



A REPORT
TO THE
ARIZONA LEGISLATURE

Financial Audit Division

Financial Statement Audit

Pima County
Development Services
Enterprise Fund
June 30, 2002



Debra K. Davenport
Auditor General

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Pima County
Development Services Enterprise Fund
Report on Audit of Financial Statements
June 30, 2002

Table of Contents	Page
Independent Auditors' Report	1
Statement of Net Assets	2
Statement of Revenues, Expenses, and Changes in Fund Net Assets	3
Statement of Cash Flows	4
Notes to Financial Statements	6



**STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL**

DEBRA K. DAVENPORT, CPA
AUDITOR GENERAL

WILLIAM THOMSON
DEPUTY AUDITOR GENERAL

Independent Auditors' Report

Members of the Arizona State Legislature

The Board of Supervisors of Pima County, Arizona

We have audited the accompanying financial statements of Pima County's Development Services Enterprise Fund as of and for the year ended June 30, 2002, as listed in the table of contents. These financial statements are the responsibility of the County's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with U.S. generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1, Pima County Development Services Enterprise Fund's financial statements are intended to present the financial position, and the changes in financial position and cash flows of only that portion of the business-type activities and aggregate remaining fund information of Pima County that is attributable to the transactions of the Pima County Development Services Enterprise Fund. They do not purport to, and do not, present fairly the financial position, and the changes in financial position and cash flows of the County in conformity with U.S. generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Pima County Development Services Enterprise Fund as of June 30, 2002, and the changes in financial position and cash flows for the year then ended in conformity with U.S. generally accepted accounting principles.

As described in Note 2, Pima County adopted the provisions of GASB Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, for the year ended June 30, 2002, to implement a new financial reporting model. Also, as described in Note 2, the County changed its policy for capitalizing assets by raising its capitalization threshold. This represents a change in the application of an accounting principle.

Debbie Davenport
Auditor General

December 31, 2002

Pima County
 Development Services Enterprise Fund
 Statement of Net Assets
 June 30, 2002

Assets

Current assets:

Cash and cash equivalents	\$6,051,016
Interest receivable	22,204
Accounts receivable	785
Due from other Pima County funds	336
Due from other governments	540
Prepaid expenses	<u>27</u>
Total current assets	<u>6,074,908</u>

Noncurrent assets:

Equipment	817,504
Less accumulated depreciation	<u>(485,383)</u>
Total noncurrent assets	<u>332,121</u>
Total assets	<u>6,407,029</u>

Liabilities

Current liabilities:

Accrued employee compensation	740,761
Accounts payable	168,062
Due to other Pima County funds	<u>10,676</u>
Total current liabilities	<u>919,499</u>

Net Assets

Invested in capital assets, net of related debt	332,121
Unrestricted	<u>5,155,409</u>
Total net assets	<u>\$5,487,530</u>

See accompanying notes to financial statements.

Pima County
 Development Services Enterprise Fund
 Statement of Revenues, Expenses,
 and Changes in Fund Net Assets
 Year Ended June 30, 2002

Operating revenues:	
Charges for services	\$7,754,172
Other	<u>154,865</u>
Total operating revenues	<u>7,909,037</u>
Operating expenses:	
Employee compensation	5,557,972
Operating supplies and services	955,990
Utilities	96,980
Repairs and maintenance	112,810
General and administrative	1,396,691
Consultants and professional services	171,517
Depreciation	<u>108,736</u>
Total operating expenses	<u>8,400,696</u>
Operating loss	(491,659)
Nonoperating revenues (expenses):	
Interest income	158,422
Loss on disposal of capital assets	<u>(10,731)</u>
Total nonoperating revenues (expenses)	<u>147,691</u>
Decrease in net assets	(343,968)
Total net assets, July 1, 2001, as restated	<u>5,831,498</u>
Total net assets, June 30, 2002	<u>\$5,487,530</u>

See accompanying notes to financial statements.

Pima County
Development Services Enterprise Fund
Statement of Cash Flows
Year Ended June 30, 2002

Cash flows from operating activities:	
Receipts from customers for goods and services	\$ 7,770,213
Receipts from other Pima County funds for goods and services	140,035
Receipts from miscellaneous operations	154,800
Payments to employees	(5,139,726)
Payments to suppliers for goods and services	(838,112)
Payments to other Pima County funds for goods and services	<u>(2,332,968)</u>
Net cash used for operating activities	<u>(245,758)</u>
Cash flows from capital and related financing activities:	
Purchase of capital assets	<u>(41,210)</u>
Net cash used for capital and related financing activities	<u>(41,210)</u>
Cash flows from investing activities:	
Interest received on investments	<u>180,460</u>
Net cash provided by investing activities	<u>180,460</u>
Net decrease in cash and cash equivalents	(106,508)
Cash and cash equivalents, July 1, 2001	<u>6,157,524</u>
Cash and cash equivalents, June 30, 2002	<u>\$ 6,051,016</u>
	(continued)

See accompanying notes to financial statements.

