



December 2, 2002

Honorable Mayor and City Council  
City of Albuquerque, New Mexico

We are pleased to submit the Comprehensive Annual Financial Report (CAFR) of the City of Albuquerque, New Mexico, (City), for the fiscal year ended June 30, 2002. The report was prepared by the Finance and Administrative Services Department. The responsibility for the accuracy of the data presented and the completeness and fairness of presentation, including all disclosures, rests with the City. As indicated by the opinion of our independent auditors, the report fairly presents the financial position and results of operations of the City as measured by the financial activity of its various funds. The report has been set forth in a manner that will give the reader a broad understanding of the City's financial affairs. It includes disclosures necessary for the reader to gain an understanding of the City's financial activities.

This is the first year the City prepares the CAFR using the new financial reporting requirements as prescribed by the Governmental Accounting Standards Board Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments* (GASB 34). This new GASB Statement requires that management provide a narrative introduction, overview, and analysis to accompany the basic financial statements in the form of a Management's Discussion & Analysis (MD&A). This letter of transmittal is designed to complement the MD&A and should be read in conjunction with it. The MD&A can be found immediately following the report of the independent auditors.

The City's Comprehensive Annual Financial Report consists of five major sections:

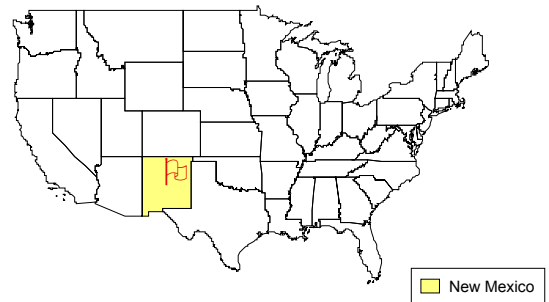
- (1) **The Introductory Section** includes this letter of transmittal that provides information about the organizational structure of the City, the City's economy, internal control structure, budgetary controls, cash management, and risk management.
- (2) **The Financial Section** is prepared in accordance with the GASB 34 requirements by including the MD&A and the Basic Financial Statements including notes. The Basic Financial Statements include government-wide financial statements that present an overview of the City's entire financial operations and the fund financial statements that present the financial information of each of the City's major funds, as well as non-major governmental, proprietary, fiduciary, and other funds. Also included in this section is the Independent Auditors' Report on the financial statements and schedules.
- (3) **The Statistical Information Section** contains tables that includes general information about the City and comparative data for prior fiscal years.
- (4) **Single Audit Information** includes the Schedule of Expenditures of Federal Awards as required by the Single Audit Act, and the related findings and recommendations by the City's independent auditors.
- (5) **State Compliance and Operational Findings** includes certain schedules required by the State Auditor's Office.

The CAFR of the City includes all government activities, organizations and functions for which the City is financially accountable. The criteria used to determine financial accountability are based upon and consistent with the pronouncements of the Governmental Accounting Standards Board, which sets criteria for defining the financial reporting entity. The City of Albuquerque is a major municipal government providing a full range of services to approximately 562,000 citizens. Included in these services are traditional city functions such as police and fire protection, culture and recreation, public works, road and traffic signal maintenance, water and sewer services, and refuse collection. In addition, the City operates parking facilities, a transit system, an international airport, corrections and detention facilities, and a housing authority. The City does not have relationships with any other organizations not included in this CAFR of such nature and significance that exclusion would render the City's financial statements incomplete or misleading.

