# NAPA COMMUNITY
# REDEVELOPMENT AGENCY
# COMPONENT UNIT FINANCIAL STATEMENTS
# FOR THE YEAR ENDED
# JUNE 30, 2011

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**NAPA COMMUNITY REDEVELOPMENT AGENCY**
**COMPONENT UNIT FINANCIAL STATEMENTS**
**FOR THE YEAR ENDED**
**JUNE 30, 2011**

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## INDEPENDENT AUDITORS' REPORT

To the Honorable Members of
The Board of Directors of the Napa
Community Redevelopment Agency

We have audited the financial statements of the governmental activities and each major fund of the Napa Community Redevelopment Agency, a component unit of the City of Napa, California, as of and for the year ended June 30, 2011, as listed in the table of contents. These basic component unit financial statements are the responsibility of the Agency's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards in the United States of America and the standards for 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 as to whether the basic component unit financial statements are free of material misstatement. An audit includes examining on a test basis evidence supporting the amounts and disclosures in the component unit financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall basic component unit financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the basic component unit financial statements referred to above present fairly in all material respects the respective financial position of the governmental activities and each major fund of the Napa Community Redevelopment Agency as of June 30, 2011, and the respective changes in the financial position thereof and the respective budgetary comparisons listed as part of the basic component unit financial statements for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As disclosed in Note 14, the State of California adopted ABx1 26 on June 28, 2011, which suspends all new redevelopment activities except for limited specified activities as of that date and dissolves redevelopment agencies effective October 1, 2011. The State simultaneously adopted ABx1 27 which allows redevelopment agencies to avoid dissolution by opting into an "alternative voluntary redevelopment program" requiring specified substantial annual contributions to local schools and special districts. These conditions raise substantial doubt about the Agency's ability to continue as a going concern. However, on August 11, 2011, the California Supreme Court issued a partial stay of ABx1 26 and a full stay of ABx1 27, but the partial stay did not include the section of ABx1 26 that suspends all new redevelopment activities. As a result, the accompanying financial statements have been prepared assuming that the Agency will continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

As of July 1, 2010, the Agency adopted the provisions of Governmental Accounting Standards Board Statement Number 54 (GASB 54), *Fund Balance Reporting and Governmental Fund Type Definitions*. As discussed in Note 9 to the financial statements, the provisions of this statement affect the classification of fund balances reported in the financial statements.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 20, 2011, on our consideration of the Authority'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.

Management's Discussion and Analysis is not a required part of the basic component unit financial statements but is supplementary information required by the Governmental Accounting Standards Board. 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 made for the purpose of forming an opinion on the component unit financial statements taken as a whole. The supplemental information listed in the Table of Contents is presented for purposes of additional analysis and is not a required part of the component unit financial statements of the Agency. Such information has been subjected to the auditing procedures applied in our audit of the component unit financial statements, and in our opinion is fairly stated in all material respects in relation to the component unit financial statements taken as a whole.

Maze & Associates

December 20, 2011

## FINANCIAL HIGHLIGHTS

The Napa Community Redevelopment Agency (Agency) supports the City of Napa with housing and economic development resources to enhance the economic prosperity of the downtown business district and Soscol Gateway area, and improve the community's supply of affordable housing.

The Agency is financed with incremental property tax generated on appreciated property values within the Agency's two project areas; the 324-acre Parkway Plaza Project Area (Parkway Plaza, established in 1969) and the 376-acre Soscol Gateway Project Area (Soscol Gateway, established in 2007.) Property values in both project areas have continued growth for the recent year ended June 30, 2011. During this period, tax revenues for Parkway Plaza increased 8% over the prior year while Soscol Gateway had a decrease in tax increment of 46%. This was the third year that tax revenues were received for Soscol Gateway. The decrease in tax increment revenue for Soscol Gateway is due to an anomaly in FY10 that was caused by a large exempt business filing bankruptcy, which resulted in it losing its tax exempt status and the property values being added back to the tax roll. We anticipated the values to be adjusted downward in FY 2010-11 to correct for any overstatement of value given current market conditions. The Agency remains in good financial condition and is on track with its project area Five-Year Implementation Plans, while continuing to monitor changes and projected changes in assessed valuations.

State code requires twenty percent of redevelopment tax revenues to be set-aside for low- & moderate-income housing programs. The Agency deposits the 20 percent set-aside in its Low-Moderate Income Housing Fund, utilizes a portion of the proceeds to make annual debt payments on tax-exempt housing bonds, and transfers the remainder to the City of Napa Housing Authority for expenditure on affordable housing projects and programs.

## OVERVIEW OF THE BASIC COMPONENT UNIT FINANCIAL REPORT

This Basic Component Unit Financial Report is presented in the following sections:

1) This introductory section, *Management's Discussion and Analysis*

2) *Basic Component Unit Financial Statements*, including:
    a. *Agency-wide financial statements*
    b. *Fund financial statements*
    c. *Notes to financial statements*

### The Basic Component Unit Financial Statements

The *Basic Component Unit Financial Statements* are comprised of the *Agency-wide Financial Statements* and the *Fund Financial Statements.* These two sets of financial statements provide different views of the Agency's financial activities and financial position.

The *Agency-wide Financial Statements* provide a longer-term view of the Agency's activities as a whole. *The Statement of Net Assets* provides information about the financial position of the Agency, including all of its capital assets and long-term liabilities on the accrual basis of accounting, similar to that used by commercial enterprises. The *Statement of Activities* provides information about the Agency's revenues and expenses, also on the accrual basis of accounting, with the emphasis on measuring net revenues or expenses of the Agency's programs.

The *Fund Financial Statements* report the Agency's operations in more detail than the government-wide statements and focus primarily on the short-term activities of the Agency's Funds. These statements measure only current revenues and expenditures and fund balances. They exclude capital assets, long-term debt and other long-term amounts.

## FINANCIAL ACTIVITIES OF THE AGENCY AS A WHOLE

### Governmental Net Assets

The following is a summary of the Agency's net assets, as measured on the accrual basis of accounting. All of the Agency's programs are governmental-type programs.

Table 1

| | June 30, 2010 | June 30, 2011 |
|---|---|---|
| Assets | | |
| Cash and investments | $ 8,412,644 | $ 7,815,893 |
| Other assets | 1,111,461 | 604,694 |
| Capital assets | 10,018,548 | 6,300,341 |
| Total assets | 19,542,653 | 14,720,928 |
| Liabilities | | |
| Long-term debt outstanding | 19,020,000 | 17,290,000 |
| Other liabilities | 3,741,597 | 7,985,901 |
| Total liabilities | 22,761,597 | 25,275,901 |
| Net assets: | | |
| Invested in capital assets, net of debt | 10,018,548 | |
| Restricted | 2,782,045 | 5,235,147 |
| Unrestricted | (16,019,537) | (15,790,120) |
| Total net assets | $ (3,218,944) | $ (10,554,973) |

The Agency's $15million of assets are primarily comprised of $ 7.8 million of cash and investments, of which $6.1million is restricted debt reserves and bond proceeds pending bond project development. The Agency's $25.3 million of liabilities represent $ 17.3 million of long term debt.

The Agency's unrestricted net assets are negative $15.8 million. The Agency's financing structure is typical of most California redevelopment agencies in that long-term bonds have been sold to enhance current development in the project area, which will in turn generate incremental property tax revenues to retire bonds and restore the Agency's unrestricted net assets over the life of the Agency.

### Agency Activities

The Agency generated $ 6.2 million of property tax and investment income during the year. These resources were used to fund the Agency's debt service, project area development, and administrative costs. Twenty percent of tax revenues were set aside for affordable housing; the Agency contributes this set-aside to the Housing Authority of the City of Napa (Authority) for current affordable housing activities during the fiscal year. An additional five percent of the Parkway Plaza's 80 percent funds (non housing set-aside) are being held in an Agency "discretionary housing fund" to apply toward future affordable housing projects or activities.

The following is a summary of the program expenses, revenues, and changes in net assets for the year ended June 30, 2011. These balances are reported on the accrual basis of accounting.

| Table 2 | | |
|---|---|---|
| | June 30, 2010 | June 30, 2011 |
| Program expenses: | | |
| General government | $ 3,062,038 | $ 3,070,794 |
| Redevelopment projects | 871,924 | 613,429 |
| Affordable housing | 627,082 | 845,463 |
| City of Napa capital projects | 827,584 | 3,639,374 |
| Interest on long-term debt | 1,057,795 | 977,101 |
| Other | | 4,499,913 |
| Total program expenses | 6,446,423 | 13,646,074 |
| General revenues: | | |
| Property tax increment | 6,278,468 | 6,234,788 |
| Interest income | 207,176 | 18,850 |
| Other | 469,186 | 56,407 |
| Total general revenues | 6,954,830 | 6,310,045 |
| Change in net assets | $ 508,407 | $ (7,336,029) |

## FUND FINANCIAL STATEMENTS

The fund financial statements present the Agency's financial position and activities from an operational view, since these statements measure only the current revenues, expenditures and fund balances available to finance the Agency's current operations. These statements exclude capital assets, long-term debt and other long-term amounts.

