THE PRESIDIO TRUST

Financial Statements

YEAR ENDED SEPTEMBER 30, 1999, WITH REPORT OF INDEPENDENT AUDITORS

Financial Statements

FOR YEAR ENDED SEPTEMBER 30, 1999

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Management's Discussion and Analysis

OVERVIEW

The Presidio Trust (the Trust) is the federal entity created by Congress to be the guardian of the natural, scenic, recreational and cultural resources of the Presidio of San Francisco in partnership with the National Park Service (NPS). The Trust is managing the Presidio's transformation from a post of the U.S. Army to a first-of-its-kind sustainable national park serving both a vibrant internal community and millions of visitors.

The Trust is rehabilitating the historic structures that distinguish the Presidio as a National Historic Landmark District and enhancing the extraordinary natural environment that led Congress to include the Presidio in the Golden Gate National Recreation Area in 1972. As mandated by law, the Trust is on a path to achieve financial self-sufficiency by Fiscal Year 2013.

The Trust is directed by the Presidio Trust Act to operate in accordance with the general objectives of the 1994 General Management Plan Amendment for the Presidio and the Government Corporation Control Act. As an independent federal entity, the Trust has a direct relationship with the Office of Management and Budget and is required to submit annual reports to Congress.

In July 1998, the Trust submitted to Congress its *Financial Management Program* (the Program). The Program outlines how the Trust will reduce its reliance on appropriated funds and achieve financial self-sufficiency. The Program calls for declining appropriations levels each successive year and no appropriations in Fiscal Year 2013 and beyond.

Presidio operations are currently financed through a direct appropriation, initiated in Fiscal Year 1999, which will decrease over the next 13 years, borrowings from the U.S. Treasury for the renovation of properties, reimbursable agreements with other government agencies, and rental leases for both residential and non-residential property. Additionally, the Presidio Trust manages service-related entities, including water treatment, electrical distribution and telecommunications for the Presidio.

MISSION, ORGANIZATIONAL STRUCTURE AND GOALS

Mission

The mission of the Trust is to preserve and enhance the Presidio as a National Park and National Historic Landmark District in an urban area. In order to assure its continued preservation as a National Park, Congress has mandated that the Trust achieve financial self-sufficiency by Fiscal Year 2013.

To achieve its mission, the Trust is creating at the Presidio a model of sustainability – an innovative approach to park management that ensures consideration of long-term environmental, community and economic effects in all Trust decision-making.

In a step unusual for a government agency, the Trust developed in 1998 a 30-year financial model for the Presidio that provides a blueprint for achieving financial self-sufficiency by Fiscal Year 2013. The model formed the basis for the Trust's *Financial Management Program* (the Program), which was presented to Congress on July 8, 1998. The Program provides for an annual decline in direct appropriations from Congress resulting in zero appropriations in Fiscal Year 2013 and details the level of capital investment needed prior to that break-even year in order to achieve sufficient annual cash flow to operate and maintain the park indefinitely.

At the end of Fiscal Year 1999, the Trust began a strategic planning process designed to produce one-, two- and five-year plans during Fiscal Year 2000. These plans will be used to develop annual budgets and evaluate performance. In addition, the Trust's financial model is currently being updated to reflect changes in the market and actual conditions in the park. Through ongoing strategic planning and financial modeling, the Trust will be able to effectively measure its performance in meeting the goals and objectives necessary to achieve its mission of park preservation and enhancement.

Organizational Structure

The Presidio Trust was established as a wholly owned government corporation of the Federal government. Authority is vested in a 7-member Board of Directors. The President of the United States appoints six members of the Board. The Secretary of the Interior or his designee also serves on the Board. The Trust's 360-member staff is directed by an Executive Director and is organized into five divisions, each managed by a Deputy Director or the General Counsel who reports to the Executive Director.

In establishing the Presidio Trust as a wholly-owned government corporation, Congress created an organization that could operate in the marketplace, make real-time decisions and reinvest revenues into the park in order to generate sufficient cash flow to eventually operate the park without federal appropriations.

The Trust Act provided significant operational latitude in staffing, contracting, leasing and the retention of revenues. The Trust manages park operations and leasing functions through a combination of direct staffing and contracting. By Fiscal Year 2013, the Trust projects operational savings of at least 20%. Significant savings have already been achieved in maintenance operations.

Goals

Achieving Financial Self-Sufficiency

On July 8, 1998, the Presidio Trust submitted its *Financial Management Program* (the Program) to Congress, as required by Public Law 104-333. The Program provides a schedule of annually decreasing appropriations necessary to achieve financial self-sufficiency by Fiscal Year 2013. The level of investment delineated in this schedule is critical to achieving a continuous break-even status after Fiscal Year 2013. To ensure that the Trust would achieve and maintain financial self-sufficiency, a 30-year financial model was developed. The model indicates, given sufficient investment in early years, the Trust will achieve financial self-sufficiency in Fiscal Year 2013 and will require no subsequent appropriations. The Trust charts its progress against this financial model and is pleased to report that, to date, the financial targets set in the Program are being met.

Government appropriations for the Trust have already begun to decline as the Trust's leasing program takes hold. The Trust has requested $23.4 million for operations in Fiscal Year 2001, a decrease of 4% from $24.4 million in Fiscal Year 2000.

In Fiscal Year 1999, the Trust:

- achieved nearly $14 million in revenue through its residential and non-residential leasing activities and utilities income;
- saved $5.2 million over estimated costs through the efficient execution of infrastructure upgrades;
- attracted $6.6 million in private capital for the rehabilitation of the Sixth Army Headquarters building on the Main Post.

Establishing a Sustained Revenue Stream:
The Presidio contains nearly 500 historic structures. These buildings, and several hundred non-historic buildings, are the keys to providing revenue that will enable the Presidio Trust to become financially self-sustaining.

Since assuming administrative jurisdiction over Trust lands and facilities, the Presidio Trust has moved aggressively on a program of rehabilitation and leasing of residential and non-residential buildings.

In Fiscal Year 1999, the Trust signed a lease agreement for the former Sixth Army Headquarters with the San Francisco Film Centre, which has invested over $6 million into rehabilitation of the historic Headquarters building. By the end of Fiscal Year 1999, the Trust had 717,000 square feet of non-residential building space under lease.

The Trust has also entered into exclusive negotiations with Lucasfilm, Ltd. to redevelop 900,000 square feet at the Letterman Complex. Final negotiations will commence upon completion of the environmental process in the spring of 2000. During Fiscal Year 2001, the obsolete hospital and research complex will be deconstructed. Construction of a new complex at the site that is more compatible with the Presidio's historic character will also begin in Fiscal Year 2001. The project will be privately funded, and it is estimated that it will ultimately provide 14% of the Trust's annual revenue requirement.

The Trust is moving expeditiously to make housing units ready for occupancy. Thus far, the Trust has brought an additional 463 housing units into service with funding provided primarily through Treasury borrowing. By the end of Fiscal Year 1999, 740 of the Presidio's 1,116 total housing units were occupied. As a result, revenue from housing is projected to more than double in Fiscal Year 2000 to $11.6 million. In Fiscal Year 2001, housing revenues are projected to rise to $14 million.

