

**REDEVELOPMENT AGENCY
OF THE CITY OF MONTEREY
BASIC COMPONENT UNIT FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2010**

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**REDEVELOPMENT AGENCY
OF THE CITY OF MONTEREY**

**Basic Component Unit Financial Statements
June 30, 2010**

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INDEPENDENT AUDITORS' REPORT

Board of Directors
Redevelopment Agency of the City of Monterey
Monterey, CA

We have audited the financial statements of the governmental activities and each major fund of the Redevelopment Agency of the City of Monterey, a component unit of the City of Monterey, as of and for the year ended June 30, 2010, which collectively comprise the Redevelopment Agency of the City of Monterey's basic financial statements as listed in the table of contents. These basic financial statements are the responsibility of the Redevelopment Agency of the City of Monterey's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with U.S. generally accepted auditing standards 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 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.

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities and each major fund of the Redevelopment Agency of the City of Monterey as of June 30, 2010, and the respective changes in financial position, where applicable, and the budgetary comparison for the special revenue fund for the year then ended in conformity with U.S. generally accepted accounting principles.

Management's Discussion and Analysis is supplementary information required by the Governmental Accounting Standards Board, but is not a required part of the basic financial statements. We have applied certain limited procedures to this information, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information, but we did not audit this information and we express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 23, 2010 on our consideration of the Redevelopment Agency of the City of Monterey'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.

R. J. Ricciardi, Inc.

R.J. Ricciardi, Inc.
Certified Public Accountants

San Rafael, California
December 23, 2010

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REDEVELOPMENT AGENCY OF THE CITY OF MONTEREY

(A Component Unit of the City of Monterey, California)

MANAGEMENT'S DISCUSSION AND ANALYSIS

Please read this overview in conjunction your reading of the accompanying Basic Financial statements.

A. THE PURPOSE OF THE AGENCY

The Agency is a component unit of the City of Monterey; it is controlled by the City, which appoints the Agency's Board of Directors. City employees perform all the duties and functions required of the Agency.

The Agency's purpose under California law is to eliminate urban blight in the City of Monterey; it is given certain powers under the law to assist it in that endeavor. The Agency may not assess or receive property taxes, but it may receive any increases in property taxes over amounts received in the year before the property in the Agency's area became subject to redevelopment (called the Base Year). The increases are called Property Tax Increments. One-fifth of the property tax increments received must be used to increase the supply of low and moderate-income housing.

B. FISCAL YEAR 2009-10 FINANCIAL HIGHLIGHTS

Financial highlights of the year include the following:

- Agency general revenues were \$8,213,279.
- Low & Moderate Income Housing Fund revenues of \$2,659,570 were \$1,124,024 more than the prior year, while expenditures of \$891,718 were \$1,626,507 less than the prior year; ending fund balance increased \$1,767,852.
- Debt Service Fund revenues of \$6,629,321 were \$211,421 more than the prior year, while expenditures of \$4,826,243 were \$1,681,446 less than the prior year.

C. THE BASIC FINANCIAL STATEMENTS

The Basic Financial Statements comprise the Agency-wide Financial Statements and the Fund Financial Statements; these two sets of financial statements provide two 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, and comprise the Statement of Net Assets and the Statement of Activities. The Statement of Net Assets provides information about the financial position of the Agency as a whole, including all its capital assets and long-term liabilities on the full accrual basis, similar to that used by corporations. The Statement of Activities provides information about all the Agency's revenues and all its expenses, also on the full accrual basis, with the emphasis on measuring net revenues or expenses of each the Agency's programs. The Statement of Activities explains in detail the change in Net Assets for the year.

All of the Agency's activities are grouped into Government Activities.

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

REDEVELOPMENT AGENCY OF THE CITY OF MONTEREY

(A Component Unit of the City of Monterey, California)

Major Funds account for the major financial activities of the Agency and are presented individually with subordinate schedules presenting the detail for each of these other funds. The Agency reports both of its Funds as Major Funds; their purpose is explained in Note 1.C. to the financial statements.

The Agency-wide Financial Statements

The Statement of Net Assets and the Statement of Activities present information about the following:

- **Governmental activities**—All of the Agency's basic services are considered to be governmental activities, including general government and community development. These services are supported by general Agency revenues such as property tax increments.

Agency-wide financial statements are prepared on the accrual basis, which means they measure the flow of all economic resources of the Agency as a whole.

Fund Financial Statements

The Fund Financial Statements provide detailed information about each of the Agency's most significant funds, called Major Funds. Each Major Fund is presented individually. Major Funds present the major activities of the Agency for the year, and may change from year to year as a result of changes in the pattern of Agency's activities.

