# HERCULES REDEVELOPMENT AGENCY

## FINANCIAL STATEMENTS

## JUNE 30, 2010

**HERCULES REDEVELOPMENT AGENCY**
**Financial Statements**
**June 30, 2010**

## TABLE OF CONTENTS

MOSS, LEVY & HARTZHEIM LLP
CERTIFIED PUBLIC ACCOUNTANTS

PARTNERS
RONALD A LEVY, CPA
CRAIG A HARTZHEIM, CPA
HADLEY Y HUI, CPA

9107 WILSHIRE BLVD., SUITE 400
BEVERLY HILLS, CA 90210
TEL: 310.273.2745
FAX: 310.273.1689
www.mlhcpas.com

## INDEPENDENT AUDITOR'S REPORT

Members of the Board of the Hercules Redevelopment Agency
Hercules Redevelopment Agency
Hercules, California

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

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the basic financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the basic 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 opinions.

In our opinion, the basic 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 Agency as of June 30, 2010, and the respective changes in financial position thereof, for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1 of the notes to the basic financial statements effective July 1, 2009, the Hercules Redevelopment Agency adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*; GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*; GASB Statement No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*; and GASB Statement No. 58, *Accounting and Financial Reporting for Chapter 9 Bankruptcies*.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 29, 2010, on our consideration of the Agency's internal control over financial reporting and 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 on financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting and compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 10, the Schedules of Revenues, Expenditures, and Changes in Fund Balances – Budget and Actual – Redevelopment Agency Operating Special Revenue Fund on page 40, and Affordable Housing Special Revenue Fund on page 41 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Agency's basic financial statements as a whole. The Schedules of Revenues, Expenditures, and Changes in Fund Balances – Budget and Actual – Redevelopment Agency Debt Service Fund on page 43 and Redevelopment Agency Capital Projects Fund on page 44 are presented for purposes of additional analysis and are not required parts of the financial statements. These schedules are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

The accompanying financial statements have been prepared assuming that the Agency will continue as a going concern. As discussed in Note 14 to the financial statements, the Agency has suffered a deficit during the fiscal year and has a net assets deficit of $48,448,511 at June 30, 2010. The Redevelopment Agency Operating Special Revenue Fund and Affordable Housing Special Revenue Fund also have fund deficits of $8,065,251 and $2,173,320 respectively at June 30, 2010. The Agency's tax increment revenue was insufficient to pay the current year's debt service. These conditions raise substantial doubt about its ability to continue as a going concern. Management's plans regarding those matters also are described in Note 14. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

Moss, Levy & Hartzheim

Moss, Levy & Hartzheim, LLP
Beverly Hills, California
December 29, 2010, except for loans receivable, construction in progress, due to the City of Hercules, deferred revenue, and advances from the City of Hercules, as to which the date is April 11, 2011.

*City of Hercules Redevelopment Agency*

*Management's Discussion and Analysis*

*For The Fiscal Year Ended June 30, 2010*

The management of the City of Hercules Redevelopment Agency (the Agency) offers readers of the Agency's Financial Statements this narrative overview and analysis of the basic financial activities of the Agency for the fiscal year ended June 30, 2010.

Governmental Accounting and Standards Board Statement No. 34, "Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments", known as GASB 34, requires, among other things, that the Agency provide this management discussion and analysis of its financial activities for the fiscal year. GASB 34 represents an effort to make governmental reporting clearer and more understandable to readers. It allows a reader to focus on longer term financial issues as well as short-term financial aspects of the Agency. This document should be read in conjunction with the accompanying Basic Financial Statements, including the notes to those statements to get a complete picture of the Agency's finances.

## I. Financial Highlights

This year the Agency's assessed property values continued to decrease in the merged project area and is reflected in the associated decrease in tax increment revenue. As a result, revenue was not sufficient to cover debt related expenses and to provide funding for both housing and non-housing priorities. Shortfalls were made up by one time borrowing from other City funds. It is anticipated that this interim remedy cannot continue and therefore, the City is taking significant measures to ensure expenditures are aligned with revenues. Should these measures fall short, some additional borrowing from City funds may be necessary.

### Projects

*Waterfront Project* - The 42 acre Waterfront Project continues to move forward. During the second half of 2009-2010, the City held several public workshops to develop conceptual design for the Intermodal Transit Center including the train station building and public plaza. Throughout the fiscal year the City coordinated the design development with several key stakeholders and funding partners which included, Capital Corridor Joint Powers Authority (CCJPA), Union Pacific Railroad, AMTRAK, WestCAT, Water Emergency Transit Authority, East Bay Regional Park District, Bio-Rad and Hercules Bayfront LLC. The City has secured $22 million in committed grant funds and continues to search for additional grant opportunities.

Project design components were developed in close cooperation with stakeholders and approving agencies. In cooperation with the Federal Transportation Authority the City coordinated the preparation of an Environmental Impact Report (EIR) and Environmental Impact Statement (EIS). Seven construction bid packages were advanced to the 90% design level including plans and specifications.

*Extension of the Merged Project Area* - In June of 2009, the Agency's Board, upon the recommendation of the Redevelopment Agency, adopted the 2009 Hercules Redevelopment Plan Amendment (Ordinance No. 450) which added the Sycamore Crossings and Hill Town sites (58 acres) to the merged project area. The Ordinance also extended the time limit on the effectiveness of the Dynamite Plan, the time limit on the payment of indebtedness and the receipt of property taxes by an additional period of ten (10) years. Finally, it reinstated eminent domain powers on limited and defined portions of the Dynamite Redevelopment Project for a period of twelve (12) years.

It is anticipated that the 2009 Amendment will result in substantial benefit to the public and will contribute to the revitalization of blighted areas through increased economic vitality and additional housing and commercial opportunities.

*Land Held For Resale* - The Agency is researching the opportunity for development of its 17-acre parcel, acquired from Wal-Mart, and its 6.37-acre parcel at San Pablo Avenue at Victoria Crescent, with the objective of providing opportunities for biotech, research and development, and manufacturing businesses to expand or relocate from other Bay Area locations. These two parcels have the potential to expand the existing North Shore Business Park.

*Sycamore Crossing* - Just south of the Gelsar/RFI/Lewis site, the Agency continued land-use planning and engineering studies on the 11-acre "Sycamore Crossings" site, which will provide retail, commercial, and hospitality opportunities in an urban format of blocks and streets. The design work to relocate the 24-inch waterline to San Pablo Avenue is complete. The design work for the relocation of the two 24-inch sanitary sewer lines has been completed and is under construction.

*Sycamore North* - At the former Gelsar/RFI/Lewis site, construction continued on the mixed use "Sycamore North" project. Upon completion, it is proposed that the project will provide affordable and market-rate housing units along with 36,046 square feet of leasable shop front retail space.

*New Town Center* - Entitlements were obtained in February 2009 for the 35-acre New Town Center transit-oriented district. The district received new General Plan land use designation and zoning for higher-density mixed use around transit. The conveyance of the Park-N-Ride parcel to a Developer under the 2005 Disposition Development Agreement (DDA) occurred in August, 2009.

The Agency also pursued the civil engineering and environmental studies in support of obtaining approvals from Caltrans for the relocation of freeway access ramps around the New Town Center district. Caltrans approved the Project Study Report (PSR) in June 2010. Finally, the Agency purchased a 3.8 acre improved parcel for the purpose of relocating a Caltrans maintenance facility which is now located within the New Town Center district.

*Palm Project* - The site design for the Palm Commercial Center has been completed and is ready for entitlement.

## Other Financial Information

The following are the amounts received from tax increments in fiscal year 2009-10 with comparative totals for the previous five fiscal years:

| Fiscal Year Receipt | 2004-05 | 2005-06 | 2006-07 | 2007-08 | 2008-09 | 2009-10 |
|---|---|---|---|---|---|---|
| Total for the Fiscal Year | $9,449,358 | $10,366,886 | $13,409,462 | $13,473,319 | $12,750,860 | $10,405,553 |

As of June 30, 2010, Agency's assets were $143.9 million and liabilities were $192.4 million. The liabilities exceeded assets by $48.4 million (Net Assets). This was a decrease of $15.9 million (49%) from prior year of negative $32.5 million. The factors impacting the negative net assets are the contribution of capital assets from construction-in-progress projects that are taking place in the Redevelopment Project Areas as mentioned above and advances from the City to the Redevelopment Agency.

As of June 30, 2010, the Agency's funds (all governmental) reported combined ending fund balances of $28.4 million as opposed to $67.3 million in 2009, representing a decrease of $38.9 million or 58%.

Agency's total net debt increased $2.5 million (1%) during the fiscal year. The reason for this increase was the advances from the City of Hercules in the amount of $2.9 million to provide financing for the New Town Center Project, $2.6 million interest on all the advances from the City and annual repayments of $3.3 million made for bonded debt, notes payable, and advances from the City.

## II. Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the Agency's basic financial statements. The City of Hercules Redevelopment Agency basic financial statements are comprised of three components: 1) Government-Wide Financial Statements, 2) Fund Financial Statements, and 3) Notes to the Basic Financial Statements.

The basic financial statements include only the Agency, which is a component unit of the City and is reported in the City's Comprehensive Annual Financial Report (CAFR) using the blended method.

Government-Wide Financial Statements: The Government-Wide Financial Statements are statements required by GASB 34 that present the financial picture of the Agency and provide readers with a broad view of the Agency's finances. These statements present governmental activities and include all assets of the Agency (including capital assets) as well as all liabilities (including long-term debt). Additionally, certain interfund receivables, payables, and other interfund activity have been eliminated as prescribed by GASB 34.

The Statement of Net Assets and the Statement of Activities report information about the Agency as a whole and about its activities. These statements include *all* assets and liabilities of the Agency using the *accrual basis of accounting,* which is similar to the accounting used by most private-sector companies. All of the current year's revenues and expenses are taken into account, regardless of when cash is received or paid.

The Statement of Net Assets presents information on all of the Agency's assets and liabilities, with the difference between the two reported as net assets. The Agency, while a separate legal entity, acts as a financial conduit for the City and as such does not hold title to the assets it helps construct. Therefore, its net assets are not necessarily any indication of its financial health.

The Statement of Activities presents information showing how the government's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes). Additionally, certain interfund receivables, payables, and other interfund activity have been eliminated as prescribed by GASB 34.

The Agency only has governmental activities, including public works related activity and administration, which are reflected in the Statement of Net Assets and the Statement of Activities. Property tax increment and interest income finance these activities.

Fund Financial Statements: The Agency, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Fund Financial Statements provide detailed information about the Agency's most significant funds, called Major Funds. The concept of Major Funds, and the determination of which are Major Funds, was established by GASB 34 and replaces the concept of combining like funds and presenting them in total.

Instead, each Major Fund is presented individually, with all Non-major Funds combined in a single column on each fund statement. Subordinate schedules present the detail of these Non-major Funds. Major Funds present the major activities of the Agency for the fiscal year. All funds have been determined to be major funds.

Fund Financial Statements are prepared on the modified accrual basis of accounting, which means they measure only current financial resources and uses. Additionally, one will find the capital assets and other long-lived assets, along with long-term liabilities presented only in the Government-Wide Financial Statements.

The Agency's Major Funds include the Operating Fund, the Capital Projects Fund, the Debt Service Fund and the Affordable Housing Fund and are reported in detail in the Fund Financial Statements.

> *Operating Special Revenue Fund:* The Operating Special Revenue Fund is used to account for staff time and other operating costs of the Agency (e.g., non-capital studies or analysis and other consultants)
>
> *Capital Projects Fund:* The Capital Projects Fund is used to account for the capital expenditures of the Agency, other than housing.
>
> *Debt Service Fund:* The Debt Service Fund is used to account for the repayment of principal and interest on debt as well as pass through obligations to other taxing agencies or non-taxing entities.
>
> *Affordable Housing Fund:* The Affordable Housing Fund is used to account for the 20% set aside of the tax increment that is required by State Law to be used for low and moderate income housing purposes.