Demand for Presidio housing is very strong; 97% of available housing is leased and there is currently a waiting list for housing units. The Trust's residential leasing program is constrained only by the extent to which housing units can be rehabilitated and made ready for lease. Treasury borrowing, authorized for Fiscal Year 2000, will make it possible to bring an additional 102 historic housing units and associated infrastructure on-line this year.

Capital Investment in the Presidio:
Capital investment in residential and non-residential buildings and related infrastructure is critical to establishing adequate inflows of revenue. This investment is particularly important in the Trust's early years. Although the Trust is implementing a variety of leasing strategies to attract private funds for building rehabilitation, there is a critical need for capital investment by

the Trust to prepare facilities for lease and upgrade infrastructure. Recognizing this need, Congress provided authorization in Public Law 104-333 for the Trust to borrow up to $50 million at any given time from the Treasury, subject to appropriation acts.

The Trust's 1998 *Financial Management Program* and supporting documentation identifies investments over a fifteen-year period funded through a mixture of tenant-funded renovation and new development and Trust-funded rehabilitation of buildings and infrastructure. In Fiscal Year 2000, the Trust will spend $25.4 million on capital projects.

Environmental Remediation
In Fiscal Year 1999, the Trust signed a first-of-its-kind environmental remediation agreement that will expedite environmental cleanup at the Presidio by nearly two decades. The agreement, signed in May 1999 with the Department of Defense (Army) and Department of the Interior, transfers lead agency status for the Presidio's cleanup from the Army to the Trust. Environmental remediation will be managed by the Trust and will be funded with Army funds transferred to the Trust from the Army. To date the Trust has received $50 million ($25 million in Fiscal Year 1999) of the total $100 million cleanup cost (two of the four annual installments). The Trust projects environmental remediation spending to be $13 million in Fiscal Year 2001.

As part of the agreement, the Trust also purchased an environmental insurance policy to cover cost overruns of up to an additional $100 million. The Army retains responsibility for all unknown contaminants and has also agreed to step back into the process if costs exceed by $10 million the $100 million received from the Army plus insurance proceeds.

The Trust considers this landmark agreement to be essential to its efforts to achieve financial self-sufficiency. Only by controlling the pace, quality and direction of the cleanup can the Trust be assured that remediation activities will coincide with leasing and reuse priorities. The Trust has received strong support for this effort from state and federal regulatory agencies, the Restoration Advisory Board, and the general public.

PERFORMANCE MEASURES

As part of its strategic planning, the Trust is in the process of developing measures of program and financial performance that are consistent with the Trust's strategic plans. These measures will be consistent with the Trust's *Financial Management Program*, and will reflect changes in policy and market conditions as they occur.

FINANCIAL RESOURCES AND RESULTS OF OPERATIONS

The accompanying financial statements summarize the Trust's financial position, show the net cost of operations and changes in net position, provide information on budgetary resources and financing, and present the sources of revenues and expenditures during Fiscal Year 1999. Highlights of the financial information are presented in the following financial statements.

Net Cost Of Operations

The net operating cost of $38.2 million is shown on the Statement of Net Cost. These costs were reduced by $23.1 million of earned revenues to arrive at Fiscal Year 1999 net cost of operations of $15.1 million.

Financial Position

The Trust's total assets were $73.3 million at the end of Fiscal Year 1999. Of this, $44.6 million consisted of investments in U.S. Treasury bills through the Bureau of Public Debt. There was also $52.0 million in liabilities, which included $20.0

million in debt to the U.S. Treasury and advances of $21.5 million from the Army for environmental remediation. The Trust's net position was $21.3 million at the end of Fiscal Year 1999.

Budgetary Resources

The Trust's budgetary resources were $83.0 million which consisted of $14.8 million in appropriations, $20.0 million in borrowing authority, $2.2 million in transferred funds and $46.0 million in collections. Obligations incurred against these resources were $45.0 million. Unobligated balances at the end of Fiscal Year 1999 were $37.9 million. This unobligated balance is due primarily to the advance from the Army of remediation funds and to Treasury borrowing that was restricted as to use.

Financing Sources Other Than Earned Revenues

Financing sources other than earned revenues funded the Trust's net cost of operations. The Trust reported $35.9 million of other financing sources on the Statement of Changes in Net Position. This consisted of $14.3 million in appropriations used, $19.4 million (net) in assets transferred from the NPS, and $2.2 million from other sources.

LIMITATIONS OF THE FINANCIAL STATEMENTS

The Trust has prepared its financial statements to report its financial position and results of operation. These financial statements have been prepared from the Trust's general ledger and subsidiary reports in accordance with the formats prescribed by the Office of Management and Budget. These statements are in addition to the financial reports used to monitor and control budgetary resources, which are prepared from the same books and records. These statements should be read with the realization that the Trust is a component of the U.S. government, a sovereign entity. One implication of this is that liabilities cannot be liquidated without authorizing legislation.

The accuracy of the information contained in the principal financial statement and the quality of internal control rests with management.

Report of Independent Auditors

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Report of Independent Auditors

To the Board of Directors of
The Presidio Trust

We have audited the accompanying balance sheet of the Presidio Trust (the Trust) as of September 30, 1999, the related statements of net cost, budgetary resources, financing, and changes in net position, for the year then ended. These financial statements are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements based on our audit.

Except as discussed in the following paragraph, we conducted our audit in accordance with generally accepted auditing standards, the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin 98-08, *Audit Requirements for Federal Financial Statements,* as amended. These standards and requirements 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.

On July 1, 1998, the Trust assumed jurisdiction over approximately 1,100 acres of federal land and over 800 buildings from the National Park Service. The United States Army previously administered the property. Many of the structures are greater than 40 years old and pursuant to Trust depreciation policies were fully depreciated at the point of transfer. SFFAS #6—*Accounting for Property, Plant and Equipment (PPE)*— requires PPE to be recognized when title passes to the entity. Additionally, SFFAS #6 requires that the cost of general PPE transferred from other federal entities be either the cost recorded by the transferring entity, net of accumulated depreciation; if such amounts can not be reasonably ascertained, the cost of the PPE is to be its fair value at the time transferred.

As discussed in Note 5, due to the lack of available information from the National Park Service and the United States Army, the Trust valued buildings less than 40 years old by using appropriate construction industry indices, less an accumulated depreciation adjustment to ascertain net asset value at the date of the Trust's formation. However, improvements made to buildings over 40 years old and land improvements have been valued at zero net book value but may still have a net cost value. Per SFFAS #6, the Trust should record these improvements at fair value. Estimating the values of these improvements would be a process that the Trust considers to be lengthy, cost prohibitive and which would result in information that is meaningless to the users of the Trust's financial statements. In addition, The Letterman Hospital facility, which was constructed within the last 40 years, is also reflected at a net book value of $0 due to limitations in valuing a hospital facility that is designated for demolition in year 2000. We were unable to satisfy ourselves as to the estimate of the carrying amount for these assets.