## ECONOMIC CONDITION AND OUTLOOK

### Summary of Local Economy

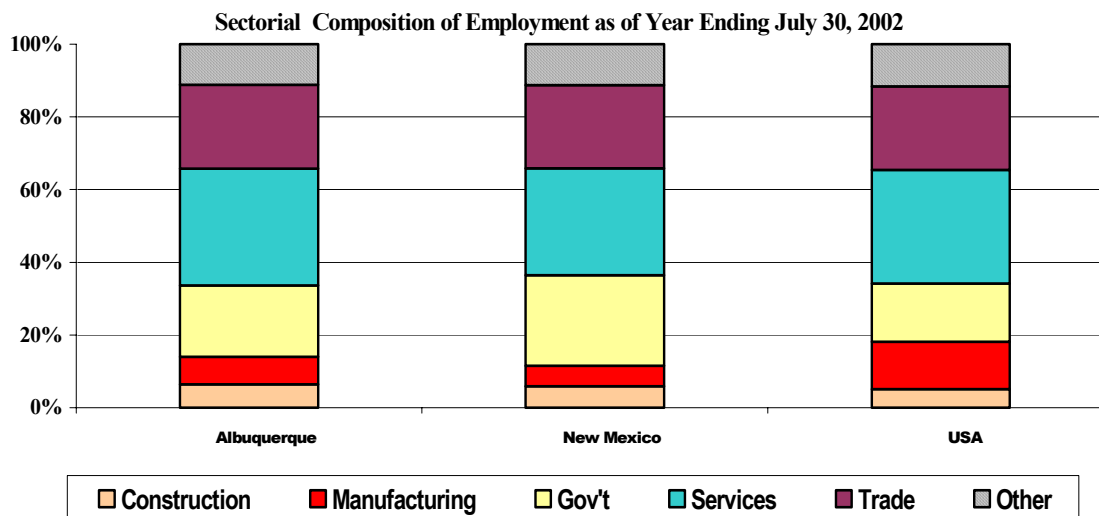
Albuquerque is the largest city in New Mexico, accounting for roughly one-quarter of the state's population. Albuquerque is the major commercial, trade, service and financial center of the state. It is located in the central part of the state, at the intersection of two major interstate highways, and served by both rail and air. The Albuquerque Metropolitan Statistical Area (MSA) includes Bernalillo, Sandoval and Valencia Counties. The largest employers in the Albuquerque area are the University of New Mexico, Albuquerque Public Schools, Sandia National Labs (SNL), and Kirtland Air Force Base.



The Albuquerque economy is a desirable place to live with a basically strong economy with a growing diversity. The economy in 1990's, took off after the national recession of 1991. Through 1996, the economy grew rapidly as the semiconductor industry moved into Albuquerque. These expansions included firms such as Intel, Philips, and Sumitomo. Along with this expansion, residential and commercial construction grew rapidly. Annual growth in non-agricultural employment peaked at 6.1% in 1994 but remained strong into 1996, but as expansions were completed and construction ended, employment growth slowed dramatically. This was added to by a continued reduction of employment and spending by the Department of Energy at SNL. In 1997, the economy slowed further, as a financial crisis in Asia, caused a large reduction in purchases of computer chips. This "Asian Flu" hit the local economy and manufacturing declined resulting in growth in total non-agricultural employment of around 1.5% in 1998 and 1999. In 2000, employment began to turn around as manufacturing started growing. The semiconductor industry again gained employment and expanded plants that along with road construction helped bring employment growth up to 3% in 2000. Large construction projects to build the Big-I (interchange of I-40 and I-25) and Intel's construction of a new fabrication plant drove up construction employment. This was short-lived, as the national economy stumbled in 2001. The terrorist attacks of September 11, 2001 accelerated this slowdown. The manufacturing sector in New Mexico as well as the U.S. was hardest hit. This combined with the slowdown in large construction projects left the Albuquerque MSA with no employment growth for the last quarter of 2001 and minimal growth in the first half of 2002. In Albuquerque unemployment rates that had declined to 3.5% in 2000 increased to over 5% in July of 2002.

The Albuquerque economy has an industry composition that is similar to the U.S. as a whole. Manufacturing is a smaller portion of employment, but even with the recent slowdown, it has held a relatively stable share of employment. In the U.S. the manufacturing share of employment has declined from about 18% in 1990 to 13% in 2002. In the 1960s manufacturing made up over 30% of the U.S. economy.

The following chart shows the composition of employment for the State, the U.S. and Albuquerque as of the second quarter 2002.