Pima County
 Development Services Enterprise Fund
 Statement of Cash Flows
 Year Ended June 30, 2002
 (continued)

Reconciliation of operating loss to net cash used for operating activities:	
Operating loss	\$ (491,659)
Adjustments to reconcile operating loss to net cash used for operating activities:	
Depreciation	108,736
Changes in assets and liabilities:	
Accounts receivable	(65)
Due from other Pima County funds	(336)
Due from other governments	16,040
Prepaid expenses	6,325
Accrued employee compensation	120,456
Accounts payable	(15,931)
Due to other Pima County funds	<u>10,676</u>
Net cash used for operating activities	<u>\$ (245,758)</u>

Noncash investing, capital, and noncapital financing activities:

During the year ended June 30, 2002, the Development Services Enterprise Fund disposed of assets with an original cost of \$40,391 and accumulated depreciation of \$29,660 for a loss on disposal of \$10,731.

See accompanying notes to financial statements.

Pima County
Development Services Enterprise Fund
Notes to Financial Statements
June 30, 2002

Note 1 - Summary of Significant Accounting Policies

The accounting policies of the Pima County Development Services Enterprise Fund conform to generally accepted accounting principles applicable to governmental units adopted by the Governmental Accounting Standards Board (GASB). During the year ended June 30, 2002, Pima County implemented GASB Statement No. 34, as amended by GASB Statement No. 37, which prescribes a new reporting model for state and local governments. The County also implemented GASB Statement No. 38, which prescribes new and revised note disclosures. As a result, the Fund has adopted the reporting requirements for business-type activities. A summary of the Fund's more significant accounting policies follows.

A. Reporting Entity

The Fund is accounted for as an enterprise fund of Pima County, Arizona, and is responsible for issuing zoning permits and enforcing and administering building and zoning codes and land development ordinances in Pima County. The financial statements present only the Development Services Enterprise Fund and are not intended to present the balances and activity of Pima County or its business-type activities and enterprise funds. The Fund's management has the day-to-day financial accountability for the Fund and is directed by an administrator appointed by the Pima County Board of Supervisors. However, ultimate financial accountability for the Fund remains with Pima County.

B. Fund Accounting

The Fund's accounts are maintained in accordance with the principles of fund accounting to ensure that limitations and restrictions on the Fund's available resources are observed. The principles of fund accounting require that resources be classified for accounting and reporting purposes into funds in accordance with the activities or objectives specified for those resources. A fund is considered a separate accounting entity, and its operations are accounted for in a separate set of self-balancing accounts that comprise its assets, liabilities, net assets, revenues, and expenses.

The Fund's financial transactions are recorded and reported as an enterprise fund because its operations are financed and operated in a manner similar to private business enterprises, in which the intent of the Board of Supervisors is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges.

The Fund follows those Financial Accounting Standards Board Statements and Interpretations issued on or before November 30, 1989; Accounting Principles Board Opinions; and Accounting Research Bulletins, unless those pronouncements conflict with GASB pronouncements.

Pima County
Development Services Enterprise Fund
Notes to Financial Statements
June 30, 2002

C. Basis of Accounting

Basis of accounting relates to the timing of the measurements made, regardless of the measurement focus applied, and determines when revenues and expenses are recognized in the accounts and reported in the financial statements. The financial statements of the Fund are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recognized when they are earned, and expenses are recognized at the time liabilities are incurred, regardless of when the related cash flow takes place. Interfund transactions with other Pima County funds are recorded in the appropriate revenue or expense account.

D. Basis of Presentation

The financial statements include a statement of net assets; a statement of revenues, expenses, and changes in fund net assets; and a statement of cash flows.

A statement of net assets provides information about the assets, liabilities, and net assets of the Fund at the end of the year. Assets and liabilities are classified as either current or noncurrent. Net assets are classified according to external donor restrictions or availability of assets to satisfy the Fund's obligations. Invested in capital assets net of related debt represents the net value of capital assets less the debt incurred to acquire or construct the asset. Restricted net assets represent grants, contracts, and other resources that have been externally restricted for specific purposes. Unrestricted net assets include all other net assets, including those that have been designated by management to be used for other than general operating purposes.

