

**LOS ANGELES COUNTY
CHILDREN AND FAMILIES
FIRST - PROPOSITION 10 COMMISSION**
(a Component Unit of the
County of Los Angeles, California)

Basic Financial Statements
with Independent Auditor's Reports

For the Year Ended June 30, 2005

**LOS ANGELES COUNTY
CHILDREN AND FAMILIES FIRST - PROPOSITION 10 COMMISSION
FOR THE YEAR ENDED JUNE 30, 2005**

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Champions For Our Children

August 30, 2005

COMMISSIONERS

Los Angeles County
Supervisor
Gloria Molina
Chair

Nancy Au
Vice Chair

Board of Commissioners
First 5 LA
750 N. Alameda Street
Los Angeles, CA 90012

Dear Commissioners:

Jane Boeckmann

Renatta M. Cooper

Thomas L. Garthwaite, M.D.

Neal Kaufman, M.D., M.P.H.

Marvin J. Southard, D.S.W.

The Annual Financial Report of the Los Angeles County Children’s and Families First Proposition 10 Commission (a.k.a. First 5 LA) is hereby submitted. Responsibility for the accuracy of the data and the completeness and fairness of the presentation, including all disclosures rests with the management of First 5 LA. To the best of our knowledge and belief, the enclosed data is accurate in all material aspects and is reported in a manner that presents fairly the financial position and changes to financial position of First 5 LA. All disclosures necessary to enable the reader to gain an understanding of First 5 LA’s financial activities have been included.

Corina Villaraigosa

Carolyn R. Wilder

The Annual Financial Report is presented in four sections: Introductory, Financial, Compliance and Statistical sections.

- The Introductory Section includes the transmitted letter, a list of Commissioners and First 5 LA’s organization chart.
- The Financial Section includes the independent auditor’s report on the basic financial statements, management’s discussion and analysis, basic financial statements and Schedule of Revenues, Expenditures and Changes in Fund Balance – Budget and Actual.
- The Compliance Section includes the independent auditor’s report on Internal Control Over Financial Reporting and on Compliance and Other Matters Required by Government Auditing Standards
- The Statistical Section includes scheduled financial information generally presented on a multi-years basis.

EX OFFICIO MEMBERS
Jacquelyn McCroskey, D.S.W.

Matt S. Rezvani

Deanne Tilton

Harriette F. Williams, Ed.D.

EXECUTIVE DIRECTOR
Evelyn V. Martinez

750 N. Alameda Street
Los Angeles, CA 90012
PH: 213.482.5902
FAX: 213.482.5903
www.first5.org
contact@first5.org

Generally Accepted Accounting Principles (GAAP) for local governments requires management to provide a narrative introduction, overview and analysis to accompany the basic financial statements. The introduction, overview and analysis are presented in the form of the Management’s Discussion and Analysis (MD&A). The letter of transmittal was designed to complement and to be read in conjunction with the MD&A.

A public entity.

Projects of First 5 LA

First 5 LA was created by the Los Angeles County Board of Supervisors in December 1998 following the passage of Proposition 10, through which California voters made an unprecedented investment in early childhood development. Our activities have been built on research regarding early brain development and the understanding that the emotional, physical and environmental surroundings that a child experiences in the first five years of life set the foundation for future development. During the first five years, First 5 LA has made a lasting positive impact in Los Angeles County through its allocation of more than \$700 million toward grants and programs that improve the well-being of young children and families in Los Angeles County.

Planning

Strategic Plan

First 5 LA has adopted a Strategic Plan for fiscal years 2004-2009 detailing our continuing commitment to partnering with the Los Angeles County community to improve the lives of expectant parents, children from the prenatal stage through age 5 and their families through the allocation of \$830 million as follows:

Three Goal Areas:

Early learning	\$500 million
Health	\$150 million
Safe Children & Families	\$ 75 million

One Focus Area:

Prenatal to three age groups	<u>\$105 million</u>
Total	<u>\$830 million</u>

This will be the guide by which we will plan, develop, implement, and evaluate our activities through 2009.

Financial Information

Internal Control

The management of First 5 LA is responsible for establishing and maintaining internal controls designed to ensure that the assets of the public entity are protected from loss, theft, or misuse. Management is also responsible for ensuring that adequate accounting data are compiled to allow for the preparation of the basic financial statements in conformity with accounting principles generally accepted in the United States of America. Internal controls are designed to provide reasonable, but not absolute, assurance that these objectives are met. The concept of reasonable assurance recognizes that: (1) the cost of a control should not exceed the benefits likely to be derived; and (2) the valuation of costs and benefits requires estimates and judgments by management.

Budgetary Control

The objective of budgetary control is to ensure that spending is limited to the total amount authorized by the Board of Commissioners. The budget for fiscal year 2004-2005 was adopted on June 24, 2004. The Executive Director has discretion to adjust the budget as may be needed within the total amount of the originally adopted budget. Monthly financial updates are provided to the Board of Commissioners.

Cash and Investment Balance and Fund Balance

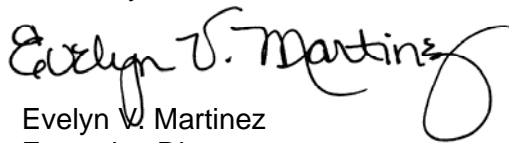
The cash and investment balance of First 5 LA increased from \$ \$678,498,162 at June 30, 2004 to \$726,919,867 at June 30, 2005. The increase was primarily attributed to grantees spending less than anticipated. The increase is also attributed to additional state tax allocations received primarily due to the distribution of one-time monies from a bankruptcy settlement, accumulated interest earnings in the state fund used for state tax allocation and revenue adjustments made by the State.

The fund balance of \$696,950,362 at June 30, 2004 as restated increased to \$743,630,598 at June 30, 2005 primarily due to the excess of revenue over expenditures.

Risk Management

First 5 LA manages its risk exposure in part through the purchase of Workers Compensation, Property, Computer, General Liability, Auto, Crime, Directors and Officers and Umbrella and Excess liability insurance.

