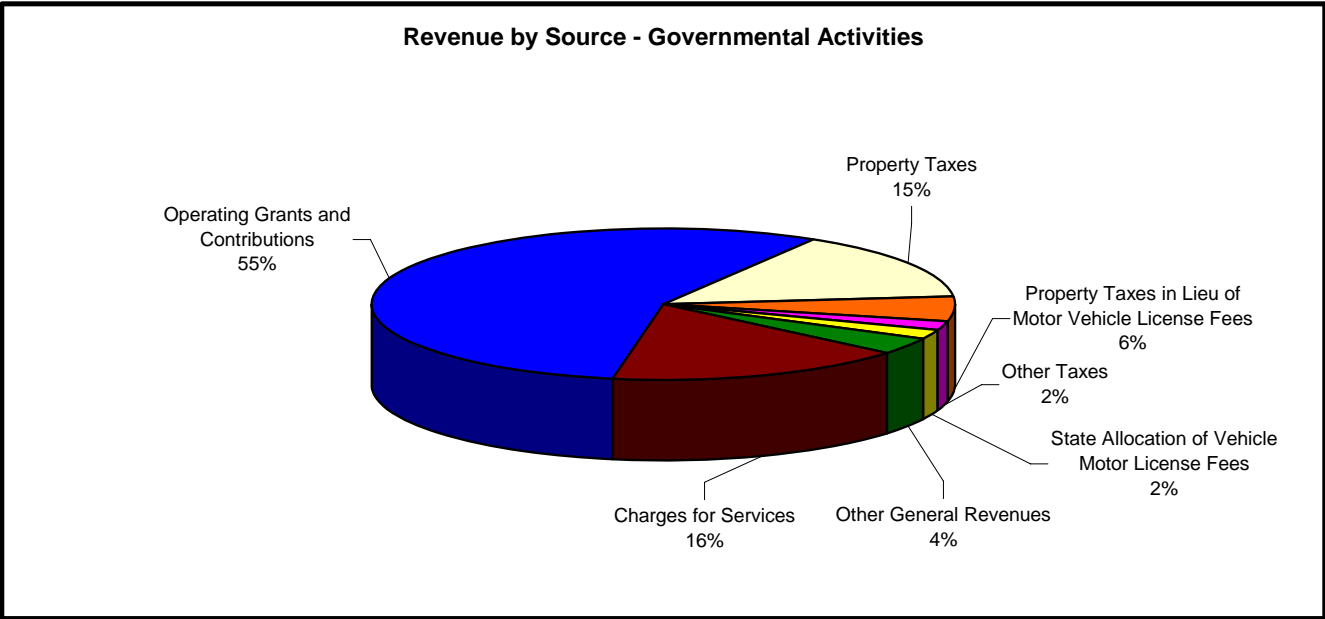
- Property Taxes increased by \$36,240 due to the continued growth in the assessed property valuations.
- Property Taxes in Lieu of Vehicle License Fees (VLF) increased by \$16,921 as a result of an increase in the assessed property valuations and a one time Property Tax in Lieu of VLF payment from the State for an underpayment in FY 2004-05, which was recognized in FY 2005-06.
- Operating Grants and Contributions increased by \$20,615 due to a growth of receipts from Proposition 172, a permanent state-wide half-cent sales tax for support of local public safety activities.
- General Government expenditures increased \$41,623 due to an increase of \$28,543 in retirement costs and an increase of \$13,080 due to the additional costs associated with the 48th District Congressional District Primary Special Elections.
- Public Protection expenditures increased by \$15,208, primarily due to increases in employee salary and benefits.
- Public Ways and Facilities expenditures increased by \$13,914 due to an increase in capital projects and work completed on Laguna Canyon Road and various intersection improvements along El Toro Road.

In addition to the above, the County received \$1,375 of deferred pass-through tax incremental revenue from the City of Yorba Linda Redevelopment Agency. This is the third and final annual installment payment agreed to by the Yorba Linda Redevelopment Agency.

The following chart presents a comparison of expenses by function and the associated program revenues for governmental activities:

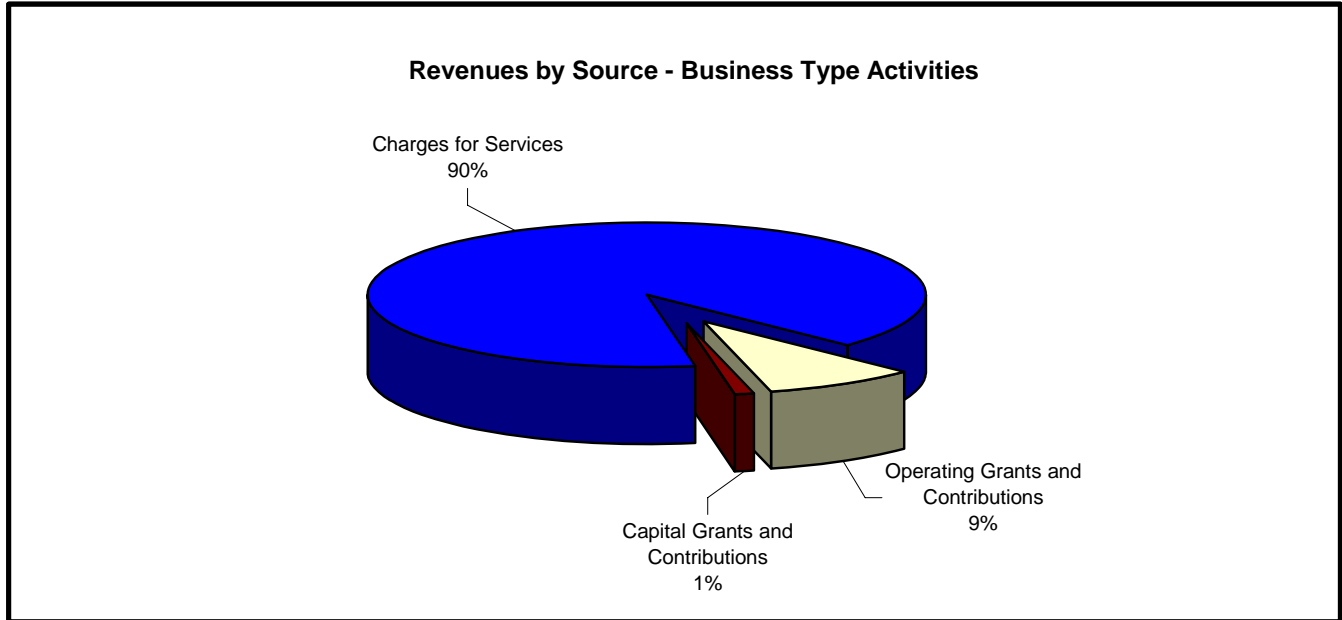


The chart below presents the percentage of total revenues by source for governmental activities:



Business-Type Activities

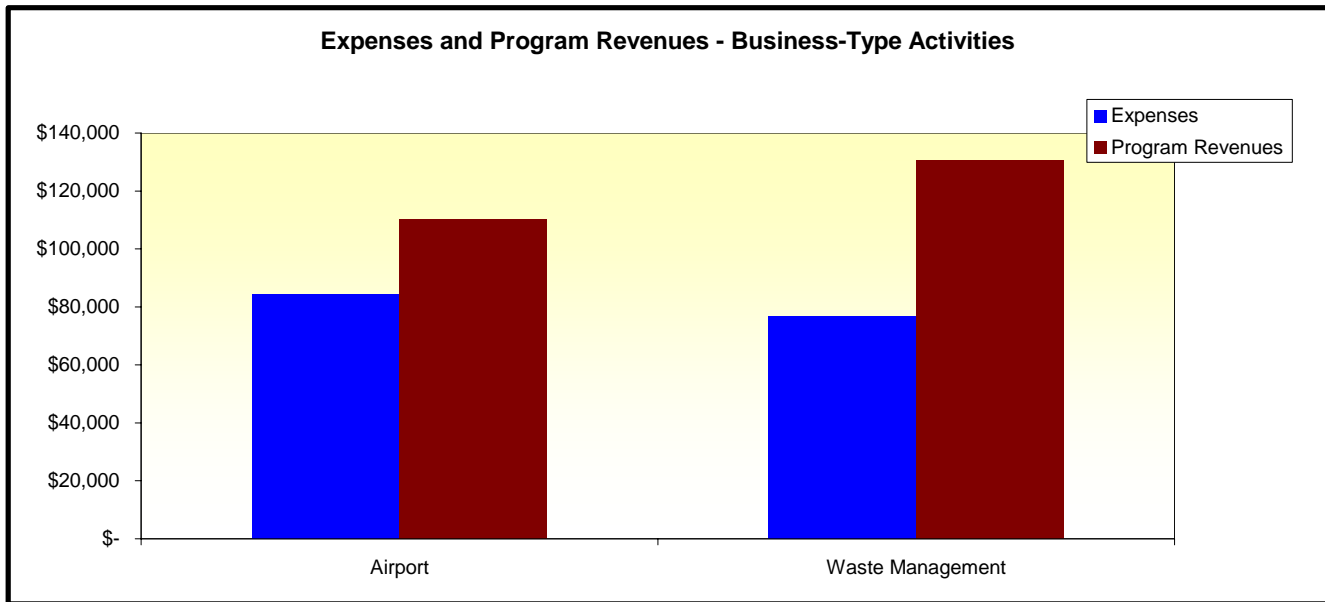
The County has two business-type activities: Airport and Waste Management. In keeping with the intent of recovering all or a significant portion of their cost through user fees and charges, business-type activities reported Charges for Services as their largest source of revenues. Operating Grants and Contributions, as well as Capital Grants and Contributions, were the other revenue sources for Airport and Waste Management activities. Capital Grants and Contributions include revenues received from the Federal Aviation Administration for use in airport construction projects.



At the end of FY 2005-06, business-type activities reported total revenues of \$243,596, an increase of \$8,508 from the prior year. Expenses, including transfers to the governmental activities, totaled \$172,568, resulting in a decrease of \$9,426 from the previous year. The program revenues (Charges for Services, Operating Grants and Contributions, and Capital Grants and Contributions) financed the majority of expenses recorded for the business-type activities. Other factors concerning the finances of the County's two enterprise funds are discussed in the Proprietary Funds section of the "Financial Analysis of the County's Funds." At the end of FY 2005-06, there was an increase of \$71,028 in net assets as compared to an increase of \$53,094 in FY 2004-05. The increase in net assets was mostly due to increased revenues; however, there was also a decrease in expenses. Key elements for the net increase are as follows:

- A \$6,276 increase in rents and concession from airline rent, parking, car rental, and lease concessions due to the increased number of passengers and the level of traveler activities at the airport.
- A \$8,694 increase in interest revenue due to the upward trend of interest rates.
- A \$4,647 increase in revenue due to lawsuit settlements paid to the Airport.
- A \$8,983 decrease in grant revenues due to the expiration of several grants in FY 2005-06.
- A \$2,020 increase in maintenance costs for elevators, loading bridge, baggage conveyor, pavement repairs, terminal corrosion control, and contingency expenses.
- A \$3,765 increase in professional services expenses primarily due to an increase in services provided by the Sheriff Department.
- A \$7,990 decrease in expenses resulting from an adjustment to the estimated future costs for landfill closure and postclosure care costs.
- A \$6,195 decrease in settlement payments for postclosure care costs.

The following chart displays expenses and the associated program revenues by function for the business-type activities:



FINANCIAL ANALYSIS OF THE COUNTY'S FUNDS

The County uses fund accounting to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities.

Governmental Funds

Governmental funds are accounted for using a current financial resources measurement focus. With this measurement focus, only current assets and current liabilities generally are included on the balance sheet. Such information may be useful in evaluating the County's near-term financing requirements.

In particular, unreserved fund balance may serve as a valuable measure of the government's resources that are available for spending at the end of the fiscal year. This amount is available for spending at the discretion of the County's Board of Supervisors in order to achieve the established function of the respective funds. Other than the General Fund, all other County funds are restricted for the particular purpose that each fund was established for. For example, special revenue funds have either legal or operational requirements to restrict expenditures for specified purposes, and debt service funds are restricted for payment of principal and interest on general long-term debt. Commitments by the County related to executory contracts for goods or services are recorded and established as reservations of fund balances in the governmental funds.