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In our opinion, except for the effects of adjustments to the financial statements, if any, that might have been determined to be necessary had we been able to examine evidence supporting the recorded balances of certain improvements within the property, plant and equipment accounts, the financial statements referred to above present fairly, in all material respects, the financial position of the Trust at September 30, 1999, and its net costs, changes in net position, budgetary resources, and reconciliation of net costs to budgetary obligations for the year then ended, in conformity with generally accepted accounting principles.

Our audit was conducted for the purpose of forming an opinion on the financial statements referred to in the first paragraph. The information presented in the Overview of the Trust and the Supplemental Information of the Trust is not a required part of the financial statements, but is supplementary information required by Office of Management and Budget Bulletin 97-01, *Form and Content of Agency Financial Statements*. Such information has not been subjected to the auditing procedures applied in the audit of the principal financial statements, and accordingly, we express no opinion on it.

In accordance with *Government Auditing Standards*, we have issued our reports dated January 28, 2000, on our consideration of the Trust's internal controls and on its compliance with applicable laws and regulations. These reports are an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Ernst & Young LLP

January 28, 2000

Fiscal Year 1999 Financial Statements

BALANCE SHEET

September 30, 1999

ASSETS		
Intragovernmental		
Trust fund investments [NOTE 2]	$	44,576,854
Accounts receivable, net [NOTE 3]		2,712,919
		47,289,773
Accounts receivable, net [NOTE 3]		890,107
Cash and other monetary assets [NOTE 4]		208,280
General property plant and equipment, net [NOTE 5]		24,873,847
Other assets		37,981
		26,010,215
TOTAL ASSETS		73,299,988
LIABILITIES AND NET POSITION		
Liabilities covered by budgetary resources		
Intragovernmental		
Fund balance due to treasury [NOTE 7]		890,880
Accounts payable		2,249,583
Advances for environmental cleanup costs [NOTE 8]		21,475,422
		24,615,885
Accounts payable		4,575,027
Security deposits [NOTE 10]		820,231
Accrued payroll & benefits		1,144,500
Total liabilities covered by budgetary resources		31,155,643
Liabilities Not Covered by Budgetary Resources		
Debt [NOTE 9]		20,000,000
Accrued leave		780,991
Other unfunded liabilities		50,944
		20,831,935
TOTAL LIABILITIES		51,987,578
NET POSITION		
Unexpended appropriations [NOTE 11]		522,246
Cumulative results of operations		20,790,164
TOTAL NET POSITION		21,312,410
TOTAL LIABILITIES & NET POSITION	$	73,299,988

The accompanying notes are an integral part of these financial statements.

STATEMENT OF NET COST
Year ended September 30, 1999

Program Costs **(NOTE 12)**	$	38,211,411
Less earned revenues		
Intragovernmental		11,420,035
With the public **(NOTES 12, 14)**		11,705,483
		23,125,518
NET COST OF OPERATIONS	$	15,085,893

STATEMENT OF CHANGES IN NET POSITION
Year ended September 30, 1999

Net cost of operations	$	15,085,893
Financing sources (other than exchange revenues)		
Appropriations used		14,280,754
Transfer in at inception – property		19,392,558
Transfer in at inception – cash **(NOTE 14)**		2,202,745
Total financing sources		35,876,057
Net results of operations		20,790,164
Net change in cumulative results of operations		20,790,164
Increase in unexpended appropriations		522,246
Change in net position		21,312,410
Net position, beginning of period		0
NET POSITION, END OF PERIOD	$	21,312,410

The accompanying notes are an integral part of these financial statements.

STATEMENT OF BUDGETARY RESOURCES

Year ended September 30, 1999

BUDGETARY RESOURCES		
Budget authority	$	34,803,000
Unobligated balances–beginning of period		0
Net transfers prior-year balance, actual		2,202,745
Spending authority from offsetting collections		45,981,360
TOTAL BUDGETARY RESOURCES		82,987,105
STATUS OF BUDGETARY RESOURCES		
Obligations incurred		45,069,289
Unobligated balances–available		37,917,816
TOTAL, STATUS OF BUDGETARY RESOURCES		82,987,105
OUTLAYS		
Obligations incurred		45,069,289
Less: spending authority from offsetting collections and adjustments		(45,981,360)
Less: obligated balance, net–end of period		(5,640,310)
TOTAL OUTLAYS	$	(6,552,381)

The accompanying notes are an integral part of these financial statements.

STATEMENT OF FINANCING

Year ended September 30, 1999

RESOURCES USED TO FINANCE ACTIVITIES	
Budgetary	
Budgetary resources obligated for orders, delivery of goods and services to be received, or benefits to be provided to others	$ 45,069,289
Less: offsetting collections, and recoveries of prior year authority	(45,981,360)
Net budgetary resources used to finance activities	(912,071)
Non-budgetary	
Property received from others without reimbursements	19,392,558
Funds received from others without reimbursement	2,202,745
Net non-budgetary resources used to finance activities	21,595,303
TOTAL RESOURCES USED TO FINANCE ACTIVITIES	20,683,232
RELATIONSHIP OF TOTAL RESOURCES TO THE NET COST OF OPERATIONS	
Increase in budgetary resources obligated to order goods and services not yet received or benefits not yet provided	2,211,998
Resources that do not affect net cost of operations	(22,295,653)
Resources that finance the acquisition of assets or liquidation of liabilities	26,327,946
TOTAL RESOURCES USED TO FUND ITEMS NOT PART OF THE NET COST OF OPERATIONS	6,244,291
TOTAL RESOURCES USED TO FINANCE THE NET COST OF OPERATIONS	14,438,941
COMPONENTS NOT REQUIRING OR GENERATING RESOURCES	
Expenses or exchange revenue related to the disposition of assets or liabilities, or allocation of their costs over time	
Expenses related to use of assets	1,326,251
Losses from re-evaluation of assets and liabilities	63,955
Increase in exchange revenue receivable from the public	(902,358)
Increase in restricted cash	(208,280)
Other	(464,551)
Expenses that will be financed with budgetary resources recognized in future periods	831,935
TOTAL COMPONENTS NOT REQUIRING OR GENERATING RESOURCES	646,952
NET COST OF OPERATIONS	$ 15,085,893

The accompanying notes are an integral part of these financial statements.

Notes to Financial Statements

September 30, 1999

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The Presidio Trust (the Trust), an executive agency, is a wholly-owned government corporation established by Congress in 1996 through enactment of the Presidio Trust Act (P.L. 104-333). The Trust's mission is to:

- preserve and enhance the Presidio as part of the national park system
- achieve financial self-sufficiency by Fiscal Year 2013.

From 1846 to 1994, the Presidio acted in the capacity of a U.S. military installation. In 1994, the National Park Service (NPS) assumed full control of the Presidio until 1998 when the Trust assumed responsibility for approximately 1,100 acres of non-coastal areas.

The Trust is guided by the Presidio Trust Act to operate in accordance with the general objectives of the 1994 General Management Plan Amendment for the Presidio and the Government Corporation Control Act. It currently finances operations through appropriations, which will decrease each year and end in Fiscal Year 2012, borrowings from the U.S. Treasury for the renovation of properties, reimbursable agreements with other government agencies, and rental leases for both residential and non-residential property. The Trust is overseen by a seven member board of directors including a designee from the Department of the Interior (DOI) and six individuals appointed by the President.