Sincerely,



Evelyn V. Martinez
Executive Director

**LOS ANGELES COUNTY
CHILDREN AND FAMILIES FIRST – PROPOSITION 10 COMMISSION
BOARD OF COMMISSIONERS**

Board Members (9)

Gloria Molina Chair	Maria Veloz Vice Chair
Nancy Au Renatta Cooper Neal Kaufman Carolyn Wilder	Jane Boeckmann Thomas L. Garthwaite Marvin J. Southard

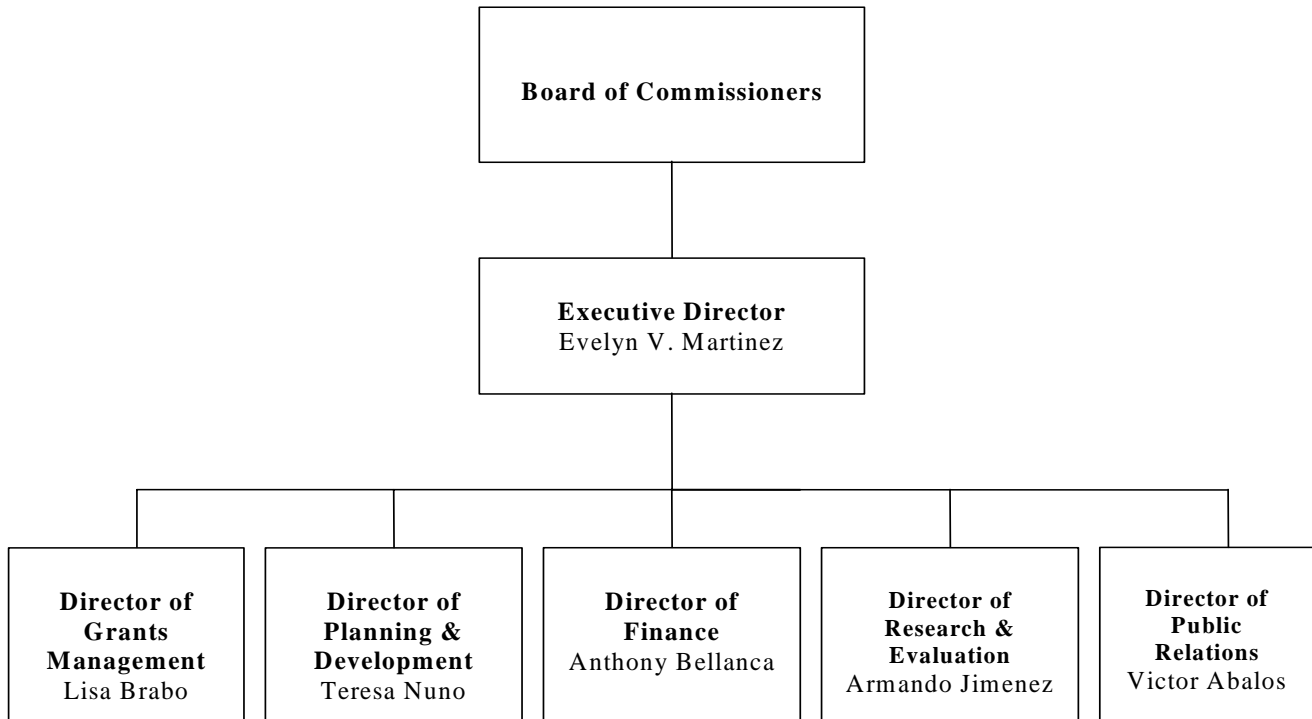
Ex-Officio Members (4)

Jacquelyn McCroskey Deanne Tilton	Matt Rezvani Harriette F. Williams
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Alternates (2)

Jonathan Fielding	John Hatakeyama
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**LOS ANGELES COUNTY
CHILDREN AND FAMILIES FIRST – PROPOSITION 10 COMMISSION
ORGANIZATION CHART**





MACIAS GINI & COMPANY_{LLP}

515 S. Figueroa Street, Ste. 325
Los Angeles, California 90071

213.612.0200 PHONE
213.286.6426 FAX

Board of Commissioners
Los Angeles County Children and Families
First – Proposition 10 Commission
Los Angeles, California

INDEPENDENT AUDITOR'S REPORT

We have audited the accompanying financial statements of the governmental activities and general fund of the Los Angeles County Children and Families First – Proposition 10 Commission (Commission), a component unit of the County of Los Angeles, California, as of and for the year ended June 30, 2005, which collectively comprise the Commission's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Commission's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Commission's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes 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, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and general fund of the Commission as of June 30, 2005 and the respective changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 2 to the basic financial statements, the Commission elected to classify its activities as a governmental fund from an enterprise fund in the prior year. In addition, as discussed in Note 3, effective July 1, 2004, the County adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 40. – *Deposits and Investment Risk Disclosures – an amendment of GASB Statement No. 3.*

In accordance with *Government Auditing Standards*, we have also issued our report dated August 30, 2005, on our consideration of the Commission's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The Management's Discussion and Analysis on pages 8 to 12 is not a required part of the basic financial statements, but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Commission's basic financial statements. The introductory section, supplemental schedule and statistical section are presented for purposes of additional analysis and are not a required part of the basic financial statements. The Schedule of Revenues, Expenditures and Changes in Fund Balance – Budget and Actual, has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory and statistical sections have not been subjected to the auditing procedures applied in the audit for the basic financial statements and, accordingly, we express no opinion on them.

Maurer Jini & Company LLP

Certified Public Accountants

Los Angeles, California
August 30, 2005

Management's Discussion and Analysis (Unaudited)

This section of the Los Angeles County Children and Families First – Proposition 10 Commission, (aka First 5 LA) annual financial report presents management's discussion and analysis of the Commission's financial performance during the year ended June 30, 2005. Please read in conjunction with the Commission's basic financial statements and accompanying notes.