### Debt Service Fund

The Agency's Debt Service Funds are the primary funds of the Agency. They are used to record tax increment revenues from the County, to transfer the statutory housing set-aside funds to the Agency's Low-Mod Special Revenue Funds, to fund debt service on the Agency's long-term bonds, and finally, to transfer administration and project appropriations to the Capital Projects Funds for implementation. Revenue decreased from $ 6.6 million in 2010 to $ 6.3 million in 2011, with the majority of the decrease attributable to decreased property tax increment for the Soscol Gateway project area. The Agency implemented a Public Projects Financing Agreement with the City of Napa in 2011 which called for a transfer of funds from the Agency to the City to cover a variety of projects already in the progress. Because of this large transfer, the Agency has total fund balance of negative $1.3 million as of June 30, 2011.

### Low-Mod Income Special Revenue Fund

These funds account for the portion of property tax increment required under California law to be set aside to fund low- and moderate-income housing expenditures. Twenty percent of current year tax increment revenues, in the amount of $1,246,957, were set-aside for this purpose.

The Parkway Plaza Low-Mod Special Revenue Fund also accounts for debt transactions and balances supporting the $4 million of bonds issued for affordable housing projects. These include debt proceeds, the debt service reserve, costs of issuance, and the annual debt service on the bonds. Residual revenues, after debt service of $416,845, have been contributed to the Housing Authority.

### Capital Projects Fund

The Agency's Capital Projects Funds are used to account for the Agency's Implementation Plans. Resources are transferred into each of the two project areas' funds from the associated Debt Service Fund as projects are appropriated. Many of the projects are multi-year in nature, given the long lead-time on development activities. Therefore, actual expenditures may follow the year of initial appropriation. During the year ended June 30, 2011, the Agency expended $5.4 million, $0.5 million more than the previous year. The fund balance of $2.6 million consists of cumulative appropriations for projects in progress at year-end.

## CAPITAL ASSETS

As of June 30, 2011, the Agency had $6.3 million invested in land and buildings within the project areas, net of accumulated depreciation; a decrease of $3.7 million from the previous year. This decrease was due to the conveyance of 19 parcels of land to the City in March 2011 due to required findings in accordance with the Health and Safety Code. Major projects are outlined below.

## ECONOMIC OUTLOOK AND MAJOR INITIATIVES

Assessed valuations in the Parkway Plaza project area continue to grow at a slow but steady pace, in large part due to the significant number of newly acquired properties and upgrading of existing buildings. In the 2010-11 fiscal year, net taxable value increased 11.6 percent over the previous fiscal year, representing a value increase of $56.5 million. With fairly recent completion of several private development projects and changes in ownership due to sales of condominium units, new values will continue to be added to the rolls in Parkway Plaza and assessed valuations are expected to continue to trend upward, albeit modestly. Soscol Gateway experienced a 19 percent net decrease in assessed valuation, representing $ $42.7 million in lost value. In the 2009-10 fiscal year, the project area experienced a spike in assessed valuation that resulted from the bankruptcy of Copia, a non-profit entity with large properties that lost their tax-exempt status. The City anticipated the values would be adjusted downward by the County Assessor the following fiscal year, and combined with the recession and associated decline in property values, it is not a surprise the assessed valuations declined. Despite this drop, the assessed values have increased roughly 50 percent since the project area's formation in 2007.

During fiscal year 2010-11, the California legislature enacted legislation to eliminate redevelopment agencies but to allow jurisdictions to opt in to a voluntary redevelopment program, which in turn resulted in a lawsuit filing by the California Redevelopment Association against the State of California. The California Supreme Court issued a stay to allow agencies to continue to operate until a decision is made, but the practical effect is agencies have had to slow down activity because they are prohibited from appropriating funds or entering into contracts for projects. Despite this major impediment, the Agency completed the following activities during the fiscal year:

- Design and bid documents for the Pedestrian Improvement Program, Phase V. This phase of the program will install curb, gutter, sidewalk, and curb ramps, and street trees and lights, in a residential neighborhood adjacent to the commercial downtown. The project bidding is on hold pending the outcome of the redevelopment court case.

- Design and bid documents for a downtown park called "Riverfront Green." This park, currently under construction, includes pedestrian and bicycle pathways, drought-tolerant landscaping, benches and public art, and is at the northern end of the Napa River Trail and on the eastern bank of the Napa River.

- An historic context statement and intensive level survey, and historic design guidelines, for properties in the Downtown Specific Plan study area.
- Design and bidding of a trash enclosure on a public plaza. The contract execution is pending the outcome of the redevelopment court case.
- Implementation of the second Napa Art Walk exhibition in the Parkway Plaza redevelopment project area.
- Preliminary design of an interior drainage system in the Soscol Gateway redevelopment project area.

The Agency continues to work closely with the Napa County Flood Control and Water Conservation District and the U. S. Army Corps of Engineers on a number of improvement projects, including final design and construction of the Agency/City-sponsored downtown boat dock; construction coordination for Flood Protection Project activities including Napa Creek improvements; and facilitation of City review of design and construction documents for the Oxbow Commons bypass channel to ensure they comply with the Agency-prepared schematic plans and City requirements.

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## CONTACTING THE AGENCY

These Component Unit Financial Statements are intended to provide citizens, taxpayers, investors, and creditors with a general overview of the Agency's finances. Questions about this Report should be directed to the Agency at 1600 Clay Street, Napa, California, (707) 257-9502. The mailing address is Post Office Box 660, Napa, California, 94559-0660.

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## STATEMENT OF NET ASSETS AND STATEMENT OF ACTIVITIES

The Statement of Net Assets and the Statement of Activities summarize the entire Agency's financial activities and financial position. They are prepared on the same basis as is used by most businesses, which means they include all the Agency's assets and all its liabilities, as well as all its revenues and expenses. This is known as the full accrual basis—the effect of all the Agency's transactions is taken into account, regardless of whether or when cash changes hands, but all material internal transactions between Agency funds have been eliminated.

The Statement of Net Assets reports the difference between the Agency's total assets and the Agency's total liabilities, including all the Agency's capital assets and all its long-term debt. The Statement of Net Assets presents similar information to the old balance sheet format, but presents it in a way that focuses the reader on the composition of the City's net assets, by subtracting total liabilities from total assets.

The Statement of Net Assets summarizes the financial position of the Agency's financial position in a single column.

The Statement of Activities reports increases and decreases in the Agency's net assets. It is also prepared on the full accrual basis, which means it includes all the Agency's revenues and all its expenses, regardless of when cash changes hands. This differs from the "modified accrual" basis used in the Fund financial statements, which reflect only current assets, current liabilities, available revenues and measurable expenditures.

The format of the Statement of Activities differs considerably from those used in the past. It presents the Agency's expenses that are listed by program first. Program revenues—that is, revenues which are generated directly by these programs—are then deducted from program expenses to arrive at the net expense of each program. The Agency's general revenues are then listed and the Change in Net Assets is computed and reconciled with the Statement of Net Assets.

These financial statements along with the fund financial statements and footnotes are called *Component Unit Financial Statements.*

# NAPA COMMUNITY REDEVELOPMENT AGENCY
## STATEMENT OF NET ASSETS
## JUNE 30, 2011

| | |
|---|---|
| ASSETS | |
| Cash and investments (Note 3) | $1,719,402 |
| Restricted cash and investments (Note 3) | 6,096,491 |
| Receivables: | |
| Federal, State and other governments | 154,308 |
| Interest | 35,300 |
| Deferred charges | 415,086 |
| Capital assets (Note 7): | |
| Non-depreciable | 519,390 |
| Depreciable | 5,780,951 |
| Total Assets | 14,720,928 |
| LIABILITIES | |
| Accounts payable and accrued liabilities | 56,249 |
| Interest payable | 281,513 |
| Deposits payable | 813,633 |
| Deferred revenue | 99,694 |
| Due to City (Note 4) | 4,194,166 |
| Payable to Housing Authority | 20,922 |
| Payable to City (Note 4) | 789,724 |
| Long-term debt (Note 8): | |
| Due within one year | 1,730,000 |
| Due in more than one year | 17,290,000 |
| Total Liabilities | 25,275,901 |
| NET ASSETS (Note 9): | |
| Restricted | |
| Capital projects | 2,576,616 |
| Debt service | 2,658,531 |
| Unrestricted | (15,790,120) |
| Total Net Assets (Deficit) | ($10,554,973) |

See accompanying notes to financial statements

# NAPA COMMUNITY REDEVELOPMENT AGENCY
## STATEMENT OF ACTIVITIES
## FOR THE YEAR ENDED JUNE 30, 2011

| | |
|---|---|
| Program expenses: | |
| Governmental Activities: | |
| General government | $3,070,794 |
| Redevelopment projects | 613,429 |
| Affordable housing | 845,463 |
| City of Napa Capital projects (Note 4) | 3,639,374 |
| Interest on long-term debt | 977,101 |
| Total program expenses | 9,146,161 |
| General revenues: | |
| Property tax increment | 6,234,788 |
| Interest income | 18,850 |
| Miscellaneous | 56,407 |
| Transfer to the City of Napa (Note 4) | (4,499,913) |
| Total general revenues and transfers | 1,810,132 |
| Change in Net Assets | (7,336,029) |
| Net Assets, (Deficit) beginning | (3,218,944) |
| Net Assets, (Deficit) ending | ($10,554,973) |

See accompanying notes to financial statements

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## FUND FINANCIAL STATEMENTS

Only individual major funds are presented in the Fund Financial Statements, while non-major funds are combined in a single column. Major funds are defined generally as having significant activities or balances in the current year.