A statement of revenues, expenses, and changes in fund net assets provides information about the Fund's financial activities during the year. Revenues and expenses are classified as either operating or nonoperating, and all changes in net assets are reported. Generally, charges for services and other fees generated for issuing zoning permits and enforcing building, zoning, and land development rules and regulations are considered to be operating revenues. Other revenues, such as investment income, are not generated from operations and are considered to be nonoperating revenues.

A statement of cash flows provides information about the Fund's sources and uses of cash and cash equivalents during the year. Increases and decreases in cash and cash equivalents are classified as either operating, noncapital financing, capital financing, or investing.

The measurement focus of the fund is on the flow of economic resources. With this measurement focus, all assets and all liabilities associated with the operation of the Fund are included on the statement of net assets. Net assets is segregated into invested in capital assets, net of related debt; restricted; and unrestricted. The operating statement presents increases (e.g., revenues) and decreases (e.g., expenses) in total net assets.

Pima County
 Development Services Enterprise Fund
 Notes to Financial Statements
 June 30, 2002

E. Cash and Cash Equivalents

For purposes of the statement of cash flows, cash and cash equivalents consist of cash on hand, cash and investments held by the Pima County Treasurer, and investments with the State Treasurer. All investments are stated at fair value.

F. Capital Equipment

Capital equipment is recorded at cost. The Fund capitalizes equipment valued at more than \$5,000. Depreciation of such assets is charged as an expense against operations. These assets are depreciated over their estimated useful lives using the straight-line method. The estimated useful lives range from 6 to 16 years.

G. Compensated Absences

Compensated absences consist of annual leave and a calculated amount of sick leave earned by employees based on services already rendered. Employees may accumulate up to 240 hours of annual leave, but must forfeit any annual leave hours in excess of the maximum that are unused at the end of the payroll period in which the employee's anniversary date falls. Upon termination, all unused and unforfeited annual leave benefits are paid to employees. Accordingly, annual leave benefits are accrued as a liability in the financial statements. Employees may accumulate an unlimited number of sick leave hours. Generally, sick leave benefits provide for ordinary sick pay and are cumulative, but do not vest with employees and, therefore, are not accrued in the financial statements. However, for employees who retire with 20 years or more of continuous service or who have a combined total of age and years of service equal to 80 points, some sick leave benefits do vest based on various criteria, and, therefore, are accrued.

Note 2 - Accounting Changes

As a result of implementing GASB Statement No. 34, the fund's aggregate fund equity balances reported as of June 30, 2001, have been restated as beginning net assets. Additionally, as of July 1, 2001, Pima County changed its capitalization threshold from \$1,000 to \$5,000 and applied that policy change retroactively. The cumulative effect of these changes follows:

Fund equity, June 30, 2001, as previously reported	\$6,199,484
Cumulative effect of change in capitalization threshold	<u>(367,986)</u>
Total fund equity, July 1, 2001, as restated	<u>\$5,831,498</u>
Net assets—Invested in capital assets, net of related debt	\$ 410,378
Net assets—Unrestricted	<u>5,421,120</u>
Total net assets, July 1, 2001, as restated	<u>\$5,831,498</u>

Pima County
Development Services Enterprise Fund
Notes to Financial Statements
June 30, 2002

Note 3 - Cash and Cash Equivalents

Cash and cash equivalents on the statement of net assets consist of \$550 of cash on hand, \$406,984 of cash and investments held by the County Treasurer, and \$5,643,482 of investments with the State Treasurer.

The cash and investments held by the County Treasurer represent a proportionate interest of the County Treasurer's investment pool portfolio. The Fund's portion is not identified with specific investments and is not subject to custodial credit risk.

Investments with the State Treasurer are in the State Treasurer's Local Government Investment Pool. The State Board of Deposit provides oversight for the State Treasurer's pools, and the Local Government Investment Pool Advisory Committee provides consultation and advice to the Treasurer. The fair value of a participant's position in the pool approximates the value of that participant's pool shares. Those shares are not identified with specific investments and are not subject to custodial credit risk.