Financial Highlights

- The Commission received \$151,565,586 from the State compared to \$143,452,634 received in the prior fiscal year, an increase of \$8,112,952, or 6%.
- The Commission had expenses totaling \$99,771,382 in FY 2004-05, which is an increase of \$14,207,386, or 17% compared to \$85,563,996 million in FY 2003-04.
- The Commission's assets increased from \$714,881,627 in FY 2003-04 to \$776,801,380 in FY 2004-05 by \$61,919,753 or 9%.
- The Commission's liabilities decreased from \$18,041,115 in FY 2003-04 to \$15,007,549 in FY 2004-05 by \$3,033,566 or 17%.

Overview of the Financial Statements

This annual financial report consists of two parts, this management's discussion and analysis and the basic financial statements, including government-wide financial statements, fund financial statements and notes to the basic financial statements. The Commission's financial statements offer key, high-level financial information about its activities.

Government-Wide Financial Statements

The government-wide financial statements are designed to provide readers with a broad overview of the Commission's finances, in a manner similar to a private-sector business. These statements provide both long-term and short-term information about the Commission's overall financial status.

The statement of net assets includes information on all of the Commission's assets and liabilities with the difference between assets and liabilities reported as net assets. Changes in net assets may serve as a useful indicator of whether the financial position of the Commission is improving or deteriorating.

The statement of activities presents information showing how the Commission's net assets changed during the fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows.

Fund Financial Statements

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. Fund accounting is used to ensure and demonstrate compliance with finance-related legal requirements. All of the Commission's activities are accounted for in the general fund.

Governmental fund financial statements focus on near-term inflows and outflows of spendable resources and on balances of spendable resources available at the end of the year.

While a nine-member Board of Commissioners governs the Commission, the Commission was created by and ultimately is under the authority of the Los Angeles County Board of Supervisors, in accordance with California State Law, through its appointment of the Board of Commissioners and its ability to remove the commissioners at will. Consequently, the County of Los Angeles Auditor-Controller's Office has designated the Commission as a "discretely presented component unit" of the County of Los Angeles and includes a summary of the Commission's basic financial statements in the County's basic financial statements.

Government-wide Financial Statements Analysis

The following is a summary of the Commission's assets, liabilities and net assets comparing FY 2004-05 with FY 2003-04.

	FY 2004-05	FY 2003-04	Percent Increase (Decrease)
Assets:			
Current and other assets	\$ 763,434,218	\$ 706,300,365	8%
Capital assets	13,367,162	8,581,262	56%
Total assets	<u>776,801,380</u>	<u>714,881,627</u>	9%
Liabilities:			
Long-term liabilities	199,791	8,691,112	(98%)
Other liabilities	14,807,758	9,350,003	58%
Total liabilities	<u>15,007,549</u>	<u>18,041,115</u>	(17%)
Net Assets:			
Restricted	748,426,669	696,757,952	7%
Invested in capital assets	13,367,162	82,560	161%
Total net assets	<u>761,793,831</u>	<u>696,840,512</u>	9%
Total liabilities and net assets	<u>\$ 776,801,380</u>	<u>\$ 714,881,627</u>	9%

The Commission's total assets of approximately \$776.8 million increased by \$61.9 million, or 9% compared with the prior year. The change in current and other assets of approximately \$ 57 million or 8% is primarily due to revenues exceeding expenditures. First 5 LA's received additional allocations due to the distribution of one-time monies made by the State from a bankruptcy settlement, accumulated interest earnings in the State fund used for tax allocation and revenue adjustments made by the State. Also, interest earned is a contributing factor primarily due to additional cash invested and the significant increase in interest rate yield. Another contributing factor is grantees under expended projected expenditures.

The increase in capital assets of \$4.8 million, or 56% increase, is due to the Commission exercising the purchase option under the capital lease for the acquisition of the building which houses the Commission's operations.

The decrease in long-term liabilities of \$8.4 million is due to the pay off of the Commission's capital lease obligation for the acquisition of the new building. Other liabilities increased by 58% due to greater

payables to grantees which correlates with new grantees in the current fiscal year and the full-year implementation for the SRI programs for existing grantees.

The increase in the invested in capital assets (net assets) of \$13.2 million is due to the acquisition of the building and elimination of the corresponding debt.

The following is a summary of the Commission's revenue, expenses and change in net assets comparing FY 2004-05 with 2003-04.

	FY 2004-05	FY 2003-04	Percent Increase (Decrease)
Revenues:			
Program revenues			
Tobacco taxes	\$ 138,542,842	\$ 134,067,268	3%
State School Readiness	11,820,145	9,385,366	26%
State School Matching Funds	1,202,599	-	100%
Total program revenues	<u>151,565,586</u>	<u>143,452,634</u>	6%
General revenues			
Investment income	13,158,681	8,520,520	54%
Other income	434	-	100%
Total general revenues	<u>13,159,115</u>	<u>8,520,520</u>	54%
Total revenues	<u>164,724,701</u>	<u>151,973,154</u>	8%
Expenses:			
Provider grants	92,727,156	79,133,367	17%
Salaries and benefits	5,250,528	4,809,497	9%
Operating services	933,586	951,337	(2%)
Consultant services	129,320	128,168	1%
Professional services	310,463	431,267	(28%)
Other expenses	275,395	66,353	315%
Depreciation	144,934	44,007	229%
Total expenses	<u>99,771,382</u>	<u>85,563,996</u>	17%
Change in net assets:	64,953,319	66,409,158	(2%)
Net assets – beginning	<u>696,840,512</u>	<u>630,431,354</u>	11%
Net assets – ending	<u>\$ 761,793,831</u>	<u>\$ 696,840,512</u>	9%

Revenues

The Commission received total revenues of approximately \$164.7 million in FY 2004-05, which was an increase of \$12.7 million, or 8% compared with the prior year's total revenues of \$151.9 million. The increase in First 5 LA revenues is primarily due to the following explanations:

Tobacco Tax Revenues

Tobacco tax revenue increased from \$134.0 million in FY 2003-04 to \$138.5 million in FY 2004-05, an increase of \$4.5 million, or 3%. This increase is primarily due to First 5 LA receiving additional State

allocation due to the distribution of one-time monies from a bankruptcy settlement, accumulated interest earnings in the state fund used for tax allocation and revenue adjustments made by the State.

