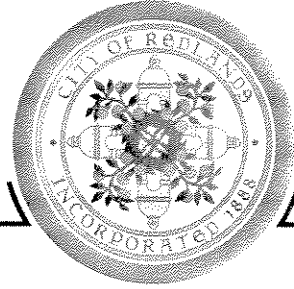


**INTRODUCTORY SECTION**

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# City of Redlands



December 21, 2007

To the Members of the City Council and Citizens of the City of Redlands:

It is the policy of the City of Redlands to annually publish a complete set of financial statements presented in conformity with generally accepted accounting principles (GAAP) and audited in accordance with generally accepted auditing standards by a firm of certified public accountants. Pursuant to that requirement, we hereby issue the comprehensive annual financial statements of the City of Redlands ("the City") for the fiscal year ended June 30, 2007.

This report consists of management's representations concerning the finances of the City. Consequently, management assumes full responsibility for the completeness and reliability of all the information presented in this report. To provide a reasonable basis for making these representations, management of the City has established a comprehensive internal control framework that is designed both to protect the City's assets from loss, theft, or misuse and to compile sufficient reliable information for the preparation of the City's financial statements in conformity with GAAP. Because the cost of internal controls should not outweigh their benefits, the City'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 misstatement. As management, we assert that, to the best of our knowledge and belief, this financial report is complete and reliable in all material respects.

The City's financial statements have been audited by MAYER HOFFMAN MCCANN, P.C., an independent firm of certified public accountants. The goal of the independent audit was to provide reasonable assurance that the financial statements of the City for the fiscal year ended June 30, 2007, are free of material misstatement. The independent audit involved examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements; assessing the accounting principles used and significant estimates made by management; and evaluating the overall financial statement presentation. The independent auditor concluded, based upon the audit, that there was a reasonable basis for rendering an unqualified opinion that the City's financial statements for the fiscal year ended June 30, 2007, were fairly presented in conformity with GAAP. The independent auditor's report is presented as the first component of the financial section of this report.

The independent audit of the financial statements of the City was part of a broader, federally mandated "Single Audit" designed to meet the special needs of federal grantor agencies. The standards governing Single Audit engagements require the independent auditor to report not only on the fair presentation of the financial statements, but also on the audited City's internal controls and legal requirements involving the administration of federal awards. These reports are available in the City's separately issued Single Audit Report.

GAAP requires that management provide a narrative introduction, overview, and analysis to accompany the basic financial statements in the form of Management's Discussion and Analysis

*"Preserving the Past, Protecting the Future"*



(MD&A). This letter of transmittal is designed to complement MD&A and should be read in conjunction with it. The City's MD&A can be found immediately following the report of the independent auditors.

## **PROFILE OF THE GOVERNMENT**

The City of Redlands, incorporated in 1888, is located 63 miles east of Los Angeles, 110 miles north of San Diego, and 500 miles southeast of San Francisco. It lies within the San Bernardino Valley in the southwestern portion of San Bernardino County, covering an area of 36 square miles, within the heart of the Inland Empire. It serves a population of 71,375 residents.

The City was incorporated under the general laws of the State of California and enjoys all the rights and privileges applicable to a General Law City. It is a municipal corporation governed by a five-member city council in which all policy-making and legislative authority is vested. The City Council is responsible, among other things for passing ordinances, adopting the budget, appointing committees, and hiring both the City Manager and City Attorney. The City Manager is the chief administrative officer of the City and as such is responsible for carrying out the policies and ordinances of the City Council, for overseeing the day-to-day operations of the City, and for recommending appointment of department heads to the Council for approval. The Council is elected on a non-partisan basis. Council members serve four-year staggered terms, with elections occurring every two years. The mayor is elected by a majority vote of the Council.

The City provides a full range of services, including police and fire protection, animal control, emergency medical aid, building safety regulation and inspection, street lighting, beautification, sewer and water utilities, solid waste collection and disposal, land use planning and zoning, housing and community services, maintenance and improvement of streets and related structures, traffic safety maintenance and improvement, and a full range of recreational and cultural programs for citizen participation, as well as being the home of the historic A. K. Smiley Public Library.