If the Trust fails to achieve self-sufficiency by Fiscal Year 2013, the net assets would be transferred to the General Services Administration for disposition.

Basis of Presentation

The financial statements have been prepared to report the financial position and results of operations of the Trust. The statements were prepared from the Trust's accounting records in accordance with generally accepted accounting principles (GAAP), and the form and content specified by the Office of Management and Budget (OMB) in OMB Bulletin 97-01. GAAP for federal entities is the standard proscribed by the Federal Accounting Standards Advisory Board (FASAB), designated by the American Institute of Certified Public Accountants (AICPA) as the official accounting standards setting body of the Federal government. Fiscal Year 1999 was the first year of operations for the Trust, and accordingly, these financial statements are the first ever prepared by the Trust.

Basis of Accounting

The Trust accounts for its assets, liabilities, net position, revenues, expenses, and other financing sources in accordance with the requirements of the U.S. Government Standard General Ledger (SGL). Use of sub-accounts allows transactions to be recorded at a more detailed level and provides relevant management information.

While the statements are on an accrual basis, transactions are recorded using both the accrual and cash basis of accounting, and a budgetary basis of accounting. Under the accrual method, expenses are recognized when resources are consumed, without regard to the payment of cash. Under the cash method and the budgetary method, expenses are recognized when cash is outlayed. Budgetary accounting facilitates compliance with legal constraints and controls over the use of Federal funds.

Balance Sheet

The balance sheet presents amounts of future economic benefits owned or managed by the Trust (assets), amounts owed (liabilities), and amounts which comprise the difference (net position). The major components are described below.

ASSETS include assets that the Trust holds and has the authority to use in its operations.

LIABILITIES represent amounts owed by the Trust as the result of transactions that have occurred. Liabilities funded by available budgetary resources include: (1) new budget authority, (2) spending authority from offsetting collections, (3) recoveries of unexpired budget authority, (4) unobligated balances of budgetary resources at the beginning of the year, and (5) permanent indefinite appropriation or borrowing authority.

Liabilities not covered by budgetary resources are incurred when funding has not yet been made available through Congressional appropriations or current earnings. The Trust recognizes such liabilities for employee annual leave earned but not yet taken.

NET POSITION contains the following components:

Unexpended Appropriations include the portion of the Trust's appropriations represented by undelivered orders and unobligated balances.

Cumulative Results of Operations represent the net results of operations since the inception of the program.

Statement of Net Cost

The Statement of Net Cost shows the components of the net cost of the Trust's operations for the period.

Program/Activity Costs represent the gross costs or expenses incurred by the Trust for all activities.

Earned Revenues or exchange revenues arise when a Government entity provides goods and services to the public or to another Government entity for a fee.

Net Cost of Operations is the difference between the program's gross costs and its related exchange revenues.

Statement of Changes in Net Position

The Statement of Changes in Net Position shows the net cost of operations less financing sources other than exchange revenues, and the net position at the end of period. Major components are described below.

Financing Sources (Other than Exchange Revenues) arise primarily from exercise of the Government's power to demand payments from the public (e.g., taxes, duties, fines, and penalties). These include appropriations used, transfers of assets from other Government entities, donations, and imputed financing.

Appropriations Used for financial statement purposes are recognized as a financing source as expenses are incurred.

Statement of Budgetary Resources

The Statement of Budgetary Resources provides information about the availability of budgetary resources as well as their status at the end of the year. Major components are described below.

Budget Authority represents the funds available through appropriations, direct spending authority, obligation limitations, unobligated balances at the beginning of the period or transferred in during the period, spending authority from offsetting collections, and any adjustments to budgetary authority.

Obligations Incurred consists of expended authority, recoveries of prior year obligations and the change in undelivered orders.

Statement of Financing

The Statement of Financing is a reconciliation of the preceding statements. Accrual-based measures used in the Statement of Net Cost differ from the obligation-based measures used in the Statement of Budgetary Resources, especially in the treatment of liabilities. A liability not covered by budgetary resources may not be recorded as a funded liability in the budgetary accounts of the Trust's general ledger, which supports the Report on Budget Execution (SF-133) and the Statement of Budgetary Resources. Therefore, these liabilities are recorded as contingent liabilities on the general ledger. Based on appropriation language, they are considered "funded" liabilities for purposes of the Balance Sheet, Statement of Net Cost and Statement of Changes in Net Position.

Use of Estimates in Preparing Financial Statements

Preparation of financial statements in accordance with federal accounting standards requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from those estimates.

Revenue Recognition

Rental revenue is recognized using the straight-line method over the term of the lease. Any amounts deferred that are not payable until future years are included in deferred rent receivable. Deferred rent receivable totaled $37,981 in 1999 and is included in other assets.

Intra-Governmental Relationships and Transactions

In the course of its operations, the Trust has relationships and financial transactions with numerous Federal agencies.

Department of the Interior
An interagency agreement exists between the Trust and the DOI for the DOI to provide payroll services.

Department of the Treasury – Financial Management Service (FMS)
FMS maintains a treasury account for revenues collected. All banking activities are conducted in accordance with the directives issued by FMS.

Department of the Army
The Department of the Army (Army) is to provide to the Trust, each year through Fiscal Year 2002, funds for the development and implementation of environmental remediation in accordance with a memorandum of agreement between the parties (see Note 8 for additional discussion).

National Park Service
In accordance with a memorandum of agreement between the Trust and NPS, the Trust is to provide environmental remediation on NPS lands in the Presidio using funds received from the Army. The Trust receives police and fire protection services from NPS and reimburses NPS accordingly.

2. TRUST FUND INVESTMENTS

The Trust is required by P.L. 104-333 to invest all excess cash into governmental securities with the Bureau of Public Debt (BPD). Investments as of September 30, 1999, are scheduled below:

Intergovernmental securities	*Maturity Date*	*Interest Rate*	*Par Value*	*Unamortized Discount*	*Net*
Non-marketable/Market Based	10/01/99	5.25%	$8,450,000	0	$8,450,000
Non-marketable/Market Based	12/02/99	4.83%	7,088,000	(59,911)	7,028,089
Non-marketable/Market Based	12/31/99	4.80%	10,000,000	0	10,000,000
Non-marketable/Market Based	12/31/99	4.80%	10,000,000	0	10,000,000
Non-marketable/Market Based	06/22/00	4.74%	9,429,000	(330,235)	9,098,765
			$44,967,000	$(390,146)	$44,576,854

The two investments with December 31, 1999, maturity dates are investments of the proceeds from Trust borrowings from the Treasury (see Note 9). The BPD invests these proceeds until the Trust must access the cash. The amortized cost of these securities approximates market value. The Trust amortizes discounts on the straight-line method rather than the effective interest method; however, due to the short-term nature of the securities, the straight-line method approximates the effective interest method.