### Major Industries

**Services** The service sector is the largest source of employment in the MSA, accounting for 32% of the non-agricultural civilian employment in FY/01. This sector has grown in importance in both Albuquerque and in the U.S. It is a diverse sector including jobs in medical services, hotels, amusement, movies, legal work, commercial research, business services, engineering, and architectural services. The Business Services sector is important and includes the growing temporary employment agencies, many of the call centers, back office operations, and employment at SNL. Reductions in Department of Energy spending and reductions in employment at SNL have impacted this sector. Since 1994 Employment at SNL, operated by Lockheed Martin, decreased about 1,700 and currently has a workforce of 6,600 people. Employment at SNL has stabilized, and is in part due to national security issues associated with the terrorist threat is now expanding. The labs will add several hundred jobs in the next few years. Also, a Center for Integrated Nanotechnologies is part of a proposal for five nano-technology research centers to be developed by the Energy Department's Office of Science will be built in Albuquerque and Los Alamos. In addition, the Labs efforts in spinning off technology appear to be paying off. The Sandia Research Park, opened with its first occupant EMCORE, now has additional high-tech occupants taking advantage of the location and ability to access SNL facilities and staff. Also located on the Park is the SNL International Programs Building. This houses the Cooperative Monitoring Center and International Security Center. The function of these programs is to strengthen national and international security and reduce the threat of weapons of mass destruction.

As a major regional medical center the medical services industry has several of the largest employers in the area. The health services industry has been one of the fastest growing sectors in the Albuquerque area. This growth has recently slowed in part due to changes and uncertainties regarding health care financing, Medicare, and announced cutbacks at local medical centers

The business services sector includes many of the call centers and back office operations. However, the labor department has reclassified some of these jobs into other sectors. For instance: The "Finance, Insurance & Real Estate" class (FIRE) includes Nations Bank credit card service center, and Citicorp credit processing center; The "Transportation, Communications, & Utilities" class (TCU) includes T-Mobile (formerly VoiceStream Wireless) customer service and technical support center and MCI Consumer Markets telemarketing operation. This category includes John Hancock, which has recently announced closure of their plant with about 120 layoffs.

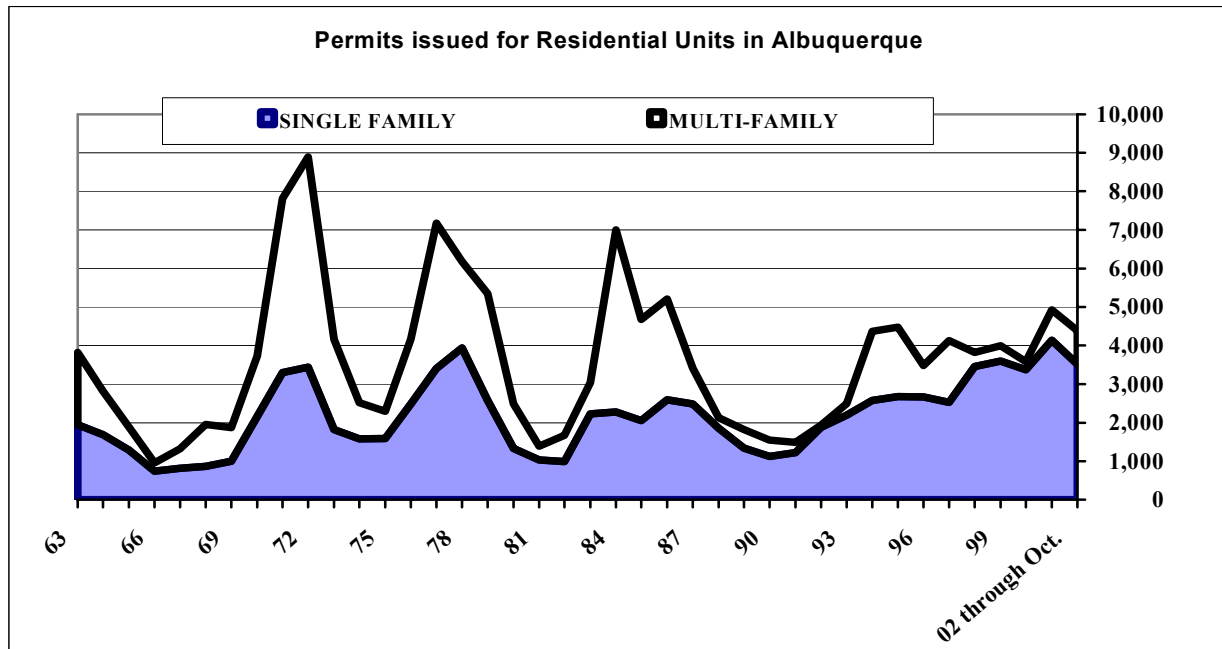
**Trade (retail and wholesale):** The trade sector is a strong catalyst for growth in the area. Many major national chains have expanded in the area and general growth and low interest rates have helped fuel consumer spending. The completion of Cottonwood Mall and other retail space does bring with it a concern that retail has been overbuilt in the area.