At June 30, 2006, the County's governmental funds reported total fund balances of \$1,898,401 which is a decrease of \$50,542 in comparison with the prior year. Of the total fund balances for the governmental funds, \$1,236,229 (65%) constitutes *unreserved fund balances*.

A significant amount of these unreserved fund balances are designated by the Board of Supervisors for the following uses in the next fiscal year and are deemed to be restrictions, commitments, or limitations, which affect the availability of fund resources in the next fiscal year:

Funds	Planned Uses of Unreserved Fund Balances
General Fund	- Deferred maintenance projects at various County facilities, Americans with Disabilities Act (ADA) improvement projects, re-budgeted capital projects, and projects at the County Central Utility Facility, which include refurbishment of the steam and chilled water system and the co-generation project.
Roads	- Construction and maintenance of roadways, and for specialized engineering services to other governmental units and the public.
Public Library	- Library services for the unincorporated areas as well as some of the incorporated areas within the County.
Flood Control District	- Planning, construction, operation, and maintenance of regional flood protection and water conservation works, such as dams, control channels, retarding basins and other flood control infrastructure.
Harbors, Beaches and Parks	- Development and maintenance of County harbors, tidelands and related aquatic recreational facilities, as well as the acquisition, operation and maintenance of County beaches, inland regional park recreation facilities and community park sites in the unincorporated areas.
Other Public Protection	- Safety and law enforcement activities such as child support programs, automated fingerprint identification systems and investigation teams.
Other Governmental	- Construction of various capital projects including affordable housing and for accounting of revenues received and reserved for future incorporation agreements and mental health services.

The remaining fund balances are *reserved*. Reserved fund balances primarily represent assets that are not available for spending or assets with restrictions imposed by parties outside the County.

Comparative Analysis of Changes in Fund Balances

The following schedule presents a summary of revenues and other financing sources, expenditures and other financing uses, and the net changes in fund balances for the governmental funds for the current and previous fiscal years:

**GOVERNMENTAL FUNDS
COMPARATIVE SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
For the Year Ended June 30, 2006**

	Revenues and Other Financing Sources		Expenditures and Other Financing Uses		Net Change in Fund Balances	
	2006	2005	2006	2005	2006	2005
General Fund	\$ 2,529,721	\$ 2,442,533	\$ 2,492,928	\$ 2,424,356	\$ 36,793	\$ 18,177
Roads	53,185	38,765	62,822	43,881	(9,637)	(5,116)
Public Library	35,476	32,433	32,709	30,972	2,767	1,461
Tobacco Settlement	28,708	31,031	32,378	32,179	(3,670)	(1,148)
Refunding Bonds and Recovery COPs & Debt Prepayment	17,106	119,543	280,503	100,445	(263,397)	19,098
Flood Control District	83,926	72,629	63,441	125,086	20,485	(52,457)
Harbors, Beaches, and Parks	89,396	81,359	75,213	72,429	14,183	8,930
Other Public Protection *	104,464	91,815	63,684	43,480	40,780	48,335
Other Governmental	815,809	351,716	704,655	280,159	111,154	71,557
Total	\$ 3,757,791	\$ 3,261,824	\$ 3,808,333	\$ 3,152,987	\$ (50,542)	\$ 108,837

* New Major Governmental Fund (In FY 2004-05, this fund was included in Other Governmental)

In addition to the effects of expenditure-driven grants, the following information provides explanations for the significant changes in fund balance:

General Fund

The General Fund is the chief operating fund of the County. At the end of FY 2005-06, there was an increase in fund balance of \$36,793. Revenues for the General Fund exceeded expenditures. Property tax revenues increased by \$66,617 as a result of the continued growth in the assessed property valuations, an increase in Property Tax in Lieu of VLF, and a one time Property Tax in Lieu of VLF payment from the State for an underpayment in FY 2004-05. Intergovernmental revenues also increased by \$52,673 as a result of a one time payment from the State for repayment of a VLF gap loan and the termination of the VLF intercept following the refunding of the 1995A Refunding Recovery Bonds and the 1996 Recovery Certificate of Participation Bonds. For more information on the refunding, refer to Note 10, Long-Term Obligations.

At the end of FY 2005-06, retirement costs increased by \$37,602. Salaries and wages for Public Protection increased by \$16,305. The Registrar of Voters expenditures increased by \$13,080 for special elections. Debt Service expenditures also increased by \$20,774 due to the 2005 Refunding Recovery bonds issuance costs and debt service payments. For more information, refer to Note 10, Long-Term Obligations.

Roads

This fund accounts for the maintenance and construction of roadways, and for specialized engineering services to other governmental units and the public. At the end of FY 2005-06, there was a decrease in fund balance of \$9,637 compared to last year's decrease in fund balance of \$5,116. In comparison to last year, revenues from Intergovernmental revenues increased \$6,908 primarily due to revenue received from Proposition 42, the Transportation Congestion Improvement Act, and the widening of the Glassell Street Bridge. Expenditures increased by \$13,914 due to an increase in capital projects and work completed on Laguna Canyon Road and various intersection improvements along El Toro Road.

Public Library

This fund accounts for library services for the unincorporated areas as well as some of the incorporated areas within the County. There was a \$2,767 increase to fund balance this fiscal year. The Public Library Fund had an increase of \$2,685 in property tax revenues from rising home prices and new housing construction in the areas for which it receives property tax revenue. A decrease in revenues of \$444 is due to a decrease in developer deposits used for construction or improvements. In comparison to the prior year, expenditures increased for retirement costs, building improvements and overall operations by \$2,444.

Tobacco Settlement

This fund accounts for tobacco settlement monies allocated to the County from the State of California, pursuant to the Master Settlement Agreement between the major tobacco companies and 46 states (including California), the District of Columbia and four U.S. Territories. At the end of FY 2005-06, fund balance continued to decline by \$3,670, primarily due to a decrease in revenues of \$2,528 from settlement monies. The participating tobacco manufacturers withheld a portion of the settlement payment claiming a decline in sales due to a lack of diligence by the participating states, including California, in enforcing the Master Settlement Agreement laws.