In order to better understand the Agency's long-term and short-term requirements, it is useful to compare the Agency's Governmental Fund Statements with the governmental activities in the Government-Wide Financial Statements. A reconciliation is provided for both the Governmental Funds Balance Sheet to the Government-Wide Statement of Net Assets, and the Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances to the Government-Wide Statement of Activities to facilitate this comparison.

The Agency adopts an annual appropriated budget for all of its funds. A set of budgetary comparison schedules has been provided to demonstrate compliance with this budget on pages 36 through 40 of this report.

Notes to the Basic Financial Statements: The notes provide additional information that is essential to a full understanding of the data provided in the Government-Wide and Fund Financial Statements. The notes to the basic financial statements can be found on pages 21 through 38 of this report.

Other Information: In addition to the basic financial statements and accompanying notes, this report also presents certain Required Supplementary Information concerning the Agency's budget to actual results in its Special Revenue Funds. Required Supplementary Information can be found on pages 39 through 41 of this report.

## III. Government-Wide Financial Analysis

The largest portion of the Agency's net assets reflects amounts invested in capital assets (e.g., land, buildings, machinery, and equipment). Unlike most other types of governmental bodies, which provide day-to-day services, the main purpose of the Agency is to provide capital funds for the development of a certain geographical area of the City.

The following analysis focuses on the net assets and changes in net assets of the Agency's Governmental Activities, presented in the Government-Wide Statement of Net Assets and Statement of Activities.

**Redevelopment Agency Net Assets**
At June 30,
(Amounts expressed in millions of dollars)

| | 2010 | 2009 |
|---|---|---|
| Current assets | $ 45.1 | $ 81.1 |
| Noncurrent assets | 98.8 | 73.8 |
| Total assets | 143.9 | 154.9 |
| Current liabilities | 22.3 | 19.7 |
| Noncurrent liabilities | 170.0 | 167.7 |
| Total liabilities | 192.3 | 187.4 |
| Net assets: | | |
| Invested in capital assets, net of related debt | | |
| Restricted | 48.8 | 82.2 |
| Unrestricted | (97.2) | (114.7) |
| Total net asset (deficit) | $ (48.4) | $ (32.5) |

The Agency's total net assets decreased $15.9 million during the fiscal year. The decrease was primarily attributable to $2.4 million decline in tax increment, $1.9 million decline in use of money and property, $5.0 million Supplemental Educational Revenue Augmentation Fund ("SERAF") obligation, $5.6 million of additional debt advanced by the City, and the $4.4 million of completed capital assets transferred to the City..

**Redevelopment Agency**
**Changes in Net assets**
Fiscal year ended June 30,
(Amounts expressed in millions of dollars)

| | 2009-10 | 2008-09 |
|---|---|---|
| General Revenues and Transfers: | | |
| Property tax (tax increment) | $ 10.4 | $ 12.8 |
| Investment Income | 0.1 | 2.0 |
| Miscellaneous and transfers | 2.6 | (0.1) |
| Total general revenues and transfers | 13.1 | 14.7 |
| Net expenses | 28.9 | 33.0 |
| Change in net assets (decrease) | (15.8) | (18.3) |
| Net assets, July 1, | (32.5) | 9.7 |
| Prior Period Adjustment | (0.1) | (23.9) |
| Net assets - July 1, restated | (32.6) | (14.2) |
| Net assets - June 30, | $ (48.4) | $ (32.5) |

Tax increment revenues decreased by $2.4 million (18%) because of the downturn in property values and a decreased development growth in the merged project area. Declined interest rates created less use of money and property. Expenditures decreased by $4.1 million from prior fiscal year due to less capital projects completed and transferred to the City.

## IV. Financial Analysis of the Agency's Funds

As noted earlier, the Agency uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental funds: The focus of the Agency's Governmental Funds is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the Agency's financing requirements. In particular, unreserved fund balances may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year. It should, however, be noted that most of the unreserved amounts have been designated by the Agency for specific uses.

- *Operating Special Revenue Fund:* This fund has a deficit fund balance of $8.1 million, which is a decrease $8.5 million from fiscal year 2009. The fund had $8.4 million in revenue (19% decrease), $10.5 million in expenditures (118% increases) and $6.5 million net transfer out for debt service payment (38% decrease).

- *Affordable Housing Fund:* The Agency is required by State law to set aside 20% of the tax increment revenue in a separate fund for low and moderate-income housing purposes. This fund had total revenue of $2.3 million and expenditures/transfers out of $4.5 million. Transfer out included $2.0 million for 2007 A and B Allocation Bonds repayments. The ending fund balance was negative $2.2 million, a decrease of $1.3 million from the prior fiscal year. The decrease in the fund balance was due in part to the acquisition of three foreclosed properties through the homeownership retention program and the activity in the first time homebuyers program.

- *Debt Service Fund:* The debt service fund had total revenues, proceeds from issuance of long-term debt and transfers-in in the amount of $10.7 million. The expenditures including debt service principal and interest and pass-through payments to other taxing agencies amounted to $13.6 million. The fund balance decreased by $27.3 million due primarily to the transferring out of bond proceeds from the 2005 Tax Allocation Bonds, 2007 A and B Tax Allocation Bonds and 2007 Series A Tax Allocation Bonds for completion and construction in progress of redevelopment capital projects.

- *Capital Project Fund*: Fund balance decreased by $1.8 million (34%) to $3.5 million. The fund had $29.3 million in expenditures for capital projects including major ones like Intermodal Transit Center, Sycamore North Project, and the acquisition of the yellow freight parcel.

## V. Budgetary Highlights

The original budget was from a one year budget and was structured differently than how the Agency ultimately accounted for its programs. The funds were restructured, and the budget was redistributed to those new funds. There were adjustments of $11.3 million to the budgets during the fiscal year that included projects and programs from Operating Special Revenue Fund, Affordable Housing Fund Debt Service Fund and Capital Project Fund.

The Agency's Operating Fund original revenue budget was $5.3 million more than actual. The variance was primarily due to the additional drop in assessed property valuation. At the same time, expenditures increased over projections as a result of the $5.0 million for the Supplemental Educational Revenue Augmentation Fund (SERAF) obligation. The combined effects contributed to the downward variance of $8.2 million on the Fund Balance, which dropped to negative $8.1 million.

The $26 million downward variance between budget-to-actual transfers out in the Capital Project Fund was attributed to the extension of phasing of several major projects.

## VI. Capital Asset and Debt Administration

<u>Capital assets:</u> As noted earlier the Agency acts as financial conduit for the City of Hercules and as a result, its investments in capital assets are usually recorded as City assets rather than Agency assets.

The capital expenditures during the fiscal year were minimal with money being spent on the Sycamore Downtown project and the train station project. Most of the year was spent in planning the development of the coming projects.

<u>Long-term debt:</u> At the end of the current fiscal year, the Agency had total debt outstanding of $173.7 million. The tax increment revenue of the Agency secures all debt of the Agency.

The Agency's bonded debt decreased by $3.3 million during the fiscal year. The decrease was due to the scheduled annual repayment of existing debt.

Additional information on the Agency long-term debt can be found in note number 6 on pages 30 through 34 of this report.

## VII. Economic Factors and Next Year's Budgets

The Agency's primary source of revenue is tax increment. Property values and new construction in the redevelopment area are the key economic factors that define the future resources of the Agency. The Agency does have some undeveloped land and there are discussions with developers underway to develop those parcels. As a result, any revenue growth is expected to come from those developments over the next few years with increases attributable to growth in assessed value.

Additionally, it is anticipated that with the adoption of the 2009 Hercules Redevelopment Plan Amendment and the potential to extend debt out another 10 years, that the Agency will be in a better position to eliminate the deficit fund balances in the Operating Special Revenue Fund and the Affordable Housing Funds.

These factors were considered in preparing the Agency's one year budget for the fiscal year 2010-11.

## Requests for Information

This financial report is designed to provide a general overview of the City of Hercules Redevelopment Agency's finances for residents, taxpayers, investors, creditors, and anyone else with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Finance Department, 111 Civic Drive, Hercules, California 94547. A copy of this financial report is also located at the City's website at http://www.ci.hercules.ca.us, by selecting "Finance" under "Department & Services" and then selecting "Comprehensive Annual Financial Reports".

# BASIC FINANCIAL STATEMENTS

# GOVERNMENT-WIDE FINANCIAL STATEMENTS

# HERCULES REDEVELOPMENT AGENCY

STATEMENT OF NET ASSETS

June 30, 2010

| | Governmental Activities |
|---|---|
| **ASSETS** | |
| Current assets: | |
| Cash and investments | $ 882,264 |
| Cash and investments with fiscal agents | 38,331,928 |
| Accounts receivable | 139,244 |
| Interest receivable | 530,285 |
| Land held for resale | 5,214,077 |
| Total current assets | 45,097,798 |
| Noncurrent assets: | |
| Loans receivable | 11,907,825 |
| Deferred charges - net of accumulated amortization | 3,741,744 |
| Total other noncurrent assets | 15,649,569 |
| Capital assets: | |
| Non-depreciable: | |
| Land | 31,657,561 |
| Construction in progress | 44,955,988 |
| Depreciable: | |
| Land improvements, buildings and improvements, machinery and equipment, and infrastructure | 9,326,325 |
| Less: accumulated depreciation | (2,781,667) |
| Total capital assets | 83,158,207 |
| Total noncurrent assets | 98,807,776 |
| **Total assets** | 143,905,574 |
| **LIABILITIES** | |
| Current liabilities: | |
| Accounts payable | 9,679,735 |
| Accrued wages | 61,072 |
| Accrued interest payable | 2,664,715 |
| Due to City of Hercules | 6,296,844 |
| Long-term debt - due within one year | 3,585,925 |
| Total current liabilities | 22,288,291 |
| Noncurrent liabilities: | |
| Advances from the City of Hercules | 38,531,655 |
| Long-term debt - due in more than one year | 131,534,139 |
| Total noncurrent liabilities | 170,065,794 |
| **Total liabilities** | 192,354,085 |
| **NET ASSETS** | |
| Restricted for: | |
| Capital projects | 39,901,805 |
| Affordable housing | 8,880,547 |
| Unrestricted | (97,230,863) |
| **Total net assets** | $ (48,448,511) |

See Accompanying Notes to Basic Financial Statements

# HERCULES REDEVELOPMENT AGENCY

STATEMENT OF ACTIVITIES

For the Fiscal Year Ended June 30, 2010

| | | Program Revenues | | |
|---|---|---|---|---|
| Functions/Programs | Expenses | Charges for Services | Capital Contributions and Grants | Net (Expense) Revenue and Change in Net Assets |
| Governmental activities: | | | | |
| Community development | $ 19,761,523 | $ 98,686 | $ - | $ (19,662,837) |
| Interest on long-term debt | 9,232,764 | | | (9,232,764) |
| Total governmental activities | $ 28,994,287 | $ 98,686 | $ - | (28,895,601) |
| General Revenues: | | | | |
| Taxes and assessments | | | | 10,405,553 |
| Use of money and property | | | | 83,527 |
| Miscellaneous revenue | | | | 88,891 |
| Transfer from City of Hercules | | | | 2,431,133 |
| Total general revenues and transfers | | | | 13,009,104 |
| Change in net assets | | | | (15,886,497) |
| Net assets, July 1, 2009 | | | | (32,509,773) |
| Prior period adjustments | | | | (52,241) |
| Net assets, July 1, 2009, restated | | | | (32,562,014) |
| Net assets, June 30, 2010 | | | | $ (48,448,511) |

See Accompanying Notes to Basic Financial Statements

## GOVERNMENTAL FUND FINANCIAL STATEMENTS

**Redevelopment Agency Operating Special Revenue Fund**
This fund accounts for the operating costs of the Redevelopment Agency.