Non Agricultural Employment in the Albuquerque MSA (000's)				
Category	FY 2002	Share of FY/01 Employment	Growth FY/00 to FY/01	Annualized Average Growth FY/97-FY/02
<b>Total Non-Agricultural</b>	<b>360.17</b>		<b>0.4%</b>	<b>1.8%</b>
Trade	83.69	23%	0.0%	0.5%
Services	115.29	32%	0.5%	1.7%
Government	70.05	19%	3.0%	1.5%
Manufacturing	27.76	8%	-3.2%	-1.2%
Construction	23.68	7%	-3.4%	1.8%
TCU	20.18	6%	1.9%	5.0%
FIRE	19.53	5%	1.3%	3.0%
Military	6.44	N/A	0.0%	-2.0%

**Manufacturing** Albuquerque's small manufacturing sector accounts for about 8% of total non-agricultural employment and is one of the area's most dynamic sectors. Investments by Intel, Philips and other high tech firms have helped to create a critical mass of activity in Albuquerque that has attracted interest by other firms; competitors, suppliers, and customers. Albuquerque is now rated as one of the top high tech centers in the U.S. as ranked by Forbes Magazine and others. Intel has completed its \$2 billion expansion which Intel calls the most advanced chip plant in the world. Unfortunately many of the other firms in the semiconductor and high-tech area have not fared as well. Philips has laid off several hundred workers, Lightpath Technology has consolidated its operations in Florida, and EMCORE has laid off over 100 workers. The over-expansion and collapse of the telecommunications industry has been one of the major problems. The manufacturing sector lost about 1,300 jobs from August 2001 to August 2002. Adding to this is the November announcement by Philips Semiconductor that they will close their plant in October 2003. This will cost approximately 600 jobs. At its peak Philips employed over 1,000 workers. The losses seem to be slowing, but a recovery in the semi-conductor is needed for the industry to fully recover.

**Construction.** The construction sector is a source of growth and of volatility in the Albuquerque economy. Growth in employment and in gross receipts in construction tends to be quite cyclical. As shown in the following chart the residential building market exemplifies this. The booms of 1972, 1978, and 1984 were very large, and followed by very steep declines. This was accentuated by the multifamily housing market and certain tax rules that encouraged large development. In the 1990s, there has been a more or less sustained growth in single-family home construction. In this period, multifamily housing construction has been relatively small compared to other booms. Growth in the single-family market suffered a small slowdown in 1997, but since 1991 has generally continued upward in record numbers of houses permitted. Several factors have helped spur this growth: reductions in the median prices of homes—the percentage of entry level homes has doubled from 10% to 20% of the market since 1997; lower interest rates, easier lending rules and programs to help first time home buyers. This market niche within the City was also helped by the reduction of residential construction (moderately priced) in nearby Rio Rancho. The number of multi-family units permitted has been limited. In 1997 there were 1,600 units permits issued while only 967 units were permitted in the three years 1998 through 2000. This picked up some with 792 units permitted in 2001 and 871 units through September of 2002. Not counted in this number are 69 units in the Old Albuquerque High project that were permitted as alterations rather than new units.