Tobacco Taxes for State School Readiness Program

Tobacco tax revenue for State School Readiness program increased from \$9.3 million in FY 2003-04 to \$11.8 million in FY 2004-05, an increase of \$2.5 million, or 26%. The increase is due primarily to the implementation of all SRI cycles and all grantees completing a full year (12 months) of services.

State Commission Matching Grant

In November 2004, the Commission began participating in First 5 California’s Health Access for All Children Initiative. The majority of this project’s investment is designated to specifically and exclusively assist with the payment of insurance premiums for an expanded health insurance program regardless of immigration status, and for children who are ineligible for Medi-Cal and Healthy Families and who have a family income at or below 300% of the Federal Poverty Level (FPL). Under the agreement the State reimburses the Commission 20% of actual expenditures incurred through the enrollment of health insurance for children zero to five through the Healthy Kids initiative.

Investment Income

The Commission earned \$13.1 million of investment income in FY 2004-05, which was a 54% increase compared to the \$8.5 million earned in the prior year. This increase is due to the additional cash invested and a significantly higher yield on the interest rate.

Expenses

The Commission expended approximately \$99.8 million in FY2004-05 compared to \$85.5 million in FY 2003-04 resulting in an increase of \$14.3 million or 17%. The increase is primarily due to the following explanations:

Provider Grants

The Commission provided approximately \$92.7 million in FY 2004-05 compared to \$79.1 million in FY 2003-04, which is an increase of \$13.6 million or 17%. The increase is primarily due to the following new grantees ramping up to full implementation, where in FY 2003-04 many grantees were in their implementation stages.

Grantees	Allocation	FY 2003-04	FY 2004-05
LAUP	\$ 580,000,000	\$ -	\$ 9,920,353
CDI – Small (Group 4, 4b, 5)	2,700,000	-	1,900,000
Human Service Association	6,403,064	492,048	1,517,533

Salaries and Benefits

The Commission expended approximately \$5.3 million in FY 2004-05 compared to \$4.8 million in FY 2003-04 on salaries and benefits, which is an increase of \$441,031 or 9%. The increase is due primarily to merit increases, cost of living adjustments and the filling of several vacant positions.

Other Expenses

Other expenses increased from \$66,353 in FY 2003-04 to \$275,395 in FY 2004-05, which is an increase of approximately \$209,042. This is primarily due to the settlement of a claim.

Depreciation

Depreciation expense increased from \$44,007 in FY 2003-04 to \$144,934 in FY 2004-05, which is an increase of approximately \$100,000. This is due to the added depreciation of the building and additional equipment and furniture purchased in FY 2004-05.

Capital Assets

The \$4.8 million increase in capital outlay in FY 2004-05 is a result of the Commission exercising the purchase option under the capital lease for the acquisition of the building, which houses the Commission's operations and the purchase of equipment and furnishings for the new building. Additional information on capital assets can be found in Note 4 of this report.

Long-term Debt

The Commission paid off its capital lease obligation when it exercised its purchase option to acquire the building, which houses its operations. Additional information on long-term debt can be found in Note 5 of this report.

Other Potentially Significant Matters

The State projects a continuing decrease of State Tax Allocations revenue and decrease in the share allocated to First 5 LA due to a proportionally lower birth rate combining for a projected annual revenue decrease estimated at 6% a year through FY 2008-09.

Contacting the Commission's Financial Management

This financial report is designed to provide the public with an overview of the Commission's financial operations and condition. If you have questions about this report or need additional information, you can contact the Commission's Director of Finance at 750 N. Alameda Street, Los Angeles, California 90012.

LOS ANGELES COUNTY
CHILDREN AND FAMILIES FIRST - PROPOSITION 10 COMMISSION
STATEMENT OF NET ASSETS AND GOVERNMENTAL FUND BALANCE SHEET
JUNE 30, 2005

	<u>General Fund</u>	<u>Adjustments (Note 1)</u>	<u>Statement of Net Assets</u>
Assets			
Cash in banks	\$ 8,037,450	\$ -	\$ 8,037,450
Investments	718,882,417	-	718,882,417
State receivable	29,007,893	-	29,007,893
Investment income receivable	4,339,447	-	4,339,447
Grantee receivable	3,161,975		3,161,975
Capital assets:			
Not depreciated	-	2,039,000	2,039,000
Depreciable capital assets (net)	-	11,328,162	11,328,162
Other assets	5,036	-	5,036
Total assets	<u>\$ 763,434,218</u>	<u>\$ 13,367,162</u>	<u>\$ 776,801,380</u>
Liabilities			
Accounts payable and accrued liabilities	\$ 14,807,758	\$ -	\$ 14,807,758
Deferred revenue	4,995,862	(4,995,862)	-
Compensated absences			
Due within one year	-	41,956	41,956
Due in more than one year	-	157,835	157,835
Total liabilities	<u>19,803,620</u>	<u>(4,796,071)</u>	<u>15,007,549</u>
Fund balance/net assets			
Fund balance			
Reserved			
Reserved for obligations	714,865	(714,865)	-
Reserved for local initiative	699,098,261	(699,098,261)	-
Reserved for First 5 California initiatives	43,817,472	(43,817,472)	-
Total fund balance	<u>743,630,598</u>	<u>(743,630,598)</u>	<u>-</u>
Net assets			
Restricted net assets	-	748,426,669	748,426,669
Invested in capital assets	-	13,367,162	13,367,162
Total net assets	<u>-</u>	<u>761,793,831</u>	<u>761,793,831</u>
Total liabilities and fund balances/net assets	<u>\$ 763,434,218</u>	<u>\$ 13,367,162</u>	<u>\$ 776,801,380</u>

See accompanying notes to the basic financial statements.