All the Agency's Funds are Governmental Funds; financial statements for these Funds are prepared on the modified accrual basis, which means they measure only current financial resources and uses. Capital assets and other long-lived assets, along with long-term liabilities, are not presented in the Governmental Fund Financial Statements.

Comparisons of Budget and Actual financial information are presented only for the Low & Moderate Income Housing Fund; the Debt Service Fund is not budgeted.

D. FINANCIAL ACTIVITIES OF THE AGENCY AS A WHOLE

This analysis focuses on the net assets and changes in net assets of the Agency's Governmental Activities in the Agency-wide Statement of Net Assets and Statement of Activities that follow.

The Agency's net deficit from governmental activities declined to a deficit of \$19,320,958 in 2010 from a deficit of \$25,892,154 in 2009. It is important to note that the reason for this deficit is the accounting treatment required for the Repayment Agreement the Agency has with the City that amounted to \$36,691,700 at June 30, 2010. This is the amount owed by the Agency to the City for capital assets and other expenditures made by the City on the Agency's behalf. The Agency has no capital assets as all assets constructed with Agency funds are transferred to the City under capital leases. Therefore, the Repayment Agreement liability is the primary component of the Agency's unrestricted net assets deficit.

The positive \$4,860,308 Change in Net Assets reflected in the Statement of Activities was due to a number of factors including:

- Cash and investments, including with fiscal agent, increased by \$4,493,032 largely due to sales of Low/Mod income units at Ocean Harbor House. These units will be replaced in the coming year(s).
- Long-term debt and interest payable declined \$2,364,989 as no new debt was issued and repayments of that amount were made on existing debt.
- The Repayment Agreement balance declined \$1,126,774 as payments were made to the City.

REDEVELOPMENT AGENCY OF THE CITY OF MONTEREY

(A Component Unit of the City of Monterey, California)

- Restricted net assets totaled \$14,213,152 at June 30, 2010, all of which may only be used for low-and moderate-income-housing.
- Unrestricted net assets is normally the part of net assets that can be used to finance day-to-day operations without constraints established by debt covenants or other legal requirements. However, it also includes long-term debt issued to finance infrastructure and capital assets that have been transferred to the City of Monterey.

Fiscal Year 2009-10 Government Activities

The Agency's fiscal 2010 revenue came primarily from property tax increments, which amounted to \$6,290,353, an increase of \$178,404 over the prior year. Investment earnings contributed an additional \$264,942 in fiscal 2010, an increase of \$4,832.

Agency expenses of \$3,352,972 in fiscal 2010 were for interest (\$181,629), administration (\$2,279,625) and community development (\$891,718).

E. THE AGENCY'S FUND FINANCIAL STATEMENTS

At June 30, 2010, the Agency's governmental funds reported a combined fund balance of \$16,478,368, which is an increase of \$5,281,819 compared with last year. The Low & Moderate Income Housing Fund accounts for \$14,213,152 in fund balance, while the Debt Service Fund reflected a fund balance of \$2,265,216.

The increase in fund balance resulted mainly sales of Low/Mod income housing in the Low and Moderate Income Housing Fund.

The Agency makes loans to qualified moderate-income residents or employees of the City to assist in the purchase of their principal residence. At June 30, 2010, the outstanding balance of these loans was \$1,547,339. Interest on these loans is at below market rates, and principal payments are deferred if the properties are occupied by qualified individuals.

The Agency also has agreed to provide project subsidy loans; the balance on these loans at June 30, 2010 was \$8,257,848.

All these loans are accounted for in the Low & Moderate Income Housing Fund and explained in detail in Note 3 to the financial statements.

F. DEBT ADMINISTRATION

Each of the Agency's debt issues is discussed in detail in Note 5 to the financial statements. At June 30, the Agency's debt comprised of one Revenue Bond issue (1999) with interest rates of from 4.30% to 4.6%, secured by property tax increment revenues.

ECONOMIC OUTLOOK AND MAJOR INITIATIVES

The Agency's primary revenue source is property tax increments, as discussed above. These increments are expected to continue to increase as property values in the Redevelopment area increase. However, as a component unit of the City of Monterey, the Agency's economic outlook and major initiatives are tied to those of the City,

REDEVELOPMENT AGENCY OF THE CITY OF MONTEREY

(A Component Unit of the City of Monterey, California)

which are discussed in detail in the City's Transmittal Letter and Management's Discussion & Analysis segments of its Comprehensive Annual Financial Report for the year ended June 30, 2010.

CONTACTING THE AGENCY'S FINANCIAL MANAGEMENT

These financial statements are intended to provide citizens, taxpayers, investors and creditors with a general overview of the Agency's financial condition and results of operations. Questions should be directed to the Finance Department at City Hall, Monterey, CA 93940.