3. ACCOUNTS RECEIVABLE, NET

Accounts receivable as of September 30, 1999, is comprised of the following:

	Government	*Non-Government*	*Total*
Gross accounts receivable	$2,764,623	$902,358	$3,666,981
Less allowance for losses	(51,704)	(12,251)	(63,955)
Net accounts receivable	$2,712,919	$890,107	$3,603,026

Receivables consist of amounts owed from rental properties, security deposits, and service district charges. The Trust fully reserves all receivables over 90 days old.

4. CASH AND OTHER MONETARY ASSETS

The Presidio Trust does not maintain any bank accounts. The Residential Property Management Firm under contract with the Trust maintains four bank accounts at West America Bank for the purpose of depositing rental revenues and security deposits, and paying all related expenses of the property management company. Any excess revenues over $10,000 are transferred monthly to the Trust. The combined balance in these accounts as of September 30, 1999, was $208,280.

5. GENERAL PROPERTY, PLANT AND EQUIPMENT

Property, Plant and Equipment (PPE) includes fixed assets owned by the Trust as the result of purchases by the Trust and/or transfers from other governmental entities, primarily the NPS. In general, the Trust capitalizes fixed assets valued in excess of $25,000 and with a useful life of two or more years. These assets are depreciated over their useful lives in accordance with Trust guidelines.

Specific Trust capitalization and depreciation guidelines are as follows:

Classification	*Estimated Useful Life*	*Straight Line Depreciation*	*Cost*	*Accum. Depreciation*	*Net Balance at 9/30/99*
Land and Land Rights	N/A	$ 0	$ 0	$ 0	$ 0
Improvements to Land	N/A	0	0	0	0
Construction-in-Progress	N/A	0	774,128	0	774,128
Buildings, Improvements and Related Renovations and Rehabilitations prior to takeover by the Trust	40 years ①				
• Over 40 years old		714,094	28,563,790	13,093,652	15,470,138
• Under 40 years old	0	0	0	0	0
Buildings, Improvements and Related Renovations and Rehabilitations since takeover by the Trust	40 years ①	56,427	4,514,126	56,427	4,457,699
Other Property, Plant and Equipment (including furnishings and equipment)	②	683,578	8,216,756	4,044,874	4,171,882
		$1,454,099	$42,068,800	$17,194,953	$24,873,847

① Buildings, Improvements and Related Renovations and Rehabilitations useful life of 40 years or less for improvements and renovations depending on remaining building life.

② Other Property, Plant and Equipment estimated useful life based on capitalization and depreciation policy.

Additionally, the Trust capitalizes expenditures for improvements to infrastructure based upon the following criteria:

- costs exceed $25,000;
- are not considered to be repairs and maintenance;
- extend the useful life of the building for at least 20 years.

Furnishings and equipment purchased for a unit cost in excess of $25,000 are also capitalized. Construction-in-Progress may include not only direct costs, but also an assigned indirect cost component, including architectural fees and legal expenses.

Land is considered to be general PPE and, in accordance with SFFAS #6, is to be recorded at cost. The land comprising the Presidio was acquired as an outcome of the resolution of hostilities between the United States and the government of Mexico in the mid-19th century. As such, no cost can be affixed to the land and land rights.

Most of the Trust's PPE was transferred to the Trust from the NPS. After extensive investigation, the Trust determined that historical cost information for buildings, building improvements and land and infrastructure improvements was not available from the NPS and/or the Army. Therefore:

- any building over 40 years old, and the cost of related renovations or rehabilitations prior to the Trust's formation, is considered fully depreciated and is reflected at a book value of $0.

- any structure less than 40 years old (built in 1959 or later) is carried at estimated replacement cost reduced for the effects of inflation by using appropriate construction industry indices, less an accumulated depreciation adjustment, to ascertain net asset value at the date of the Trust's formation. The Letterman Hospital facility, which was constructed within the last 40 years and is designated for demolition in Fiscal Year 2001, is reflected at a net book value of $0 at the date of the Trust's formation due to the inherent limitations in the use of a replacement cost analysis for a hospital facility.

- other PPE transferred to the Trust from the NPS is capitalized at historical cost less depreciation that would have been taken over its useful life, based on the Trust's depreciation guidelines.

- land and infrastructure improvements are reflected at a net book value of $0.

The Trust determines depreciation and amortization using straight-line methodology. For financial statement purposes, a pro-rated share of depreciation expense for the asset is recorded in the year of acquisition or project completion depending on the month of acquisition.

6. DIRECT LOANS AND LOAN GUARANTEE, NON-FEDERAL BORROWERS

The Trust has authority to operate the following direct loan and/or loan guarantee programs:

- The Trust is empowered to provide direct loans to non-Federal borrowers. As of September 30, 1999, the Trust had not exercised this authority.

- The Trust is empowered to guarantee loans of non-Federal borrowers for construction and renovation. As of September 30, 1999, the Trust had not exercised this authority.

7. FUND BALANCE WITH TREASURY

The Trust's Fund Balance with Treasury was a negative amount as the result of the Trust's over-investment in overnight securities with the BPD on September 30, 1999.

8. ADVANCES FOR ENVIRONMENTAL CLEANUP COSTS

The Army closed its base at the Presidio and, in September 1994, transferred administrative jurisdiction of the Presidio to the NPS through the DOI for incorporation into the Golden Gate National Recreation Area.

Executive Order 12580 delegated the responsibility to conduct the environmental cleanup of the Presidio to the Army. Under an interagency agreement with the DOI, the Army retained this responsibility as one of the terms of the jurisdictional transfer and initiated certain actions to address environmental conditions at the Presidio.

When Congress created the Trust in 1996, it separated the administrative jurisdiction of the Presidio into two areas: Area A, over which DOI retained authority, and Area B, which was transferred to the Trust in July 1998.

Under a Memorandum of Agreement (the Presidio MOA) among the Trust, DOI and the Army, the Trust assumed the Army's responsibilities as lead agency for the environmental cleanup in both Area A and Area B. The Army agreed to provide $100 million to the Trust in equal installments of $25 million over a four-year period commencing during Fiscal Year 1999 in exchange for the Trust's assumption of such responsibilities.[1] As of September 30, 1999, the Trust had received $25 million from the Army under the Presidio MOA. An additional $25 million was received by December 1999. These funds are recorded as Advances for Environmental Cleanup Costs on the Trust's financial statements.

Under a separate memorandum of agreement between the Trust and DOI (the Area A MOA), the Trust confirmed its agreement to take over lead agency responsibility for the cleanup of Area A of the Presidio. The Area A MOA also set out specific time periods, priorities and processes for remedy selection for environmental cleanup of Area A. Cleanup includes enumerated sites where a potential environmental threat (Substance and Condition) is presently known or may exist based on past Army studies or records. Cleanup also includes unknown contamination which is any environmental threat at or from the Presidio other than an enumerated site that existed at the Presidio before October 1, 1994 (Presidio base closure) or was the result of an Army act or omission on or after October 1, 1994.

The Trust assumed the Army's responsibility as the lead cleanup agency, and performs all cleanup work at enumerated sites using the Army's funds, and is the point of contact for all regulatory agencies and for the public. The Army retained responsibility to fund and to perform all environmental cleanup work of unknown contamination as well as sole responsibility for the clean up of radioactive materials, chemical and biological warfare agents, and unexploded ordnance if discovered at the Presidio.