LOS ANGELES COUNTY
CHILDREN AND FAMILIES FIRST - PROPOSITION 10 COMMISSION
STATEMENT OF ACTIVITIES AND GOVERNMENTAL FUND REVENUES,
EXPENDITURES AND CHANGES IN FUND BALANCE
FOR THE YEAR ENDED JUNE 30, 2005

	<u>General Fund</u>	<u>Adjustments (Note 1)</u>	<u>Statement of Activities</u>
Revenues			
Program revenues			
Tobacco taxes	\$ 138,542,842	\$ -	\$ 138,542,842
State School Readiness	7,551,557	4,268,588	11,820,145
State Commission Matching Grant	475,325	727,274	1,202,599
Total program revenues	<u>146,569,724</u>	<u>4,995,862</u>	<u>151,565,586</u>
General revenues			
Investment income	13,158,681	-	13,158,681
Other revenues	434	-	434
Total general revenues	<u>13,159,115</u>	<u>-</u>	<u>13,159,115</u>
Total revenues	<u>159,728,839</u>	<u>4,995,862</u>	<u>164,724,701</u>
Expenditures/expenses			
Provider grants	92,727,156	-	92,727,156
Salaries and benefits	5,243,147	7,381	5,250,528
Operating services	933,586	-	933,586
Consultant services	129,320	-	129,320
Professional services	310,463	-	310,463
Other expenses	275,395	-	275,395
Capital lease payments	8,498,702	(8,498,702)	-
Capital outlay	4,930,834	(4,930,834)	-
Depreciation	-	144,934	144,934
Total expenditures/expenses	<u>113,048,603</u>	<u>(13,277,221)</u>	<u>99,771,382</u>
Excess of revenues over expenditures	46,680,236	(46,680,236)	-
Change in net assets	-	64,953,319	64,953,319
Fund balance/net assets			
Beginning of year - restated	696,950,362	(109,850)	696,840,512
End of year	<u>\$ 743,630,598</u>	<u>\$ 18,163,233</u>	<u>\$ 761,793,831</u>

See accompanying notes to the basic financial statements.

**LOS ANGELES COUNTY
CHILDREN AND FAMILIES FIRST – PROPOSITION 10 COMMISSION
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2005**

NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

With passage of a ballot initiative in November 1998, California (the “State”) voters approved the establishment of the Los Angeles County Children and Families First – Proposition 10 Commission (the “Commission”), a component unit of Los Angeles County. A nine-member Board of Commissioners governs the Commission. The Commission was created by and ultimately is under the authority of the Los Angeles County Board of Supervisors, in accordance with California State Law, through its appointment of the Board of Commissioners and its ability to remove the commissioners at will. The Commission is a public entity legally separate and apart from the County. The initiative, Proposition 10, mandated an additional 50-cent-per-pack tax on cigarettes and a comparable increase in the tax of other tobacco products and required that the new funds be used on programs focused exclusively on early childhood development for children prenatal up to five years of age.

Following the directive of Proposition 10 to fund programs at the community level, each of the State’s 58 counties created a Proposition 10 Commission as well as a trust fund to receive Proposition 10 revenues. In Los Angeles County, the Board of Supervisors passed an ordinance in December 1998 to establish the Los Angeles County Children and Families First – Proposition 10 Commission, and in May 1999, the Commission held its first meeting, elected officers and established a number of ad hoc committees to address organizational and planning issues. The Commissioners and others who were involved in the effort regarded Proposition 10 as an extraordinary and unprecedented opportunity to begin making a difference in the lives of pregnant women, young children and their families, and to do so at a point in their lives when it can make the most difference. In August 2002, the Commission introduced a new branding identity, First 5 LA, to signify the importance of the first five years of life.

The Commission’s mission statement is “To optimize the development and well-being of all children, from the prenatal stage until their fifth birthday by increasing resources, ensuring access to services, and improving the abilities to families, communities and providers of services.” Among the five desired outcomes originally outlined in their strategic plan, the Commission identified School Readiness as its overarching goal and highest priority. School readiness incorporates many dimensions of child development and is integrally related to the Commission’s other long-term outcomes areas: Good Health, Safety and Survival, Economic Well-Being, and Social and Emotional Well-Being.

Upon termination of the Commission, all assets of the Commission shall be returned to the State of California. The liabilities of the Commission shall not become liabilities of the County upon either termination of the Commission or the liquidation or disposition of the Commission’s remaining assets.

**LOS ANGELES COUNTY
CHILDREN AND FAMILIES FIRST – PROPOSITION 10 COMMISSION
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2005**

**NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
(Continued)**

Basis of Accounting and Measurement Focus

Government-wide Financial Statements

Government-wide financial statements consist of the statement of net assets and the statement of activities. These statements are presented on an economic resources measurement focus. All economic resources and obligations of the reporting government are reported in the financial statements.

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. With this measurement focus, all assets and liabilities associated with operation of the Commission's fund are included on the statement of net assets. The statement of activities presents a comparison of the direct expenses and program revenues for the Commission's governmental activities. Program revenues include grants and contributions restricted for the operational requirements of a particular program. Grants and similar items are recognized as revenue as soon as all eligibility requirements have been met. Program revenues include tobacco taxes, state school readiness and state school matching funds. General revenues are all revenues that do not qualify as program revenues and include investment income and other income.

Fund Financial Statements

The fund financial statements consist of the balance sheet and the statement of revenues, expenditures and changes in fund balance of the Commission's general fund. These statements are presented on a current-financial resources measurement focus. Generally, only current assets and current liabilities are included on the balance sheet. The statement of revenues, expenditures and changes in fund balance for the governmental fund generally presents increases (revenues) and decreases (expenditures) in net current assets. All operations of the Commission are accounted for in the general fund.

The fund financial statements have been prepared on the modified accrual basis of accounting. Revenues are recognized in the accounting period in which they become both measurable and available to finance expenditures of the current period. Revenues are considered available if they are received within 60 days after year-end. Revenues susceptible to accrual include tax revenues and investment income. Expenditures are recognized in the accounting period in which the fund liability is incurred except for compensated absences which are recorded only when payment is due.