REDEVELOPMENT AGENCY OF THE CITY OF MONTEREY

(A Component Unit of the City of Monterey, California)

AGENCY-WIDE FINANCIAL STATEMENTS

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 the Agency's 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 Agency's net assets, by subtracting total liabilities from total assets.

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

The Agency's Governmental Activities include the activities of its Debt Service Fund.

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.

REDEVELOPMENT AGENCY
OF THE CITY OF MONTEREY
STATEMENT OF NET ASSETS
JUNE 30, 2010

	<u>Governmental Activities</u>
ASSETS	
Cash and investments available for operations	\$ 4,761,930
Restricted cash and cash equivalents	2,486,448
Interest receivable	58,376
Due from other funds	-
Project subsidy loans	8,257,848
Down payment assistance loans	1,547,339
Capital lease receivable	3,765,000
Property held for resale	<u>374,803</u>
Total Assets	<u>21,251,744</u>
LIABILITIES	
Accounts payable and accrued liabilities	87,184
Interest payable	28,818
Long term debt:	
Due within one year	1,275,000
Due in more than one year	<u>39,181,700</u>
Total Liabilities	<u>40,572,702</u>
NET ASSETS (DEFICIT)	
Restricted for:	
Low and Moderate Income Housing	<u>14,213,152</u>
Total Restricted Net Assets	<u>14,213,152</u>
Unrestricted	<u>(33,534,110)</u>
Total Net Assets	<u>\$ (19,320,958)</u>

See accompanying notes to financial statements

REDEVELOPMENT AGENCY
OF THE CITY OF MONTEREY
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2010

<u>Functions/Programs</u>	
Governmental Activities:	
General government	\$ 2,279,625
Community development	891,718
Interest on long term debt	<u>181,629</u>
 Total program expenses	 <u>3,352,972</u>
General revenues:	
Taxes: Property tax increment	6,290,353
Investment income	264,942
Rental income	46,667
Interest portion of facility lease	350,138
Other	<u>1,261,179</u>
 Total general revenues	 <u>8,213,279</u>
 Change in Net Assets	 4,860,307
Net Assets-Beginning (as restated)	<u>(24,181,266)</u>
Net Assets-Ending	<u>\$ (19,320,958)</u>

See accompanying notes to financial statements

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REDEVELOPMENT AGENCY OF THE CITY OF MONTEREY

(A Component Unit of the City of Monterey, California)

FUND FINANCIAL STATEMENTS

Fund Financial Statements are compiled so that only individual major funds are presented, 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; no distinction is made between Fund types.

MAJOR GOVERNMENTAL FUNDS

The Redevelopment Agency of the City of Monterey determined all its funds to be major funds, as follows:

LOW AND MODERATE INCOME HOUSING FUND

This fund accounts for revenue sources legally restricted for expenditures for the specified purposes of low and moderate income housing.

DEBT SERVICE FUND

This fund accounts for tax increment revenues, bond proceeds and related interest income required to be set aside for future debt service. The fund is used to repay principal and interest on indebtedness of the Agency. Debt service funds are referred to as "Special Funds" by the California Health and Safety Code and the Agency's bond resolutions.

REDEVELOPMENT AGENCY
OF THE CITY OF MONTEREY
GOVERNMENTAL FUNDS
BALANCE SHEET
JUNE 30, 2010

	Low and Moderate Income Housing Special Revenue	Debt Service	Total Governmental Funds
ASSETS			
Cash and investments available for operations	\$ 2,884,102	\$ 1,877,828	\$ 4,761,930
Restricted cash and cash equivalents	581,948	1,904,500	2,486,448
Interest receivable	42,791	15,585	58,376
Due from other funds	-	-	-
Advances to other funds	1,472,383	-	1,472,383
Project subsidy loans	8,257,848	-	8,257,848
Down payment assistance loans	1,547,339	-	1,547,339
Capital lease receivable	-	3,765,000	3,765,000
Property held for resale	374,803	-	374,803
	<u>\$ 15,161,214</u>	<u>\$ 7,562,913</u>	<u>\$ 22,724,127</u>
LIABILITIES			
Accounts payable and accrued liabilities	\$ 26,870	\$ 60,314	\$ 87,184
Advances from other funds	-	1,472,383	1,472,383
Deferred revenue	921,192	3,765,000	4,686,192
	<u>948,062</u>	<u>5,297,697</u>	<u>6,245,759</u>
FUND BALANCES			
Fund balances			
Reserved for:			
Encumbrances	100,904	-	100,904
Long-term receivables	9,805,187	-	9,805,187
Property held for resale	374,803	-	374,803
Advances to other funds	1,472,383	-	1,472,383
Debt Service Funds	-	2,265,216	2,265,216
Unreserved:			
Special Revenue Funds	2,459,875	-	2,459,875
	<u>14,213,152</u>	<u>2,265,216</u>	<u>16,478,368</u>
Total Fund Balances	<u>14,213,152</u>	<u>2,265,216</u>	<u>16,478,368</u>
Total Liabilities and Fund Balances	<u>\$ 15,161,214</u>	<u>\$ 7,562,913</u>	<u>\$ 22,724,127</u>