**Affordable Housing Special Revenue Fund**
This fund accounts for Redevelopment Area tax increment monies to be expended for low and moderate income housing purposes.

**Redevelopment Agency Debt Service Fund**
This fund accounts for the accumulation of resources used for the payment of principal and interest on the Redevelopment Agency tax allocation bonds and notes payable. It is funded primarily through tax increment revenue and transfers from other City funds.

**Redevelopment Agency Capital Projects Fund**
This fund accounts for major capital projects undertaken by the Redevelopment Agency.

**HERCULES REDEVELOPMENT AGENCY**

GOVERNMENTAL FUNDS

BALANCE SHEET

June 30, 2010

| | Redevelopment Agency Operating Special Revenue Fund | Affordable Housing Special Revenue Fund | Redevelopment Agency Debt Service Fund |
|---|---|---|---|
| **ASSETS** | | | |
| Cash and investments | $ - | $ - | $ 116,955 |
| Cash and investments with fiscal agents | | | 38,331,928 |
| Accounts receivable | 138,604 | 640 | |
| Interest receivable | 125,000 | 399,598 | 5,687 |
| Due from the City of Hercules | | | |
| Due from other funds | | 40,834 | |
| Loans receivable | 1,953,556 | 10,654,269 | |
| Land held for resale | | 1,352,037 | |
| Total assets | $ 2,217,160 | $ 12,447,378 | $ 38,454,570 |
| **LIABILITIES AND FUND BALANCES** | | | |
| **Liabilities:** | | | |
| Accounts payable | $ 5,090,330 | $ 46,695 | $ 1,162,267 |
| Accrued wages | 55,858 | 5,214 | |
| Deferred revenue | 2,217,160 | 11,053,867 | |
| Due to the City of Hercules | 2,919,063 | 3,514,922 | |
| Due to other funds | | | 2,171,043 |
| Total liabilities | 10,282,411 | 14,620,698 | 3,333,310 |
| **Fund Balances:** | | | |
| Reserved: | | | |
| Capital projects | | | 36,387,549 |
| Future commitments | 39,733 | 146,862 | 115,537 |
| Land held for resale | | 1,352,037 | |
| Unreserved, undesignated | | | |
| Reported in: | | | |
| Special Revenue Funds | (8,104,984) | (3,672,219) | |
| Capital Projects Fund | | | |
| Debt Service Fund | | | (1,381,826) |
| Total fund balances (deficits) | (8,065,251) | (2,173,320) | 35,121,260 |
| Total liabilities and fund balances | $ 2,217,160 | $ 12,447,378 | $ 38,454,570 |

See Accompanying Notes to Basic Financial Statements

| Redevelopment Agency Capital Projects Fund | Total |
|---|---|
| $ 765,309 | $ 882,264 |
| | 38,331,928 |
| | 139,244 |
| | 530,285 |
| 137,141 | 137,141 |
| 2,130,209 | 2,171,043 |
| | 12,607,825 |
| 3,862,040 | 5,214,077 |
| $ 6,894,699 | $ 60,013,807 |
| | |
| $ 3,380,443 | $ 9,679,735 |
| | 61,072 |
| | 13,271,027 |
| | 6,433,985 |
| | 2,171,043 |
| 3,380,443 | 31,616,862 |
| | |
| | 36,387,549 |
| 8,482,533 | 8,784,665 |
| 3,862,040 | 5,214,077 |
| | |
| | (11,777,203) |
| (8,830,317) | (8,830,317) |
| | (1,381,826) |
| 3,514,256 | 28,396,945 |
| $ 6,894,699 | $ 60,013,807 |

THIS PAGE IS INTENTIONALLY LEFT BLANK

**HERCULES REDEVELOPMENT AGENCY**

RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET
TO THE GOVERNMENT-WIDE STATEMENT OF NET ASSETS
June 30, 2010

| | | |
|---|---|---|
| **TOTAL FUND BALANCES - GOVERNMENTAL FUNDS** | | $ 28,396,945 |
| Amounts reported for Governmental Activities in the Statement of Net Assets are different from those reported in the Governmental Funds because of the following: | | |
| Capital assets net of accumulated depreciation used in Governmental Activities are not current assets or financial resources and therefore are not reported in the Governmental Funds. | | |
| Non-depreciable | $ 76,613,549 | |
| Depreciable | 9,326,325 | |
| Accumulated depreciation | (2,781,667) | |
| Total capital assets, net | | 83,158,207 |
| Revenues which are deferred on the Governmental Funds Balance Sheet because they are not available currently are reported as revenues in the Statement of Activities and Changes in Net Assets and accordingly increase the net assets on the Statement of Net Assets. | | |
| Deferred revenue | $ 13,271,027 | |
| Allowance for forgiveness loan | (700,000) | 12,571,027 |
| Interest payable on long-term debt does not require current financial resources. Therefore, interest payable is not reported as a liability in the Governmental Funds Balance Sheet. | | (2,664,715) |
| Issuance costs related to long-term liabilities are expenditures in the Governmental Funds financial statements. However, these costs are capitalized and amortized over the life of the bonds in the Government-wide financial statements, and reported net of accumulated amortization as deferred charges. | | 3,741,744 |
| Long-term liabilities are not due and payable in the current period and therefore they are not reported in the Governmental Funds Balance Sheet. | | |
| 2005 Tax Allocation Bonds | $ (50,660,000) | |
| Premium on 2005 Tax Allocation Bonds | (1,813,308) | |
| Deferred loss on refunding for the 2005 Tax Allocation Bonds | 242,635 | |
| 2007 Housing Tax Allocation Bonds, Series A | (12,670,000) | |
| 2007 Housing Tax Allocation Bonds, Series B | (12,275,000) | |
| Premium on 2007 Housing Tax Allocation Bonds, Series B | (72,368) | |
| 2007 Tax Allocation Bonds, Series A | (57,280,000) | |
| Long-term Notes Payable | (402,023) | |
| Advances from the City of Hercules | (38,721,655) | |
| Total long-term liabilities | | (173,651,719) |
| **NET ASSETS OF GOVERNMENTAL ACTIVITIES** | | $ (48,448,511) |

See Accompanying Notes to Basic Financial Statements

**HERCULES REDEVELOPMENT AGENCY**
GOVERNMENTAL FUNDS
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
For the Fiscal Year Ended June 30, 2010

| | Redevelopment Agency Operating Special Revenue Fund | Affordable Housing Special Revenue Fund | Redevelopment Agency Debt Service Fund |
|---|---|---|---|
| **Revenues:** | | | |
| Taxes and assessments | $ 8,324,442 | $ 2,081,111 | $ - |
| Use of money and property | (258,173) | (103,978) | 122,839 |
| Program income | 285,842 | 189,876 | |
| Charges for services | 279 | 98,407 | |
| Miscellaneous | 80,857 | 8,034 | |
| Total revenues | 8,433,247 | 2,273,450 | 122,839 |
| **Expenditures:** | | | |
| Current: | | | |
| Community development | 10,465,343 | 2,430,539 | 3,079,195 |
| Capital outlay | | | |
| Debt service: | | | |
| Principal | | | 3,190,926 |
| Interest and fiscal agent fees | | | 7,318,681 |
| Total expenditures | 10,465,343 | 2,430,539 | 13,588,802 |
| Excess of revenues over (under) expenditures | (2,032,096) | (157,089) | (13,465,963) |
| **Other financing sources (uses):** | | | |
| Proceeds from issuance of long-term debt | | | 754,337 |
| Transfer in from the City of Hercules | 288,036 | 35,000 | |
| Transfers in | 1,208,056 | 882,329 | 9,844,536 |
| Transfers out | (7,992,569) | (2,046,967) | (24,387,210) |
| Total other financing sources (uses) | (6,496,477) | (1,129,638) | (13,788,337) |
| Net changes in fund balances | (8,528,573) | (1,286,727) | (27,254,300) |
| Fund balances (deficits) - July 1, 2009 | 463,322 | (886,593) | 62,375,560 |
| Fund balances (deficits) - June 30, 2010 | $ (8,065,251) | $ (2,173,320) | $ 35,121,260 |

See Accompanying Notes to Basic Financial Statements

| Redevelopment Agency Capital Projects Fund | Total |
|---|---|
| $ - | $ 10,405,553 |
| | (239,312) |
| | 475,718 |
| | 98,686 |
| | 88,891 |
| | 10,829,536 |
| | 15,975,077 |
| 29,286,378 | 29,286,378 |
| | 3,190,926 |
| 1,925,962 | 9,244,643 |
| 31,212,340 | 57,697,024 |
| (31,212,340) | (46,867,488) |
| 4,817,064 | 5,571,401 |
| 2,108,097 | 2,431,133 |
| 23,747,210 | 35,682,131 |
| (1,255,385) | (35,682,131) |
| 29,416,986 | 8,002,534 |
| (1,795,354) | (38,864,954) |
| 5,309,610 | 67,261,899 |
| $ 3,514,256 | $ 28,396,945 |

**HERCULES REDEVELOPMENT AGENCY**

RECONCILIATION OF THE GOVERNMENTAL FUNDS STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES TO THE GOVERNMENT-WIDE STATEMENT OF ACTIVITIES

For the Fiscal 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 Balances, 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 - GOVERNMENTAL FUNDS** | $ | (38,864,954) |
| Amounts reported for governmental activities in the Statement of Activities are different because of the following: | | |
| Governmental Funds report capital outlays as expenditures. However, in the Statement of Activities, the cost of those assets is capitalized and allocated over their estimated useful lives and reported as depreciation expense. | | |
| Capital outlay expenditures are therefore, added back to fund balances | | 28,380,931 |
| Depreciation expense not reported in governmental funds | | (310,729) |
| The construction in progress project was completed and transferred to the City of Hercules during the current year. This included land, buildings, and improvements. | | (4,360,332) |
| Certain revenues are offset by deferred revenue in the governmental funds because they are not available to pay for current period expenditures. This amount represents the amount by which current year deferred revenue exceeded prior year and includes the $700,000 allowance for forgiveness loan. | | 1,637,183 |
| Addition and amortization of premium, deferred bond discounts and loss on refunding does not require the use of current available resources, and therefore, is not included in the funds. This activity is included in the Statement of Activities. | | (68,071) |
| Bond proceeds provide current financial resources to governmental funds, but issuing debt increases long-term liabilities in the Statement of Net Assets. Costs associated with the issuance of long-term debt are reported as expenditures in the governmental funds, but in the Statement of Net Assets, the costs are deferred and amortized throughout the period during which the related debt is outstanding. Repayment of bond principal is an expenditure in the governmental funds, but in the Statement of Net Assets the repayment reduces long-term liabilities: | | |
| Issuance of long term debt is subtracted from the fund balance | | (5,571,401) |
| Repayment of debt principal is added back to fund balance | | 3,190,926 |
| The amounts below included in the Statement of Activities do not provide (require) the use of current financial resources and therefore, are not reported as revenue or expenditures in governmental funds (net change): | | |
| Interest payable | | 79,950 |
| **CHANGE IN NET ASSETS OF GOVERNMENTAL ACTIVITIES** | $ | (15,886,497) |

See Accompanying Notes to Basic Financial Statements

# NOTES TO BASIC FINANCIAL STATEMENTS

## NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The basic financial statements of the Redevelopment Agency (Agency) of the City of Hercules, California, (City) have been prepared in conformity with accounting principles generally accepted in the United States of America (USGAAP) as applied to governmental agencies. The Governmental Accounting Standards Boards (GASB) is the accepted standard setting body for establishing governmental accounting and financial reporting principles. The more significant of the Agency's accounting policies are described below.

### A. Reporting Entity

The Agency was formed in 1983 for the purpose of renovating designated Redevelopment Project Areas within the limits of the City. The Agency is a component unit of the City, and is accounted for as separate funds in the City's basic financial statements.

