

***CITY OF HERCULES  
CALIFORNIA***

**ANNUAL FINANCIAL REPORT  
For the fiscal year ended  
June 30, 2012**

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**CITY OF HERCULES**

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For the fiscal year ended June 30, 2012

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## **FINANCIAL SECTION**

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## INDEPENDENT AUDITOR'S REPORT

To the Honorable Mayor and Members  
of the City Council of the City of Hercules  
Hercules, California

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Hercules (City), California, as of and for the fiscal year ended June 30, 2012, which collectively comprise the City's basic financial statements, as listed in the table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* as issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our 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, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Hercules, California, as of June 30, 2012, and the respective changes in financial position and cash flows, where applicable thereof, for the fiscal year then ended, in conformity with accounting principles generally accepted in the United States of America.

As described in Note 18 to the financial statements, Assembly Bill X1 26 was upheld and declared constitutional by the California Supreme Court on December 29, 2011. As part of the decision, the Supreme Court established the date of dissolution for redevelopment agencies to be February 1, 2012. The redevelopment agencies in California, including the Hercules Redevelopment Agency (Agency), was terminated and successor agencies were appointed to wind down the affairs of the former redevelopment agencies in accordance with the provisions of Assembly Bill X1 26. The City of Hercules has elected to be appointed as the Redevelopment Successor Agency for purposes of winding down the redevelopment affairs of the Agency attributable to City redevelopment project areas. As a result, the net assets associated with City redevelopment projects were transferred to the City and recorded in a private purpose trust fund on February 1, 2012. The City elected to not be the Housing Successor Agency and did not retain any assets associated with the housing functions.

As described in Note 20 to the financial statements, the City's General Fund has outstanding loans of \$21.1 million owed by the former redevelopment agency (Agency), now a private purpose trust fund of the City. This outstanding loan represents approximately 83 percent of the City's General Fund's assets. The written agreement between the Agency and the City to fund costs on behalf of the Agency was signed within two years of the creation of the Agency. Under Assembly Bill X1 26 (Redevelopment Dissolution Act), a written agreement between a redevelopment agency and the city that created it that provided loans or other startup funds for the redevelopment agency that were entered into within two years of the formation of the redevelopment agency are not invalid. The City is currently working with the State Department of Finance to determine the outcome of these loans. The possible outcome of this matter cannot presently be determined. Accordingly, no provision for any allowance for doubtful accounts has been made in the financial statements for possible forgiveness of these loans.

To the Honorable Mayor and Members  
of the City Council of the City of Hercules  
Hercules, California

In accordance with the *Government Auditing Standards*, we have also issued a report dated April 1, 2014, on our consideration of the City's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Management has omitted the Management's Discussion and Analysis that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing 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. Our opinion on the basic financial statements is not affected by this missing information.

Accounting principles generally accepted in the United States of America require that the budgetary comparison schedules and the trend information of the post-employment benefits other than pensions 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.



Roseville, California  
April 1, 2014

## **BASIC FINANCIAL STATEMENTS**

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## **GOVERNMENT-WIDE FINANCIAL STATEMENTS**

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**CITY OF HERCULES**

Statement of Net Assets  
June 30, 2012

|  | Primary Government         |                             |                       |
|--|----------------------------|-----------------------------|-----------------------|
|  | Governmental<br>Activities | Business-Type<br>Activities | Totals                |
| <b>ASSETS</b>                                      |                            |                             |                       |
| Cash and investments                               | \$ 11,545,132              | 8,014,060                   | \$ 19,559,192         |
| Cash with fiscal agent                             | 2,338,839                  | 14,047,755                  | 16,386,594            |
| Accounts receivable                                | 2,313,907                  | 412,761                     | 2,726,668             |
| Interest receivable                                | 46,972                     | --                          | 46,972                |
| Prepaid expenses                                   | 9,601                      | --                          | 9,601                 |
| Inventories  | 19,028                     | 262,156                     | 281,184               |
| Loans receivable                                   | 2,473,669                  | --                          | 2,473,669             |
| Lease receivable                                   | 9,533,758                  | --                          | 9,533,758             |
| Due from private purpose trust fund                | 14,191,903                 | --                          | 14,191,903            |
| Internal balances                                  | 1,321,057                  | (1,321,057)                 | --                    |
| Deferred charges - net of accumulated amortization | 379,769                    | 590,214                     | 969,983               |
| Land held for resale                               | 15,646,868                 | 13,774,145                  | 29,421,013            |
| Other post employment benefit asset                | 258,336                    | --                          | 258,336               |
| Capital assets:                                    |                            |                             |                       |
| Nondepreciable                                     | 7,337,355                  | 3,005,645                   | 10,343,000            |
| Depreciable, net of accumulated depreciation       | 66,833,826                 | 18,179,684                  | 85,013,510            |
| Total Assets                                       | <u>134,250,020</u>         | <u>\$ 56,965,363</u>        | <u>\$ 191,215,383</u> |
| <b>LIABILITIES</b>                                 |                            |                             |                       |
| Accounts payable                                   | \$ 695,983                 | \$ 1,119,406                | \$ 1,815,389          |
| Accrued wages                                      | 225,061                    | 9,717                       | 234,778               |
| Accrued interest payable                           | 561,391                    | 477,552                     | 1,038,943             |
| Deposits payable                                   | 114,237                    | --                          | 114,237               |
| Claims and judgments payable                       | 123,671                    | --                          | 123,671               |
| Noncurrent liabilities:                            |                            |                             |                       |
| Due within one year                                | 776,180                    | 372,300                     | 1,148,480             |
| Due in more than one year                          | 23,681,659                 | 23,651,277                  | 47,332,936            |
| Total Liabilities                                  | <u>26,178,182</u>          | <u>25,630,252</u>           | <u>51,808,434</u>     |
| <b>NET ASSETS</b>                                  |                            |                             |                       |
| Invested in capital assets, net of related debt    | 67,178,014                 | 11,246,807                  | 78,424,821            |
| Restricted for:                                    |                            |                             |                       |
| Public safety                                      | 82,726                     | --                          | 82,726                |
| Streets and roads                                  | 4,598,488                  | --                          | 4,598,488             |
| Development  | 21,950,080                 | --                          | 21,950,080            |
| Unrestricted                                       | 14,262,530                 | 20,088,304                  | 34,350,834            |
| Total Net Assets                                   | <u>\$108,071,838</u>       | <u>\$ 31,335,111</u>        | <u>\$ 139,406,949</u> |