The annual budget serves as the foundation for the City's financial planning and control. Prior to the beginning of the fiscal year, the City Manager submits a budget for the upcoming year to the City Council. Public hearings are held before final approval of the budget. The City Manager is authorized to transfer budgeted amounts between departments within any fund; however, any revisions that alter the total expenditures of any fund must be approved by the City Council. The City maintains budgetary controls to ensure compliance with provisions embodied in the annual appropriated budget approved by the City Council. Activities of the general fund, special revenue funds, debt service funds, capital projects funds, enterprise funds and internal service funds are included in the annual budget. The level of control (level at which expenditures may not exceed budget) is the fund. The City also maintains an encumbrance accounting system as one technique of accomplishing budgetary control. Encumbered amounts lapse at year-end; however encumbrances are re-appropriated each year by separate action of the City Council. Budget-to-actual comparisons are provided in this report for each individual governmental fund for which an appropriated annual budget has been adopted. For the general fund and major special revenue funds, this comparison is presented as part of the required supplementary information in the accompanying financial statements. For governmental funds that have appropriated annual budgets, other than the general fund and major special revenue funds, this comparison is presented in the supplementary section of the accompanying financial statements.

## ECONOMIC CONDITION AND OUTLOOK

The information presented in the financial statements is perhaps best understood when it is considered from the broader perspective of the specific environment within which the City operates.

**Local economy.** City of Redlands' economy is based largely in the service and trade sectors (health care, retail trade, government, and education) and light manufacturing. The region has a varied manufacturing and industrial base that adds to the relative stability of the unemployment rate which is at 3.9%. Since 2000, the annual unemployment rate for the City has ranged from a low of 3.4% to a high of 4.5%.

The City has significant land still available for industrial/commercial/office use with only a portion of these areas utilized. Major industries with headquarters or divisions located within the City's boundaries or in close proximity include computer hardware and software manufacturers, electrical controls and automobile component manufacturers, and several financial and insurance institutions. Major employers in the City or within the vicinity include the Redlands Unified School District, ESRI (Environmental Systems Research Institute), Loma Linda University Medical Center, the Jerry L. Pettis Veterans Hospital, the VA Loma Linda Healthcare System, Redlands Community Hospital, the United States Post Office and the University of Redlands. Several large warehouse distribution centers have been developed over the past few years, including Hershey (JENCO), Bechton-Dickenson, Stater Bros. and Salton, with each adding several hundred employees to the job mix.

The City's property tax base has shown steady growth since fiscal year 2000-2001 with an average annual increase in assessed valuation of 15.3%. The City of Redlands experienced a net taxable value increase of 17.4% for the 2006-2007 tax roll. The increase experienced county wide was 17.9%. The assessed value increase from the prior year was \$939.6 million, with \$98.8 million or 10.5% of that amount attributable to the 2% CPI adjustment granted by the County assessor. The largest assessed value increase on a single parcel, \$27.5 million, was reported on an industrial property owned by United Prologis. The largest value increase in the City is attributed to the Mountainview Power Company, LLC, which increased in value from \$300.4 million to \$549.8 million. The taxable value of residential property in the City increased by \$515 million (13.85%), commercial property increased by \$98.4 million (17.56%), and industrial property increased by \$68 million (26.45%). From fiscal year 2000-2001 to 2006-2007 assessed valuation for the City of Redlands increased 107% reaching \$6.3 billion.

Development activity occurring in fiscal year 2006-2007 remained strong although residential growth continued to experience a slow down. There were permits issued for 154 single family detached residences with a building valuation of \$43,003,355 and permits for multifamily structures had a valuation of \$1,018,322. Building valuation for commercial buildings was up significantly from last fiscal year with permits for 50 commercial buildings being issued with a building valuation of 92,052,538, an increase of 76% over last year. Overall building valuation for permits issued in fiscal year 2006-2007 increased to \$201,335,000, a 67% increase over last year.

The strongest activity was industrial development. There was over 2.6 million square feet of industrial buildings completed this past year. AMB Property Corporation constructed two regional distribution centers; one with 1,313,470 square feet and the second with 699,350 square

feet. Western Realco completed a five building industrial park with 271,093 square feet. Thrifty Oil Company also developed a 140,380 square foot multiple building industrial park.

Industrial development will remain strong. There is 1.7 million square feet of industrial development under construction and another 1.1 million square feet of industrial development that is either approved or in the planning process. Some of the significant industrial projects under construction include: PGP Partners, developing a six building industrial park with 711,000 square feet of floor area; Rossmore Enterprises, developing a five building industrial park with 288,126 square feet; Western Realco, constructing a 411,879 square foot warehouse distribution facility; and MKJ-McCalla, developing an eight building business park with a combined building area of 135,570 square feet.