See accompanying notes to financial statements

REDEVELOPMENT AGENCY
 OF THE CITY OF MONTEREY
 RECONCILIATION OF THE
 GOVERNMENTAL FUNDS -- BALANCE SHEET
 WITH THE
 STATEMENT OF NET ASSETS
 JUNE 30, 2010

Total fund balances (deficits) reported on the governmental funds balance sheet \$ 16,478,368

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:

ACCRUAL OF NON-CURRENT REVENUES AND EXPENSES

Revenues which are deferred on the Fund Balance Sheets because they are not available currently
 are taken into revenue in the Statement of Activities. 4,686,192

LONG TERM ASSETS AND LIABILITIES

The assets and liabilities below are not due and payable in the current period and therefore are not
 reported in the Funds:

Long-term debt due within one year	(1,275,000)
Long-term debt in more than one year	(39,181,700)
Interest payable	<u>(28,818)</u>

NET ASSETS OF GOVERNMENTAL ACTIVITIES \$ (19,320,958)

See accompanying notes to financial statements

REDEVELOPMENT AGENCY
OF THE CITY OF MONTEREY
GOVERNMENTAL FUNDS
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE
FOR THE YEAR ENDED JUNE 30, 2010

	Low and Moderate Income Housing Special Revenue	Debt Service	Total Governmental Funds
REVENUES:			
Property tax increment	\$ 1,249,483	\$ 5,040,870	\$ 6,290,353
Investment income	125,056	139,886	264,942
Rental income	46,667	-	46,667
Facility lease	-	1,425,750	1,425,750
Other	1,238,364	22,815	1,261,179
	<u>2,659,570</u>	<u>6,629,321</u>	<u>9,288,891</u>
Total Revenues			
EXPENDITURES:			
Current:			
General government	-	2,254,875	2,254,875
Community development	891,718	-	891,718
Payment on advances	-	1,126,774	1,126,774
Non-current:			
Principal	-	1,230,000	1,230,000
Interest	-	189,844	189,844
Fiscal charges	-	24,750	24,750
	<u>891,718</u>	<u>4,826,243</u>	<u>5,717,961</u>
Total Expenditures			
NET CHANGE IN FUND BALANCES	1,767,852	1,803,078	3,570,930
Beginning Fund Balances (as restated)	<u>12,445,300</u>	<u>462,138</u>	<u>12,907,438</u>
Ending Fund Balances	<u>\$ 14,213,152</u>	<u>\$ 2,265,216</u>	<u>\$ 16,478,368</u>

See accompanying notes to financial statements

REDEVELOPMENT AGENCY
 OF THE CITY OF MONTEREY
 RECONCILIATION OF THE
 NET CHANGE IN FUND BALANCES - TOTAL GOVERNMENTAL FUNDS
 WITH THE
 STATEMENT OF ACTIVITIES
 FOR THE YEAR ENDED JUNE 30, 2010

The schedule below reconciles the Net Changes in Fund Balances reported on the Governmental Funds Statement of Revenues, Expenditures and Changes in Fund Balance, which measures only changes in current assets and current liabilities on the modified accrual basis, with the Change in Net Assets of Governmental Activities reported in the Statement of Activities, which is prepared on the full accrual basis.

NET CHANGE IN FUND BALANCES - TOTAL GOVERNMENTAL FUNDS	\$ 3,570,930
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Amounts reported for governmental activities in the Statement of Activities are different because of the following:

LONG TERM DEBT PROCEEDS AND PAYMENTS

Repayment of long term debt is an expenditure in the governmental funds, but in the Statement of Net Assets the repayment reduces long-term liabilities.

Repayment of debt principal, bonds	1,230,000
Repayment of debt principal, Repayment Agreement	1,126,774
Interest payable attributed to prior fiscal year	37,033
(reduction in interest payable from last year of \$8,215, \$37,033-\$28,818)	

ACCRUAL OF 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):

Deferred revenue	(1,075,612)
(Current year deferred revenue less current year principal payment and prior year deferred revenue, (\$921,192-\$1,230,000-\$766,804)	
Interest payable	(28,818)

CHANGE IN NET ASSETS OF GOVERNMENTAL ACTIVITIES	\$ 4,860,307
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See accompanying notes to financial statements