Refunding Recovery Bonds and Recovery Certificates of Participation and Debt Prepayment

This fund accounts for the debt service transactions handled by the trustee bank for the 1995 Refunding Recovery Bonds and the 1996 Recovery Certificates of Participation. This fund also accounts for early debt reduction of the County's outstanding bonds. At the end of FY 2005-06, there was a decrease in fund balance of \$263,397. The decrease is primarily due to the refunding and defeasance of both the 1995 Refunding Recovery Bonds and the 1996 Recovery Certificates of Participation. Due to the refunding, this fund was closed in FY 2005-06. For more information, refer to Note 10, Long-Term Obligations.

Flood Control District

This fund accounts for the planning, construction and operation of flood control and water conservation works, such as dams, basins, and trunk channels, and for the retardation, conservation and controlled discharge of storm waters. At the end of FY 2005-06, there was an increase in fund balance of \$20,485 compared to last year's decrease in fund balance of \$52,457. Property tax revenues increased by \$4,715. In comparison to last year, expenditures decreased by \$66,398. The decrease in expenditures is primarily attributed to significant land purchases in FY 2004-05 for the Prado Dam project.

Harbors, Beaches and Parks

This fund accounts for the development of aquatic recreational facilities and the acquisition, operation and maintenance of County beaches, inland regional park recreational facilities and community park sites in the unincorporated areas. At the end of FY 2005-06, there was a \$14,183 increase in fund balance. Property tax revenues increased by \$3,493. An increase in transfers in of \$8,673 is due to an allocation from the bankruptcy debt refinancing savings.

Other Public Protection

This group of funds is used to account for safety and law enforcement activities. Revenues consist primarily of Federal and State grants. At the end of FY 2005-06, there was an increase in fund balance of \$40,780 compared to last year's increase in fund balance of \$48,335. Intergovernmental revenues increased \$19,697 due to the transfer of revenues from the agency funds to newly established funds and a Federal grant award for the State Criminal Alien Assistance Program (SCAAP). A decrease of \$9,481 in revenues from Charges for Services is a result of a decline in document recording services due to the slow down in the real estate sales activity. Transfers also increased \$21,484 due to increased General Fund expenditures of purpose-restricted revenues related to Proposition 36, the Substance Abuse and Crime Prevention Act, and Proposition 172, a permanent state-wide half-cent sales tax dedicated to the support of local public safety activities.

Other Governmental Funds

At the end of FY 2005-06, there was an increase in fund balance of \$111,154 compared to last year's increase in fund balance of \$71,557. In FY 2005-06, Other Public Protection became a major governmental fund and is no longer part of this group of funds. Other financing sources increased by \$82,466, primarily due to the issuance of the 2005 Lease Revenue Refunding Bonds. Contributions from Property Owners revenue decreased by \$50,115 due to fewer bond issuances in FY 2005-06 compared to last year. This year's Capital Outlay expenditures decreased by \$10,275 due to a decrease in construction reimbursements to developers for capital projects.

The following chart shows the fund balances for governmental funds for the current and previous fiscal year:

COMPARATIVE FUND BALANCE
Governmental Funds
June 30, 2006 and 2005

	2006	2005	Increase (Decrease) %
General Fund	\$ 358,135	\$ 321,342	11 %
Roads	103,211	112,848	(9)%
Public Library	7,306	4,539	61 %
Tobacco Settlement	5,995	9,665	(38)%
Refunding Bonds and Recovery COPs & Debt Prepayment *	--	263,397	(100)%
Flood Control District	226,646	206,161	10 %
Harbors, Beaches, and Parks	64,157	49,974	28 %
Other Public Protection	223,313	182,533	22 %
Other Governmental Funds	909,638	798,484	14 %
Total	\$ 1,898,401	\$ 1,948,943	(3)%

* The Refunding Bonds and Recovery COPs Debt Prepayment fund was closed in FY 2005-06.

Proprietary Funds

The proprietary fund financial statements provide the same type of information as the government-wide financial statements, only in more detail. The proprietary funds financial statements provide separate information for the Airport and Waste Management operations, both of which are considered to be major funds of the County. Internal Service Funds are combined into a single, aggregated presentation in the proprietary fund financial statements.

Comparative Analysis of Changes in Fund Net Assets

The following table presents the Enterprise Funds' actual revenues and other financing sources, expenses and transfers, and changes in fund net assets for the current and previous fiscal year:

ENTERPRISE FUNDS COMPARATIVE SCHEDULE OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS For the Year Ended June 30, 2006						
	Revenues, Contributions and Transfers		Expenses and Transfers		Change in Fund Net Assets	
	2006	2005	2006	2005	2006	2005
Airport	\$ 113,044	\$ 110,324	\$ 83,559	\$ 78,835	\$ 29,485	\$ 31,489
Waste Management	130,475	124,706	88,509	102,510	41,966	22,196
Total	\$ 243,519	\$ 235,030	\$ 172,068	\$ 181,345	\$ 71,451	\$ 53,685

Airport

This fund accounts for major construction and self-supporting aviation related activities rendered at John Wayne Airport (JWA). Last year's increase in fund net assets was \$31,489; this year the fund net assets increased by \$29,485 primarily because of the following factors:

- A \$2,594 increase in interest revenue due to the upward trend of interest rates.
- A \$1,547 increase in Professional Services expenses due to increase in services provided by the Sheriff's department.

Waste Management

This fund is used to account for the operation, expansion, and closing of existing landfills and the opening of new landfills. Monies are collected through gate tipping fees, which users pay based primarily on tonnage. At the end of FY 2005-06, there was an increase in fund net assets of \$41,966, compared to the prior year change of \$22,196, primarily due to the following factors:

- A \$6,101 increase in interest revenue due to the upward trend of interest rates.

For further comparative analysis of changes in Fund Net Assets, please see the Business-Type Activities.

GENERAL FUND BUDGETARY HIGHLIGHTS

This section provides a summary of the primary factors involved in the variances between: 1) the Original Budget and the Final Amended Budget; and 2) the Final Amended Budget and the Actual Amounts for the General Fund. In addition to the effects of expenditure-driven grants, the following information provides explanations for significant variances. Refer to the Budgetary Comparison Statement for details on this budgetary comparison.