The Trust must use the funds transferred from the Army to address environmental cleanup of enumerated sites. If any funds are left after cleanup of the enumerated sites, the Trust can use the excess to address other environmental conditions at or emanating from the Presidio. If cleanup costs for the enumerated sites exceed the $100 million from the Army plus insurance proceeds (see discussion of the Trust's environmental insurance policies below) by $10 million, the Army must seek additional appropriated funds for the enumerated sites. The Army is excused from this requirement if the Trust's mismanagement or inefficient use of funds causes the cost overrun.

[1] The Trust agreed to accept the amount of $100 million based upon a feasibility study and estimated cost of environmental liability prepared by its environmental consultant, including an as yet undetermined amount related specifically to the property transferred to the Trust.

The Presidio MOA may be terminated if the Army fails to provide the agreed funds to the Trust to perform the environmental cleanup of the Presidio. If the Presidio MOA is terminated, the status of the Parties reverts back to the legal rights and obligations as they existed before the Presidio MOA.

The Trust obtained two policies of environmental insurance: a Remediation Stop Loss (RSL) policy and a Real Estate Environmental Liability (REEL) policy. The RSL policy provides the Trust with insurance against cost overruns in implementing environmental remedies that have been approved by the appropriate regulatory agencies. The RSL policy has a liability limit of $100 million. The Army and DOI are each named as an additional insured on the policy. The REEL policy provides the Trust with insurance associated with the discovery of Unknown Contamination. The REEL policy has a limit of $10 million per claim and $50 million in the aggregate. DOI is a named insured under the REEL policy.

The Trust is also required to set aside a total of $25 million ($6.25 million per year through Fiscal Year 2002) until all environmental remediation of Area A is completed.

9. DEBT

	Beginning Balance	*Net Borrowing*	*Ending Balance*
Debt to the Treasury			
Note A	$ 0	$10,000,000	$10,000,000
Note B	0	10,000,000	10,000,000
Total	$ 0	$20,000,000	$20,000,000

The Presidio Trust Act granted the Trust the authority to borrow from the U.S. Treasury. The aggregate amount of outstanding obligations at any one time is limited to $50 million. These borrowings are intended to finance building and infrastructure rehabilitation by the Trust. Borrowing is contingent on the Secretary of the Treasury determining that the projects to be funded from the proceeds are creditworthy. In 1999, the Trust and the Secretary of the Treasury established a written borrowing agreement to advance funds for capital improvement projects, direct loans, and loan guarantees. The Trust must execute a promissory note for any requested amount to evidence the obligation of the Trust to repay the Treasury the sum advanced, together with any late charges that might be incurred.

An advance request for capital improvement projects was made to the Treasury for $20 million. A Non-expenditure Transfer Authorization (SF1151) was prepared by the BPD and signed by the Executive Director of the Trust. The request form was dated July 6, 1999, and the advance was transferred to the Trust's Treasury account on July 8, 1999. In exchange, the Trust provided two promissory notes for $10 million each to the BPD. These notes have a maturity date of December 31, 1999, and incur interest at 4.8%.

1) Note A

Principal amount is $10 million, the amount of the actual request intended for the capital improvement projects activities in, on, or in support of the particular Trust assets, specifically the Baker Beach Apartments. The note includes a pledge by the Trust to the Treasury of all rents, revenues, income, and proceeds arising out the Trust's administration, operation, and leasing of the assets that have been improved.

The Trust represented to the Treasury that the revenues have not been pledged in favor of any other person and will not as long as Note A is outstanding. Note A can be modified by amendments, extensions, and renewals as may be agreed upon time to time by the Treasury and the Trust.

2) Note B

Principal amount is $10 million, the difference between the $20 million advance request and the amount of Note A described above. The Trust was instructed to place this amount in an escrow account. The note included a pledge, by the Trust to the Treasury, for the amount in the escrow account and any interest it earns. The escrow account is used by the BPD to invest into governmental securities that bear the same rate as the Trust's interest rate for the borrowed funds. The Trust also represented that the escrow account has not been pledged to any person and will not as long as Note B is outstanding. If the note has not been paid by the maturity date, then the amount will be returned to the Treasury.

The BPD invested the funds of the escrow account into government securities through their investment department. The interest earned was recorded in a governmental interest receipt account and used to pay the interest owed to the Treasury.

The Trust incurred $220,931 in interest cost in 1999, all of which was included in program costs. The loan agreements have been extended to June 30, 2000. The BPD has reinvested the funds to June 30, 2000, at an interest rate of 5.68%.

10. SECURITY DEPOSITS

The residential lease management company, John Stewart Company, collects security deposits from the residential tenants and transfers the deposits to the Trust. The Trust also collects security deposits from certain non-residential leases managed by the Trust.

11. UNEXPENDED APPROPRIATIONS

Appropriations	$	1,313
Undelivered orders		520,933
Total Unexpended Appropriations	$	522,246

There is an additional $1,689,752 of undelivered orders related to budgetary resources other than appropriated funds.

12. PROGRAM COSTS BY OBJECT CLASS

Personal Services and Benefits	$	15,714,295
Contractual Services		10,331,282
Travel and Transportation		413,822
Rental, Communication, and Utilities		4,609,540
Printing and Reproduction		327,793
Supplies and Materials		2,141,811
Equipment and Fixed Assets		4,446,034
Other		226,834
Total Program Costs	$	38,211,411

Certain residential lease operating expenses, aggregating approximately $820,000 has been deducted from residential lease operating income in the Statement of Net Cost.

13. LEASES

Trust as Lessor

Operating Leases

Description of Lease Arrangements: The Trust's properties are being leased under operating leases that expire over the next 50 years. The Trust expects that these leases will be renewed or replaced by other leases in the normal course of business. In addition, the golf course lease is a contingent rental agreement wherein the monthly rental revenue is a percent of the lessee's monthly revenue; the Trust recognizes this revenue when payment is received.

Additionally, the Trust has three other lessees that operate under contingent rental agreements wherein the monthly rent is a percent of the lessee's monthly revenue; however, the lessees remit their monthly rental payments to a separate government improvement account at a commercial bank. The rental payments are accumulated and used for improvements to the leased building at the lessee's discretion. The Trust does not have signatory authority over the bank accounts and receives no rental payments related to these leases. All improvements funded from these accounts must be mutually approved by both the lessee and the Trust.

The Trust also provides housing free of charge or at reduced rental rate to certain employees of the Trust and other governmental agencies.

Minimum future lease payments to be received under non-cancelable operating leases are as follows:

Fiscal Year		
2000	$	532,446
2001		909,780
2002		855,898
2003		855,898
2004		855,898
Thereafter		9,881,739
Total	$	13,891,659

14. TRANSFER IN AT INCEPTION – CASH

Prior to the transfer of the golf course assets to the Trust, Arnold Palmer Golf Management Company (Arnold Palmer), the golf course management company, was required by the NPS to place all rental revenues into a government improvement account (GIA). In 1998, the NPS transferred funds out of the GIA and, at inception of the Trust, the NPS transferred $2,202,745 to the Trust. In 1999, Arnold Palmer closed the GIA and transferred $1,521,391 to the Trust. Such amount is reflected as earned revenue in the Statement of Net Cost.