Office development is expanding and becoming a higher percentage of development than in past years. There was 75,717 square feet of office development built this year which includes a 39,178 square foot medical office condominium project by Edward Anderson and an eight building 36,539 square foot office condominium by Plum Lane Partners, LLC. There is 436,768 square feet of office development under construction and over 400,000 square feet of office development either approved or in the planning process. Some of the major office projects under construction include: Kaiser Foundation Hospitals, developing a three story 120,159 square foot medical office building; Redlands Spectrum LP, constructing a 101,127 square foot fifteen building office park; and James Didion, constructing a three story medial complex with a building area of 52,559 square feet.

Retail development is steady and there are a number of significant projects approved and ready for development. There was 109,481 square feet of retail development completed this fiscal year. The most significant retail projects include: the Country Inn, a 52,288 square foot 79 unit hotel; R.P. Wages, a 20,851 square foot retail development on Alabama Street; and Realty Bancorp Equities who completed a 13,650 square foot Walgreens Drug Store.

There is another 78,916 square feet of retail development under construction. This includes a 69,666 square foot automobile dealership being built for a new Toyota of Redlands. There is 590,261 square feet of retail development that is either approved or in the planning process. Approved projects include: Redlands Land Acquisition Company, LP., developing a 150,300 square foot commercial center containing retail, restaurant and health club; Citrus Packing LLC, developing a four building commercial center with 110,512 square feet of floor area; and the Ayres Hotel Company, Inc., building a 52,158 square foot, two-story, 107 room Ayres Hotel.

Residential development activity has continued at a slower pace than in prior years. There were 302 dwelling units completed this year. The primary residential projects included: KB Homes (Tract 16556), a 107 unit single family subdivision; Ryland Homes (Tract 16747), a 52 lot single family planned residential development; Quantum Structures (Tract 13986), an 85 unit town-home development; and Buckeyes Limited Partnership (Tract 17691), a 24 unit residential condominium.

There are 129 single family detached homes and a 64 unit attached condominium development under construction. Beazer Homes (Tract 16390) has 81 of its 139 unit subdivision under

construction. The 64 unit condominium development (Tract 16548) is being developed by Quantum Structures.

Redlands is ready to "bounce back" from the residential slow down once the market place is prepared to proceed with increased production. The inventory of approved projects would allow for 1,173 dwelling units to be developed with 741 detached single family homes and 432 attached units. Some of the key residential projects include: Standard Pacific Homes (Tract 16689), a 209 unit residential planned development; Granite Homes (Tract 16586), an 80 lot single family residential planned unit development; Quantum Structures (Tract 17693), a 77 unit residential town-home development; and Adrian Gaus, a 71 unit senior housing complex located north of Lugonia Avenue.

In addition to the development projects noted above, the City has the following other major projects completed or in process at June 30, 2007: Redlands Sports Park Phase I, a 45 acre park with eight lighted soccer fields and a large multipurpose field, was completed in fiscal year 2006-2007, except for some street paving work and the restroom building; Alabama and Orange Street Bridges, both four lane bridges crossing the Santa Ana River that allow all weather access between the City of Redlands and the City of Highland, were completed in fiscal year 2006-2007. A major project for fiscal year 2006-2007, the Civic Center ADA Improvements project, designed to remove barriers to the disabled at City Hall, was completed in September, 2007.

**Long-term financial outlook/planning.** Over the last few years the City has faced financial challenges as a result of the State Budget crisis, increases in PERS rates, increases in employee contracts, and employee retirements. As a result, up until fiscal year 2006-2007, the City's General Fund expenditures exceeded revenues, thereby causing a steady reduction in unreserved fund balance. Although the City experienced significant growth in property taxes, sales taxes and development during these years, its revenues still were not able to keep pace with its expenditures. Accordingly, the City began to focus on financial policy decisions to balance the budget, establish minimum reserve levels, as well as review service levels, enhance revenue opportunities, evaluate reorganizations and develop capital improvement plans. These actions helped the City's General Fund achieve a net increase in fund balance of \$1.4 million during fiscal year 2006-2007. This kind of innovation and teamwork by the Council, staff and the citizens of Redlands will be critical to the City's financial future, particularly in light of the fact that the City does not expect the growth over the next few years to continue at the same record levels that it has over the last few years.

**Cash management policies and practices.** During the year, temporarily idle cash was invested in demand deposits, certificates of deposits, obligations of the U.S. Treasury and its agencies, commercial paper, mutual funds, and the state of California Local Agency Investment Fund. The City's current investment policy is to keep its portfolio as liquid as necessary to meet the City's needs, minimize credit and market risks, and still maintain an acceptable yield. Accordingly, most city funds are invested in the State's Local Agency Investment Fund or in Federal Agency securities. All investments were held by the City or held in the City's name by Bank of New York's safekeeping department. The maturities of the investments range from 1 day to 1,818 days, with an average weighted maturity of 385 days. The average yield on investments was 4.77 per cent at June 30, 2007.