Original Revenue Budget vs. Final Amended Revenue Budget

The following provides a summary of the primary factors attributable to the increase or decrease in the General Fund final amended budget revenues compared to the original budget revenues:

Intergovernmental Revenues

- A \$48,033 revenue increase in the County General Fund due to the one-time repayment of the VLF gap loan. The gap loan occurred in FY 2003-04 when the State reduced the VLF payments to the counties with plans to repay the loan in FY 2006-07. However, the gap loan was repaid early in September 2005 and resulted in a one-time payment of \$26,500. Additionally, an increase in revenues of \$21,533 was due to the refunding of the 1995 and 1996 Recovery Bonds in August 2005. The VLF that had been intercepted by the State Controller to repay the recovery bonds was eliminated due to this refunding. The increase in VLF revenue will be used to pay debt service on the 2005 Refunding Recovery Bonds. Note 10, Long-Term Obligations, provides additional information on the Refunding Recovery Bonds 2005 Series A.

Other Revenue

- An increase of \$22,865 is mostly due to revenues from retirement billings to departments for their portion of the annual required contribution to the Orange County Employees Retirement System (OCERS). See Budgetary Comparison Statement for additional information.

Transfers In

- A \$23,342 increase in budgeted revenues in the Health Care Agency (HCA) for transfers from Purpose Restricted Special Revenue Funds such as the newly established Proposition 63 Mental Health Services Act (MHSA), the Substance Abuse Crime Prevention Act (SACPA), and the Center for Disease Control Bioterrorism Fund.
- A decrease of \$11,535 in the Sheriff-Coroner Department because various capital projects and major purchases originally budgeted in the General Fund are now budgeted in other funds.

Bonds Issuance Proceeds

- A \$126,000 increase in budgeted revenues for the County General Fund following the issuance of the Taxable Pension Obligation Bonds, Series 2006 (the 2006 POBs). See Note 9, Short-Term Obligations, for additional information.

Proceeds of Refunding Bonds

- A \$146,005 increase in budgeted other financing sources for the County General Fund following the issuance of the 2005 Refunding Recovery Bonds. See Note 10, Long-Term Obligations, for additional information.

Original Expenditure Budget vs. Final Amended Expenditure Budget

The following provides a brief summary of the primary factors attributable to the increase in the General Fund final amended budget expenditures compared to the original budget expenditures:

Miscellaneous

- A \$28,030 increase in appropriations to offset year-end payments to OCERS and for unanticipated payments of attorney fees and expenses associated with the *William B. Bunker vs. County of Orange* pending litigation. See Note 16, Estimated Liability for Other Litigation and Claims, for additional information.

2005 Lease Revenue Bonds

- A \$10,416 increase was appropriated for debt service payments on the 2005 Lease Revenue Refunding Bonds. See Note 10, Long-Term Obligations, for additional information.

Refunding Recovery Bonds, 2005 Series A

- A \$175,073 increase in appropriations to refund and defease the outstanding 1995 Refunding Recovery Bonds and to pay the costs of issuance for the 2005 Refunding Recovery Bonds. See Note 10, Long-Term Obligations, for additional information.

Prepaid Pension Obligation

- A \$126,000 increase in appropriations to prepay 50% of the County's FY 2006-07 employer pension contribution to OCERS at a discounted rate. See Note 9, Short-Term Obligations, for more information.

Health Care Agency

- A \$9,038 increase in appropriations due mainly to the addition of 27 new positions and anticipated current year activities for the Proposition 63 MHSA Community Services and Support plan. Proposition 63 is intended to reduce the long-term adverse impact resulting from untreated serious mental illness.

Final Amended Revenue Budget vs. Actual Revenue Amounts

The following information provides a summary of the primary factors that caused the variance in the General Fund actual revenues compared to the final amended budget revenues:

Taxes

- A \$70,669 positive variance in the County General fund for the one-time payment from the State for an underpayment of Property Tax and VLF in FY 2004-05, as well as higher than anticipated revenue for secured property taxes, property transfer activity and supplemental property tax in lieu of VLF.

Charges for Services

- A \$6,076 negative variance in the HCA due to lower than anticipated revenue for mental health services.
- A \$17,532 negative variance in Resources and Development Management Department (RDMD) due to reduced expenditures from lower reimbursable indirect charges and less direct billable hours.

Transfers In

The following are a result of not transferring money from Purpose-Restricted Special Revenue Funds:

- A variance of \$25,794 in the Sheriff Department due to higher vacancies, credits for charges for law enforcement services and deferred spending for Homeland Security and other grants that will be transferred in the next fiscal year.
- A variance of \$27,230 in HCA transfers from Proposition 63 MHSA, SACPA and the Orange County Tobacco Settlement Fund because expenditures were lower than budgeted.

Bond Issuance Proceeds

- A negative variance of \$46,426 in the Prepaid Pension Obligation fund because the actual amount of the bond debt issuance was lower than the estimated amount.

Final Amended Expenditure Budget vs. Actual Expenditure Amounts

The following provides a summary of the primary factors causing the significant variance in the General Fund actual expenditures as compared to the final amended budget expenditures:

Capital Projects

- A \$55,322 positive variance due to the deferral of major capital projects to the next fiscal year, including the conversion of the Central Utility Facility to add cogeneration electrical, the construction of the parking structure at the Animal Care Facility, the repavement of various roadways at the Los Pinos Conservation Camp, the replacement of the fence at Juvenile Hall, the rehabilitation of the Central Justice Center and various maintenance projects for the Sheriff Department.

Health Care Agency

- A positive variance of \$39,465 due to lower than budgeted capital project costs and savings in human services contracts.

Sheriff-Coroner

- A \$15,262 positive variance due to maintaining a higher than budgeted vacancy factor and savings from lower health insurance costs.
- A \$11,278 positive variance due to lower than anticipated Homeland Security Grant related expenditures.

Social Services Agency

- A \$17,412 positive variance due to a lower than anticipated caseload for the California Work Opportunity and Responsibility to Kids (CalWORKS) program.
- A \$13,539 positive variance due to a decreased allocation for the California Work Integrated Network (CalWIN) Program causing spending reductions in professional services.