Adjustments Between Fund Financial Statements and Government-Wide Financial Statements

Capital Assets

Capital assets are not considered to be financial resources and therefore, are not reported as an asset in the fund financial statements. Capital assets in the amount of \$13,367,162 are capitalized and reported at cost, net of accumulated depreciation, in the government-wide financial statements. Capital assets purchased during the year in the amount of \$4,930,834 are expensed on the fund financial statements and capitalized on the government-wide financial statements. Depreciation expense for the year ended June 30, 2005 amounted to \$144,934 and is included in the government-wide financial statements.

**LOS ANGELES COUNTY
CHILDREN AND FAMILIES FIRST – PROPOSITION 10 COMMISSION
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2005**

**NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
(Continued)**

**Adjustments Between Fund Financial Statements and Government-Wide Financial Statements
(Continued)**

Deferred Revenue

Under the modified accrual basis of accounting, revenue is recognized in the fund financial statements if it has been collected after year-end within the Commission's established availability period of 60 days, the uncollected balance is deferred at year-end in the fund financial statements. Deferred revenue of \$4,995,862 was recognized as revenue in the government-wide financial statements at June 30, 2005.

Long-Term Liabilities

As of June 30, 2005 the Commission estimated its liability for vested compensated absences to be \$199,791. Compensated absence obligations are considered long-term in nature and are reported in the fund financial statements as expenditures in the period paid or when due and payable at year-end under the modified accrual basis of accounting. The compensated absences have been accrued in the government-wide financial statements and are included in long-term liabilities. The change in compensated absences during the year of \$7,381 is reported in the statement of activities and does not require the use of current financial resources.

During the fiscal year, the Commission exercised their purchase option to purchase their current office building. In fiscal year 2003 the building and capitalized lease was recorded in their financial statements. This purchase option reduced their long-term liabilities by \$8,498,702 on the government-wide financial statements and was recorded as an expenditure in the fund financial statements.

Fund Balance and Net Assets

The net assets of the Commission are invested in capital assets and constrained by state law for use for early childhood development and school readiness programs. As such, in accordance with GASB No. 34, the fund balance has been reclassified to restricted net assets and invested in capital assets on the statement of net assets.

Investments

The Commission participates in the common investment pool of Los Angeles County, which is recorded at fair value.

Capital Assets

Capital assets are composed of buildings, building improvements, computers, office equipment and furniture and fixtures and are recorded at cost. The Commission capitalizes assets with cost in excess of \$5,000 and a useful life greater than one year. The Commission depreciates capital assets using a straight-line method over the estimated useful life of fifty years for buildings, four years for computers and five years for office equipment and furniture and fixtures. Building improvements are depreciated over the remaining useful life of the building.

**LOS ANGELES COUNTY
CHILDREN AND FAMILIES FIRST – PROPOSITION 10 COMMISSION
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2005**

**NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
(Continued)**

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

NOTE 2 – BEGINNING FUND BALANCE AND NET ASSETS

Fund Balance

In prior years the Commission was treated as an enterprise fund. In the current year the Commission has elected to classify its activities as a governmental fund in accordance with GASB Statement No. 34 *Basic Financial Statements – and Management’s Discussion and Analysis for State and Local Governments* and consistent with the recommendation of the First 5 Management Guide adopted by the California First 5 Association of California and California Children’s and Families Commission. The effect of this classification resulted in a beginning fund balance at June 30, 2004 of \$696,950,362.

Net Assets

The Commission has elected to adjust revenue recorded in the current fiscal year that was earned in the prior fiscal year to the proper period. The affect of this adjustment was to increase the beginning net assets balance by \$12,220,228 and decrease revenue in the current fiscal year.

The following summarizes the adjustments to beginning net assets and fund balance at June 30, 2004:

As previously reported:	\$ 684,620,224
Add June revenue	<u>12,220,288</u>
Restated government-wide net assets at June 30, 2004	<u>696,840,512</u>
Less capital assets	(8,581,262)
Add compensated absences	192,410
Add capital lease	<u>8,498,702</u>
Restated fund balance at June 30, 2004	<u><u>\$ 696,950,362</u></u>

**LOS ANGELES COUNTY
CHILDREN AND FAMILIES FIRST – PROPOSITION 10 COMMISSION
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2005**

NOTE 2 – BEGINNING FUND BALANCE AND NET ASSETS (Continued)

In addition, plan assets of the deferred compensation plan were recorded as an asset and liability of the Commission. The Commission acts as an agent of these funds, however an insurance company was appointed as the fiduciary of the plan funds therefore these funds should not be recorded on the Commission's financial statements. An amount of \$654,835 has been removed as an asset and liability of the Commission in the prior year. The affect of this transaction has no affect on the beginning net assets balance.

NOTE 3 – CASH AND INVESTMENTS

In March 2003, GASB issued Statement No. 40 *Deposits and Investment Risk Disclosures - an Amendment of GASB Statement No. 3*. The deposits and investments of state and local governments are exposed to risks that have the potential to result in losses. This statement establishes and modifies disclosure requirements related to common deposit and investment risks: credit risk (including custodial credit risk and concentration of credit risk), interest rate risk, and foreign currency risk. As an element of interest rate risk, this statement requires certain disclosures of investments that have fair values that are highly sensitive to changes in interest rates. Deposits and investment policies related to the risk identified in this statement are also disclosed. The Commission implemented this new reporting requirement for its fiscal year 2005 basic financial statements.

The *California Government Code* requires California banks and savings and loan associations to secure the Commission's deposits by pledging government securities as collateral. The market value of pledged securities must equal 110 percent of an agency's deposits. California law also allows financial institutions to secure an agency's deposits by pledging first trust deed mortgage notes having a value of 150 percent of an agency's total deposits and collateral is considered to be held in the name of the Commission. At June 30, 2005, cash held by the financial institutions of \$11,562,933 was entirely insured and collateralized as described above. The book balance at June 30, 2005 was \$8,037,450.