**Risk management.** The City is self-insured for both worker's compensation and general commercial and automobile liability for the first \$1,000,000 and \$500,000 per occurrence, respectively. The City has purchased excess coverage of \$25,000,000 per occurrence with a \$25,000,000 aggregate for worker's compensation and \$10,000,000 per occurrence with a

\$10,000,000 aggregate for liability. Liability claims are administered internally by the Finance Department and City Attorney, while Worker's Compensation claims are monitored by the Administrative Services Department and a third party administrator. Both self-insurance programs are being accounted for in separate internal service funds in which resources are being accumulated to meet current and potential losses. Additional information on the City's risk management activity can be found in the Notes to the Basic Financial Statements.

**Pension and other postemployment benefits.** The City contributes to the California Public Employees Retirement System, an agent multiple-employer public employee defined benefit pension plan for its employees. Each year, an independent actuary engaged by the pension plan calculates the amount of the annual contribution that the City must make to the pension plan to ensure that the plan will be able to fully meet its obligations to retired employees on a timely basis. As a matter of policy, the City fully funds each year's annual required contribution to the pension plan as determined by this funding policy. A discussion of the amortization of the unfunded actuarial liability associated with employee services rendered to date is discussed in Note 9 of the Notes to the Financial Statements.

The City also provides postretirement health care benefits, in accordance with applicable Memoranda of Understanding and the California Government Code, to all employees who retire from the City of Redlands. As of the end of the current fiscal year, there were 228 retirees eligible to receive these benefits, which are financed on a pay-as-you-go basis. Additional information regarding the City's pension arrangements and postemployment benefits can be found in the Notes to the Financial Statements.

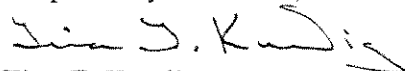
#### Awards and Acknowledgements

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement of Excellence in Financial Reporting to the City of Redlands for its comprehensive annual financial reports for the fiscal years ended June 30, 2003, 2004, 2005 and 2006. In order to be awarded a Certificate of Achievement, a government must publish an easily readable and efficiently organized comprehensive annual financial report. This report must satisfy both generally accepted accounting principles and applicable legal requirements.

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

The preparation of the comprehensive annual financial report was made possible by the dedicated service of the entire staff of the Finance department. Special recognition is due to the Assistant Finance Director, Tom Steele, and Senior Accountant, Nicolette Kay, for their extraordinary effort in overseeing the compilation of the accounting data and interfacing with our auditors, to accounting staff members Kim Braun and Mary Ellen Lambert for their support, to the accounting firm of MAYER HOFFMAN MCCANN, P.C. and to Teresa Ballinger, Reprographics Technician.

Respectfully submitted,



Tina T. Kundig  
Finance Director

# Certificate of Achievement for Excellence in Financial Reporting

Presented to

City of Redlands  
California

For its Comprehensive Annual  
Financial Report  
for the Fiscal Year Ended  
June 30, 2006

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



*Oliver S. Cox*

President

*Jeffrey R. Egan*

Executive Director

CITY OF REDLANDS  
PRINCIPAL OFFICERS

CITY COUNCIL (Elected)	Jon P. Harrison, Mayor Patricia L. Gilbreath, Mayor Pro Tem Peter R. Aguilar, Councilmember Michael T. Gallagher, Councilmember Gilberto Gil, Councilmember
CITY MANAGER	N. Enrique Martinez
CITY CLERK (Elected)	Lorrie C. Poyzer
CITY TREASURER (Elected)	Michael Reynolds
CITY ATTORNEY	Daniel J. McHugh
ADMINISTRATIVE SERVICES DIRECTOR (Acting)	Tina T. Kundig
COMMUNITY DEVELOPMENT DIRECTOR	Jeffrey L. Shaw
FINANCE DIRECTOR	Tina T. Kundig
FIRE CHIEF	James J. Drabinski
LIBRARY DIRECTOR	Larry E. Burgess
MUNICIPAL UTILITIES DIRECTOR	Gary G. Phelps
POLICE CHIEF	James R. Bueermann
PUBLIC WORKS DIRECTOR	Ronald C. Mutter
REDEVELOPMENT DIRECTOR (Interim)	Steven H. Dukett



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