### B. Basis of Accounting/Measurement Focus

The accounts of the Agency are organized on the basis of funds, each of which is considered a separate accounting entity. The operations of each fund are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues, and expenditures. Governmental resources are allocated to and accounted for in individual funds based upon the purposes for which they are to be spent and the means by which spending activities are controlled.

*Government-Wide Financial Statements*

The Agency's government-wide financial statements include a Statement of Net Assets and a Statement of Activities. These statements present summaries of governmental activities for the Agency.

These statements are presented on an *"economic resources"* measurement focus and the accrual basis of accounting. Accordingly, all of the Agency's assets and liabilities, including capital assets, as well as infrastructure assets and long-term liabilities, are included in the accompanying Statement of Net Assets. The Statement of Activities presents changes in net assets. Under the accrual basis of accounting, revenues are recognized in the period in which they are earned while expenses are recognized in the period in which the liability is incurred. The type of transactions reported as program revenues for the Agency is charges for services.

Certain eliminations have been made as prescribed by GASB Statement No. 34 in regards to interfund activities, payables and receivables. All internal balances in the Statement of Net Assets have been eliminated. The following interfund activities have been eliminated:

- Transfers in/out
- Due from/to other funds
- Advances from/to other funds

*Governmental Fund Financial Statements*

Governmental fund financial statements include a Balance Sheet and a Statement of Revenues, Expenditures, and Changes in Fund Balances for all major governmental funds. An accompanying schedule is presented to reconcile and explain the differences in the balance sheet as presented in these statements to the net assets presented in the government-wide financial statements. All of the Agency's funds are presented as major funds.

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

### B. Basis of Accounting/Measurement Focus (Continued)

*Governmental Fund Financial Statements (Continued)*

All governmental funds are accounted for on a spending or *"current financial resources"* measurement focus and the modified accrual basis of accounting. Accordingly, only current assets and current liabilities are included on the balance sheets. The Statement of Revenues, Expenditures, and Changes in Fund Balances presents increases (revenues and other financing sources) and decreases (expenditures and other financing uses) in net current assets.

Revenues are recorded when received in cash, except for those revenues subject to accrual (generally 60 days after year-end) are recognized when due. The primary revenue sources, which have been treated as susceptible to accrual by the Agency, are property tax and investment earnings. Expenditures are recorded in the accounting period in which the related fund liability is incurred.

Deferred revenues arise when potential revenues do not meet both the "measurable" and "available" criteria for recognition in the current period. Deferred revenues also arise when the government receives resources before it has a legal claim to them, as when grant monies are received prior to incurring qualifying expenditures. In subsequent periods, when both revenue recognition criteria are met or when the government has a legal claim to the resources, the deferred revenue is removed and revenue is recognized.

The Reconciliation of the Fund Financial Statements to the Government-wide Financial Statements is provided to explain the differences created by the integrated approach of GASB Statement No. 34.

### C. Cash and Investments

The Agency pools cash resources from all funds within the City of Hercules in order to facilitate the management of cash. The balance in the pooled cash account is available to meet current operating requirements. Cash in excess of current requirements is invested in various interest-bearing accounts and other investments for varying terms.

In accordance with GASB Statement No. 40, *Deposit and Investment Disclosures (Amendment of GASB Statement No. 3),* certain disclosure requirements for Deposits and Investment Risks were made in the following areas:

- Interest Rate Risk
- Credit Risk
  - Overall
  - Custodial Credit Risk
  - Concentrations of Credit Risk

In addition, other disclosures are specified including use of certain methods to present deposits and investments, highly sensitive investments, credit quality at fiscal year-end, and other disclosures.

The Agency has implemented GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools.* Highly liquid market investments with maturities of one year or less at time of purchase are stated at amortized cost. All other investments are stated at fair value. Market value is used as fair value for those securities for which market quotations are not readily available. Interest earned on investments is allocated using the LAIF factor to selected funds by the City.

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

### C. Cash and Investments (Continued)

The Agency participates in an investment pool managed by the State of California titled Local Agency Investment Fund (LAIF) which has invested a portion of the pooled funds in Structured Notes and Asset-Backed Securities. LAIF's investments are subject to credit and market risk with the full faith and credit of the State of California collateralizing these investments. In addition, these Structured Notes and Asset-Backed Securities are subject to market risk as to change in interest rates.

Cash equivalents are considered amounts in demand deposits and short-term investments with a maturity date within three months of the date acquired by the Agency and are presented as "Cash and investments" in the basic financial statements.

### D. Capital Assets

The Agency's assets are capitalized at historical cost or estimated historical cost. Agency policy has set the capitalization threshold for reporting capital assets at $2,500. Gifts or contributions of capital assets are recorded at fair value when received. Depreciation is recorded on the straight-line basis over the estimated useful lives of the assets as follows:

| | |
|---|---|
| Buildings and improvements | 25 years |
| Machinery and equipment | 5 – 20 years |
| Improvements other than buildings | 15 years |
| Infrastructure | 15 – 50 years |

### E. Long-Term Obligations

In the government-wide financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities. Bond premiums and discounts and issuance costs, if material, are deferred and amortized over the life of the bonds using the straight-line method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuance are reported as other financing sources while discounts on debt issuance are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

### F. Fund Balances

In the fund financial statements, governmental funds report reservations of fund balances for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balances represent tentative management plans that are subject to change.

The following is a listing of the Agency's reserves and designations:

*Reserved for Land Held for Resale* – Represents amounts provided to indicate that land held for resale is not "available" as a resource to meet expenditures of the current year.

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

### F. Fund Balances (Continued)

Reserved for Capital Projects represents the portion of fund balance that is reserved for capital projects per debt agreements.

Reserved for Future Commitments represents funds that are reserved for future miscellaneous commitments.

### G. Net Assets

In the government-wide financial statements, net assets are classified in the following categories:

Restricted Net Assets – This amount is restricted by external creditors, grantors, contributors, or laws or regulations of other governments.

Unrestricted Net Assets – This amount is all net assets that do not meet the definition of "invested in capital assets, net of related debt" or "restricted net assets."

### H. Use of Restricted/Unrestricted Net Assets

When an expense is incurred for purposes for which both restricted and unrestricted net assets are available, the Agency's policy is to apply restricted net assets first.

### I. Property Taxes

Under California law, property taxes are assessed and collected by the County of Contra Costa (County). Under the Teeter plan, the County remits the full assessment regardless of the amounts received. The County assesses, bills, and collects property taxes as follows:

| | |
|---|---|
| Lien Date | January 1 |
| Levy Date | July 1 |
| Due Date | November 1 and February 1 |
| Collection Date | December 10 and April 10 |

The Agency is required to set aside a portion of tax increments received to increase and improve the community's supply of low and moderate-income housing. The amount set aside each year is required to equal 20% of the tax increment receipts from the redevelopment area which amounted to $2,081,111 for the fiscal year ended June 30, 2010.

Unsecured personal property taxes do not constitute a lien against real property unless the taxes become delinquent. Payment must be made in one installment, which is delinquent if not paid by August 31 of the fiscal year. Significant penalties are imposed by the county for late payments.

### J. Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Actual results could differ from those estimates.

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

### K. New Accounting Pronouncements

The Agency has implemented the requirements of Governmental Accounting Standards Board (GASB) Statement No. 51, No. 53, No. 57, and No. 58 during the fiscal year ended June 30, 2010.

GASB Statement No. 51 – Accounting and Financial Reporting for Intangible Assets

For the fiscal year ended June 30, 2010, the Agency implemented GASB Statement No. 51, "*Accounting and Financial Reporting for Intangible Assets*". This Statement is effective for financial statements for periods beginning after June 15, 2009. The objective of this Statement is to establish accounting and financial reporting requirements for intangible assets to reduce the inconsistencies, thereby enhancing the comparability of the accounting and financial reporting of such assets among state and local governments. The implementation of this Statement did not have an effect on these financial statements.

GASB Statement No. 53 – Accounting and Financial Reporting for Derivative Instruments

For the fiscal year ended June 30, 2010, the Agency implemented GASB Statement No. 53, "*Accounting and Financial Reporting for Derivative Instruments*". This Statement is effective for financial statements for periods beginning after June 15, 2009. This Statement addresses the recognition, measurement, and disclosure of information regarding derivative instruments entered into by state and local governments. The implementation of this Statement did not have an effect on these financial statements.

GASB Statement No. 57 – OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans

For the fiscal year ended June 30, 2010, the Agency implemented GASB Statement No. 57, "*OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*". This Statement establishes standards for the measurement and financial reporting of actuarially determined information by agent employers with individual-employer OPEB plans that have fewer than 100 total plan members and by the agent multiple-employer OPEB plans in which they participate. The implementation of this Statement did not have an effect on these financial statements.

GASB Statement No. 58 – Accounting and Financial Reporting for Chapter 9 Bankruptcies

For the fiscal year ended June 30, 2010, the Agency implemented GASB Statement No. 58, "*Accounting and Financial Reporting for Chapter 9 Bankruptcies*". This Statement is effective for reporting periods beginning after June 15, 2009. The objective of this Statement is to provide accounting and financial reporting guidance for governments that have petitioned for protection from creditors by filing for bankruptcy under Chapter 9 of the United States Bankruptcy Code. It requires governments to remeasure liabilities that are adjusted in bankruptcy when the bankruptcy court confirms (that is, approves) a new payment plan. The implementation of this Statement did not have an effect on these financial statements.

## NOTE 2 – CASH AND INVESTMENTS

The Agency pools its cash and investments with the City in order to achieve a higher return on investment. Certain funds, which are held and invested by independent outside custodians through contractual agreements, are not pooled. These funds include cash with fiscal agents.

| | | |
|---|---|---|
| Statement of net assets: | | |
| Cash and investments | $ | 882,264 |
| Cash and investments held with fiscal agents | | 38,331,928 |
| Total cash and investments | $ | 39,214,192 |

Cash and investments at June 30, 2010 consisted of the following:

| | | |
|---|---|---|
| Cash and investments pooled with the City of Hercules | $ | 882,264 |
| Investments | | 38,331,928 |
| Total cash and investments | $ | 39,214,192 |

The investments made by the Agency are limited to those allowable under State statutes and the Agency's investment policy and may include the following types of investments:

| | |
|---|---|
| Certificates of Deposit | Government Agency Securities |
| Bankers Acceptances | Treasury Bills and Notes |
| Commercial Paper | Passbook Savings Accounts |
| Repurchase Agreements | Mutual Funds |
| Medium-Term Corporate Notes | State of California Local Agency Investment Fund |

### Investments Authorized by Debt Agreements

Investment of debt proceeds held by trustees is governed by provisions of the debt agreements, rather than the general provisions of the California Government Code or the Agency's investment policy. The table below identifies the investment types that are authorized for investments held by trustee. The table also identifies certain provisions of the debt agreements that address interest rate risk, credit risk, and concentration of credit risk.

| Authorized Investment Type | Maximum Maturity | Maximum Percentage of Portfolio | Maximum Investment in One Issuer |
|---|---|---|---|
| Local Agency Investment Fund (State Pool) | N/A | None | $50 million |
| U.S. Treasury Obligations | 30 years | 20% | None |
| U.S. Government Agency Issues | 30 years | 20% | None |
| Insured Deposits with Banks and Savings and Loans | N/A | None | None |
| Bankers Acceptance (must be dollar denominated) | 6 months | 40% | 30% |
| Commercial Paper | 6 months | 15% | 10% |
| Negotiable Time Certificates of Deposit | 5 years | 30% | $100,000 |
| Non-negotiable Time Certificates of Deposit | 5 years | 30% | $100,000 |
| Federally insured Time Deposits | 1 year | 20% | None |
| Repurchase Agreements | 30 days | None | None |
| Reverse Repurchase Agreements | 92 days | 20% | None |
| Medium-Term Notes | 5 years | 30% | 15% |
| Money Market Funds | N/A | None | None |
| Mutual Funds | N/A | 20% | None |
| Insured or Passbook Savings Accounts | N/A | None | $100,000 |
| Guaranteed Investment Contracts | N/A | None | None |

## NOTE 2 – CASH AND INVESTMENTS (CONTINUED)

### Disclosures Relating to 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 Agency 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 flows and liquidity needed for operations.