Resources and Development Management Department

- A \$2,418 positive variance due to salary and employee benefits savings from the deletion of long-term vacant positions and position freezes.
- A \$2,666 positive variance due to the reduction or delay of professional services expenditures in Planning and Development Services (PDS).
- A \$11,276 positive variance due to an increase in intra-agency services and supplies billing offsets from the PDS merger with RDMD.
- A \$2,935 positive variance due to an increase in intra-fund transfers from other General Fund agencies.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

At June 30, 2006, the County's capital assets for both the governmental and business-type activities amounted to \$2,874,747 net of accumulated depreciation. The investment in capital assets includes land, structures and improvements, equipment, infrastructure (roads, bridges, flood channels, trails, traffic signals, and harbors), and construction in progress. The total decrease in the County's investment in capital assets for the current year was 1% (a 2% decrease for governmental activities and a 1% decrease for business-type activities).

Capital assets for the governmental and business-type activities are presented below to illustrate changes:

CAPITAL ASSETS (Net of Depreciation) June 30, 2006							
	Governmental		Business-Type		Total		Increase
	Activities		Activities				(Decrease)
	<u>2006</u>	<u>2005</u>	<u>2006</u>	<u>2005</u>	<u>2006</u>	<u>2005</u>	<u>% Change</u>
Land	\$ 575,715	\$ 567,243	\$ 34,108	\$ 34,108	\$ 609,823	\$ 601,351	1 %
Structures and Improvements	499,847	510,827	194,875	184,739	694,722	695,566	(1)%
Equipment	97,292	103,739	26,762	23,357	124,054	127,096	(2)%
Infrastructure	805,760	801,263	209,221	196,237	1,014,981	997,500	2 %
Construction in Progress	395,319	427,674	35,848	68,967	431,167	496,641	(13)%
Total	\$ 2,373,933	\$ 2,410,746	\$ 500,814	\$ 507,408	\$ 2,874,747	\$ 2,918,154	(1)%

The following lists the significant expenditures for capital assets in FY 2005-06:

General Fund

- \$7,686 for the construction of three new housing units for the Youth Leadership Academy at Juvenile Hall, which will increase the capacity to 120 beds.
- \$4,913 for the floor-by-floor refurbishment at the Central Justice Center.
- \$2,199 for the purchase of a helicopter for the Sheriff Department.
- \$1,156 for facility improvements for Animal Care Services.

Flood Control District

- \$5,623 for the Huntington Beach Channel improvement project.
- \$4,481 for land acquisitions for the Santa Ana River Prado Dam Project.

Waste Management

- \$6,224 for the Desilting Basin Improvement Project at the Prima Deshecha landfill.
- \$5,191 for the purchase of six tractors.
- \$4,561 for the expansion of the Frank R. Bowerman (FRB) Landfill.

Additional information on the County's capital assets can be found in Note 4, Changes in Capital Assets.

Commitments for Capital Expenditures

At the end of FY 2005-06, significant commitments for capital expenditures included the following:

- \$276,000 for the Santa Ana River Mainstem Project.
- \$44,650 for land acquisition and structural improvement projects for the Flood Control District.
- \$17,766 to expand Laguna Canyon Road from State Route 73 to Interstate 405.
- \$5,764 for the O'Neill Park Sewer Conversion project to improve water quality.

Additional information on the County's commitments for capital expenditures can be found in Note 14, Construction and Other Significant Commitments.

Short-Term Debt

The following summarizes the County's short-term debt activity during FY 2005-06:

Taxable Pension Obligation Bonds, Series 2006 On January 30, 2006, the County issued the 2006 POBs in the principal amount of \$105,991. The 2006 POBs were issued in order to prepay a portion of the County's FY 2006-07 actuarially required contribution rate related to amortization of unfunded actuarial accrued liability to OCERS. Additional information on the County's short-term debt activity can be found in Note 9, Short-Term Obligations.

Long-Term Debt

At June 30, 2006, the County had a total debt obligation outstanding of \$1,066,393, excluding capital lease obligations, compensated absences and other liabilities. During the year, \$842,251 of the bonds, including \$805,905 of bankruptcy related debt, were retired and \$565,762 were added, which resulted in a net decrease of 21% on the County's outstanding bond obligation. The County is limited by law in issuing general obligation bonded debt to 1.25 percent of the last equalized property tax roll. However, this does not affect the financing of any of the County's planned facilities or services because as of the end of the fiscal year, the County had no net general obligation bonded debt. The County's debt obligations are in the form of revenue bonds, certificates of participation, and other forms of debt not covered by the general obligation bonded debt limitation.

The following table summarizes the County's outstanding bonds at June 30, 2006:

LONG-TERM DEBT BOND OBLIGATIONS							
June 30, 2006							
	Governmental		Business-Type		Total		Increase
	Activities		Activities				(Decrease)
	2006	2005	2006	2005	2006	2005	% Change
Revenue Bonds	\$ 673,655	\$ 261,180	\$ 165,225	\$ 181,240	\$ 838,880	\$ 442,420	90 %
Certificates of Participation	8,092	589,909	--	--	8,092	589,909	(99)%
Pension Obligation Bonds	99,714	111,772	--	--	99,714	111,772	(11)%
Recovery Bonds	131,631	210,705	--	--	131,631	210,705	(38)%
Add: Premium on Bonds Payable	34,112	5,009	3,422	4,210	37,534	9,219	307 %
Less: Deferred Amount on Refunding	(39,239)	(5,744)	(10,219)	(12,520)	(49,458)	(18,264)	171 %
Total	\$ 907,965	\$ 1,172,831	\$ 158,428	\$ 172,930	1,066,393	\$ 1,345,761	(21)%

The following summarizes the County's long-term debt issuance during FY 2005-06:

Lease Revenue Refunding Bonds, Series 2005 On August 16, 2005, the Orange County Public Financing Authority (OCPFA) issued its \$419,756 Lease Revenue Refunding Bonds Series 2005 (Series 2005 Bonds) at a premium of \$19,973. The proceeds of the bonds, together with certain monies contributed by the County and other funds available to the trustee of the Recovery COPs, were used to (1) defease certain non-callable Recovery COPs, (2) refund the remaining COPs, (3) fund a debt service reserve fund for the Series 2005 Bonds, and (4) pay costs of issuance of the Series 2005 Bonds.