The City of Napa Redevelopment Agency determined all its funds to be major funds in fiscal 2011. They are:

**Parkway Plaza and Soscol Gateway Special Revenue Funds** – Used to account for the proceeds of specific revenue services that are legally restricted to be expended for specific purposes, specifically for property tax increments set aside for low and moderate income housing projects.

**Parkway Plaza and Soscol Gateway Debt Service Funds** – Used to account for the accumulation of resources (primarily property tax increment revenues) to be used for the payment of debt.

**Parkway Plaza and Soscol Gateway Capital Projects Funds** – Used to account for financial resources to be used for the administration and implementation of the Project Area's redevelopment plan.

# NAPA COMMUNITY REDEVELOPMENT AGENCY
## GOVERNMENTAL FUNDS
## COMBINING BALANCE SHEETS
## JUNE 30, 2011

| | | Parkway Plaza | |
|---|---|---|---|
| | Special Revenue-<br>Low-and-Mod<br>Income Housing | Debt<br>Service | Capital<br>Projects |
| ASSETS | | | |
| Cash and investments (Note 3) | $15,362 | | |
| Restricted cash and investments (Note 3) | 435,882 | $2,230,603 | $3,430,006 |
| Receivables: | | | |
| Federal, State and other governments | | 141,905 | |
| Interest | 3,356 | 25,271 | |
| Total Assets | $454,600 | $2,397,779 | $3,430,006 |
| LIABILITIES | | | |
| Accounts payable | | | $50,549 |
| Payable to Housing Authority | $20,922 | | |
| Advances from the City (Note 4) | | | |
| Due to City (Note 4) | | $3,351,725 | 842,441 |
| Deferred revenue | | 87,291 | |
| Deposits payable | | 655,404 | 1,106 |
| Total Liabilities | 20,922 | 4,094,420 | 894,096 |
| FUND BALANCES (DEFICIT) (Note 9): | | | |
| Restricted | 433,678 | 2,230,603 | 2,535,910 |
| Unassigned | | (3,927,244) | |
| Total Fund Balance (Deficit) | 433,678 | (1,696,641) | 2,535,910 |
| Total Liabilities and Fund Balance (Deficit) | $454,600 | $2,397,779 | $3,430,006 |

See accompanying notes to financial statements

| Soscol Gateway Special Revenue-Low-and-Mod Income Housing | Soscol Gateway Debt Service | Soscol Gateway Capital Projects | Total Governmental Funds |
|---|---|---|---|
| $288,404 | $1,372,121 | $43,515 | $1,719,402 |
| | | | 6,096,491 |
| | 12,403 | | 154,308 |
| 1,128 | 2,654 | 2,891 | 35,300 |
| $289,532 | $1,387,178 | $46,406 | $8,005,501 |
| | | $5,700 | $56,249 |
| | | | 20,922 |
| | $789,724 | | 789,724 |
| | | | 4,194,166 |
| | 12,403 | | 99,694 |
| | 157,123 | | 813,633 |
| | 959,250 | 5,700 | 5,974,388 |
| $289,532 | 427,928 | 40,706 | 5,958,357 |
| | | | (3,927,244) |
| 289,532 | 427,928 | 40,706 | 2,031,113 |
| $289,532 | $1,387,178 | $46,406 | $8,005,501 |

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NAPA COMMUNITY REDEVELOPMENT AGENCY
Reconciliation of the
GOVERNMENTAL FUNDS - BALANCE SHEET
with the
STATEMENT OF NET ASSETS
JUNE 30, 2011

| | | |
|---|---|---|
| TOTAL FUND BALANCES, as reported on the Governmental Funds Balance Sheet | | $2,031,113 |
| Amounts reported for Governmental Activities in the Statement of Net Assets are different from those reported in the Governmental Funds above because of the following: | | |
| CAPITAL ASSETS | | |
| Capital assets used in Governmental Activities are not current assets or financial resources and therefore are not reported on the Fund Balance Sheets | | 6,300,341 |
| ACCRUAL OF NON-CURRENT REVENUES AND EXPENSES | | |
| Unamortized bond issuance costs, which were reported as expenditures when paid in the fund statement, have been capitalized as deferred charges on the Statement of Net Assets | | 415,086 |
| LONG-TERM LIABILITIES | | |
| The liabilities below are not due and payable in the current period and therefore are not reported on the Fund Balance Sheet | | |
| Long-term debt: | | |
| Due in less than one year | (1,730,000) | |
| Due in more than one year | (17,290,000) | (19,020,000) |
| Interest payable | | (281,513) |
| NET ASSETS (DEFICIT) OF GOVERNMENTAL ACTIVITIES, as reported on the Statement of Net Assets | | ($10,554,973) |

See accompanying notes to financial statements

NAPA COMMUNITY REDEVELOPMENT AGENCY
GOVERNMENTAL FUNDS
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
FOR THE YEAR ENDED JUNE 30, 2011

| | Parkway Plaza | | |
|---|---|---|---|
| | Special Revenue-Low-and-Mod Income Housing | Debt Service | Capital Projects |
| REVENUES | | | |
| Property tax increment | | $5,660,392 | |
| Interest income | $13,283 | (20,376) | ($8,556) |
| Charges for services | | 17,708 | 1,899 |
| Miscellaneous revenues | | 25,000 | |
| Total Revenues | 13,283 | 5,682,724 | (6,657) |
| EXPENDITURES | | | |
| Redevelopment: | | | |
| Salaries | | | 288,048 |
| Materials and supplies | | | 14,374 |
| County fees and passthroughs | | 937,391 | |
| Services | | 67,692 | 402,193 |
| Capital outlay | | | 27,696 |
| Transfers to City (Note 4) | | | 4,446,415 |
| Housing (Note 5) | 727,463 | | |
| Debt service: | | | |
| Principal | 250,000 | 1,365,000 | |
| Interest and fiscal charges | 166,845 | 758,219 | |
| Total Expenditures | 1,144,308 | 3,128,302 | 5,178,726 |
| EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES | (1,131,025) | 2,554,422 | (5,185,383) |
| OTHER FINANCING SOURCES (USES) | | | |
| Contributions (to) City of Napa (Note 4) | | (1,548,958) | |
| Contributions from City of Napa (Note 4) | | | 11,800 |
| Transfers in (Note 4) | 1,132,078 | | 6,630,063 |
| Transfers (out) (Note 4) | | (7,762,141) | |
| Total Other Financing Sources (Uses) | 1,132,078 | (9,311,099) | 6,641,863 |
| NET CHANGE IN FUND BALANCES | 1,053 | (6,756,677) | 1,456,480 |
| FUND BALANCES (DEFICIT), BEGINNING | 432,625 | 5,060,036 | 1,079,430 |
| FUND BALANCES (DEFICIT), ENDING | $433,678 | ($1,696,641) | $2,535,910 |

See accompanying notes to financial statements

| Soscol Gateway | | | |
|---|---|---|---|
| Special Revenue-Low-and-Mod Income Housing | Debt Service | Capital Projects | Total Governmental Funds |
| | $574,396 | | $6,234,788 |
| $6,271 | 12,918 | $15,310 | 18,850 |
| | | | 19,607 |
| | | | 25,000 |
| 6,271 | 587,314 | 15,310 | 6,298,245 |
| | | 180,066 | 468,114 |
| | | | 14,374 |
| | 116,331 | | 1,053,722 |
| | 7,213 | 14,731 | 491,829 |
| | | 697 | 28,393 |
| | | 53,498 | 4,499,913 |
| 118,000 | | | 845,463 |
| | | | 1,615,000 |
| | 21,575 | | 946,639 |
| 118,000 | 145,119 | 248,992 | 9,963,447 |
| (111,729) | 442,195 | (233,682) | (3,665,202) |
| | | | (1,548,958) |
| | | | 11,800 |
| 114,879 | 789,122 | 405,137 | 9,071,279 |
| | (520,016) | (789,122) | (9,071,279) |
| 114,879 | 269,106 | (383,985) | (1,537,158) |
| 3,150 | 711,301 | (617,667) | (5,202,360) |
| 286,382 | (283,373) | 658,373 | 7,233,473 |
| $289,532 | $427,928 | $40,706 | $2,031,113 |