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 investments by maturity:

| | | Remaining Maturity (in Months) | | | | | |
|---|---|---|---|---|---|---|---|
| Investment Type | Totals | 12 Months Or Less | 13 to 24 Months | 25-36 Months | 37-48 Months | 49-60 Months | More Than 60 Months |
| Held by debt trustees: | | | | | | | |
| Money Market Funds | $ 38,331,928 | $ 38,331,928 | $ - | $ - | $ - | $ - | $ - |
| | $ 38,331,928 | $ 38,331,928 | $ - | $ - | $ - | $ - | $ - |

### Investments with Fair Values Highly Sensitive to Interest Rate Fluctuations

Interest rate risk is the market value fluctuation due to overall changes in the interest rates. It is mitigated by limiting the average maturity of the Agency's portfolio not to exceed three years. The Agency has no investments that are highly sensitive to interest rate fluctuations.

As a means of maintaining liquidity and minimizing interest rate risk, the Agency's investment policy limits are as follows:

| Maturity | % of Portfolio |
|---|---|
| Up to one year | 10% (Minimum) |
| one year to five years | 60% (Maximum) |
| more than five years | 30% (Maximum) |

### Disclosures Relating to Credit Risk

Generally, 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. Presented below is the minimum rating required by (where applicable) the California Government Code, the Agency's investment policy, or debt agreements, and the actual rating as of fiscal year end for each investment type.

| | | | | Rating as of Fiscal Year End | | | |
|---|---|---|---|---|---|---|---|
| Investment Type | Amount | Minimum Legal Rating | Exempt From Disclosure | AAA | AA | A | Not Rated |
| Held by debt trustees: | | | | | | | |
| Money Market Funds | $ 38,331,928 | N/A | $ - | $ 38,331,928 | $ - | $ - | $ - |
| Total | $ 38,331,928 | | $ - | $ 38,331,928 | $ - | $ - | $ - |

## NOTE 2 – CASH AND INVESTMENTS (CONTINUED)

### Concentration of Credit Risk

The investment policy of the Agency contains limitations on the amount that can be invested in any one issuer. The Agency has no investments (other than the money market funds) that are more than 5% of total Agency investments.

### 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. The California Government Code and the Agency's investment policy do not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits or investments, other than the following provision for deposits. The California Government Code requires that a financial institution secure deposits made by state or local governmental units by pledging securities in an undivided collateral pool held by a depository regulated under state law (unless so waived by the governmental unit). The fair value of the pledged securities in the collateral pool must equal at least 110% of the total amount deposited by the public agencies. California law also allows financial institutions to secure Agency deposits by pledging first trust deed mortgage notes having a value of 150% of the secured public deposits.

See the City of Hercules' Comprehensive Annual Financial Report for more information relating to custodial credit risk for amounts reported as cash and investments pooled with the City.

The Agency's investments are carried at fair value as required by accounting principles generally accepted in the United States of America. 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 investment income for that fiscal year.

## NOTE 3 – LOANS RECEIVABLE

Loans receivable at June 30, 2010 consisted of the following:

| | |
|---|---|
| Bridge Housing Corporation | $ 1,799,198 |
| Eden Housing | 700,000 |
| Radston's Office Plus | 375,000 |
| First Time Homebuyers | 4,002,890 |
| Affordable Housing | 4,539,702 |
| Business Development Loans | 1,703,556 |
| Home Emergency Loans | 12,077 |
| Subtotal | 13,132,423 |
| Less: Reported as interest receivable | 524,598 |
| Allowance for uncollectible loan | 700,000 |
| Total | $ 11,907,825 |

The Agency loaned the Bridge Housing Corporation (Corporation) $1,400,000 to finance construction of a sixty unit senior citizen housing development next to City Hall. On September 8, 1998, the Agency approved an addition to the loan of $114,600 for a total of $1,514,600. On January 1, 1999, the loan began to accrue interest at the rate of 3.5% per year and is repayable in 2041, subject to certain conditions. The construction was completed in September 1999. On March 2, 2000, the Corporation repaid $115,000 to the Agency. As of June 30, 2010, the Corporation's loan balance was $1,799,198, which includes $399,598 of interest presented as interest receivable.

## NOTE 3 – LOANS RECEIVABLE (CONTINUED)

On July 1, 2002, the Agency loaned Eden Housing, Inc. $700,000 to assist in the development of low and moderate income housing for senior citizens. The loan does not bear interest. The repayment of the loan is only due and payable if a default has been declared by the Agency and the borrower fails to cure the default. Upon expiration of the 55-year Regulatory Agreement, the loan will be forgiven and the promissory note will be cancelled by the Agency. The balance outstanding as of June 30, 2010 was $700,000. An allowance of $700,000 has been established for this loan, due to its terms.

On December 5, 2000, the Agency entered into a promissory note agreement with the Radston's Office Plus (Payors) in the amount of $250,000 with interest at 5% per annum. All principal and interest are deferred until December 5, 2010. Commencing on December 5, 2010, the Payors shall pay a lump-sum cash amount of $125,000 which represents all deferred and unpaid interest only. The principal balance of $250,000 will be fully amortized and paid over the next ten years at $2,652 per month, principal and interest, commencing on December 5, 2010. The loan is secured by a Deed of Trust on real property. As of June 30, 2010, the outstanding balance of the loan was $375,000, which includes $125,000 of interest presented as interest receivable.

The Agency has provided various loan programs for First Time Homebuyers. In general, they provide secondary financing for low and moderate buyers in the City of Hercules that have deferred payments in order to allow the buyer to maximize their purchasing capacity. The loan has a repayment period of 20 years and payment is deferred in the first 10 years of the loan. The loan has a simple interest rate is at 3%, which will not be accrued during the deferred period. The balance outstanding as of June 30, 2010 was $4,002,890.

The Agency has provided various loan programs for Affordable Housing assistance. The first is the Below Market Rate Program, which provides secondary financing for low to moderate income persons who currently earn less than one hundred twenty percent of the current annual median income for the Contra Costa County area. This is available to City employees as well. The repayment period varies from 10 to 30 years with a deferred period of 10 to 20 years and no interest will be accrued. The second is the Rehabilitation and Beautification Program, which provides financial assistance to rehabilitate properties. Borrowers are individuals and families who currently earn less than one hundred twenty percent of the current annual median income for the Contra Costa County area. The loan has a repayment period of 20 years and payment is deferred for the first 10 years of the loan. The loan has a simple interest rate of 3%, which will not be accrued during the deferred period. The balance outstanding of the Affordable Housing Assistance loans as of June 30, 2010 was $4,539,702.

The City and Agency established the Business Development Loan Program (BDLP) to provide low cost financial assistance to businesses within the City of Hercules. The BDLP offers a secured loan of up to $75,000, a term not greater than 20 years, and a simple interest rate of 3% per annum. All applicants are evaluated and prioritized according to established program criteria and if funded are subject to various terms, conditions, and fees. These fees will be deducted from the final loan award by the escrow administrator at the time of funding. The balance outstanding as of June 30, 2010 was $1,703,556.

On September 19, 2002, the Agency entered into several home emergency loans in various amounts with interest at 5% per annum. The principal amount of the loans including interest is to be due and payable in one lump sum if the owners cease to occupy the property or upon any transfer, refinance, sale, or conveyance of all or part of the property. The balance outstanding as of June 30, 2010 was $12,077.

## NOTE 4 – LAND HELD FOR RESALE

Land held for resale of $3,862,040 is comprised of one parcel of land in the Dynamite Project area and the remaining $1,352,037 is comprised of six parcels of land that were purchased by the Agency. The parcels are purchases within the project area and are being held for future development. The properties are being carried at a net realizable value, which approximates cost.

## NOTE 5 – CAPITAL ASSETS

Capital asset activity for the fiscal year ended June 30, 2010, consisted of the following:

| | Balance July 1, 2009 | Additions | Deletions | Transfers | Balance June 30, 2010 |
|---|---|---|---|---|---|
| **Governmental Activities** | | | | | |
| Nondepreciable capital assets: | | | | | |
| Land | $ 29,638,038 | $ 1,860,323 | $ - | $ 159,200 | $ 31,657,561 |
| Construction in progress | 22,954,912 | 26,520,608 | | (4,519,532) | 44,955,988 |
| Total nondepreciable capital assets | 52,592,950 | 28,380,931 | | (4,360,332) | 76,613,549 |
| Depreciable capital assets: | | | | | |
| Land improvements | 11,379 | | | | 11,379 |
| Buildings and improvements | 4,965,778 | | | | 4,965,778 |
| Machinery and equipment | 116,445 | | | | 116,445 |
| Infrastructure | 4,232,723 | | | | 4,232,723 |
| Total depreciable capital assets | 9,326,325 | | | | 9,326,325 |
| Accumulated depreciation: | | | | | |
| Land improvements | (9,973) | (572) | | | (10,545) |
| Buildings and improvements | (2,049,530) | (99,436) | | | (2,148,966) |
| Machinery and equipment | | (5,810) | | | (5,810) |
| Infrastructure | (411,435) | (204,911) | | | (616,346) |
| Total accumulated depreciation | (2,470,938) | (310,729) | | | (2,781,667) |
| Net depreciable capital assets | 6,855,387 | (310,729) | | | 6,544,658 |
| Net capital assets | $ 59,448,337 | $ 28,070,202 | $ - | $ (4,360,332) | $ 83,158,207 |

Several projects were completed during the fiscal year ended June 30, 2010 and were transferred to the City of Hercules in the amount of $4,357,043.

Depreciation expense for the fiscal year ended June 30, 2010 was $310,729, which was allocated to community development expense on the Statement of Activities.

## NOTE 6 – LONG-TERM OBLIGATIONS

The Agency's long-term obligation transactions for the fiscal year ended June 30, 2010, were as follows:

| | Balance July 1, 2009 | Prior Period Adjustments | Additions | Reductions | Balance June 30, 2010 | Due within one year |
|---|---|---|---|---|---|---|
| **Governmental activities:** | | | | | | |
| 2005 Tax Allocation Bonds | $ 52,180,000 | $ - | $ - | $ (1,520,000) | $ 50,660,000 | $ 1,575,000 |
| Premium on 2005 Tax Allocation Bonds | 1,885,840 | | | (72,532) | 1,813,308 | 72,532 |
| Deferred loss on refunding for the 2005 Tax Allocation Bonds | (252,340) | | | 9,705 | (242,635) | (9,705) |
| 2007 Housing Tax Allocation Bonds, Series A | 12,910,000 | | | (240,000) | 12,670,000 | 255,000 |
| 2007 Housing Tax Allocation Bonds, Series B | 12,525,000 | | | (250,000) | 12,275,000 | 260,000 |
| Premium on 2007 Housing Tax Allocation Bonds, Series B | 75,514 | | | (3,146) | 72,368 | 3,146 |
| 2007 Tax Allocation Bonds, Series A | 58,410,000 | | | (1,130,000) | 57,280,000 | 1,185,000 |
| Long-term Notes Payable | 452,949 | | | (50,926) | 402,023 | 54,952 |
| Advances from the City of Hercules | 32,973,013 | 177,241 | 5,571,401 | | 38,721,655 | 190,000 |
| Total long-term obligations | $ 171,159,976 | $ 177,241 | $ 5,571,401 | $ (3,256,899) | $ 173,651,719 | $ 3,585,925 |

## NOTE 6 – LONG-TERM OBLIGATIONS (CONTINUED)

### A. 2005 Tax Allocation Bonds

On August 5, 2005, the Redevelopment Agency issued Hercules Merged Project Area Tax Allocation Bonds, Series 2005, in the amount of $56,260,000. The proceeds of the bonds were used to finance certain public capital improvements within the Agency's Merged Project Area and refund the Agency Subordinate Tax Allocation Bonds, Series 2001. The Bonds mature annually each August 1 from 2006 to 2035, in amounts ranging from $740,000 to $2,960,000 and bear interest at rates ranging from 3.50% to 5.00%. Interest is payable semi-annually on February 1 and August 1. The Bonds maturing on or after August 1, 2016, are subject to optional redemption prior to maturity at the option of the Agency on or after August 1, 2015, as a whole or in part, on any interest payment date, at a price equal to the principal amount, plus accrued interest on the redemption date. The bonds are payable exclusively from pledged tax revenues to be derived from the project area and from the amounts on deposit in certain funds and accounts, including the reserve account and the revenue account.