REDEVELOPMENT AGENCY
OF THE CITY OF MONTEREY
LOW AND MODERATE INCOME HOUSING SPECIAL REVENUE FUND
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE
BUDGET AND ACTUAL
FOR THE YEAR ENDED JUNE 30, 2010

	Budget Amounts		Actual Amounts	Variance with
	Original	Final		Final Budget Positive (Negative)
REVENUES:				
Property tax increment	\$ 837,515	\$ 837,515	\$ 1,249,483	\$ 411,968
Investment income	100,000	100,000	125,056	25,056
Rental income	46,667	46,667	46,667	-
Other	-	-	1,238,364	1,238,364
Total Revenues	984,182	984,182	2,659,570	1,675,388
EXPENDITURES:				
Current:				
Community development	11,397,779	11,397,779	891,718	10,506,061
NET CHANGE IN FUND BALANCE	<u>\$ (10,413,597)</u>	<u>\$ (10,413,597)</u>	1,767,852	<u>\$ 12,181,449</u>
Beginning Fund Balance (as restated)			<u>12,445,300</u>	
Ending Fund Balances			<u>\$ 14,213,152</u>	

See accompanying notes to financial statements

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. ORGANIZATION AND PURPOSE

The Redevelopment Agency of the City of Monterey was created under the provisions of the Community Redevelopment Law (California Health and Safety Code) to redevelop certain areas in the City of Monterey. The Custom House Redevelopment plan was originally adopted in July 1961 and was amended in March 1980 to provide an improved physical, social and economic environment in the Agency's project area. The Cannery Row Redevelopment Plan and the Greater Downtown Monterey Redevelopment Plan were adopted in July 1981 and July 1983 respectively. The Agency is authorized to finance the Plan from various sources, including assistance from the City, the State and federal governments, property tax increments, interest income and the issuance of Agency bonds.

The Agency is an integral part of the City of Monterey and the accompanying component unit financial statements are included as a component unit of the basic financial statements prepared by the City.

B. BASIS OF PRESENTATION

The Agency's Basic Financial Statements are prepared in conformity with accounting principles generally accepted in the United State of America. The Governmental 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.

Agency-wide Statements: The Statement of Net Assets and the Statement of Activities include the financial activities of the overall Agency. Eliminations have been made to minimize the double counting of internal activities.

The Statement of Activities presents a comparison between direct expenses and those revenues that are classified as general revenues, including all taxes and investment income.

Fund Financial Statements: The fund financial statements provide information about the Agency. Separate statements for each governmental fund are presented. The emphasis of fund financial statement is on major individual funds, each of which is displayed in a separate column.

C. 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. The Agency considers all its funds to be major governmental funds. A summary of these funds follows:

Low and Moderate Income Housing Special Revenue Fund – This fund accounts for revenue sources legally restricted for expenditures for the specified purposes of low and moderate income housing.

Debt Service Fund – The Debt Service Fund accounts for tax increment revenues, bond proceeds and related interest income required to be set aside for future debt service. The funds are used to repay principal and interest on indebtedness of the Agency. Debt service funds are referred to as "Special funds" by the California Health and Safety Code and the Agency's bond resolutions.

D. BASIS OF ACCOUNTING

The Agency-wide financial statements are reported using the *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.

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 thirty days after year-end. Expenditures are recorded when the related fund liability is incurred, except for claims and judgements and principal and interest on long-term debt. Revenues susceptible to accrual are interest revenue, certain other intergovernmental revenues, and certain charges for services.

Proceeds of governmental long-term debt and acquisitions under capital leases are reported as *other financing sources* in governmental funds.

Non-exchange transactions, in which the City gives or receives value without directly receiving or giving equal value in exchange, include grants, entitlements, and donations. Revenue from grants, entitlements, and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied.

Other revenues susceptible to accrual include taxes, intergovernmental revenues, interest and charges for services.

E. CASH EQUIVALENTS

The Agency considers all highly liquid restricted investments with a maturity of three months or less when purchased to be cash equivalents.

F. BUDGETARY REPORTING AND BUDGETARY ACCOUNTING

The Agency follows these procedures in establishing the budgetary data reflected in the component unit financial statements.

1. Prior to June 30, the Treasurer submits to the Agency Board a proposed operating budget for the fiscal year commencing the following July 1. The operating budget includes proposed expenditures and means of financing them.
2. Public hearings are conducted to obtain taxpayer comments.
3. The budget is legally enacted through passage of a resolution during the second Board meeting in the month of June.
4. The Executive Director is authorized to transfer budgeted amounts; however, any revisions that alter the total expenditures of any fund must be approved by the Agency Board.
5. Formal budgetary integration is employed as a management control device during the year for the Special Revenue fund. Budgets are adopted on a basis consistent with generally accepted accounting principles.

Budget amounts are as amended by the Agency Board.