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

**CITY OF HERCULES**

Statement of Activities  
For the Year Ended June 30, 2012

| Functions/Programs             | Expenses                 | Program Revenues        |                                    |                                  |
|--------------------------------|--------------------------|-------------------------|------------------------------------|----------------------------------|
|                                |                          | Charges for Services    | Operating Grants and Contributions | Capital Grants and Contributions |
| Primary Government:            |                          |                         |                                    |                                  |
| Governmental activities:       |                          |                         |                                    |                                  |
| General government             | \$ 5,503,393             | \$ 116,028              | \$ 68,619                          | --                               |
| Public safety                  | 4,692,607                | 327,329                 | 235,450                            | --                               |
| Public works                   | 5,301,525                | 2,285,931               | 1,223,715                          | --                               |
| Parks and recreation           | 2,148,213                | 1,487,192               | --                                 | --                               |
| Community development          | 2,247,460                | 302,960                 | --                                 | --                               |
| Interest on long term debt     | 1,147,415                | --                      | --                                 | --                               |
| Total governmental activities  | <u>21,040,613</u>        | <u>4,519,440</u>        | <u>1,527,784</u>                   | <u>--</u>                        |
| Business-Type Activities:      |                          |                         |                                    |                                  |
| Sewer                          | 3,236,147                | 4,970,329               | --                                 | --                               |
| Hercules Municipal Utility     | 3,329,348                | 2,693,486               | --                                 | --                               |
| Total business-type activities | <u>6,565,495</u>         | <u>7,663,815</u>        | <u>--</u>                          | <u>--</u>                        |
| <br>Total City                 | <br><u>\$ 27,606,108</u> | <br><u>\$12,183,255</u> | <br><u>\$ 1,527,784</u>            | <br><u>\$ --</u>                 |

General revenues

Taxes:

  Secured and unsecured property taxes

  Sales and use taxes

  Franchise taxes

  Other taxes

  Unrestricted motor vehicle taxes in-lieu

  Use of money and property

  Miscellaneous revenue

    Total general revenues

Change in net assets before extraordinary item

Extraordinary item - RDA Dissolution

Change in net assets

  Net Assets - Beginning of Year

  Net Assets - End of Year

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

Net (Expense) Revenue and  
Changes in Net Assets

| Primary Government         |                             |                       |
|----------------------------|-----------------------------|-----------------------|
| Governmental<br>Activities | Business-Type<br>Activities | Total                 |
| \$ (5,318,746)             |                             | \$ (5,318,746)        |
| (4,129,828)                |                             | (4,129,828)           |
| (1,791,879)                |                             | (1,791,879)           |
| (661,021)                  |                             | (661,021)             |
| (1,944,500)                |                             | (1,944,500)           |
| (1,147,415)                |                             | (1,147,415)           |
| <u>(14,993,389)</u>        | --                          | <u>(14,993,389)</u>   |
| --                         | \$ 1,734,182                | 1,734,182             |
| --                         | (635,862)                   | (635,862)             |
| --                         | <u>1,098,320</u>            | <u>1,098,320</u>      |
| <u>(14,993,389)</u>        | <u>1,098,320</u>            | <u>(13,895,069)</u>   |
| 6,116,169                  | --                          | 6,116,169             |
| 1,628,386                  | --                          | 1,628,386             |
| 645,196                    | --                          | 645,196               |
| 2,209,580                  | --                          | 2,209,580             |
| 1,393,766                  | --                          | 1,393,766             |
| 2,083,873                  | 123,150                     | 2,207,023             |
| 1,109,636                  | 46,310                      | 1,155,946             |
| <u>15,186,606</u>          | <u>169,460</u>              | <u>15,356,066</u>     |
| 193,217                    | 1,267,780                   | 1,460,997             |
| <u>42,806,674</u>          | --                          | <u>42,806,674</u>     |
| 42,999,891                 | 1,267,780                   | 44,267,671            |
| <u>65,071,947</u>          | <u>30,067,331</u>           | <u>95,139,278</u>     |
| <u>\$ 108,071,838</u>      | <u>\$ 31,335,111</u>        | <u>\$ 139,406,949</u> |