The annual debt service requirements to maturity at June 30, 2010, are as follows:

| Fiscal Year Ended June 30, | Principal | Interest | Total |
|---|---|---|---|
| 2011 | $ 1,575,000 | $ 2,390,336 | $ 3,965,336 |
| 2012 | 1,640,000 | 2,327,266 | 3,967,266 |
| 2013 | 1,705,000 | 2,264,856 | 3,969,856 |
| 2014 | 1,765,000 | 2,199,536 | 3,964,536 |
| 2015 | 1,835,000 | 2,119,841 | 3,954,841 |
| 2016-2020 | 9,785,000 | 9,151,094 | 18,936,094 |
| 2021-2025 | 8,715,000 | 6,977,257 | 15,692,257 |
| 2026-2030 | 11,100,000 | 4,536,109 | 15,636,109 |
| 2031-2035 | 11,765,000 | 1,480,639 | 13,245,639 |
| 2036 | 775,000 | 19,025 | 794,025 |
| Subtotal | 50,660,000 | 33,465,959 | 84,125,959 |
| Plus Premium | 1,813,018 | | 1,813,018 |
| Less Deferred Loss on Refunding | (9,705) | | (9,705) |
| Total | $ 52,463,313 | $ 33,465,959 | $ 85,929,272 |

In connection with the issuance of the 2005 Tax Allocation Bonds, the Agency recorded a deferred loss on refunding of debt which is reported as part of long-term debt. This deferred loss was in connection with interest payments made to the escrow agent for future payments of interest. The total amount of the deferred loss was $291,160 which will be amortized over the life of the bond. The amortization for the fiscal year 2009-2010 was $9,705, and the accumulated amortization at June 30, 2010 was $48,525.

### B. 2007 Housing Tax Allocation Bonds Series A and B

On July 26, 2007, the Redevelopment Agency issued Hercules Merged Project Area Housing Tax Allocation Bonds, 2007 Series A, in the amount of $13,130,000 and 2007 Series B, in the amount of 12,760,000. The proceeds of the bonds were used to finance certain public capital improvements within the Agency's Merged Project Area. The Bonds mature annually each August 1 from 2009 to 2033, in amounts ranging from $220,000 to $950,000 and bear interest at rates ranging from 3.50% to 6.125%. Interest is payable semi-annually on February 1 and August 1. The Bonds maturing on or after August 1, 2018, are subject to optional redemption prior to maturity at the option of the Agency on or after August 1, 2017, as a whole or in part, on any interest payment date, at a price equal to the principal amount, plus accrued interest on the redemption date. The bonds are payable exclusively from pledged tax revenues to be derived from the project area and from the amounts on deposit in certain funds and accounts, including the reserve account and the revenue account.

HERCULES REDEVELOPMENT AGENCY
NOTES TO BASIC FINANCIAL STATEMENTS
JUNE 30, 2010

## NOTE 6 – LONG-TERM OBLIGATIONS (CONTINUED)

### B. 2007 Housing Tax Allocation Bonds Series A and B (Continued)

The annual debt service requirements to maturity at June 30, 2010 of the 2007 Series A and B bonds are as follows:

| Fiscal Year Ended June 30, | 2007 Series A Principal | 2007 Series A Interest | 2007 Series A Total |
|---|---|---|---|
| 2011 | $ 255,000 | $ 754,056 | $ 1,009,056 |
| 2012 | 270,000 | 739,619 | 1,009,619 |
| 2013 | 285,000 | 724,356 | 1,009,356 |
| 2014 | 300,000 | 707,968 | 1,007,968 |
| 2015 | 315,000 | 690,441 | 1,005,441 |
| 2016-2020 | 1,875,000 | 3,149,979 | 5,024,979 |
| 2021-2025 | 2,505,000 | 2,501,026 | 5,006,026 |
| 2026-2030 | 3,360,000 | 1,612,406 | 4,972,406 |
| 2031-2034 | 3,505,000 | 445,134 | 3,950,134 |
| Total | $ 12,670,000 | $ 11,324,985 | $ 23,994,985 |

| Fiscal Year Ended June 30, | 2007 Series B Principal | 2007 Series B Interest | 2007 Series B Total |
|---|---|---|---|
| 2011 | $ 260,000 | $ 564,786 | $ 824,786 |
| 2012 | 315,000 | 553,241 | 868,241 |
| 2013 | 325,000 | 540,351 | 865,351 |
| 2014 | 340,000 | 526,775 | 866,775 |
| 2015 | 350,000 | 512,506 | 862,506 |
| 2016-2020 | 1,990,000 | 2,324,780 | 4,314,780 |
| 2021-2025 | 2,470,000 | 1,832,500 | 4,302,500 |
| 2026-2030 | 3,130,000 | 1,155,941 | 4,285,941 |
| 2031-2034 | 3,095,000 | 315,794 | 3,410,794 |
| Subtotal | 12,275,000 | 8,326,674 | 20,601,674 |
| Plus Premium | 72,368 | | 72,368 |
| Total | $ 12,347,368 | $ 8,326,674 | $ 20,674,042 |

### C. 2007 Tax Allocation Bonds Series A

On December 20, 2007, the Redevelopment Agency issued Hercules Merged Project Area Tax Allocation Bonds, 2007 Series A, in the amount of $60,555,000. The proceeds of the bonds will be used to finance certain public capital improvements within the Agency's Merged Project Area. The Bonds mature annually each August 1 from 2009 to 2043, in amounts ranging from $260,000 to $3,315,000 and bear interest at rates ranging from 3.50% to 5.00%. Interest is payable semi-annually on February 1 and August 1. The Bonds maturing on or after August 1, 2018, are subject to optional redemption prior to maturity at the option of the Agency on or after February 1, 2018, as a whole or in part, on any interest payment date, at a price equal to the principal amount, plus accrued interest on the redemption date. The bonds are payable exclusively from pledged tax revenues to be derived from the project area and from the amounts on deposit in certain funds and accounts, including the reserve account and the revenue account.

## NOTE 6 – LONG-TERM OBLIGATIONS (CONTINUED)

### C. 2007 Tax Allocation Bonds Series A (Continued)

The annual debt service requirements to maturity at June 30, 2010, are as follows:

| Fiscal Year Ended June 30, | Principal | Interest | Total |
|---|---|---|---|
| 2011 | $ 1,185,000 | $ 2,670,983 | $ 3,855,983 |
| 2012 | 1,240,000 | 2,610,358 | 3,850,358 |
| 2013 | 1,300,000 | 2,546,858 | 3,846,858 |
| 2014 | 1,360,000 | 2,480,358 | 3,840,358 |
| 2015 | 1,430,000 | 2,410,608 | 3,840,608 |
| 2016-2020 | 2,160,000 | 11,734,135 | 13,894,135 |
| 2021-2025 | 5,710,000 | 10,829,463 | 16,539,463 |
| 2026-2030 | 6,465,000 | 9,371,384 | 15,836,384 |
| 2031-2035 | 9,625,000 | 7,716,215 | 17,341,215 |
| 2036-2040 | 17,310,000 | 4,132,020 | 21,442,020 |
| 2041-2044 | 9,495,000 | 702,812 | 10,197,812 |
| Total | $ 57,280,000 | $ 57,205,194 | $ 114,485,194 |

### D. Long-Term Notes Payable

In 1987, the Agency entered into Owner Participation Agreements with certain property owners (East Group and Bio Rad Laboratories) in the Redevelopment Area. Under the terms of these agreements, the Agency signed notes under which it promised to reimburse the owners by the year 2016 for the amount of incremental assessments levied on their properties, up to the cost of constructing public improvements. Payment on these notes is contingent on the property taxes and special assessments levied on these owners. As of June 30, 2010, the Agency's long-term notes payables were as follows:

| | |
|---|---|
| East Group | $ 151,513 |
| Bio Rad Laboratories | 250,510 |
| Total | $ 402,023 |

The annual debt service requirements to maturity for the East Group Note Payable as of June 30, 2010 are as follows:

| Fiscal Year Ended June 30, | Principal | Interest | Total |
|---|---|---|---|
| 2011 | $ 20,601 | $ 11,614 | $ 32,215 |
| 2012 | 22,112 | 10,018 | 32,130 |
| 2013 | 23,887 | 8,304 | 32,191 |
| 2014 | 25,661 | 6,453 | 32,114 |
| 2015 | 27,709 | 4,464 | 32,173 |
| 2016 | 31,543 | 2,317 | 33,860 |
| Total | $ 151,513 | $ 43,170 | $ 194,683 |

## NOTE 6 – LONG-TERM OBLIGATIONS (CONTINUED)

### D. Long-Term Notes Payable (Continued)

The annual debt service requirements to maturity for the Bio Rad Laboratories Note Payable as of June 30, 2010 are as follows:

| Fiscal Year Ended June 30, | Principal | Interest | Total |
|---|---|---|---|
| 2011 | $ 34,351 | $ 19,366 | $ 53,717 |
| 2012 | 36,871 | 16,704 | 53,575 |
| 2013 | 39,830 | 13,847 | 53,677 |
| 2014 | 42,788 | 10,760 | 53,548 |
| 2015 | 46,203 | 7,443 | 53,646 |
| 2016 | 50,467 | 3,863 | 54,330 |
| Total | $ 250,510 | $ 71,983 | $ 322,493 |

### E. Defeased Debt

**2001 Tax Allocation Bonds**

The Agency issued 2005 Tax Allocation Bonds to refund the 2001 Tax Allocation Bonds. The Agency issued subordinate tax allocation bonds, series 2001, dated September 4, 2001, totaling $6,500,000. The purpose of the bonds was to provide funds to finance certain redevelopment activities within, and of benefit to, the Hercules Merged Project Area. The interest rate on the bonds ranges from 4.50% to 6.40%. The interest is payable on each March 1 and September 1 commencing March 1, 2002. The bonds are subject to optional and mandatory early redemption provisions. The bonds are payable from and secured by a pledge of tax revenues in the Merged Project Area. Principal is due annually beginning on September 1, 2005, in amounts ranging from $215,000 to $575,000. The economic effect of refunding the bonds was a gain of $293,279. The liability for these bonds has been removed from the Agency's books and records, as they are considered defeased. The outstanding balance was paid off as of June 30, 2010.

## NOTE 7 – ADVANCES FROM CITY OF HERCULES

Advances from City of Hercules amounted to $38,721,655. These funds were to provide financing for City Hall Construction, Refugio Creek Realignment Project, Williamson Property Purchase, Wells Fargo Bank building purchase and expansion, Farber settlement, Frog Pad Park, Teen Center, upgrades to the sewer plant, and Hercules Municipal Utility's infrastructure. The interest rate charged by the City to the Agency is based on the Board's resolution approved in the fiscal year ended June 30, 2009, which was 8% as of June 30, 2010.

## NOTE 8 – PUBLIC EMPLOYEE RETIREMENT SYSTEM

*Plan Description* . The Agency participates in the City's pension plan. California Public Employees' Retirement System (PERS), an agent multiple-employer defined benefit pension plan. PERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. PERS acts as a common investment and administrative agent for participating public entities within the State of California. Benefit provisions and all other requirements are established by state statute and City ordinance. Refer to the City's basic financial statements as of June 30, 2010, for detailed information regarding the pension plan.