G. ENCUMBRANCES

Under encumbrance accounting, purchase orders, contracts and other commitments for the expenditure of monies are recorded in order to reserve that portion of the applicable appropriation. Encumbrance accounting is employed as an extension of formal budgetary integration. Encumbrances outstanding at year-end are reported as reservations of fund balance since they do not constitute expenditures or liabilities. Outstanding encumbrances at year-end are automatically reappropriated the following year. Unencumbered and unexpended appropriations lapse at year-end, except capital projects.

H. FUND BALANCES

Fund balances represent the net current assets of each fund. Net current assets generally represent a fund’s cash and receivables, less its liabilities. Portions of a fund’s balance may be reserved or designated for future expenditure.

Reserves are restrictions placed by outside entities, such as other governments, which restrict the expenditures of the reserved funds to the purpose intended by the entity which provided the funds. The Agency cannot modify or remove these restrictions or reserves.

Designations are imposed by the Agency Board to reflect future spending plans or concerns about the availability of future resources. Designations may be modified, amended or removed by Board action.

I. PROPERTY TAXES

Monterey County assesses properties and bills, collects, and distributes property taxes as follows:

	<u>Secured</u>	<u>Unsecured</u>
Valuation dates	March 1	March 1
Lien/levy dates	January 1	January 1
Due dates	50% on November 1 and March 1	July 1
Delinquent as of	December 10 & April 10	August 31

The term “unsecured” refers to taxes on personal property other than real estate, land and buildings. These taxes are secured by liens on the property being taxed. Property tax revenues are recognized by the Agency in the fiscal year they are assessed, provided they become available as defined above.

J. PROPERTY HELD FOR RESALE

As part of its Low & Moderate Income Housing Program, the Redevelopment Agency purchases and sells affordable homes in the City to low/moderate income homebuyers in accordance with the affordable housing program. Homes are sold at below-market prices, but the Agency has the right of first refusal when the purchasers wish to resell these homes to the Agency at approximately the same price and in the same condition, which the Agency may accept or decline. Homes owned by the Agency are accounted for at cost, which is below market.

NOTE 2 - CASH AND INVESTMENTS

A. DEPOSITS AND INVESTMENTS

The Agency's cash is partially included in a City-wide cash and investments pool, the details of which are presented in the City's basic financial statements and in this footnote, sections A through G. 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.

Investments are reported in the accompanying financial statements at fair value. Changes in fair value that occur during the fiscal year are recognized as investment income reported for that fiscal year. Investment income includes interest earnings, changes in fair value, and any gains or losses realized upon the liquidation or sale of investments.

The City of Monterey pools cash and investments of all funds and component units, except for assets held by fiscal agents. The Agency's share in this pool is displayed in the accompanying financial statements as cash and investments. Investment income earned by the pooled investments is allocated monthly to the various funds and component units based upon monthly cash and investment balances.

The Agency's investments held by fiscal agents are pledged for repayment or as security for certain long-term debt issuances. The California Government Code provides that these monies, in the absence of specific statutory provisions governing the issuance of bonds, may be invested in accordance with the ordinance, resolutions or indentures specifying the types of investments made by its trustee or fiscal agents. As of June 30, 2010, the Redevelopment Agency had the following investments:

Cash invested by City of Monterey	\$4,761,930
Cash and Investments held by fiscal agent:	
Cash invested with trustee	581,948
Investment Agreement	<u>1,904,500</u>
Total Cash and Investments	<u><u>\$7,248,378</u></u>

B. AUTHORIZED INVESTMENTS

See the City's financial statements for the year ended June 30, 2010 for disclosure on authorized investments.

C. INTEREST RATE RISK

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. One of the ways that the City of Monterey manages its exposure to interest rate risk is by purchasing a combination of shorter term and longer term investments and by timing cash flows from maturities so that a portion of the portfolio is maturing or coming close to maturity evenly over time as necessary to provide the cash flow and liquidity needed for operations.

Information about the sensitivity of the fair values of the Agency's investments (including investments held by bond trustee) to market interest rate fluctuations is provided by the disclosures in the notes to the basic

financial statements of the City of Monterey that show the distribution of the City's investments by maturity.

D. CREDIT RISK

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligations to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. Agency investments are not rated.

E. CONCENTRATION OF CREDIT RISK

The Agency did not have any investments in any one issuer (other than U.S. Treasury securities, mutual funds, and investment pools) that represent 5% or more of total investments for the entire entity (or for each separate major fund) for the fiscal year ended June 30, 2010.

F. CUSTODIAL CREDIT RISK

Custodial Credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty (e.g., broker-dealer) to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party.