Note 4 - Capital Asset Activity

Capital asset activity for the year ended June 30, 2002 was as follows:

	July 1, 2001 Balance (as restated)	Increases	Decreases	June 30, 2002 Balance
Equipment	\$ 816,685	\$ 41,210	\$(40,391)	\$ 817,504
Accumulated depreciation	<u>(406,307)</u>	(108,736)	29,660	<u>(485,383)</u>
Total capital assets, net	<u>\$ 410,378</u>			<u>\$ 332,121</u>

Note 5 - Related Party Transactions

Administrative and Fiscal Services—For the year ended June 30, 2002, the Fund incurred expenses from Pima County for a variety of administrative and fiscal services totaling \$1,559,081. Of that amount, \$297,790 was for temporary or part-time staffing, \$227,817 was for motor pool charges, \$475,266 was for the allocation of overhead, \$146,813 was for supplies, \$61,524 was for self-insurance premiums, and \$349,871 was for other miscellaneous charges. In addition, the Fund provided goods and services to other Pima County departments totaling \$140,035.

Pima County
Development Services Enterprise Fund
Notes to Financial Statements
June 30, 2002

Public Works Center—The Fund occupies a portion of the Public Works Center and pays rent equivalent to its pro rata share of the building expenses incurred by the Pima County Facilities Management Department. For the year ended June 30, 2002, rent expense for the Fund totaled \$558,755.

Note 6 - Risk Management

The Fund is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Fund is a participant in Pima County's self-insurance program, and in the opinion of the Fund's management, that program would cover any unfavorable outcomes from these risks. Accordingly, the Fund has no risk of loss beyond adjustments to future years' premium payments to Pima County's self-insurance program. All estimated losses for unsettled claims and actions of Pima County are determined on an actuarial basis and are included in the *Pima County Comprehensive Annual Financial Report*.

Note 7 - Retirement Plan

Plan Description—The Fund contributes to a cost-sharing multiple-employer defined benefit pension plan administered by the Arizona State Retirement System. Benefits are established by state statute and generally provide retirement, death, long-term disability, survivor, and health insurance premium benefits. The System is governed by the Arizona State Retirement System Board according to the provisions of Arizona Revised Statutes Title 38, Chapter 5, Article 2.

The System issues a comprehensive annual financial report that includes financial statements and required supplementary information. The most recent report may be obtained by writing the Arizona State Retirement System, 3300 North Central Avenue, P.O. Box 33910, Phoenix, AZ 85067-3910 or by calling (602) 240-2000 or (800) 621-3778.

Funding Policy—The Arizona State Legislature establishes and may amend active plan members' and the Fund's contribution rate. For the year ended June 30, 2002, active plan members and the Fund were each required by statute to contribute at the actuarially determined rate of 2.49 percent (2.00 percent retirement and 0.49 percent long-term disability) of the members' annual covered payroll. The Fund's contributions to the System for the years ended June 30, 2002, 2001, and 2000, were \$128,607, \$126,084, and \$120,053, respectively, which were equal to the required contributions for the year.

Pima County
Development Services Enterprise Fund
Notes to Financial Statements
June 30, 2002

Note 8 - Subsequent Events

Recent Investment Losses in the State Treasurer's Local Government Investment Pool— Pursuant to statutory authority, a portion of the Fund's monies are invested in the State Treasurer's Local Government Investment Pool (LGIP), which was established in 1980 for the collective investment of State and local government monies. Monies in the LGIP may be invested in various types of investments prescribed by law, including bonds, debentures, or other evidences of indebtedness that are issued by entities organized and doing business in the United States that have a minimum rating of "Baa" from Moody's Investors Service or "BBB" from Standard & Poor's Rating Service. In December 2002, the State Treasurer announced that the LGIP currently holds approximately \$131 million of asset-backed securities issued by an NPF-12 trust that are serviced by National Century Financial Enterprises (NCFE). Recently, NCFE has come under investigation by the Federal Bureau of Investigation, the Securities and Exchange Commission, and various state authorities for possible fraud and violations of federal and state laws. NCFE has since declared bankruptcy and the trustee for the bonds has informed the State Treasurer that the interest payment due December 1, 2002, was not received.

All LGIP participants have been allocated a proportional share of the value of the NPF-12 securities, and such securities have been placed by the State Treasurer into a separate pool (the "Separate LGIP Pool"). It is likely that the LGIP will incur a loss on the total securities held of approximately \$131 million. Of this likely loss to the LGIP, the County currently estimates the Fund would be allocated approximately \$179,000 as its proportional share as an LGIP participant. The State is pursuing legal action to the fullest extent possible to protect the interests of the LGIP participants which may eventually include the recovery of all or a portion of the investment loss.