# NAPA COMMUNITY REDEVELOPMENT AGENCY
## Reconciliation of the
## NET CHANGES IN FUND BALANCES - TOTAL GOVERNMENTAL FUNDS
## with the
## CHANGE IN NET ASSETS OF GOVERNMENTAL ACTIVITIES
## FOR THE YEAR ENDED JUNE 30, 2011

| | |
|---|---|
| NET CHANGE IN FUND BALANCES - TOTAL GOVERNMENTAL FUNDS, as reported on the Statement of Revenues, Expenditures, and Changes in Fund Balance | ($5,202,360) |
| Amounts reported for governmental activities in the Statement of Activities are different because of the following: | |
| CAPITAL ASSETS TRANSACTIONS | |
| Capital assets transferred to the City is deducted from fund balance | (3,639,374) |
| Depreciation expense is deducted from fund balance | (272,475) |
| Capital asset additions is added to fund balance | 193,642 |
| OTHER NON-CURRENT ITEMS | |
| The amounts below included in the Statement of Activities do not provide or (require) the use of current financial resources and therefore are not reported as revenue or expenditures in governmental funds (net change): | |
| Amortize bond costs of issuance | (51,886) |
| LONG-TERM DEBT TRANSACTIONS | |
| Bond proceeds provide current financial resources to governmental funds, but issuing debt increases long-term liabilities on the Statement of Net Assets. Repayment of bond principal is an expenditure in the governmental funds, but on the Statement of Net Assets the repayment reduces long-term liabilities. | |
| Repayment of debt principal is added back to fund balance | 1,615,000 |
| Decrease in interest payable is added back to fund balance | 21,424 |
| CHANGE IN NET ASSETS OF GOVERNMENTAL ACTIVITIES, as reported on the Statement of Activities | ($7,336,029) |

See accompanying notes to financial statements

NAPA COMMUNITY REDEVELOPMENT AGENCY
PARKWAY PLAZA
LOW AND MODERATE INCOME HOUSING
STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCE
BUDGET AND ACTUAL
FOR THE YEAR ENDED JUNE 30, 2011

| | Budgeted Amounts | | | |
|---|---|---|---|---|
| | Original | Final | Actual Amounts | Variance with Final Budget Positive (Negative) |
| BUDGETARY FUND BALANCE, BEGINNING | | | $432,625 | |
| REVENUES | | | | |
| Interest income | $20,000 | $1,000 | 13,283 | $12,283 |
| Total Revenues | 20,000 | 1,000 | 13,283 | 12,283 |
| EXPENDITURES | | | | |
| Housing (Note 5) | 716,725 | 716,725 | 727,463 | 10,738 |
| Debt service: | | | | |
| Principal | 250,000 | 250,000 | 250,000 | |
| Interest and fiscal charges | 167,275 | 167,275 | 166,845 | (430) |
| Total Expenditures | 1,134,000 | 1,134,000 | 1,144,308 | 10,308 |
| OTHER FINANCING SOURCES (USES) | | | | |
| Transfers in (Note 4) | 1,114,000 | 1,040,400 | 1,132,078 | 91,678 |
| Total other financing sources (uses) | 1,114,000 | 1,040,400 | 1,132,078 | 91,678 |
| NET CHANGE IN FUND BALANCE | | ($92,600) | 1,053 | $93,653 |
| BUDGETARY FUND BALANCE, ENDING | | | $433,678 | |

See accompanying notes to financial statements

# NAPA COMMUNITY REDEVELOPMENT AGENCY
## SOSCOL GATEWAY
## LOW AND MODERATE INCOME HOUSING
## STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE
## BUDGET AND ACTUAL
## FOR THE YEAR ENDED JUNE 30, 2011

| | Budgeted Amounts | | | Variance with Final Budget |
|---|---|---|---|---|
| | Original | Final | Actual Amounts | Positive (Negative) |
| BUDGETARY FUND BALANCE, BEGINNING | | | $286,382 | |
| REVENUES | | | | |
| Interest income | $2,200 | $2,200 | 6,271 | $4,071 |
| Total Revenues | 2,200 | 2,200 | 6,271 | 4,071 |
| OTHER FINANCING SOURCES (USES) | | | | |
| Transfers in (Note 4) | 115,800 | 115,800 | 114,879 | (921) |
| Transfers (out) (Note 4) | | (118,000) | (118,000) | |
| Total other financing sources (uses) | 115,800 | (2,200) | (3,121) | (921) |
| NET CHANGE IN FUND BALANCE | $118,000 | | 3,150 | $3,150 |
| BUDGETARY FUND BALANCE, ENDING | | | $289,532 | |

See accompanying notes to financial statements

## NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### *A. Organization*

The Napa Community Redevelopment Agency (the Agency) was established pursuant to the Community Redevelopment Law as codified in the Health and Safety Code of the State of California (the State). The City Council of the City of Napa (the City) adopted Ordinance No. 1557 on November 19, 1962, activating the Agency and designating itself as the governing body. Officials and staff of the City perform all staff work of the Agency.

The Agency is an integral part of the City. As such, the accompanying financial statements are also included as a blended component unit within the City's financial statements.

### *B. Project Area*

On December 15, 1969, the Agency adopted its first project area, the Parkway Plaza Redevelopment Project (Parkway Plaza) which consists of 324 acres (34 square blocks in downtown Napa). The primary objective of this project is to maintain downtown business and convert the area into a competitive, modern and attractive downtown area.

On November 6, 2007, City Council approved the formation of a second project area called Soscol Gateway Project Area (Soscol Gateway) which consists of 376 acres. The primary objective of this project is to finance infrastructure improvements that will enable and encourage new private investment in the area and to expand the supply of affordable housing.

### *C. Description of Financial Statements and Basis of Accounting*

These Component Unit Financial Statements are prepared in conformity with accounting principles generally accepted in the United States of America. The Government Accounting Standards Board is the acknowledged standard setting body for establishing accounting and financial reporting standards followed by governmental entities in the U.S.A.

The Agency's financial position and results of operations are presented from two perspectives in the following two sets of statements:

**Government-wide Statements:** The Statement of Net Assets and the Statement of Activities include the financial activities of the overall Agency using an economic resources measurement focus and the full accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred regardless of when the related cash flows take place. Revenue from taxes is recognized in the fiscal year for which the taxes are levied or assessed. Eliminations have been made to minimize the double counting of internal activities.

The Statement of Activities presents a comparison between direct expenses and program revenues for each function of the Agency's governmental activities. Direct expenses are those that are specifically associated with a program or function and, therefore, are clearly identifiable to a particular function. Program revenues include (a) charges paid by the recipients of goods or services offered by the programs, (b) grants and contributions that are restricted to meeting the operational needs of a particular program and (c) fees, grants and contributions that are restricted to financing the acquisition or construction of capital assets. Revenues that are not classified as program revenues, including all taxes, are presented as general revenues. For the year ended June 30, 2011, the Agency reports only general revenues.

## NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

**Fund Financial Statements:** All of the Agency's activities are reported in governmental funds. Governmental funds are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Under this method, revenues are recognized when measurable and available. The Agency considers all revenues reported in the governmental funds to be available if the revenues are collected within sixty days after year-end. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt, claims and judgments, and compensated absences, which are recognized as expenditures to the extent they have matured. Governmental capital asset acquisitions are reported as expenditures in governmental funds. Proceeds of governmental long-term debt and acquisitions under capital leases are reported as other financing sources.

Those revenues susceptible to accrual include taxes, intergovernmental revenues, charges for services and interest revenue. Non-exchange transactions, in which the Agency gives or receives value without directly receiving or giving equal value in exchange, include taxes, grants, entitlements, and donations. Revenue from grants, entitlements, and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied.

The Agency may fund programs with a combination of cost-reimbursement grants, categorical block grants, and general revenues. Thus, both restricted and unrestricted net assets may be available to finance program expenditures. The Agency's policy is to first apply restricted grant resources to such programs, followed by general revenues if necessary.

Certain indirect costs are included in program expenses reported for individual functions and activities.

### *D. Major Funds*

Major funds are defined as funds that have either assets, liabilities, revenues or expenditures/expenses equal to ten percent of their fund-type total and five percent of the grand total, or other funds selected for presentation by the Agency. The Agency considers all its funds to be major funds.

The Agency reported the following major funds in the accompanying financial statements for both the Parkway Plaza and Soscol Gateway Projects:

**Special Revenue Funds** – Used to account for the proceeds of specific revenue services that are legally restricted to be expended for specific purposes, specifically for property tax increments set aside for low and moderate income housing projects.

**Debt Service Funds** – Used to account for the accumulation of resources (primarily property tax increment revenues) to be used for the payment of debt.

**Capital Projects Funds** – Used to account for financial resources to be used for the administration and implementation of the Project Area's redevelopment plan.

## NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### *E. Property Tax Increment*

All property taxes are levied and collected by the County Auditor of the County of Napa and paid to the various taxing entities including the Agency. Secured taxes are due on November 1 and February 1 and become delinquent on December 10 and April 10, respectively. Unsecured taxes are due on July 1 and become delinquent on August 31. The lien date for secured and unsecured property taxes is January 1 of the preceding fiscal year. Property tax increment revenues include only property taxes resulting from increased assessed values and are recognized in the fiscal year for which the taxes have been levied, provided they become available and measurable within the current period or soon enough thereafter to be used to pay liabilities of the current period.

### *F. Use of Estimates*

The accompanying basic financial statements have been prepared on the modified accrual basis of accounting in accordance with generally accepted accounting principles. This requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

## NOTE 2 –BUDGETING

The Agency adopts a biennial operating budget on or before June 30 for each of the ensuing two fiscal years for Special Revenue funds. The operating budget takes the form of a two-year financial plan which is adopted in its entirety by the Board. A mid-period review is conducted in the off-year and appropriations are adjusted accordingly. The fiscal year begins on July 1 and ends on June 30 of the following year.

Project-length budgets (which can span a number of years) are adopted for most other governmental funds. Debt service fund budgets are revised when debt issuances are authorized.

The budget is prepared at the fund, function and department levels. The Executive Director is authorized to make transfers between the departments. All other adjustments or changes require Board approval. The legal level of budgetary control is the department level. Budget amounts shown in these financial statements include all supplemental appropriations made during the year.

## NOTE 3 - CASH AND INVESTMENTS

The Agency's dependence on incremental property tax receipts, which are received semi-annually, requires it to maintain significant cash reserves to finance operations during the remainder of the year. The Agency pools cash from all sources and all funds with the City of Napa, except Cash with Fiscal Agents so that it can be invested at the maximum yield, consistent with safety and liquidity, while individual funds can make expenditures at any time. Investments are carried at fair value.

## NOTE 3 - CASH AND INVESTMENTS (Continued)

### A. *Policies*

The City and Agency invest in individual investments and in investment pools. Individual investments are evidenced by specific identifiable pieces of paper called *securities instruments*, or by an electronic entry registering the owner in the records of the institution issuing the security, called the *book entry* system. In order to maximize security, the City and Agency employ the Trust Department of a bank as the custodian of all City and Agency managed investments, regardless of their form.

California Law requires banks and savings and loan institutions to pledge government securities with a market value of 110% of the City and Agency cash on deposit or first trust deed mortgage notes with a value of 150% of the Agency's cash on deposit as collateral for these deposits. Under California Law this collateral is held in an investment pool by an independent financial institution in the City or Agency's name and places the City and Agency ahead of general creditors of the institution pledging the collateral.

The Agency's investments are carried at fair value, as required by generally accepted accounting principles (material only). The Agency adjusts the carrying value of its investments to reflect their fair value at each fiscal year end, and it includes the effects of these adjustments in income for that fiscal year.

### B. *Classification*

Cash and investments are classified in the financial statements as shown below, based on whether or not their use is restricted under the terms of Agency debt instruments or Agency agreements. Cash and investments as of June 30, 2011, are as follows:

| | |
|---|---|
| Cash and investments available for operations | $1,719,402 |
| Restricted cash and investments | 6,096,491 |
| Total cash and investments | $7,815,893 |

### C. *Cash and Investments and Interest Rate Risk*

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Normally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates.

Information about the sensitivity of the fair values of the Agency's investments (including investments held by bond trustees) to market interest rate fluctuations is provided by the following table that shows the distribution of the Agency's cash and investments by maturity:

| Type of Investments | Less Than One Year | One to Three Years | Three to Five Years | Total |
|---|---|---|---|---|
| Local Agency Investment Fund | $12,596 | | | $12,596 |
| Money Market Funds (U.S. Securities) | 43,442 | | | 43,442 |
| Federal Agency Securities | 3,424,555 | $1,001,483 | $1,384,521 | 5,810,559 |
| Total Investments | $3,480,593 | $1,001,483 | $1,384,521 | 5,866,597 |
| *City of Napa Investment Pool (Overdraft)* | | | | 1,949,296 |
| Total Cash and Investments | | | | $7,815,893 |

**NOTE 3 - CASH AND INVESTMENTS (Continued)**

The Agency is a participant in the Local Agency Investment Fund (LAIF) that is regulated by California Government Code Section 16429 under the oversight of the Treasurer of the State of California. The Agency reports its investment in LAIF at the fair value amount provided by LAIF, which is the same as the value of the pool share. The balance is available for withdrawal on demand, and is based on the accounting records maintained by LAIF, which are recorded on an amortized cost basis. Included in LAIF's investment portfolio are collateralized mortgage obligations, mortgage-backed securities, other asset-backed securities, loans to certain state funds, and floating rate securities issued by federal agencies, government-sponsored enterprises, United States Treasury Notes and Bills, and corporations.

***D. Credit Risk***

Credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. As of June 30, 2011, the Agency's investments in Government Agency Securities and Money Market Funds were rated AAA and AAAm, respectively, as provided by Standard and Poor's investment rating system. The Local Agency Investment Fund is not rated.

***E. U.S. Credit Downgrade***

On August 5, 2011, Standard & Poor's Ratings Services (S&P) lowered its long-term credit rating on the United States of America from AAA to AA+. At the same time, S&P affirmed its A-1+ short-term rating on the United States of America.

On August 8, 2011, S&P lowered its issuer credit ratings and related issue ratings on ten of twelve Federal Home Loan Banks (FHLBs) and the senior debt issued by the FHLB System from AAA to AA+. S&P also lowered the ratings on the senior debt issued by the Federal Farm Credit Banks (FFCB) from AAA to AA+, and lowered the senior issue ratings on Fannie Mae (FNMA) and Freddie Mac (FHLMC) from AAA to AA+. The A subordinated debt rating and the C rating on the preferred stock of these entities remained unchanged. Finally, S&P affirmed the short-term issue ratings for these entities at A-1+.

## NOTE 3 - CASH AND INVESTMENTS (Continued)

### *F. Investments Authorized by the California Government Code and the Agency's Investment Policy*

The Investment Policy of the City and Agency, and the California Government Code, allow the Agency to invest in the following, provided the credit ratings of the issuers are acceptable to the Agency; and approved percentages and maturities are not exceeded. The table below also identifies certain provisions of the California Government Code or the Agency's Investment Policy where it is more restrictive:

| Authorized Investment Type | Maximum Maturity | Minimum Credit Quality | Maximum in Portfolio | Maximum Investment In One Issuer |
|---|---|---|---|---|
| Repurchase Agreements | 30 Days | N/A | 20% | 20% |
| State of California Local Agency Investment Fund (LAIF Pool) | Upon Demand | N/A | $40,000,000 | N/A |
| U.S. Treasury Bonds, Notes and Bills | 5 Years | N/A | None | None |
| U.S. Government Agency and U.S. Government-Sponsored Enterprise Obligations | 5 Years | N/A | None | None |
| Bankers' Acceptances | 180 Days | A-1, P-1 | 30% | Lesser of $2,000,000 or 5% |
| Commercial Paper | 270 Days | A | 25% | 5% |
| Negotiable Certificates of Deposit | 2 Years | A | 30% | $1,000,000 |
| Time Certificates of Deposit – Banks or Savings and Loans | 2 Years | N/A | None | $500,000 |
| Medium-Term Corporate Notes | 5 Years | A | 30% | 5% |
| Money Market Mutual Funds | N/A | AAA | 20% | 10% |

## NOTE 3 - CASH AND INVESTMENTS (Continued)

### G. *Investments Authorized by Debt Agreements*

The Agency must maintain required amounts of cash and investments with trustees or fiscal agents under the terms of certain debt issues. These funds are unexpended bond proceeds or are pledged reserves to be used if the Agency fails to meet its obligations under these debt issues. The California Government Code requires these funds to be invested in accordance with Agency resolutions, bond indentures or State statutes. The table below identifies the investment types that are authorized for investments held by fiscal agents. The bond indentures contain no limitations for the maximum investment in any one issuer or the maximum percentage of the portfolio that may be invested in any one investment type. The table also identifies certain provisions of these debt agreements:

| Authorized Investment Type | Maximum Maturity | Minimum Credit Quality |
|---|---|---|
| United States Treasury Bill, Bond, Notes | 5 years | None |
| United States Government Agency Obligations | 5 years | None |
| Federal Securities | 5 years | None |
| Bankers' Acceptance | 30 days | A-1 |
| Commercial Paper | 270 days | A-1+ |
| Certificates Deposit | 30 days | A-1 |
| Repurchase Agreement | None | A |
| Local Agency Investment Fund | N/A | None |
| Money Market Funds | N/A | AAm |
| Investment Agreement | None | AA |
| Prefunded Municipal Obligations | None | AAA |
| State Obligations | None | A |
| State Obligations - Direct Short-Term | None | A-1+ |
| State Obligations - Special Revenue Bonds | None | AA |