California Law requires banks and savings and loan institutions to pledge government securities with a market value of 110% of the Agency's cash on deposit or first trust deed mortgage notes with a value of 150% of the deposit as collateral for these deposits. Under California Law, this collateral is held in the City of Monterey's name and places the City ahead of general creditors of the institution. The City has waived collateral requirements for the portion of deposits covered by federal deposit insurance.

NOTE 3 – LOANS RECEIVABLE

A. DOWN PAYMENT ASSISTANCE LOANS

At fiscal year end, the Agency had \$1,547,339 in Down Payment Assistance Loans. These are loans to qualified moderate income residents of the City or qualified moderate income individuals employed in the City for up to 15% of the purchase price of a residence in the City (to a maximum of \$50,000). Such loans bear simple interest at 5% per annum, with principal and interest deferred for the first fifteen years. At the end of fifteen years the City reviews the income status of the borrower. Based on such review, the balance of the loan is payable in monthly installments over a period of up to 15 years, or deferred for an additional period of five years with repayment upon sale or transfer of the residence. Due to the long-term nature of the interest receivable, interest on the loans is recorded only when it becomes available as net current assets. Since these loans are not currently available for expenditure, fund balance has been reserved in this amount.

B. PROJECT SUBSIDY LOANS

At fiscal year end, the Agency had \$8,257,848 in Project Subsidy Loans, which includes accrued interest.

In October of 1997, the Agency entered into a Development Agreement and Ground Lease with a developer for the C-21 Redevelopment Mixed Use Project in the Custom House Redevelopment Project Area. Under the terms of the agreement, the developer constructed a theater/retail complex, which

included affordable housing units. The developer agreed to provide on-site management of the housing units. The Agency agreed to provide a project subsidy loan of \$2,565,000 to implement the project. No principal or interest repayment is required until 2018.

In April 2003, the Agency authorized a loan with a developer for the construction of 21 units of affordable workforce rental housing. Under the terms of the agreement, the Agency loaned \$2,235,000, at 3% interest per annum for a term of thirty (30) years, fully amortized, with monthly payments of approximately \$9,696 per month. The agreement is secured by deed of trust.

In July 2007 the City entered into a development agreement to provide a loan for the development of 18 affordable rental units in the Monterey Hotel Mixed-Use Project, on a vacant lot in the Old Town Redevelopment Project Area. As of June 30, 2010, the City has provided \$2,757,699 from Redevelopment Housing Set-Aside funds. This project is currently in a receivership status. An Inter-creditor Agreement was executed authorizing the Redevelopment Agency and Receiver to process a parcel map condominium plan for purpose of securing the RDA loan on a separate single condominium airspace parcel containing the projects 18 affordable apartment units. All parties in the project are actively working to complete the parcel map and condominium plan. The parcel map and supporting documents are expected to record prior to the end of the calendar year.

NOTE 4 – INTERFUND TRANSACTIONS

During the year ended June 30, 1987, the Special Revenue Fund advanced \$1,472,383 to the Debt Service Fund to meet its debt service requirements. The advance carries no interest and, although there is an agreement to repay, the advance has no definite repayment schedule.

NOTE 5 – CAPITAL LEASES RECEIVABLE

The Agency has entered into long-term agreements with the City of Monterey to lease land and buildings acquired with bond proceeds. Revenue from such lease agreements is used to finance the Agency’s debt service requirements. The leases are accounted for as capital leases because at the end of the lease period, the leased assets become the property of the City. A summary of the capital lease revenues receivable at June 30, 2010, follows:

For the fiscal year ended June 30:		
	<u>2011</u>	1,416,255
	2012	1,418,168
	2013	1,181,564
	Total Payments Due	<u>\$4,015,987</u>
	Less amounts representing interest	<u>250,987</u>
Total		<u><u>\$3,765,000</u></u>

\$3,765,000 of deferred revenue on the Agency’s balance sheet represents the principal portion of capital leases receivable, to be recognized as revenue when payments under capital lease agreements are received by the Agency. An additional \$921,192 of deferred revenue is comprised of interest on deferred project subsidy loans.

NOTE 6 – LONG TERM DEBT

A. LEASE REVENUE BONDS

The Agency's revenue bond balances and transactions were as follows:

	Balance June 30, 2009	Retirements	Balance June 30, 2009	Due Within One Year
Lease Revenue Bonds				
1999 Redevelopment Agency, 4.30-4.6%, due 11/1/12	\$ 4,995,000	\$ 1,230,000	\$ 3,765,000	\$ 1,275,000

In May 1999, the Agency issued \$19,045,000 of 1999 Lease Revenue Bonds with interest rates ranging from 3.0% to 4.6% to advance refund the outstanding balance of the Agency's 1992 and 1993 Lease Revenue Bonds and to provide funds to repay the Columbarium loan of the City's Cemetery Enterprise Fund. The proceeds of the 1999 Refunding Bonds, along with bond reserve monies held by Trustees for the 1992 and 1993 bonds were used to purchase U.S. government securities which were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the 1992 and 1993 refunded bonds. As a result, the 1992 and 1993 refunded bonds were considered to be defeased and the liability for those obligations was removed from the Agency's financial statements. There is no longer an outstanding balance on these defeased bonds.