## NOTE 9 – COMMITMENTS

*Hercules LLC* – An agreement with Hercules LLC was established with the Agency to assist with development of a 206 acre mixed-use project consisting of 880 residential units, 6 acres of commercial, residential or missed-use projects, and open space and park uses. Project tax increment is defined to include all increases in value over the base year amount of $7,654,000, less statutory payments to affected taxing entities. The agreement states that the Agency shall pay the developer the first 75% of the unrestricted portion (net of affordable housing set aside and required payments to affected tax entities), and the first 90% of the housing portion (affordable housing set aside) of the project tax increment funds for properties located within the project site. The financing terms for these payments are 45 years from the adoption date of Ordinance No. 351 or April 13, 1999.

Under the settlement in Fiscal Year 2009-10, Hercules, LLC will be paid nothing more out of the housing portion of project tax increment, and will receive seventy five percent (75%) of the unrestricted portion of project tax increment until February, 2024 with fifty percent (50%) thereafter.

*Pro Media* – To assist with development of a 57,600 square foot and a 27,000 square foot building at the Project Site, the Agency entered into an agreement with Pro Media Corporation. The Agreement provides for the owner to expend at least $4 million in hard construction costs. The Agreement provides for the Agency to pay the owner 60% of the Project Tax Increment, as defined above, over the financing term. The financing term commences on the date any increased property tax assessment first becomes effective on the project site from any improvements, and ends on the earliest of the following: (i) fifteen years from the commencement of the financing term, (ii) termination of the agreement, (iii) expiration of the Redevelopment Plan, or (iv) the remaining life of the Agency.

## NOTE 10 – CONTINGENCIES

Hercules LLC – The Redevelopment Agency audited the Hercules, LLC's reimbursement requests as stated in Note 9 in 2007 and discovered that Hercules, LLC had substantially inflated its reimbursement requests. Hercules, LLC was unable to provide justification for its action. The Redevelopment Agency ceased making any tax increment reimbursements to Hercules, LLC. Hercules LLC protested and filed a lawsuit claiming entitlement to those reimbursements.

The Redevelopment Agency and Hercules, LLC participated in mediation on September 10, 2008 and again on February 2, 2009, but were unable to reach a settlement of their differences or the lawsuit at any time. The case was scheduled for trial commencing January 25, 2010, but the parties voluntarily submitted the case to additional mediation.

The final round of mediation was successful and the case was settled. Under the settlement agreement, Hercules, LLC will be paid nothing more out of the housing portion of project tax increment, and will receive seventy five percent (75%) of the unrestricted portion of project tax increment until February, 2024 with fifty percent (50%) thereafter. Hercules, LLC will also be paid $3 million on or before June 22, 2011, none of which is to be paid during the 2009-10 fiscal year. Finally Hercules, LLC will be paid $968,816 as the balance of project tax increment funds due for the fiscal year 2009-2010, which funds were being held by the Redevelopment Agency pending the settlement. The Agency has recorded the amount as a liability as of June 30, 2010.

SERAF Contingency – During the fiscal year 2008-2009, the State of California experienced a severe budgetary crisis. Various "budget trailer bills" were passed by the state legislature to balance the state's budget, including bills that required California redevelopment agencies to transfer funds to the Educational Revenue Augmentation Fund (ERAF) and Supplemental Educational Revenue Augmentation Fund (SERAF) administered by the various county auditor-controllers. Noted below is a general explanation of the SERAF legislation, together with the effect of this legislation on the City of Hercules and its Redevelopment Agency (the Agency).

## NOTE 10 – CONTINGENCIES (CONTINUED)

Pursuant to AB 26 4x, a budget trailer bill, California redevelopment agencies were required to make SERAF contributions totaling $1.7 billion for the fiscal year 2009-2010 and $350 million for the fiscal year 2010-2011. Under AB 26 4x, agencies may borrow portions of the required contributions from their low and moderate income housing fund. Alternatively, sponsoring governmental agencies (the cities or counties) may elect to pay the SERAF contributions on behalf of their redevelopment agencies. On October 20, 2009, the (CRA) filed a class action lawsuit on behalf of all California redevelopment agencies challenging the SERAF obligations as unconstitutional.

The Agency's SERAF contributions are $4,992,984 for the fiscal year 2009-2010 and $1,026,977 for 2010-2011. It is the position of Agency officials that the SERAF contributions required by AB 26 4x are unconstitutional, and that the Agency is not obligated to make these contributions. The Agency has not made the contribution for 2009-2010, but has recorded the payment as a liability as of June 30, 2010.

The Agency is also presently involved in other certain matters of litigation that have arisen in the normal course of conducting Agency business. Agency management believes, based upon consultation with the Agency's Attorney, that these cases (except for the aforementioned cases), in the aggregate, are not expected to result in a material adverse financial impact on the Agency. Additionally, Agency management believes that the Agency's insurance programs are sufficient to cover any potential losses should an unfavorable outcome materialize.

## NOTE 11 – INTERFUND ACTIVITY

The following represents the interfund activity of the Agency for the fiscal year ended June 30, 2010.

### A. Due To/From Other Funds

| Funds | Interfund Receivable | Interfund Payable |
|---|---|---|
| Major Funds: | | |
| Affordable Housing Special Revenue Fund | $ 40,834 | $ - |
| Debt Service Fund | | 2,171,043 |
| Capital Projects Fund | 2,130,209 | |
| | $ 2,171,043 | $ 2,171,043 |

### B. Transfers To/From Other Funds

| Funds | Transfers In | Transfers Out |
|---|---|---|
| Major Funds: | | |
| Operating Special Revenue Fund | $ 1,208,056 | $ 7,992,569 |
| Affordable Housing Special Revenue Fund | 882,329 | 2,046,967 |
| Debt Service Fund | 9,844,536 | 24,387,210 |
| Capital Projects Fund | 23,747,210 | 1,255,385 |
| | $ 35,682,131 | $ 35,682,131 |

## NOTE 12 – PRIOR PERIOD ADJUSTMENTS

A prior period adjustment of ($52,241) was made on the government-wide Statement of Activities due to an understatement of advances from the City of Hercules in the amount of ($177,241) and an understatement of interest receivable in the amount of $125,000.

## NOTE 13 – STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY

Deficit Fund Balances/Net Assets

As of June 30, 2010 the Redevelopment Agency Operating Special Revenue fund and Affordable Housing Special Revenue fund had deficit fund balances of $8,065,251 and $2,173,320 respectively. The deficit fund balances are expected to be eliminated in future years through tax increment revenue and the increase of tax increment over the additional life of ten years.

As of June 30, 2010, the Statement of Net Assets of the Hercules Redevelopment Agency has a deficit net assets balance of $48,448,511. The Agency will be able to address its long term financial obligations with the additional ten years of tax increment flow and future resources will be sufficient to pay long-term obligations as they become due. The extension of the effectiveness of the Dynamite Plan and the time limit to repay Agency indebtedness by ten years for the Dynamite Redevelopment Project will permit the Agency to issue longer-term bonds and leverage additional capital from debt financing for projects.

Expenditures in Excess of Appropriations

The following funds had departmental expenditures in excess of budget. Sufficient revenues were available to fund these expenditures:

| Governmental Funds: | Excess Expenditures |
|---|---|
| Redevelopment Agency Debt Service Fund: | |
| Community development | $ 3,079,195 |
| Redevelopment Agency Capital Projects Fund: | |
| Interest and fiscal agent fees | 1,925,962 |

## NOTE 14 – GOING CONCERN

The accompanying financial statements have been prepared assuming that the Agency will continue as a going concern. As discussed in Note 14, the Agency has suffered a net assets deficit of $48,448,511 at June 30, 2010. The Operating Special Revenue Fund and Affordable Housing Special Revenue fund also have fund deficits of $8,065,251 and $2,173,320 respectively at June 30, 2010. The Agency's tax increment revenue was insufficient to pay the current year's debt service.

Since the adoption of the original redevelopment plan in 1983, the Agency has made efforts to eliminate such conditions of blight by funding needed infrastructure, providing housing and housing rehabilitation, public facilities, assisting existing businesses and providing incentives for new development. However, a majority of the conditions within the Redevelopment Project area have not improved, and there continues to be a substantial need to eliminate deficient public facilities and other blighting conditions within the Dynamite Redevelopment Project Area.

## NOTE 14 – GOING CONCERN (CONTINUED)

The 2009 Redevelopment Plan will facilitate the redevelopment of the Hercules Merged Project Area and eliminate conditions of blight and prevent their recurrence through acquisition, installation, development, construction, reuse of streets, facilities, utilities or other structures; redevelopment of land by private enterprises or public agencies for uses in accordance with the Original Plan and the 2009 Amendment, financing of the construction of residential, commercial and industrial buildings and the mortgage financing of residential, commercial and industrial buildings.

The Agency will be able to eliminate the net assets deficit balances by seeking and utilizing a variety of potential financing resources, including property tax increment; the nature and timing of redevelopment assistance will depend on the amount and availability of such financing resources, including tax increment, generated by new investment in the Hercules Merged Project Area and under the 2009 Amendment no public redevelopment activity in the Hercules Merged Project Area can be undertaken unless the Agency can demonstrate that is has adequate revenue to finance the activity.

The elimination of blight and the redevelopment of the Hercules Merged Project Area cannot be reasonably expected to be accomplished by private enterprise acting alone, or by governmental action, or both, without the aid and assistance of the Agency. Neither the private sector nor local government has the financial capacity, without assistance from the Agency to underwrite the costly relocating of utilities, removing of deed restrictions, decommissioning of the former Hercules Pumping Station improvements, and remediating environmental contamination which are required in the added area. The use of Agency redevelopment funds will provide the tools and financial assistance necessary to form public/private partnerships required to overcome the challenges to redevelopment in the added area. The opportunity to utilize redevelopment funds to facilitate redevelopment of the added area is in the interest of the entire community.

## NOTE 15 – SUBSEQUENT EVENTS

As of March 2011, construction on the Sycamore North Project has slowed and the building is currently being marketed for sale.

On March 8, 2011, the Agency's Board of Directors approved the transfer of four properties to the City of Hercules as repayment of long-term debt owed by the Agency to the City.

# REQUIRED SUPPLEMENTAL INFORMATION

HERCULES REDEVELOPMENT AGENCY
REQUIRED SUPPLEMENTAL INFORMATION
JUNE 30, 2010

## 1. BUDGETARY PRINCIPLES

In establishing the budgetary data reflected in the financial statements, the Agency follows the below listed procedures:

1. Public hearings are conducted to obtain public comments.

2. The Executive Director is authorized to transfer budgetary amounts within a single fund; however, any revisions that alter the total expenditures of any fund must be approved by the Agency Board.

3. Legally adopted budgets and formal budgetary integration is employed as a management control device during the year.

4. Budgets are adopted on a basis consistent with USGAAP.

5. Budgeted revenue amounts represent the original budget modified by adjustments authorized during the year. Budgeted expenditure amounts represent original appropriations adjusted for supplemental appropriations during the year which were contingent upon new or additional revenue sources and reappropriated amounts for prior year encumbrances. The Executive Director must approve adjustments to departmental budgets; however, management may amend the budgeted amounts within departmental expenditure classifications.