Supplemental Information

INTRAGOVERNMENTAL ASSETS AND LIABILITIES

Assets

Agency	*Investments*	*Accounts Receivable*
Department of the Treasury	$ 44,576,854	0
Department of the Army	0	$ 1,938,298
National Park Service	0	647,944
Other federal agencies	0	126,677
Total	$ 44,576,854	$ 2,712,919

Liabilities

Agency	*Fund Balance with Treasury*	*Accounts Payable*	*Advances for Environmental Cleanup*	*Debt*
Department of the Treasury	$ 890,880	$ 200	0	$ 20,000,000
Department of the Army	0	0	$ 21,475,422	0
National Park Service	0	2,151,748	0	0
Other	0	97,635	0	0
Total	$ 890,880	$ 2,249,583	$ 21,475,422	$ 20,000,000

DEFERRED MAINTENANCE

The Trust determined that NPS and the Army had deferred maintenance to many of the buildings that were transferred to the Trust. Using an Inventory Condition Assessment Program document from the NPS upon receipt of the property and an assessment survey by Trust personnel, the Trust determined that there is $1.2 million of deferred maintenance to buildings at the Presidio. There is no deferred maintenance for any other major class of asset.

Report of Independent Auditors on Internal Control

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Report of Independent Auditors on Internal Control

To the Board of Directors of
The Presidio Trust

We have audited the balance sheet of the Presidio Trust (the Trust) as of September 30, 1999, and the related statements of net cost, budgetary resources, financing and changes in net position, for the year then ended, and have issued our report thereon dated January 28, 2000.

Except for the matter discussed in the third paragraph of our report on the financial statements, we conducted our audit in accordance with generally accepted auditing standards; the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States; and, Office of Management and Budget (OMB) Bulletin 98-08, *Audit Requirements for Federal Financial Statements,* as amended.

In planning and performing our audit, we considered the Trust's internal control over financial reporting by obtaining an understanding of the Trust's internal control, determined whether these internal controls had been placed in operation, assessed control risk, and performed tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements. We limited our internal control testing to those controls necessary to achieve the objectives described in OMB Bulletin 98-08. We did not test all internal controls relevant to operating objectives as broadly defined by the Federal Managers' Financial Integrity Act of 1982, such as those controls relevant to ensuring efficient operations. The objective of our audit was not to provide assurance on internal control. Consequently, we do not provide an opinion on internal control.

The management of the Trust is responsible for establishing and maintaining internal control. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs on internal control policies and procedures. The objectives of internal control are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles; and data that supports reported performance measures are properly recorded and accounted for to permit preparation of reliable and complete performance information. Because of inherent limitations in any internal control, errors and irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of internal control to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions. Under standards issued by the American Institute of Certified Public Accountants, reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation of the internal control that, in our judgment, could adversely affect the agency's ability to record, process, summarize, and report financial data consistent with the assertions by management in the financial statements. Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to relatively low levels the risk that misstatements 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. However, we noted certain matters discussed in the following paragraphs involving the internal control and its operation that we consider to be reportable conditions -- the first matter noted in the following we consider to be a material weakness.

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MATERIAL WEAKNESS

Integrated Financial Management Systems

Management has informed us that the Trust's Financial Accounting System (GLOWS) was recommended by the Office of Management and Budget (OMB) and installed during FY1998 by the Treasury Department's Financial Management Service (FMS). The Trust has determined that improvements are necessary to provide adequate integrated reporting of financial data from each of the various activity sectors within the Trust. We concur in this assessment. Due to the weaknesses inherent in GLOWS, invoices and capital cost information must be entered manually in a lengthy, duplicative and costly procedure. Additionally, the lack of an integrated computerized financial accounting system impairs the ability of management to prepare interim and year end financial reports in a timely manner.

Recommendations

We recommend that Trust management implement an integrated software solution that will assist it to effectively identify, track and record transactions to increase the efficiency of its processes and reduce duplicative work steps. We understand that the Trust's management also recognizes this need and has taken steps in the direction that we have recommended.

REPORTABLE CONDITIONS

Real Property

On July 1, 1998, the Trust assumed jurisdiction over approximately 1,100 acres of federal land and over 800 buildings from the National Park Service. The United States Army previously administered the property. Many of the structures are greater than 40 years old and pursuant to Trust depreciation policies were fully depreciated at the point of transfer. SFFAS #6—Accounting for Property, Plant and Equipment (PPE)— requires PPE to be recognized when title passes to the entity. Additionally, SFFAS #6 requires that the cost of general PPE transferred from other federal entities be either the cost recorded by the transferring entity, net of accumulated depreciation; if such amounts can not be reasonably ascertained, the cost of the PPE is to be its fair value at the time transferred.

Due to the lack of available information from the National Park Service and the United States Army, the Trust valued buildings less than 40 years old by using appropriate construction industry indices, less an accumulated depreciation adjustment to ascertain net asset value at the date of the Trust's formation. However, improvements made to buildings over 40 years old and land improvements have been valued at zero net book value but may still have a net cost value. Per SFFAS #6, the Trust should record these improvements at fair value. Estimating the values of these improvements would be a process that the Trust considers to be lengthy, cost prohibitive and which would result in information that is meaningless to the users of the Trust's financial statements. In addition, The Letterman Hospital facility, which was constructed within the last 40 years, is also reflected at a net book value of $0 due to limitations in valuing a hospital facility that is designated for demolition in year 2000. We were unable to satisfy ourselves as to the estimate of the carrying amount for these assets.

Recommendations

We recommend that management explore alternative approaches to valuing building and land improvements.

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Formalized Supervisory Review

Formalized supervisory review of key processes should be an integral component of the Trust's internal controls; however, we noted numerous instances where formalized supervisory reviews either need to be implemented and/or strengthened. Lack of formal supervisory reviews may result in misstatements of the financial statements as well as increases the Trust's exposure to waste, fraud and abuse.

Recommendations

We recommend that the Trust implement policies and procedures to ensure that work performed by staff is reviewed and formally approved by a supervisor.

Control Environment

Although the Trust management is responsible for establishing a control environment throughout the organization we noted certain control deficiencies, that if not addressed, could lead to potential loss, fraud and irregularities that may not be promptly detected.

<u>Cash Controls</u>

We noted the following deficiencies related to the Trust's handling of cash receipts:

- Trust deposits are transported to the bank (custody) by the same individual responsible for recording cash receipts (recordkeeping) in the accounting system;
- The accounting department, which records and reconciles cash activity, receives the mail, including rental checks; and
- Checks awaiting deposit are held a file tray on the desk of the Accounts Receivable clerk in the Budget and Finance Department, an unsecured area.

<u>Resolution of Reconciling items</u>

We noted that reconciling items identified in the reconciliation of SF 224 to the general ledger were not resolved on a monthly basis from March through August 1999. Delays in resolving reconciling items may contribute to the difficulties in resolving them at a future date. Inappropriate or untimely resolution of reconciling items subjects the Trust to risk of loss.