The following chart illustrates the construction permits issued:



In the 1990's, commercial construction peaked in 1995, but remained at historically high levels. New commercial construction slowed substantially in 2002, due in large part to national slowdown and reduction in but much is this is offset by construction classified as additions and alterations. Presbyterian, has permitted \$30 million for renovation and expansion of their main hospital and office space. Philips issued permits for a large expansion, but this project is on hold and some of the equipment was sent to New York. Intel completed, in June 2002, a two billion dollar project that employed nearly 2000 construction workers at its peak. The public sector permits issued in 2000 was strong, the City permitted a number of projects including: the Alvarado transportation center; a crime lab; a car rental facility at the Airport; the Explora Museum and three parking garages. In 2001, a \$18 million permit was issued to renovate the AAA ballpark. Through September of 2002, public permits issued was less than one quarter of the 2001 level. State and Federal agencies, whose projects do not show up in City building permit numbers, also have built several large projects. In 2000 and 2001, the State constructed a new District Attorneys' office, expanded the Museum of Natural History, and a District Courthouse. Construction of a new metropolitan courthouse began in 2001 and a parking structure to serve Metro and District Courthouse is also under construction. The Federal government in 2001 completed a Forest Service Building and a Social Security Administration building—both in downtown. A Social Security Administration office building is currently under construction in the downtown area. The two-year \$250 million reconstruction of the Big-I (intersection of Interstates 25 and 40) was completed before the scheduled completion date of June 2002. This project employed approximately 1,000 workers at its peak and the loss of these jobs has helped curtail employment growth in the region. The expansion of the indian casinos at Isleta, Sandia, and the Santa Ana Pueblos also helped increase construction employment in the area. These projects total nearly \$200 million and include destination resort hotels at Isleta and Santa Ana Pueblos. Recent projects include a large renovation of Presbyterian hospital and renovation the Albuquerque sports stadium.

**Government.** The total number of government employees in the Albuquerque MSA increased by 7,800 between 1995 and 2001. The gain was all at the state and local level and much is due to the classification of indian casino workers as local government employees. Federal government has reduced it level of employment having a significant effect on the Albuquerque economy since the late 1980's. Military employment has declined in every year since 1989, and there have been reductions in federal government employment in each year since 1993. Reductions in federal military spending have been responsible for losses in employment at General Electric, Honeywell Defense, Avionics, and BDM. On the brighter side, the new Sandia business Park and the push for technology transfer from the labs, is reflected in the growth of high tech industries in central New Mexico. Funding from the federal government for the nuclear weapons program and nuclear security now seem relatively secure as SNL assumes new roles in a post-Cold War period involving nuclear non-proliferation, arms control, and stockpile maintenance. Kirtland AFB, with its diverse operations, has done relatively well in the waves of base consolidations and closures. Recently, Phillips Laboratory was reorganized and became part of the Air Force Research Laboratory, headquartered out of Wright Patterson Air Force Base in Ohio. The reorganization means a loss of some 200 positions at Kirtland, but the positions lost are command positions and not the research positions that are so important to the local economy in terms of incomes paid and contracts let. Offsetting the losses at Phillips, Kirtland AFB is gaining a new flight simulator center. The new Theater Air Command and Control Simulation Facility is

expected to result in more than 200 new full time jobs and many more part-time jobs. Kirtland will also gain some 73 new military positions in the 58th special Operations Wing.

### **Future Economic Outlook**

In the near term Albuquerque faces many of the same problems as the nation. The slowdown in the economy and probable recession were amplified by the terrorist attacks of September 11. How we deal with the threat of terrorism at home will have long term impacts on the economy and how Albuquerque and the U.S. will grow. Employment growth is slow and recovery seems further out into the future. Manufacturing is again one of the main factors in the slower growth.

Hopefully layoffs will be reduced. However, the semiconductor industry and the telecommunications industry nationwide are still in recession. On the plus side, Albuquerque is doing much better than our neighbors. While New Mexico had employment growth of only 0.5%, Colorado, Arizona, and Texas all suffered declines in employment. Tourism, one of New Mexico's largest industries, may not be impacted as much as in other parts of the nation. Much of the tourism in New Mexico is from surrounding states and is largely a driving destination. With lower gasoline prices and less income to devote to vacations, New Mexico may see an increase in tourism. The national labs are another strength. SNL has devoted a great deal of research to terrorism and the mission to protect the nuclear weapons arsenal becomes even more critical. The micro-systems technology or nano-technology, for which SNL is well known, may provide many novel and inexpensive answers to medical and materials sciences. A large facility will be built at the labs as a joint project between Sandia and Los Alamos National labs to expand abilities in this area. The significant investments by producers of semi-conductors and other high technology firms, may present a bit of a drag on the economy today, but the City now has the critical mass necessary to attract further investments by suppliers, customers, and other producers.