Refunding Recovery Bonds, 2005 Series A On August 18, 2005, the County issued its \$146,006 Refunding Recovery Bonds 2005 Series A (2005 Recovery Bonds) at a premium of \$9,317. The proceeds of the bonds, together with certain monies contributed by the County and other funds available to the trustee of the Recovery Bonds, were used to (1) refund and defease the outstanding Recovery Bonds, and (2) pay costs of issuance for the 2005 Recovery Bonds.

Additional information on the County's long-term debt activity can be found in Note 10, Long-Term Obligations.

Bond Ratings

The County continues to maintain the issuer ratings of Aa2 from Moody's Investors Service and A+ from Standard & Poor's (S&P). The 1995 Teeter Plan Revenue Bonds and the Orange County Development Agency (OCDA) 2003 Santa Ana Heights (SAH) Bonds are AAA insured from Fitch Ratings and S&P with a municipal bond insurance policy, but are not currently rated (NR indicates Not Rated).

In FY 2005-06, the following changes occurred in the County's underlying debt ratings as compared to the previous year:

- Issued 2005 Refunding Recovery Bonds with an A rating from S&P, Aa3 from Moody's and AA- from Fitch Ratings.
- Issued 2005 Lease Revenue Bonds with an A rating from S&P, A1 from Moody's and AA- from Fitch Ratings.
- Improved Fitch Ratings from A+ to AA- for the 1997 Airport Revenue Refunding Bonds.
- Changed Fitch Ratings from not rated to AA- for the 2003 Airport Revenue Refunding Bonds.

The County maintains the following long-term underlying debt ratings:

LONG-TERM DEBT RATINGS
 June 30, 2006

	Standard and Poor's	Moody's	Fitch
2005 Refunding Recovery Bonds	A	Aa3	AA-
2005 Lease Revenue Bonds	A	A1	AA-
1991 Parking COPs	NR	A1	NR
OCDA Neighborhood Development and Preservation Project	A	A2	NR
2002 Lease Revenue Bonds	A	A1	AA-
OCDA 2003 SAH Bonds	NR	NR	NR
1996 Pension Obligation Bonds	NR	Aa2	NR
1997 Pension Obligation Bonds	NR	Aa2	AA-
1995 Teeter Plan Revenue Bonds	NR	NR	NR
2001 Lease Revenue Bonds	NR	A2	NR
Airport 1997 Revenue Refunding Bonds	A+	Aa3	AA-
Airport 2003 Revenue Refunding Bonds	A+	Aa3	AA-
Integrated Waste Management Department 1997 Revenue Refunding Bonds	NR	A2	A+

OTHER POTENTIALLY SIGNIFICANT MATTERS

The County's management has determined that the following are significant matters that have a potential impact on the County's financial position or changes in financial position:

Governmental Activities

State Legislation

The County of Orange will benefit from infrastructure bond measures passed during the November 7, 2006 general election. Proposition 1B, the transportation bond, included a \$62,000 direct subvention to the County for streets and roads. Orange County Transportation Authority projects will garner millions more for regional transportation projects and transit improvements in Orange County. The County of Orange will also benefit from \$500,000 in flood subventions approved in Proposition 1E and \$180,000 in Proposition 84. An additional \$45,000 is included in Proposition 84 to local government agencies for the Santa Ana River Parkway, with \$30,000 equally divided between projects in Orange, San Bernardino, and Riverside Counties. The County is also expected to compete in the housing bond.

On November 7, 2006, voters also approved Proposition 83, requiring individuals convicted of a felony sex offense that requires registration and prison sentence be monitored by Global Positioning System (GPS) while on parole and for the remainder of their life. The offender is required to pay fees covering the cost of GPS based on their ability to pay. The Legislative Analyst's Office (LAO) estimates that the cost to California could be in excess of \$100,000 annually, with costs that could continue to grow in subsequent years. The proposition does not address local government's role in GPS monitoring function after the offender has completed parole. It is therefore difficult to estimate the potential financial impact at this time. At present, the Federal Courts have issued a temporary restraining order against the implementation of Proposition 83 pending further judicial review of legal issues related to its requirements.

State Budget

Governor Schwarzenegger signed the final FY 2006-07 State Budget on June 30, 2006. Total spending is set at \$127,900,000 including a \$101,300,000 general fund budget. The budget reflects an improving revenue picture and spending increases of over 9%. The State general fund has a \$6,900,000 operating shortfall that is projected to continue in the range of \$4,500,000 to \$5,000,000 over the next two fiscal years. Regarding the impact of the State budget on local government, the California State Association of Counties (CSAC) reported that "California's 58 counties and their residents were treated fairly by the 2006-2007 state budget." Shortly after the release of the budget, CSAC highlighted the following features of the State budget:

- Increased funding for public-safety programs, including juvenile crime prevention and intervention, front-line enforcement services, mentally ill diversion programs, and local correctional officer training and methamphetamine abatement.
- A package of modifications to the CalWORKS program, California's welfare program, which will ensure that more families in California are working and moving toward self-sufficiency. The package provides counties with additional resources to assist these families.
- Funding augmentations for the Foster Care program and Child Welfare Services aimed at, among other things, improving outcomes and caseload reduction.
- Flood-Control subvention funding to ease the financial burden of urgent county flood protection maintenance.
- Payback of Proposition 42 funds to help counties make badly needed road repairs.
- Additional funding for Proposition 36, which steers non-violent drug offenders away from jail and into treatment.

Some of the more significant issues by program are listed below:

Public Safety

- Citizen's Option for Public Safety (COPS) and Juvenile Justice Crime Prevention Act (JJCPA) funding is \$19,000 more than last year state-wide.
- Funding for Standards and Training for Corrections is \$19,500 state-wide.
- Funding for local emergency preparedness is \$46,000 state-wide.
- The Mentally Ill Offender Crime Reduction grant is funded at \$45,000 to curb recidivism for juvenile and adult mentally ill offenders. The grant would be made on a competitive award basis.