<u>Comprehensive Set of Accounting Policies</u>

Currently, the Trust does not have a complete, formalized comprehensive set of accounting policies and procedures. Lack of established policies and procedures may lead to incorrect and inconsistent treatment of transactions. Since this was the first year of operations for the Trust, it is understandable that some policies and procedures and their implementation were a work in progress. However, management's continued attention to identifying and correcting control weaknesses is essential to reduce the Trust's exposure to possible waste, fraud and abuse and ensure that the Trust's financial information is reliable.

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Recommendations

We recommend that the Trust finalize the development of a comprehensive set of written accounting policies and procedures. Formal documentation of such procedures support the activities of Trust personnel by ensuring consistent treatment of transactions and a smooth transition of specific activities and responsibilities in the event of employee turnover and job changes. We further recommend that such procedures provide for adequate controls over cash receipts, including segregation of receiving, recording and reconciliation functions, and the timely resolution of reconciling items.

Current EDP Environment

As management explores opportunities with respect to a future implementation of a new integrated software solution, management should also consider strengthening controls surrounding its current EDP environment.

Recommendations

We recommend policies and procedures be enhanced related to data center physical security, user access authorization, use of passwords and remote access.

* * * * * *

In addition, with respect to internal control related to performance measures reported in the Overview, we obtained an understanding of the design of significant internal control relating to the existence and completeness assertions, as required by OMB Bulletin 98-08. Our procedures were not designed to provide assurance on internal control over reported performance measures, and, accordingly, we do not provide an opinion on such controls.

We also considered the Trust's internal control over Required Supplementary Stewardship Information by obtaining an understanding of the Trust's internal control, determined whether this internal control had been placed in operation, assessed control risk, and performed tests of controls as required by OMB Bulletin 98-08 and not to provide assurance on internal control. Accordingly, we do not provide assurance on such controls.

A separate letter, dated January 28, 2000, was provided to management that further discusses weaknesses in internal control and other matters, which came to our attention as a result of our audit.

This letter is intended solely for the information and use of the management of the Trust, its Board of Directors, OMB and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

Ernst & Young LLP

January 28, 2000

Report of Independent Auditors on Compliance with Laws and Regulations

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Report of Independent Auditors on Compliance with Laws and Regulations

To the Board of Directors of
The Presidio Trust

We have audited the balance sheet of The Presidio Trust (the Trust) as of September 30, 1999, and the related statements of net cost, budgetary resources, financing and changes in net position for the year then ended, and have issued our report thereon dated January 28, 2000.

Except for the matter discussed in the third paragraph of our report on the financial statements, we conducted our audit in accordance with generally accepted auditing standards, the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States and Office of Management and Budget (OMB) Bulletin 98-08, *Audit Requirements for Federal Financial Statements,* as amended.

The management of the Trust is responsible for complying with laws and regulations applicable to the Trust. As part of obtaining reasonable assurance about whether the Trust's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statement amounts and certain other laws and regulations specified in OMB Bulletin 98-08. We limited our tests of compliance to these provisions and we did not test compliance with all laws and regulations applicable to the Trust. We caution that noncompliance may occur and not be detected by the tests performed and that such testing may not be sufficient for other purposes.

The results of our tests of compliance with the laws and regulations described in the preceding paragraph disclosed no instances of non-compliance with other laws and regulations that are required to be reported under *Government Auditing Standards* and OMB Bulletin 98-08.

The Report of Independent Auditors on Internal Control and our separate management letter includes information related to the financial management systems that were found not to comply with the requirements, relevant facts pertaining to the noncompliance, and our recommendations related to the specific issues presented. It is our understanding that management agrees with the facts as presented, and relevant comments from the Trust's management responsible for addressing the noncompliance, including management's proposed plan, will be provided as an attachment to this report.

Providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our audit and, accordingly, we do not express such an opinion.

This report is intended for the use of the management of the Trust, its Board of Directors, OMB and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

Ernst & Young LLP

January 28, 2000

The Trust's Response

The Trust is pleased to report our accomplishments in the past fiscal year, as reported in these financial statements and notes, as well as in our Year-End Report to Congress.

Fiscal Year 1999 was the first year that the Trust prepared financial statements and managed its own accounting function. On October 1, 1998, the Trust began to operate with Orion GLOWS software, an OMB-approved accounting system installed for the Trust by the Treasury Department's *Center for Applied Financial Management*. In July 1998, the Trust assumed jurisdiction over 80% of the Presidio, including historic buildings dating back to the early 19th century. This property was transferred to the Trust from the National Park Service, which had administrative jurisdiction of the Presidio from 1994 to 1998. Prior to that, the U.S. Army held jurisdiction.

The Trust also assumed operational responsibility for telecommunications services, water treatment and distribution and infrastructure. During the year, the Trust also took over responsibility for conducting environmental cleanup at the former Army post.

To deal effectively with the complexity of managing all of the functions of a municipality within a national park, the Trust has hired a total of 360 employees. We have also come to understand that the complexity of operations requires a more sophisticated software system that integrates all aspects of the Presidio Trust's various functions. Our auditors have reinforced this understanding. Currently, the Trust is undertaking an outside assessment to determine how a new computer software system should be designed to accommodate present and future needs. This assessment will be completed during fiscal year 2000, after which the Trust will move forward on installation of an integrated computerized software system.

While we are pleased that our auditors have reported that our financial statements fairly reflect financial activity of the Trust during this first year, with the exception of real estate valuation, we appreciate the need for more formalized, written accounting policies and procedures to ensure adequate internal controls are codified. We are also analyzing our current supervisory review process and formalizing the procedure to ensure all work is properly approved at the time the work is done. In addition, we are strengthening our internal controls for the handling of all cash receipts. It is our goal to ensure that we have taken all of the necessary steps to assure confidence and control over all of the accounting transactions. For example, the cash recording duties have been effectively split up and all checks are locked in a secure drawer until they are deposited. Also, a more formal procedure for EDP access approval will be completed by spring; rights and permissions are now being reviewed on a monthly basis. These are just some of the measures we are currently taking to improve our internal controls. This process is now underway and is a high priority for the Trust during fiscal year 2000.

With respect to valuing improvements made to buildings and infrastructure by the U.S. Army and National Park Service prior to the Trust's assumption of jurisdiction over the Presidio, the Trust is unable to determine the value of improvements completed by the other agencies. The Trust does not have access to auditable documentation supporting this work. Given the concern raised by auditors regarding the valuation of these items, the Trust will consider alternative methods for determining their value. Regarding valuation of the obsolete and unusable Letterman hospital and research center, the Trust anticipates deconstruction of the structures at the end of fiscal year 2000. Therefore, the Trust does not consider the hospital to have any monetary value.

Again, we appreciate the recommendations provided in this report and will consider them carefully as we improve our computer software systems during the Trust's second fiscal year. We take great pride in the fact that we have been able to manage our financial operations in an exemplary manner while also building a multi-faceted, fast-growing organization.

Very truly yours,

Mr. James Meadows
Executive Director

Craig R Middleton

Mr. Craig Middleton
Chief Operations Officer

Francene Gross

Ms. Francene Gross
Controller

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