### **FINANCIAL INFORMATION**

**Internal control structure.** The Finance and Administrative Services Department is responsible for providing financial services for the City including financial accounting and reporting, payroll and accounts payable disbursement functions, cash and investment management, debt management, purchasing, computer information systems, property management and risk management.

City management is responsible for establishing and maintaining an internal control structure designed to ensure the assets of the government are protected from loss, theft or misuse and to ensure adequate accounting data are compiled to allow for the preparation of financial statements in conformity with generally accepted accounting principles. Accounting principles for municipalities are embodied in pronouncements of the Governmental Accounting Standards Board. The Financial Accounting Standards Board, the American Institute of Certified Public Accountants and the Government Finance Officers Association also impact and influence current governmental accounting standards. The internal control structure is designed to provide reasonable, but not absolute assurance that control objectives are met. The concept of reasonable assurance recognizes that the cost of a control should not exceed the benefits likely to be derived while the establishment of an appropriate internal control structure requires estimates and judgments from management. All internal control evaluations occur within the above framework. We believe that the City's current internal control structure adequately safeguards assets and provides reasonable assurance of proper recording of financial transactions.

**Budgetary controls.** The development and approval of the annual budget is the beginning of the financial transaction process. After approval of the budget by City Council, budgetary control is maintained by a formal appropriation and encumbrance system. The appropriated amounts reflected in the accompanying financial statements represent departmental budgets by program; it is at this level at which expenditures may not exceed appropriations. Encumbrances, which represent commitments for the purchase of goods or services, are shown as a reservation of fund balance in the governmental funds in limited circumstances for property purchases. Those encumbrances will be re-appropriated in fiscal year 2003 for programs that had adequate reversions for the year ended June 30, 2002.

## Taxes.

Taxable property valuations were \$7.4 billion in 2002, a \$523 million increase from the previous year. Current property tax collections were 91.4% of the levy, compared to 91.7% in the prior year. Except for fiscal year 2000, current tax collections for the past decade have consistently exceeded 90% of the levy. The ratio of total collections (current and delinquent) to the current tax levy in 2002 was 94.8% compared to 99.4% in 2001. Cumulative total collections for the last ten years are 97.0% of the cumulative billings. Allocation of the property tax for 2002 and the preceding two fiscal years is based on the following mill levy:

<u>Purpose</u>	<u>2002</u>	<u>2001</u>	<u>2000</u>
Operational mill levy:			
Residential	2.019	2.020	1.963
Non-residential	2.544	2.544	2.380
Debt service levy	8.976	8.976	8.976

The gross receipts tax rate on receipts within the City was 5.8125% at June 30, 2002. The breakdown and sources of the gross receipts tax rate are as follows:

	<u>Tax Rate</u>	<u>Percent of Total Rate</u>
State General Fund	3.2750%	56.34%
Bernalillo County distribution	.2500	4.30
Municipal distribution - State shared	1.0000	17.20
Municipal distribution - in lieu of previous .25% municipal tax - State shared	.2250	3.87
City of Albuquerque general purpose	.5000	8.60
City of Albuquerque basic services	.2500	4.30
City of Albuquerque open space	.2500	4.30
Municipal infrastructure gross receipts tax	<u>.0625</u>	<u>1.08</u>
	5.8125%	100.00%

Additional information about revenues, tax rates, and levies is presented in the statistical section of this report.