## NOTE 3 - CASH AND INVESTMENTS (Continued)

### *H. Concentration Risk*

Significant investments in the securities of any individual issuers, other than U. S. Treasury securities, or mutual funds are required to be disclosed when they exceeds five percent of the total portfolio. The Agency has a significant portion of its portfolio invested in Federal Agency Securities, as set forth below:

| Reporting Unit | Issuer | Investment Type | Reported Amount |
|---|---|---|---|
| **Entity- Wide:** | | | |
| | Federal National Mortgage Association | Federal Agency Securities | $1,917,021 |
| | Federal Home Loan Mortgage Corporation | Federal Agency Securities | 1,677,252 |
| | Federal Farm Credit Bank | Federal Agency Securities | 681,290 |
| | Federal Home Loan Bank | Federal Agency Securities | 1,534,996 |
| **Major- Funds:** | | | |
| Parkway Plaza - Low & Moderate Income Housing Special Revenue Fund | Federal National Mortgage Association | Federal Agency Securities | 25,278 |
| Parkway Plaza - Debt Service Fund | Federal National Mortgage Association | Federal Agency Securities | 580,812 |
| | Federal Home Loan Mortgage Corporation | Federal Agency Securities | 571,488 |
| | Federal Farm Credit Bank | Federal Agency Securities | 571,236 |
| | Federal Home Loan Bank | Federal Agency Securities | 266,828 |
| Parkway Plaza - Capital Projects Fund | Federal National Mortgage Association | Federal Agency Securities | 1,310,931 |
| | Federal Home Loan Mortgage Corporation | Federal Agency Securities | 1,084,598 |
| | Federal Home Loan Bank | Federal Agency Securities | 1,257,495 |

## NOTE 4 – INTERFUND TRANSACTIONS

During fiscal year -2011, Redevelopment Agency interfund transfers were as follows:

| Fund Receiving Transfer | Fund Making Transfer | Amount Transferred | Purpose |
|---|---|---|---|
| **Parkway Plaza** | **Parkway Plaza** | | |
| Low and Moderate Income Housing | Debt Service Fund | $1,132,078 | G |
| Capital Projects | Debt Service Fund | 6,630,063 | H |
| **Soscol Gateway** | **Soscol Gateway** | | |
| Low and Moderate Income Housing | Debt Service Fund | 114,879 | G |
| Debt Service | Capital Projects | 789,122 | B |
| Capital Projects | Debt Service Fund | 405,137 | H |
| | Total | $9,071,279 | |

Transfers between Napa Community Redevelopment Agency and the City

| | | | |
|---|---|---|---|
| ***Transfers to City:*** | | | |
| | **Parkway Plaza** | | |
| General Fund | Capital Projects | $585,536 | D |
| City Capital Projects | Capital Projects | 2,805,575 | D |
| Housing Fund | Debt Service Fund | 1,055,304 | C |
| | **Soscol Gateway** | | B |
| General Fund | Capital Projects | 11,265 | E |
| City Capital Projects | Capital Projects | 42,233 | D |
| | | $4,499,913 | |
| ***Contributions to City:*** | | | |
| | **Parkway Plaza** | | |
| General Fund | Debt Service Fund | $1,500,000 | A |
| Non Major Governmental Funds | Debt Service Fund | 48,958 | B |
| | | $1,548,958 | |
| ***Contributions from City:*** | | | |
| **Parkway Plaza** | | | |
| Capital Projects | Non Major Governmental Funds | $11,800 | F |

**Purpose:**

**A** Citywide Overhead
**B** Operations
**C** Fund Capital Projects
**D** Public Projects Financing Agreement with RDA
**F** Clay Street Parking Garage Elevator
**G** 20% Set Aside for Housing
**H** Fund RDA Capital Projects

## NOTE 4 – INTERFUND TRANSACTIONS (Continued)

Interfund balances are loans between funds to provide either short-term cash flow or funding for longer-term projects. June 30, 2011, the City provided the Agency $4,194,166 of short-term loans to cover cash flow.

In fiscal year 2008 - 2009 the City's Water Fund advanced the Soscol Gateway Debt Service Fund $725,000 to begin carrying out the five year implementation plan on the Soscol Gateway project. The advance bears 4% simple interest due annually, with the first payment due March 1, 2012 and the last payment due March 1, 2021. The Soscol Gateway Debt Service Fund then transferred the same amount to the Soscol Gateway Capital Projects Fund. Balance of this advance, including accrued interest, was $789,724 at June 30, 2011June 30, 2011.

## NOTE 5– RELATED PARTY TRANSACTIONS

Below is a summary of the major financial transactions among the Agency, the City, and the City of Napa Housing Authority (Authority) during fiscal -112011. The Agency and Authority are component units of the City and City Council is accountable for their operations.

*Reimbursement of Costs* – The Agency reimburses the City for various costs incurred by the City in its capacity of administering the Agency. During fiscal -11, the Agency remitted $540,666 to the City as reimbursement for payroll, management and other administrative expenditures which are included as general governmental expenditures on the Statement of Revenues, Expenditures and Changes in Fund Balance.

*Transfer to the Authority's Low and Moderate Income Housing Fund* – According to the provisions of Section 33334.6 of the State's Health and Safety Code, the Agency is required to set aside a minimum of 20% of its property tax increment revenues for low income housing. In fiscal 2010-11, the total set aside amount approximated 20% of the Agency's property for incremental revenues. The 20% set-aside for Parkway Plaza Project Area is used to pay debt service on 2003 Series B and C bonds and the net proceeds are then transferred to the Authority. Beginning in fiscal year 2009-10, the 20% set-aside from Soscol Gateway Project Area and any fund balance from fiscal year 2008-09 are to be transferred to the Authority on an annual basis. During the year ended June 30, 2011, the Agency expended $727,463 representing contributions to the Authority from such set aside revenues.

## NOTE 6 – CAPITAL ASSETS

All capital assets are valued at historical cost or estimated historical cost if actual historical cost is not available. Contributed capital assets are valued at their estimated fair market value on the date contributed.

Capital assets with limited useful lives are depreciated over their estimated useful lives. The purpose of depreciation is to spread the cost of capital assets equitably over the life of these assets. The amount charged to depreciation expense each year represents that year's pro rata share of the cost of capital assets. Depreciation is provided using the straight line method which means the cost of the asset is divided by its expected useful life in years and the result is charged to expense each year until the asset is fully depreciated. The Agency has assigned a useful life of 35 and 40 years for its buildings and improvements, and infrastructures, respectively.

## NOTE 7 – CAPITAL ASSETS

Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during the construction phase is reflected in the capitalized value of the asset constructed, net of interest earned on the invested proceeds over the same period.

The following is a summary of capital asset activity during the year ended June 30, 2011:

| | Balance at June 30, 2010 | Additions | Transfers to the City | Balance at June 30, 2011 |
|---|---|---|---|---|
| Capital assets not being depreciated: | | | | |
| Land | $3,674,854 | | ($3,639,374) | $35,480 |
| Construction in progress | 290,268 | $193,642 | | 483,910 |
| Total capital assets not being depreciated | 3,965,122 | 193,642 | (3,639,374) | 519,390 |
| Capital assets being depreciated: | | | | |
| Building and improvements | 9,146,663 | | | 9,146,663 |
| Equipment | 7,238 | | | 7,238 |
| Infrastructure: | | | | |
| Curb/gutter/sidewalks | 1,647,646 | | | 1,647,646 |
| Street lights | 1,407,671 | | | 1,407,671 |
| Total capital assets being depreciated | 12,209,218 | | | 12,209,218 |
| Less accumulated depreciation for: | | | | |
| Building and improvements | (5,955,769) | (195,489) | | (6,151,258) |
| Equipment | | (603) | | (603) |
| Infrastructure: | | | | |
| Curb/gutter/sidewalks | (98,311) | (41,191) | | (139,502) |
| Street lights | (101,712) | (35,192) | | (136,904) |
| Total accumulated depreciation | (6,155,792) | (272,475) | | (6,428,267) |
| Net capital assets being depreciated | 6,053,426 | (272,475) | | 5,780,951 |
| Governmental-type activities capital assets, net | $10,018,548 | ($78,833) | ($3,639,374) | $6,300,341 |

## NOTE 7 – CAPITAL ASSETS (Continued)

Depreciation expense is charged to functions and programs based on their usage of the related assets. In fiscal year 2011, depreciation expense, shown above as additions to accumulated depreciation, was charged to the Redevelopment Projects Program.