Investments with the Los Angeles County Treasurer at June 30, 2005 are stated at fair value. The fair value of pooled investments is determined annually and is based on current market prices. The fair value of each participant's position in the pool is the same as the value of the pool shares. The method used to determine the value of participants' equity withdrawn is based on the book value of the participants' percentage participation at the date of such withdrawals. The fair value adjustment at June 30, 2005 decreased the Commission's investment income by \$1,719,873. The weighted average maturity of the County's Pool is approximately 132 days as of June 30, 2005. The Los Angeles County Treasury is sponsored and administered by the County of Los Angeles and oversight is conducted by the County Treasury Oversight Committee.

**LOS ANGELES COUNTY
CHILDREN AND FAMILIES FIRST – PROPOSITION 10 COMMISSION
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2005**

NOTE 4 – CAPITAL ASSETS

The capital asset balance at June 30, 2005 consists of the following activity:

	Balance June 30, 2004	Increases	Decreases	Balance June 30, 2005
Capital assets not depreciated:				
Land	\$ -	\$ 2,039,000	\$ -	\$ 2,039,000
Capital assets depreciable:				
Building	8,498,702	115,679	-	8,614,381
Building improvements	-	1,817,725	-	1,817,725
Computer equipment	206,716	418,616	-	625,332
Office equipment	-	145,811	-	145,811
Furniture and fixtures	-	394,003	-	394,003
Total depreciable capital assets	8,705,418	2,891,834	-	13,363,252
Less accumulated depreciation	124,156	144,934	-	269,090
Total capital assets, depreciable (net)	8,581,262	2,746,900	-	11,328,162
Capital assets – net	\$ 8,581,262	\$ 4,785,900	\$ -	\$ 13,367,162

In March 2005, the Commission exercised their purchase option to purchase the building that houses the Commission's operations. This agreement was entered in to in May 2003. As part of the agreement, \$587,055 is to be used for tenant improvements to the second floor in the future.

NOTE 5 – CHANGES IN LONG-TERM LIABILITIES

Long-term liability activities for the year ended June 30, 2005 were as follows:

	Balance July 1, 2004	Increases	Decreases	Balance June 30, 2005	Due Within One Year
Compensated absences (net)	\$ 192,410	\$ 7,381	\$ -	\$ 199,791	\$ 41,956
Capital leases	8,498,702	-	8,498,702	-	-
Total	\$ 8,691,112	\$ 7,381	\$ 8,498,702	\$ 199,991	\$ 41,956

**LOS ANGELES COUNTY
CHILDREN AND FAMILIES FIRST – PROPOSITION 10 COMMISSION
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2005**

NOTE 6 – FUND BALANCE

Fund balance represents the value of funds available to the Commission. Fund balance is composed of two categories, reserved and unreserved. Fund balance at June 30, 2005 are reserved for the following purposes:

Reserved for obligations:	
Tenant improvements	\$ 714,865
Reserved for local initiatives:	
Los Angeles Universal Pre-school	566,836,153
Healthy Kids	82,505,898
Community Development initiatives	46,997,028
Other initiatives	2,759,182
Reserved for First 5 California initiatives	43,817,472
Total reserved fund balance	<u>\$ 743,630,598</u>

NOTE 7 – DEFERRED COMPENSATION PLAN

The Commission offers to all employees' participation in a deferred compensation plan (Plan) adopted under the provision of section 457 of the Internal Revenue Code. The Commission contributes to the plan for an employee that has been in the Plan for one year. This contribution is equal to 100% of the employees' contribution, not to exceed 6% of the employee's annual compensation. Funds are placed in a Trust Fund and are managed by an insurance company who is the fiduciary of the Plan. These assets are not included in the Commission's financial statements. At June 30, 2005, the balance in the trust fund is \$1,708,642. The Commission contributed \$210,749 in fiscal year ended June 30, 2005.

NOTE 8 – RISK MANAGEMENT

The Commission is exposed to various risks of loss related to general liability, property liability, health benefits, workers' compensation and auto. These risks are addressed through commercial insurance policies.

No claims or suits are pending against the Commission arising out of proposed claim settlements covered by insurance. No settlements exceeded insurance coverage during the last three years.

**LOS ANGELES COUNTY
CHILDREN AND FAMILIES FIRST – PROPOSITION 10 COMMISSION
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2005**

NOTE 9 – COMMITMENTS AND CONTINGENCIES

Operating Lease

The Commission leases equipment from a third party under a lease, which expires in November 2008. The future minimum rental payments due under the lease are as follows:

Fiscal Year Ending June 30	
2006	\$ 27,155
2007	27,155
2008	27,155
2009	<u>11,315</u>
Total	<u>\$ 92,780</u>

Future Funding

The Commission has entered into future funding commitments with various entities, which are contingent on State funding.

NOTE 10 – STATE SCHOOL READINESS PROGRAM

The Commission participates in the State School Readiness Program and receives funds to be used to coordinate, develop, implement and sustain a system of collaborative school-based or linked services, programs and informal supports based on research or promising practices to improve “school readiness” for children, families, communities and schools. A local match of the program funds expended each year is required and can be met through a cash match, including Commission funds, new expenditures by school districts and local public agencies in excess of existing local investments that are specifically targeted to an element of the School Readiness Program, or funds from private sources such as foundations and businesses.

The State’s policies and procedures for reporting program costs and requesting program funding have evolved since the program’s inception, and based on current State policies, the Commission is entitled to current year funding based on achieving the matching requirements. To be eligible for FY 2004-05 State School Readiness revenues, the Commission was required to expend a one to one match for the revenue received. In the current fiscal year, the Commission expended approximately \$29 million on State School Readiness Programs, allowing the Commission to be eligible to receive \$14.5 from the State. The Commission received \$7.5 million during the fiscal year and accrued \$4.3 million at year-end. The Commission received an excess of funds in the prior year of \$2.7 million that was applied in FYE 2004-05.