Health & Social Services

- Child Support County administration funding is increased by \$4,000.
- The State will fund the Child Support System Federal penalty associated with the delay in implementing the system state-wide.
- Realignment funding for social services programs is expected to grow by nearly 7%. Because of slow growing revenues, caseload growth has not been fully paid for the past two years.
- Prop 36 Substance Abuse Treatment funding is funded with a one-time grant at current levels: \$120,000 total including \$96,000 for cities and counties. Funding is accompanied by expectations for program reforms intended to improve outcomes and accountability. An additional \$25,000 is included for a new Substance Abuse Offender Treatment Program on a 9:1 state/county match.
- AB 3632 Mental Health Services to special education students is no longer a State-mandated program. \$66,000 is included to pay back claims for FY 2004-05 and FY 2005-06. An additional \$121,000 is included for current costs.
- The Governor proposes \$200,000 state-wide for enhanced ability to respond to natural and intentional disasters. The budget includes \$16,000 for local pandemic flu preparedness and response planning.
- Increased funding by \$22,600 for Medi-Cal program awareness, enrollment and retention could increase workload in SSA by 12 positions and provide an additional \$1,700 in State and Federal funding.
- County Medi-Cal program administration salary and overhead reimbursement is increased by \$12,100.
- In-Home Supportive Services (IHSS) funding is up 4.1% with caseload growth estimated at 6.4%. IHSS administration funding to the County could increase by about \$449 and require three additional positions with a minor increase in Net County Cost. Worker wages are funded at the current level.
- The CalWORKS package provides \$90,000 for program improvements to increase federal participation rates and \$140,000 for county programs based on the FY 2005-06 level.
- Foster Care is funded at \$75,000 above the May Revise level for foster care. There is \$98,000 to improve outcomes and reduce social worker caseload. There are increases for kinship care, transitional housing placement, dependency drug courts and adoption of hard to place foster children.

Infrastructure & Environmental Resources

- The budget includes \$242,000 per year for the FY 2003-04 and FY 2004-05 suspension of Proposition 42 funding for local streets and roads is included.
- After two years of suspended State Flood Control Subvention reimbursement, \$100,000 is included to pay local governments for the state's share of costs of federally authorized, locally sponsored flood control projects. The State Department of Water Resources anticipates that Orange County will receive \$21,600 over the next three years or a little over one-third of the total \$60,900 in claims pending approval. Up to \$50,000 more is planned to be claimed in the next year.
- Public Library Foundation Act funding is increased by \$7,000 for inter library loans.

General Government

- \$170,000 is included for the first two years of a 15-year repayment plan for SB-90 mandated cost reimbursement. There is also increased funding for FY 2006-07 claims.
- The Property Tax Administration grant continues to be suspended. It could be considered for implementation in FY 2007-08.

Long-Term Financial Planning

County Accounting and Personnel System (CAPS) Upgrade

CAPS is a vital part of the County's infrastructure that is needed for business processes such as financial planning and budget development, maintaining the County's financial records, collecting costs for federal and state claiming, procuring goods and services, paying vendors, processing the County's payroll, and administering enterprise-wide human resource functions. CAPS maintains financial records for the County's budget of approximately \$4,800,000 and maintains human resource records and processes payroll for a work force of over 18,000 employees.

CAPS is based on 1980s technology and is becoming costly to maintain and operate. In addition, the vendor has informed the County that it will discontinue support of the version of software deployed at the County, within the next three to five years. If the County does not take some action with the software after the vendor discontinues support system operations, maintenance costs will grow, the risk of the systems not functioning properly will increase, and ultimately the system will become technologically obsolete and unsupported.

The County completed a strategic assessment to identify the County's business processes, developed a strategic-level needs assessment for these business processes, identified the problems with the current system in meeting the County's business needs, developed a business case for taking action, and identified and analyzed viable alternatives.

Based on the results and recommendations from the assessment, the Board of Supervisors authorized the CAPS Steering Committee to pursue an upgrade of the current CGI-AMS Advantage Financial and Procurement systems and to concurrently conduct a strategic assessment of Human Resource and Payroll functions in order to acquire the most appropriate solution set.

The County contracted with CGI, Inc. to conduct a Fit Analysis of their latest version of the Financial and Procurement software, Advantage 3.x. The primary objective of the Fit Analysis project is to determine the overall fit between the Advantage 3.x Financial/Purchasing capabilities and the County's system requirements for the following business functions: Chart of Accounts, General Accounting, Fixed Assets; Disbursements; Cost Accounting, Vendor Self Service, eCommerce (commodities purchases) and Contracts (professional services).

Other important objectives include:

- Quantify the level-of-effort and related costs to implement the upgrade
- Identify a technically capable and cost effective platform to run the systems
- Quantify the costs for operating the systems after implementation
- Develop a project plan, with required funding, for the upgrade implementation

The Fit Analysis is expected to be completed by March 2007 and will cost \$2,600, including County and Contractor staffing. Costs for the upgrade implementation are expected to range from \$10,000 to \$12,500 and will be more specifically determined during the Fit Analysis. Implementation of the first phase of the solution is expected to occur in July 2009.

The County is also currently in negotiations with a qualifying vendor for consulting services to assist the County in the development of a comprehensive vision related to its Human Resource and Payroll operations, to develop business requirements supporting the County's vision, to research and recommend one or more solutions that meet the stated requirements, and to assist in the sourcing of the appropriate solution set. The visioning and sourcing phase is expected to take one year at an approximate cost of \$1,000, including County and Contractor staffing. Implementation timeframes and associated costs of the solution set will depend on the solution(s) selected. Current estimates are for a two year implementation at a cost ranging from \$6,000 to \$8,000.

Assessment Tax System Upgrade

The County's property tax assessment, collection and allocation system processes approximately \$5,500,000 annually in property taxes for the cities, school districts and special districts within the County. The system was developed in the late 1980s and early 1990s in what is now an obsolete programming language that is becoming increasingly difficult to support. Given the critical nature of the application, its replacement is considered a strategic priority.

The County is currently conducting a Needs Assessment to document current business rules, identify opportunities for improvement, envision the future operational model and identify possible solutions and strategies for implementation. The Needs Assessment is expected to be completed by March 2007 and is expected to cost \$1,500 for consulting services. This will be followed by development and implementation of the replacement application and is expected to take from three to four years at a cost of approximately \$18,000 to \$21,000.

Requests for Information

We hope that the preceding information has provided a general overview of the County's overall financial status. For questions or comments concerning information contained in this report, please contact the Auditor-Controller's Office, County of Orange, 12 Civic Center Plaza, Santa Ana, CA 92702 or you can access our website at <http://www.ac.ocgov.com>.