In March 2011, the Agency made required findings in accordance with Health and Safety Code Sections 33430 and 33220 to allow the conveyance of nineteen parcels that had been recorded as capital assets with a book value of $3,639,374 to the City. Included in this transfer was land that was purchased with Neighborhood Development Program (NDP) and Community Development Block Grant (CDBG) funds. The properties have been developed as the Second Street garage and two surface parking lots, one on Pearl Street, the other on Main Street. An NDP Close out Agreement dated April 4, 1978, between the City and the Agency requires that any proceeds from the disposition of the land acquired with NDP or CDBG funds are to be remitted to the CDBG Program of the City for reprogramming for redevelopment purposes.

## NOTE 8– LONG-TERM DEBT

Long-term debt activity for the year ended June 30, 2011, was as follows:

| | Original Issue Amount | Balance June 30, 2010 | Retirements | Balance June 30, 2011 | Current Portion |
|---|---|---|---|---|---|
| **Governmental Activity Debt:** | | | | | |
| **Redevelopment Tax Allocation Bonds** | | | | | |
| 2003A Parkway Plaza Redevelopment Project, 2.3-4.8%, due 9/1/2019 | $22,715,000 | $17,445,000 | $1,365,000 | $16,080,000 | $1,460,000 |
| 2003B Parkway Plaza Redevelopment Project, 3.1-5.8%, due 9/1/2019 | 2,475,000 | 1,730,000 | 130,000 | 1,600,000 | 145,000 |
| 2003C Refunding Parkway Plaza Redevelopment Project, 3.1-5.8%, due 9/1/2019 | 2,050,000 | 1,460,000 | 120,000 | 1,340,000 | 125,000 |
| Total Redevelopment Tax Allocation Bonds | | $20,635,000 | $1,615,000 | $19,020,000 | $1,730,000 |

In August, 2003, the Agency issued $27 million in tax allocation bonds as follows:

**Series A Bonds** were issued to provide $12 million for redevelopment projects, $2 million for a debt reserve fund and $9 million to refund then outstanding 1993 Bonds. The 1993 Bonds were subsequently redeemed in full.

The Pledge of future Agency tax increment revenues ends upon payment of the $19.7 million in remaining debt service on the Redevelopment Agency's long-term debt which is scheduled to occur in 2020. As disclosed in the originating offering documents, pledged future tax increment revenues are expected to provide coverage over debt service of 1.7 over the life of the long-term debt. For fiscal year 2011, Agency tax increment revenue amounted to $5,660,392 which represented coverage of 2.67 times over the $2,114,033 in debt service.

## NOTE 8 – LONG-TERM DEBT (Continued)

**Series B and C Bonds** were issued to provide $2.1 million for affordable housing projects and $1.8 million for the retirement of the Housing Authority's 1999 revenue bonds. Total net proceeds of $3.9 million have been committed by the Agency to the Housing Authority (See Note 5). These bonds are secured by the Agency's 20% low & moderate housing set-aside of tax increment revenues.

The Pledge of future Housing tax increment revenues ends upon payment of the $3.7 million in remaining debt service on the Redevelopment Agency's long-term debt which is scheduled to occur in 2020. As disclosed in the originating offering documents, pledged future tax increment revenues are expected to provide coverage over debt service of 1.7 over the life of the long-term debt. For fiscal year 2011 Housing tax increment revenue amounted to $1,132,078 which represented coverage of 2.76 times over the $409,775 in debt service.

The annual debt service requirements for the Agency's Tax Allocation Bonds are shown below:

| | Governmental Activities | |
|---|---|---|
| Fiscal year ending June 30 | Principal | Interest |
| 2012 | $1,730,000 | $844,536 |
| 2013 | 1,800,000 | 774,034 |
| 2014 | 1,915,000 | 696,518 |
| 2015 | 2,010,000 | 606,933 |
| 2016 | 2,100,000 | 507,883 |
| 2017-2021 | 9,465,000 | 943,151 |
| Total | $19,020,000 | $4,373,055 |

## NOTE 9 – NET ASSETS AND FUND BALANCES

### A. *Net Assets*

Net Assets, measured on the full accrual basis of accounting, is the excess of all the Agency's assets over all its liabilities. Net Assets are divided into the following categories:

*Invested in Capital Assets, net of related debt* describes the portion of Net Assets which is represented by the current net book value of the Agency's capital assets, less the outstanding balance of any debt issued to finance these assets. None of the Agency's capital assets have been acquired with outstanding debt.

*Restricted* describes the portion of net assets which is restricted as to use by the terms and conditions of agreements with outside parties, governmental regulations, laws, or other restrictions which the City cannot unilaterally alter. These principally include bond proceeds received for use on capital projects, debt service requirements, and special revenue programs subject to limitations defined regulations and laws underlying such programs.

## NOTE 9 – NET ASSETS AND FUND BALANCES (Continued)

*Unrestricted* describes remaining balance of Net Assets. The Agency reports deficit unrestricted net assets since its business purpose has to debt-finance infrastructure, community improvements owned by the organization, and affordable housing projects. Over time, the Agency's debt will be retired with the incremental property tax revenues generated form these improvements

Governmental fund balances represent the net current assets of each fund. Net current assets generally represent a fund's cash and receivables, less its liabilities.

The Agency's fund balances are classified in accordance with Governmental Accounting Standards Board Statement Number 54 (GASB 54), *Fund Balance Reporting and Governmental Fund Type Definitions,* which requires the Agency to classify its fund balances based on spending constraints imposed on the use of resources. For programs with multiple funding sources, the Agency prioritizes and expends funds in the following order: Restricted, Committed, Assigned, and Unassigned. Each category in the following hierarchy is ranked according to the degree of spending constraint:

*Nonspendable* represents balances set aside to indicate items do not represent available, spendable resources even though they are a component of assets. Fund balances required to be maintained intact, such as Permanent Funds, and assets not expected to be converted to cash, such as prepaids, notes receivable, and land held for redevelopment are included. However, if proceeds realized from the sale or collection of nonspendable assets are restricted, committed or assigned, then Nonspendable amounts are required to be presented as a component of the applicable category.

*Restricted* fund balances have external restrictions imposed by creditors, grantors, contributors, laws, regulations, or enabling legislation which requires the resources to be used only for a specific purpose. Encumbrances and nonspendable amounts subject to restrictions are included along with spendable resources.

*Committed* fund balances have constraints imposed by formal action of the Agency Board which may be altered only by formal action of the Agency Board. Encumbrances and nonspendable amounts subject to council commitments are included along with spendable resources. As of June 30, 2011, the Agency does not have committed fund balance.

*Assigned* fund balances are amounts constrained by the Agency's intent to be used for a specific purpose, but are neither restricted nor committed. Intent is expressed by the Agency Board or its designee and may be changed at the discretion of the Agency Board or its designee. This category includes encumbrances, Nonspendables, when it is the Agency's intent to use proceeds or collections for a specific purpose, and residual fund balances, if any, of Special Revenue, Capital Projects and Debt Service Funds which have not been restricted or committed.

*Unassigned* fund balance represents residual amounts that have not been restricted, committed, or assigned. This includes the residual general fund balance and residual fund deficits, if any, of other governmental funds.

## NOTE 10 – RISK MANAGEMENT FUND

The City has established its Risk Management Fund (an Internal Service Fund) to account for its self-insurance program. Under this program the City is self-insured for general liability insurance claims up to $150 thousand per occurrence. Claims in excess of these amounts up to $15 million are insured. The Agency is covered under the City's Risk Management Program.

## NOTE 11 – PASS-THROUGHS

In order to mitigate financial impacts on other property tax supported entities caused by the Agency's adoption of the Redevelopment Projects, the Agency must pass-through a portion of property tax increments to them. During fiscal 2010-2011, the Agency paid $1,053,722 to these agencies.

In addition to the above amounts, the Agency continues to dispute a portion of the pass-through payments, as it has since 2005-06, which brings the total disputed pass-through amount to $318,363. The dispute revolves around the methodology the County utilizes to calculate the pass-through payments. In 2010, the Attorney General rendered opinion No. 10-101 that supports redevelopment agencies' calculation of pass-throughs. Counties throughout California have not yet made adjustments or credited agencies for the disputed amounts as of December 2011.

## NOTE 12 – COMMITMENT AND CONTINGENCIES

*Hazardous Materials Investigation:* Toxic substances were discovered on an Agency-owned parking garage property during construction of a new hotel. The Agency has been working with the Regional Water Quality Control Board to define the extent of the problem and develop a monitoring program, while concurrently pursuing a settlement agreement with the polluters of the property. The Agency does not expect its portion of investigation costs, legal costs, and costs associated with any necessary cleanup to be material in relation to the financial statements.

The ownership of the Clay Street garage property was transferred from the Napa Community Redevelopment Agency to the City of Napa on March 24, 2011. The Agency and City continue to pursue site closure with the San Francisco Regional Water Quality Control Board and additional studies and information were submitted in August and November 2011 to meet Water Board information requests. The City is awaiting final determination from the Water Board on site closure request and discussions thus far have been positive.