**LOS ANGELES COUNTY
CHILDREN AND FAMILIES FIRST – PROPOSITION 10 COMMISSION
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2005**

NOTE 11 - RELATED PARTY TRANSACTIONS

The Commission contracts with the County to provide banking and investment services totaling approximately \$251,000 during the year ended June 30, 2005.

NOTE 12 – SUBSEQUENT EVENT

On July 21, 2005, the Governing Board of the Commission authorized the specific investments of excess funds. On August 10, 2005 the Los Angeles County Treasurer's Office completed the purchase of \$650 million of securities specifically invested on behalf of the Commission. The securities are 'laddered' to mature quarterly over an 18-month period with \$100 million maturing each quarter except for the last quarter when \$150 million will mature.

**LOS ANGELES COUNTY
CHILDREN AND FAMILIES FIRST - PROPOSITION 10 COMMISSION
SCHEDULE OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCE - BUDGET AND ACTUAL
FOR THE YEAR ENDED JUNE 30, 2005**

	Original Budget	Final Budget	Actual	Variance Positive (Negative)
Revenues				
Tobacco taxes:				
Tobacco taxes	\$ 128,190,135	\$ 128,190,135	\$ 138,542,842	\$ 10,352,707
State School Readiness	15,000,000	15,000,000	7,551,557	(7,448,443)
State Commission Matching Grant	270,833	1,202,599	475,325	(727,274)
Investment income	9,499,388	9,499,388	13,158,681	3,659,293
Other revenues	-	-	434	434
Total revenues	152,960,356	153,892,122	159,728,839	5,836,717
Expenditures				
Provider grants	125,494,188	138,450,918	92,727,156	45,723,762
Salaries and benefits	6,792,072	6,792,067	5,243,147	1,548,920
Operating services	1,689,264	1,554,767	933,586	621,181
Consultant services	215,004	291,500	129,320	162,180
Professional services	380,604	515,100	310,463	204,637
Other expenses	158,832	158,831	275,395	(116,564)
Capital lease payments	-	-	8,498,702	(8,498,702)
Capital outlay	13,000,000	13,000,000	4,930,834	8,069,166
Total expenditures	147,729,964	160,763,183	113,048,603	47,714,580
Excess (deficiency) of revenues over (under) expenditures	\$ 5,230,392	\$ (6,871,061)	46,680,236	\$ (41,877,863)
Fund balance - Beginning of year			696,950,362	
Fund balance - End of year			\$ 743,630,598	



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Board of Commissioners
Los Angeles County Children and Families First -
Proposition 10 Commission
Los Angeles, California

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

We have audited the financial statements of the governmental activities and the general fund of the Los Angeles County Children and Families First – Proposition 10 Commission (Commission), a component unit of the County of Los Angeles, California, as of and for the year ended June 30, 2005, which collectively comprise the Commission's basic financial statements and have issued our report thereon dated August 30, 2005, which includes an explanatory paragraph to describe the classification of its activities as a governmental fund from an enterprise fund in the prior year and the adoption of Governmental Accounting Standards Board (GASB) Statement No. 40, *Deposit and Investment Risk Disclosure – an amendment of GASB Statement No. 3*. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Commission's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over financial reporting that we have reported to management of the Commission in a separate letter dated August 30, 2005.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Commission's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the Board of Commissioners, Commission management, and the California Children and Families Commission, and is not intended to be and should not be used by anyone other than these specified parties.

Maurer Jini & Company LLP

Certified Public Accountants

Los Angeles, California
August 30, 2005

**LOS ANGELES COUNTY
CHILDREN AND FAMILIES FIRST – PROPOSITION 10 COMMISSION
FINANCIAL TRENDS
INCEPTION TO FISCAL YEAR ENDED JUNE 30, 2005**

	December 21, 1998 to June 30, 2000	2001	2002	2003	2004	2005
Revenues	\$ 260,132,326	\$ 171,326,517	\$ 164,150,747	\$ 146,134,153	\$ 151,973,154	\$ 164,724,701
Expenses	688,708	15,175,349	32,155,717	63,815,499	85,563,996	99,771,382
Change in net assets	259,443,618	156,151,168	131,995,030	82,318,654	66,409,158	64,953,319
Net assets - beginning	-	259,443,618	416,117,671	548,112,701	630,431,354	696,840,512
Net assets - ending	\$ 259,443,618	\$ 415,594,786	\$ 548,112,701	\$ 630,431,355	\$ 696,840,512	\$ 761,793,831

Source: Audit Reports, fiscal years ended 2000 and 2001 presented at fund level.

Fiscal years ended 2002 – 2005 presented at government-wide level, fiscal year 2002 beginning net asset balance adjusted due to GASB 34 presentation.

**LOS ANGELES COUNTY
CHILDREN AND FAMILIES FIRST – PROPOSITION 10 COMMISSION
REVENUE CAPACITY**

TAX REVENUE PROJECTIONS FOR FYE 2006 - 2009

Tax Revenue Projection		Births		Birthrate	
FY	Dollar Amount	Year	Number	Year	Number
2005/06	\$116,893,376	2003	152,192	2003	28.141%

Tax Revenue Projection		Projected Births		Projected Birthrates	
FY	Dollar Amount	Year	Number	Year	Number
2006/07	\$111,606,529	2004	152,418	2004	27.852%
2007/08	\$106,361,189	2005	152,299	2005	27.564%
2008/09	\$101,194,446	2006	152,165	2006	27.276%

- (1) Revenues are allocated based on proportional birthrates throughout the State of California.
- (2) Revenue projections are net of Prop 99 backfill and estimated State Board of Equalization administrative costs. Projected revenue has not yet been amended for effects of Chapter 881, Statutes of 2002 (new stamp) and Chapter 890, Statutes of 2003 (Cigarette and Tobacco Products Licensing Act of 2003).
- (3) Source of birthrates: Historical births – California Department of Health Services, Center for Health Statistics. Projected births – Demographic Unit, State Department of Finance.