The Lease Revenue Bonds are special obligations of the Agency and are secured by the Agency's property tax increment revenues. Annual debt service requirements as of June 30, 2010 for the Agency's lease revenue bonds are shown below:

	For the year Ending June 30	Principal	Interest	Total
2011		1,275,000	141,255	1,416,255
2012		1,335,000	83,168	1,418,168
2013		1,155,000	26,564	1,181,564
		<u>\$3,765,000</u>	<u>\$250,987</u>	<u>\$4,015,987</u>

B. REPAYMENT AGREEMENT

At fiscal year end, the Agency's repayment agreement liability was \$36,691,700. This agreement was authorized in December 1993 by the City Council and Redevelopment Agency Board of Directors to reimburse the City for certain costs incurred on behalf of the Agency. The Repayment Agreement covers assets constructed by the City in the redevelopment areas, assets leased to the City from the Agency and projects paid for with debt financing. The Repayment Agreement requires the Agency to make repayments annually of essentially all available cash; repayments of \$1,126,774 were made in fiscal 2010.

NOTE 7 – JOINT POWERS AGREEMENT

The Agency and the City of Monterey formed the City of Monterey Joint Powers Financing Authority in 1997. The purpose of the Authority is to provide financing for the public improvements for the City, to

acquire such public capital improvements and to lease such public capital improvements. Complete financial statements for the Authority can be obtained from the City of Monterey, City Hall, Monterey, CA 93940.

NOTE 8 – PRIOR PERIOD ADJUSTMENTS

A previously unrecorded loan receivable in the Low/Mod Income Housing Fund required a \$1,710,889 prior period adjustment to the City-wide Net Assets and the Statements of Revenues, Expenditures and Changes in Fund Balance for the Governmental funds. This amount was incorrectly recorded as an expenditure during fiscal year 2008/09 and 2009/10.

AGENCY WIDE FINANCIAL STATEMENTS

Statement of Activities

Ending Net Assets, as reported on June 30, 2009	(25,892,154)
Adjustment for previously unrecorded loan receivable	<u>1,710,888</u>
Beginning Net Assets, as restated, July 1, 2009	<u><u>(24,181,266)</u></u>

FUND FINANCIAL STATEMENTS

Governmental Funds

Statement of Revenues, Expenditures and Changes in Fund Balance	Low and Moderate Income Housing Special Revenue
Ending Fund Balances, as reported on June 30, 2009	<u>10,734,411</u>
Adjustment for previously unrecorded loan receivable	<u>1,710,888</u>
Beginning Fund Balances, as restated July 1, 2009	<u><u>12,445,299</u></u>

Low and Moderate Income Housing Special Revenue Fund
Statement of Revenues, Expenditures and Changes in Fund Balance

Ending Fund Balances, as reported on June 30, 2009	<u>10,734,411</u>
Adjustment for previously unrecorded loan receivable	<u>1,710,888</u>
Beginning Fund Balances, as restated July 1, 2009	<u><u>12,445,299</u></u>

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

Board of Directors
Redevelopment Agency of the City of Monterey
Monterey, California

We have audited the basic financial statements of the Redevelopment Agency of the City of Monterey, a component unit of the City of Monterey, as of and for the year ended June 30, 2010, and have issued our report thereon dated December 23, 2010. We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Redevelopment Agency of the City of Monterey's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the basic financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Redevelopment Agency of the City of Monterey's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Redevelopment Agency of the City of Monterey'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 misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control, such there is a reasonable possibility that a material misstatement of the Redevelopment Agency of the City of Monterey's basic financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of the 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 Redevelopment Agency of the City of Monterey's basic 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. Such provisions included those provisions of laws identified in the *Guidelines for Compliance Audits of California Redevelopment Agencies*, issued by the State Controller and as interpreted in the *Suggested Auditing Procedures for Accomplishing Compliance Audits of California Redevelopment Agencies*, issued by the Governmental Accounting and Auditing Committee of the California Society of Certified Public Accountants. 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*. However, we noted certain matters that we reported to management of the Redevelopment Agency of the City of Monterey in a separate letter dated December 23, 2010.

This report is intended solely for the information and use of the audit committee, management, Board of Directors, and 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.

R.J. Ricciardi, Inc.

R.J. Ricciardi, Inc.
Certified Public Accountants

San Rafael, California
December 23, 2010