## NOTE 13 – TAX INCREMENT SHIFT TO SUPPLEMENTAL EDUCATION REVENUE AUGMENTATION FUND (SERAF)

The State of California adopted AB26 4X in July 2009 which directs that a portion of the incremental property taxes received by redevelopment agencies be paid instead to the County supplemental educational revenue augmentation fund (SERAF) in fiscal years 2009-10 and 2010-11. The State Department of Finance determines each agency's SERAF payment by November 15 of each year, and payments are due by May 10 of the applicable year. The Agency made its first SERAF payment of $1,369,653 in fiscal year 2009-10, and its second payment in the amount of $281,987 in fiscal year 2010-11.

## NOTE 14 –SUBSEQUENT EVENT

In an effort to balance its budget, the State of California adopted ABx1 26 on June 28, 2011, which suspends all new redevelopment activities except for limited specified activities as of that date and dissolves redevelopment agencies effective October 1, 2011. The State simultaneously adopted ABx1 27 which allows redevelopment agencies to avoid dissolution by the City opting into an "alternative voluntary redevelopment program" requiring specified substantial annual contributions to local schools and special districts. Concurrently with these two measures, the State passed various budget and trailer bills that are related and collectively constitute the Redevelopment Restructuring Acts. If all sponsoring communities were to opt-in to the voluntary program, these contributions amount to an estimated $1.7 billion for fiscal year 2012 and an estimated $400 million in each succeeding year. If the City fails to make the voluntary program payment, the Agency would become subject to the dissolution provisions of ABx1 26.

On July 18, 2011, the California Redevelopment Association, the League of California Cities and others challenged the validity and constitutionality of ABx1 26 and 27 to the California Supreme Court on numerous grounds, including that the acts violate certain provisions of the California Constitution. On August 11, 2011, as modified on August 17, 2011, the California Supreme Court agreed to hear the case and issued a partial stay of ABx1 26 and a full stay of ABx1 27, but the stay did not include the section of ABx1 26 that suspends all new redevelopment activities. It is anticipated that the Court will render its decision before January 15, 2012, the date the first voluntary program payment is due.

The suspension provisions of ABx1 26 prohibit all redevelopment agencies from a wide range of activities, including incurring new indebtedness or obligations, entering into or modifying agreements or contracts, acquiring or disposing of real property, taking actions to adopt or amend redevelopment plans and other similar actions, except actions required by law or to carry out existing enforceable obligations, as defined in ABx1 26. During the suspension period, an agency is required to prepare an Enforceable Obligation Payment Schedule no later than August 29, 2011, that allows it to continue to pay certain obligations. The Agency adopted its Enforceable Obligation Payment Schedule on August 26, 2011.

In addition, the suspension provisions require the State Controller to review the activities of all redevelopment agencies to determine whether an asset transfer between an agency and any public agency occurred on or after January 1, 2011. If an asset transfer did occur and the public agency that received the asset is not contractually committed to a third party for the expenditure or encumbrance of the asset, the State Controller is required to order the asset returned to the redevelopment agency. The State Controller's Office has not yet provided any information about the timing or the process for this statewide asset transfer review.

The Agency is currently subject to the suspension provisions as described above. These facts indicate that there is more than a remote possibility the Agency may not continue as a going concern beyond October 1, 2011. The continuation of the Agency beyond October 1, 2011 will initially depend upon whether the Supreme Court rules in favor of the petitioners. There are three possible consequences to the Agency from a decision of the Supreme Court, when it is rendered:

## NOTE 14 –SUBSEQUENT EVENT (Continued)

1. If the Supreme Court determines that both ABx1 26 and ABx1 27 are valid, then the City will consider whether it will enact an ordinance to opt-in to the alternative voluntary redevelopment program. If enacted, the City would be required to make annual payments to the County Auditor-Controller and the Agency would no longer be subject to the suspension provisions. The State Department of Finance calculated the City's Voluntary Program payment for fiscal year 2012 to be $1,524,902. The City filed an appeal of that amount in accordance with the provisions of Health and Safety Code Section 34194(b)(2)(L), however the State has denied the City's appeal.

2. If the Supreme Court determines that both ABx1 26 and ABx1 27 are valid and the City decides not to participate in the alternative voluntary redevelopment program, or if the Supreme Court determines that ABx1 26 is valid, but ABx1 27 is not valid, the Agency will continue to be subject to the suspension provisions and would be dissolved in accordance with certain provisions of ABx1 26. Prior to dissolution, any transfers of Agency assets subsequent to January 1, 2011 to the City, that were not obligated to third parties or encumbered may be subject to the State Controller's review discussed above and required to be returned to the Agency. Upon dissolution, all assets and obligations of the Agency would be transferred to a successor agency.

3. If the Supreme Court determines that both ABx1 26 and ABx1 27 are invalid, the Agency would no longer be subject to the suspension provisions and would continue in existence under California Redevelopment Law as it existed prior to the enactment of ABx1 26 and ABx1 27.

As of December 20, 2011, the Supreme Court has not ruled on the case and the Agency is subject to the suspension provisions as discussed above.

## SUPPLEMENTAL INFORMATION

NAPA COMMUNITY REDEVELOPMENT AGENCY
EXCESS SURPLUS CALCULATION

Excess surplus is defined in Health and Safety Code Section 33334.12(b) as any unexpended and unencumbered amount in an Agency's Low and Moderate Income Housing Fund that exceeds the greater of $1,000,000 or the aggregate amount deposited into the Low and Moderate Income Housing Fund during the preceding four fiscal years, as of the beginning of the fiscal year.

If excess surplus exists, the Agency must lawfully spend the excess or transfer it to a housing authority or other public agency in the following fiscal year, expend or encumber in the next two fiscal years or face sanctions. Essentially, agencies have a three-year window to expend, encumber, or transfer the excess surplus.

| | | Low and Moderate Income Housing Funds -- All Project Areas July 1, 2010 |
|---|---|---|
| **Opening Fund Balance -- July 1, 2010** | | $719,007 |
| **Less Unavailable Amounts:** | | |
| Encumbrances (Section 33334.12(g)(2)) | $432,625 | |
| | | (432,625) |
| Available Low and Moderate Income Housing Funds | | 286,382 |
| **Limitation (greater of $1,000,000 or four years set-aside)** | | |
| Set-Aside for last four years - fiscal years ended: | | |
| June 30, 2010 | 1,289,875 | |
| June 30, 2009 | 994,926 | |
| June 30, 2008 | 907,617 | |
| June 30, 2007 | 693,787 | |
| Total | $3,886,205 | |
| Base limitation | $1,000,000 | |
| Greater amount | | 3,886,205 |
| **Computed Excess Surplus - July 1, 2010** | | None |

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# 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*

Members of the Governing Board of
Napa Community Redevelopment Agency
Napa, California

We have audited the financial statements of Napa Community Redevelopment Agency (Agency), a component unit of the City of Napa, California, as of and for the year ended June 30, 2011, and have issued our report thereon dated December 20, 2011. The report included a special emphasis paragraph concerning proposed redevelopment dissolution and the implementation of Governmental Accounting Standards Board Statement Number 54 (GASB 54), *Fund Balance Reporting and Governmental Fund Type Definitions*. 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***

Management of the Agency is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Agency's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Agency's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Agency's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the Agency's financial statements will not be prevented, or detected and corrected on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

***Compliance and Other Matters***

As part of obtaining reasonable assurance about whether the Agency's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant 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.

As part of our audit, we prepared and issued our separate Memorandum on Internal Control dated December 20, 2011, which is an integral part of our audit and should be read in conjunction with this report.

This report is intended solely for the information and use of management, Agency Board, others within the Agency, the State Controller's Office, federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Maze & Associates

December 20, 2011

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**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH THE CALIFORNIA HEALTH AND SAFETY CODE AS REQUIRED BY SECTION 33080.1**

Members of the Governing Board of
Napa Community Redevelopment Agency
Napa, California

***Compliance***

We have audited Napa Community Redevelopment Agency's compliance with the California Health and Safety Code as required by Section 33080.1 for the year ended June 30, 2011. Compliance with the requirements referred to above is the responsibility of the Agency's management. Our responsibility is to express an opinion on the Agency's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and *Guidelines for Compliance Audits of California Redevelopment Agencies, June 2011*, issued by the State Controller.

Those standards require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the compliance requirements referred to above that could have a material effect on the Agency has occurred. An audit includes examining, on a test basis, evidence about the Agency's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the Agency's compliance with those requirements.

In our opinion, the Agency complied, in all material respects, with the compliance requirements referred to above that are applicable for the year ended June 30, 2011.

***Internal Control Over Compliance***

Management of the Agency is responsible for establishing and maintaining effective internal control over compliance with the compliance requirements referred to above. In planning and performing our audit, we considered the Agency's internal control over compliance to determine the auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Agency's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be deficiencies, significant deficiencies, or material weaknesses in internal control over compliance.

We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

This report is intended solely for the information and use of management, Agency Board, others within the Agency, the State Controller's Office, federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Maze & Associates

December 20, 2011