6. Certain appropriations carry over at the end of the fiscal year and then are rebudgeted for the coming fiscal year.

**HERCULES REDEVELOPMENT AGENCY**
SCHEDULE OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE -
BUDGET AND ACTUAL
REDEVELOPMENT AGENCY OPERATING SPECIAL REVENUE FUND
For the Fiscal Year Ended June 30, 2010

| | Budgeted Amounts | | | Variance with Final Budget Positive |
|---|---|---|---|---|
| | **Original** | **Final** | **Actual** | **(Negative)** |
| **Revenues:** | | | | |
| Taxes and assessments | $ 13,641,476 | $ 13,641,476 | $ 8,324,442 | $ (5,317,034) |
| Use of money and property | | | (258,173) | (258,173) |
| Program income | 176,000 | 530,246 | 285,842 | (244,404) |
| Charges for services | | | 279 | 279 |
| Miscellaneous | 5,000 | 75,000 | 80,857 | 5,857 |
| Total revenues | 13,822,476 | 14,246,722 | 8,433,247 | (5,813,475) |
| **Expenditures:** | | | | |
| Current: | | | | |
| Community development | 5,109,618 | 10,846,249 | 10,465,343 | 380,906 |
| Total expenditures | 5,109,618 | 10,846,249 | 10,465,343 | 380,906 |
| Excess of revenues over (under) expenditures | 8,712,858 | 3,400,473 | (2,032,096) | (5,432,569) |
| **Other financing sources (uses):** | | | | |
| Transfer in from the City of Hercules | | 4,992,984 | 288,036 | (4,704,948) |
| Transfers in | | | 1,208,056 | 1,208,056 |
| Transfers out | (8,632,653) | (8,769,313) | (7,992,569) | 776,744 |
| Total other financing sources (uses) | (8,632,653) | (3,776,329) | (6,496,477) | (2,720,148) |
| Net changes in fund balance | 80,205 | (375,856) | (8,528,573) | (8,152,717) |
| Fund balance - July 1, 2009 | 463,322 | 463,322 | 463,322 | |
| Fund balance (deficit) - June 30, 2010 | $ 543,527 | $ 87,466 | $ (8,065,251) | $ (8,152,717) |

**HERCULES REDEVELOPMENT AGENCY**
SCHEDULE OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE - BUDGET AND ACTUAL
AFFORDABLE HOUSING SPECIAL REVENUE FUND
For the Fiscal Year Ended June 30, 2010

| | Budgeted Amounts | | | Variance with Final Budget Positive |
|---|---|---|---|---|
| | Original | Final | Actual | (Negative) |
| **Revenues:** | | | | |
| Taxes and assessments | $ 3,410,371 | $ 3,410,371 | $ 2,081,111 | $ (1,329,260) |
| Use of money and property | 10,000 | 10,000 | (103,978) | (113,978) |
| Program income | 91,800 | 91,800 | 189,876 | 98,076 |
| Charges for services | 81,800 | 116,905 | 98,407 | (18,498) |
| Miscellaneous | 16,000 | 16,000 | 8,034 | (7,966) |
| Total revenues | 3,609,971 | 3,645,076 | 2,273,450 | (1,371,626) |
| **Expenditures:** | | | | |
| Current: | | | | |
| Community development | 3,134,625 | 4,486,725 | 2,430,539 | 2,056,186 |
| Total expenditures | 3,134,625 | 4,486,725 | 2,430,539 | 2,056,186 |
| Excess of revenues over (under) expenditures | 475,346 | (841,649) | (157,089) | 684,560 |
| **Other financing sources (uses):** | | | | |
| Transfer in from the City of Hercules | | | 35,000 | 35,000 |
| Transfers in | | 1,300,000 | 882,329 | (417,671) |
| Transfers out | (1,976,155) | (1,976,155) | (2,046,967) | (70,812) |
| Total other financing sources (uses) | (1,976,155) | (676,155) | (1,129,638) | (453,483) |
| Net changes in fund balance | (1,500,809) | (1,517,804) | (1,286,727) | 231,077 |
| Fund balance (deficit) - July 1, 2009 | (886,593) | (886,593) | (886,593) | |
| Fund balance (deficit) - June 30, 2010 | $ (2,387,402) | $ (2,404,397) | $ (2,173,320) | $ 231,077 |

THIS PAGE IS INTENTIONALLY LEFT BLANK

# OTHER SUPPLEMENTAL INFORMATION

**HERCULES REDEVELOPMENT AGENCY**

SCHEDULE OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE -
BUDGET AND ACTUAL
REDEVELOPMENT AGENCY DEBT SERVICE FUND
For the Fiscal Year Ended June 30, 2010

| | Final Budget | Actual | Variance with Final Budget Positive (Negative) |
|---|---|---|---|
| **Revenues:** | | | |
| Use of money and property | $ 1,900,000 | $ 122,839 | $ (1,777,161) |
| Total revenues | 1,900,000 | 122,839 | (1,777,161) |
| **Expenditures:** | | | |
| Current: | | | |
| Community development | | 3,079,195 | (3,079,195) |
| Debt service: | | | |
| Principal | 3,460,000 | 3,190,926 | 269,074 |
| Interest and fiscal agent fees | 10,327,549 | 7,318,681 | 3,008,868 |
| Total expenditures | 13,787,549 | 13,588,802 | 198,747 |
| Excess of revenues over (under) expenditures | (11,887,549) | (13,465,963) | (1,578,414) |
| **Other financing sources (uses):** | | | |
| Proceeds from issuance of long-term debt | | 754,337 | 754,337 |
| Transfers in | 17,480,858 | 9,844,536 | (7,636,322) |
| Transfers out | (49,915,476) | (24,387,210) | 25,528,266 |
| Total other financing sources (uses) | (32,434,618) | (13,788,337) | 18,646,281 |
| Net changes in fund balance | (44,322,167) | (27,254,300) | 17,067,867 |
| Fund balance - July 1, 2009 | 62,375,560 | 62,375,560 | |
| Fund balance - June 30, 2010 | $ 18,053,393 | $ 35,121,260 | $ 17,067,867 |

**HERCULES REDEVELOPMENT AGENCY**

SCHEDULE OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE - BUDGET AND ACTUAL

REDEVELOPMENT AGENCY CAPITAL PROJECTS FUND

For the Fiscal Year Ended June 30, 2010

| | Final Budget | Actual | Variance with Final Budget Positive (Negative) |
|---|---|---|---|
| **Revenues:** | | | |
| Use of money and property | $ - | $ - | $ - |
| Total revenues | | | |
| **Expenditures:** | | | |
| Capital outlay | 55,314,732 | 29,286,378 | 26,028,354 |
| Debt service: | | | |
| Interest and fiscal agent fees | | 1,925,962 | (1,925,962) |
| Total expenditures | 55,314,732 | 31,212,340 | 24,102,392 |
| Excess of revenues over (under) expenditures | (55,314,732) | (31,212,340) | 24,102,392 |
| **Other financing sources (uses):** | | | |
| Proceeds from issuance of long-term debt | | 4,817,064 | 4,817,064 |
| Transfer in from the City of Hercules | 5,278,294 | 2,108,097 | (3,170,197) |
| Transfers in | 45,982,999 | 23,747,210 | (22,235,789) |
| Transfers out | | (1,255,385) | (1,255,385) |
| Total other financing sources (uses) | 51,261,293 | 29,416,986 | (21,844,307) |
| Net changes in fund balance | (4,053,439) | (1,795,354) | 2,258,085 |
| Fund balance - July 1, 2009 | 5,309,610 | 5,309,610 | |
| Fund balance - June 30, 2010 | $ 1,256,171 | $ 3,514,256 | $ 2,258,085 |

MOSS, LEVY & HARTZHEIM LLP
CERTIFIED PUBLIC ACCOUNTANTS

**PARTNERS**
RONALD A LEVY, CPA
CRAIG A HARTZHEIM, CPA
HADLEY Y HUI, CPA

9107 WILSHIRE BLVD., SUITE 400
BEVERLY HILLS, CA 90210
TEL: 310.273.2745
FAX: 310.273.1689
www.mlhcpas.com

# 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 Board of the Hercules Redevelopment Agency
Hercules Redevelopment Agency
Hercules, California

We have audited the accompanying financial statements of the governmental activities and each major fund of the Hercules Redevelopment Agency (Agency), a component unit of the City of Hercules, California (City) as of and for the fiscal year ended June 30, 2010, and have issued our report thereon dated December 29, 2010 and April 11, 2011. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

## Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Agency's internal control over financial reporting as a basis for designing 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 a 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.

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 the internal control 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.



**OFFICES:** BEVERLY HILLS · SANTA MARIA

**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. Such provisions include those provisions of laws and regulations identified in the *Guidelines for Compliance Audits of California Redevelopment Agencies* issued by the California State Controller. 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 four instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying Schedule of Findings and Recommendations as items #2010-1 to #2010-4.

The Agency's responses to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. We did not audit the Agency's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of management, others within the organization, Board of Directors, bond trustees, and the California State Controller's Office Division of Accounting and Reporting, and is not intended to be and should not be used by anyone other than these specified parties.

Moss, Levy & Hartzheim

Moss, Levy & Hartzheim, LLP
Beverly Hills, California
December 29, 2010, except for Findings #2010-2 to #2010-4, as to which the date is April 11, 2011.

# FINDINGS AND RECOMMENDATIONS

**HERCULES REDEVELOPMENT AGENCY**
**SCHEDULE OF FINDINGS AND RECOMMENDATIONS**
**JUNE 30, 2010**

**Finding 2010-1**

Criteria or Specific Requirement
Under Health and Safety Code Section 33490, the Agency is required to adopt a new implementation plan every five years.

Condition Found
The Agency's prior implementation plan expired December 31, 2009 and no new plan was adopted.

Recommendation
Every 5 years the Agency needs to adopt a new 5 year implementation plan by December 31 as specified under the Health and Safety Codes of the State of California.

Management's Response
The Agency adopted its 5 Year Implementation Plan on January 12, 2010, twelve days past the deadline of December 31, 2010. In the future, the Agency will adopt its plan by December 31st of the year the document is due.

**Finding 2010-2**

Criteria or Specific Requirement
Under Health and Safety Code Section 33334.3(d), the Agency is required to prepare a written determination showing that planning and administrative expenditures were necessary for the production, improvement, or preservation of low and moderate income housing in the Housing Fund.

Condition Found
The Agency charged $300,000 in administrative charges to the Housing Fund during fiscal year 2009/10 and had no supporting documentation for how this amount was derived, other than it was approved in the budget.

Recommendation
We recommend that the Agency research the basis for the $300,000 of administrative charges and modify the amount, if necessary. Proper supporting documentation should be developed to substantiate the $300,000 as well.

Management's Response
The Agency will ensure it properly justifies and documents any administrative charges to the Housing Fund.

**Finding 2010-3**

Criteria or Specific Requirement
Under Health and Safety Code Section 33080.4, the Agency is required to produce and submit on a timely basis (by December 31st) to the Agency's Board of Directors and the California State Controller, a loan report that identifies loans which equal or exceed $50,000 that were found by the Agency during the previous fiscal year to have either defaulted or not complied with the terms of the agreement approved by the Agency.

Condition Found
One loan for $56,000 was defaulted on during the fiscal year ended June 30, 2010 but was never reported to the Board of Directors or the California State Controller.

Recommendation
All loans found to be in default or non compliant with the loan agreement should be reported to the Board of Directors and California State Controller by December 31st of each year.

Management's Response

During fiscal year 2009-10 the Affordable Housing program was managed by an outside consulting company. Due to miscommunication, the default notice received by the consulting company was not conveyed to the City therefore no report was made to the Board of Directors or the California State Controller. Beginning March 2011, Affordable Housing program was transferred back in-house and we are monitoring all the activities closely. We will comply with Health and Safety Code Section 33080.4 and report all loans in default or non compliant with the loan agreement to the Board of Directors and California State Controller by December 31 of each year.

**Finding 2010-4**

Criteria or Specific Requirement

Under Health and Safety Code Section 33334.3, the Agency's Housing Fund has strict guidelines on the type of expenditures allowed.

Condition Found

During the fiscal year, the Agency's Housing Fund expended $9,600 on a lobbyist, which is not an allowable expenditure.

Recommendation

We recommend that only allowable costs be expended from the Housing Fund.

Management's Response

The City's lobbyist is no longer charged to the Agency's Housing Fund.

**HERCULES REDEVELOPMENT AGENCY**
**STATUS OF PRIOR YEAR FINDINGS AND RECOMMENDATIONS**
**JUNE 30, 2010**

None noted.