**Cash management.** Pursuant to the Fiscal Agent Ordinance of the City, a pooled cash investment program was in place, and cash temporarily idle during the year was invested in those investments and deposits authorized by the City's Investment Policy. It is the City's policy to minimize investment and market risk while seeking to obtain a competitive yield on its total portfolio. Investments and deposits in the City's common investment pool totaled \$323.2 million at June 30, 2002. Of this amount, \$183.1 million was invested in repurchase agreements and \$118.5 million in securities of the Federal government and its related agencies and certificates of deposit.

The City's portfolio average life at June 30, 2002 was 481 days. The average yield on the investment portfolio was 2.86% at the end of June 2002 and 4.80% at the end of June 2001. Interest earned totaled \$15.9 million during the fiscal year. Pooled cash, investments, and accrued interest balances (in millions) at the end of the year for the last five years are as follows:

2002	\$323.2
2001	\$451.1
2000	\$477.8
1999	\$408.8
1998	\$421.8

**Risk management.** The City operates its Risk Management program as an Internal Service Fund; accountability and managerial control over workers compensation, tort liability, and other risks are maintained through this fund. The program is intended as a self-insurance program with added risk control and prevention techniques. "Insurance premiums" are received from the operating departments in the form of transfers. The added risk control and prevention techniques include employee accident prevention training and a wellness program.

The transfers to the Risk Management fund from the operating (insured) departments were \$20.7 million compared to transfers in the prior year of \$15.8 million. Claim reserves (current and long-term) as of June 30, 2002 were \$39.3 million, a increase from \$33.8 million from the previous year. The Fund experienced a net loss of \$1.1 million in 2002, a decrease from the net loss of \$6.7 million in 2000.

The deficit fund equity increased to \$14.1 million at June 30, 2002 from the \$13.0 million at June 30, 2001. The increase in the Risk Management Fund deficit is attributable to an unanticipated adverse judgment in the amount of \$4.25 million in connection with a employee dismissal suit filed against the City. The City has implemented a five year recovery plan and expects to eliminate the deficit by June 30, 2007 by increasing the annual assessment to all operating funds and through an improved loss experience that the City expects to achieve.

#### OTHER INFORMATION

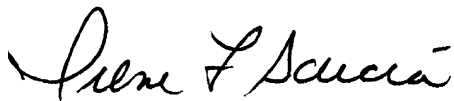
**Independent audit.** New Mexico state law requires that independent public accountants perform an annual audit of a governmental unit's accounting records and Comprehensive Annual Financial Report. The firm of Neff & Ricci LLP has performed the audit for the year ending June 30, 2002. Federal law also requires that a single audit be performed for federal grant funds as required by the Single Audit Act and OMB Circular A-133. The independent auditors' report on the financial statements and schedules is included in the financial section of this report. The independent auditors' reports related specifically to the single audit are included in the Single Audit Section.

**Awards.** The Government Finance Officers Association (GFOA) of the United States and Canada awarded a Certificate of Achievement for Excellence in Financial Reporting to the City of Albuquerque for its Comprehensive Annual Financial Report for the fiscal year ended June 30, 2001. The City has received this prestigious award every year since 1980. In order to be awarded a Certificate of Achievement, a governmental unit must publish an easily readable and efficiently organized Comprehensive Annual Financial Report, the contents of which conform to program standards. Such reports must satisfy both generally accepted accounting principles and applicable legal requirements. A Certificate of Achievement is valid for a period of one year. This report has also been prepared to meet GFOA standards and will be submitted for review.

In addition, the City also received the GFOA's Award for Distinguished Budget Presentation for its annual appropriated budget for the fiscal year beginning July 1, 2001. In order to receive this award, a governmental unit must publish a budget document that meets program criteria as a policy document, as an operations guide, as a financial plan, and as a communications medium.

**Acknowledgments.** The preparation of this report could not have been accomplished without the dedicated services of the staff of the Finance and Administrative Services Department. We wish to express our appreciation to all members of the Department who contributed to its preparation and recognize the major effort of the Accounting Division and its Financial Reporting Section in administering the City's accounting system and in preparing this report. We also wish to thank each of you for your interest and support in planning and conducting the financial operations of the City in a responsible and progressive manner.

Respectfully submitted,



Irene Garcia  
Chief Financial Officer



Sandra Doyle  
Director, Finance and Administrative Services  
Department