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

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## **FUND FINANCIAL STATEMENTS**

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## GOVERNMENTAL FUND FINANCIAL STATEMENTS

**General Fund** – This fund is used to account for all revenues and expenditures necessary to carry out basic governmental activities of the City that are not accounted for through other funds. For the City, the General Fund includes such activities as police, planning, engineering, public works, operations and maintenance, and legal and administrative services.

**Redevelopment Agency Special Revenue Fund** – This fund is used to account for the operating costs of the Redevelopment Agency and for the tax increment monies to be expended for low and moderate income housing purposes.

**Redevelopment Agency Debt Service Fund** – This fund is used to account for the accumulation of resources used for the payment of principal and interest on the Redevelopment Agency tax allocation bonds and notes payable.

**Hercules Public Financing Authority Debt Service Fund** – This fund is used to account for the accumulation of resources for, and the payment of, principal and interest on various Lease Revenue Bonds issued to cover the refinancing of the original City Hall debt issue and to generate additional resources to assist in the construction of a new library building and other general government projects.

**Redevelopment Agency Capital Projects Fund** – This fund is used to account for major capital projects undertaken by the Redevelopment Agency.

**Other Governmental Funds** – These funds are special revenue funds, a capital projects fund, and a debt service fund that have not been determined to be major funds, as defined by GASB Statement No. 34.

**CITY OF HERCULES**

Balance Sheet  
Governmental Funds  
June 30, 2012

|   | General<br>Fund          | Redevelopment<br>Agency<br>Special Revenue<br>Fund | Redevelopment<br>Agency<br>Debt Service<br>Fund |
|---|--------------------------|--|---|
| <b>ASSETS</b>                           |                          |  |   |
| Cash and investments                    | \$ 565,468               | \$ --  | \$ --   |
| Cash and investments with fiscal agent  | --                       | --   | --  |
| Accounts receivable                     | 916,393                  | --   | --  |
| Interest receivable                     | 25,601                   | --   | --  |
| Prepays                                 | 9,601                    | --   | --  |
| Due from other funds                    | 274,086                  | --   | --  |
| Inventories                             | 8,015                    | --   | --  |
| Loans receivable                        | 2,473,669                | --   | --  |
| Lease receivable                        | --                       | --   | --  |
| Land held for resale                    | 7,223,845                | --   | --  |
| Advances to other funds                 | 13,895,004               | --   | --  |
| Total Assets                            | <u>\$ 25,391,682</u>     | <u>\$ --</u>                                       | <u>\$ --</u>                                    |
| <b>LIABILITIES</b>                      |                          |  |   |
| Accounts payable                        | \$ 262,173               | \$ --  | \$ --   |
| Accrued wages                           | 206,610                  | --   | --  |
| Deposits payable                        | 114,237                  | --   | --  |
| Claims and judgments payable            | 123,671                  | --   | --  |
| Unavailable revenue                     | 2,473,669                | --   | --  |
| Due to other funds                      | 753,631                  | --   | --  |
| Total Liabilities                       | <u>3,933,991</u>         | <u>--</u>  | <u>--</u>                                       |
| <b>FUND BALANCES</b>                    |                          |  |   |
| Nonspendable                            | 21,136,465               | --   | --  |
| Restricted                              | --                       | --   | --  |
| Assigned                                | 561,482                  | --   | --  |
| Unassigned                              | (240,256)                | --   | --  |
| Total Fund Balances                     | <u>21,457,691</u>        | <u>--</u>  | <u>--</u>                                       |
| <br>Total Liabilities and Fund Balances | <br><u>\$ 25,391,682</u> | <br><u>\$ --</u>                                   | <br><u>\$ --</u>                                |

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

| Hercules<br>Public Financing<br>Authority Debt<br>Service Fund | Redevelopment<br>Agency<br>Capital Projects<br>Fund | Other<br>Governmental<br>Funds | Total                |
|--|---|--------------------------------|----------------------|
| \$ --  | \$ --   | \$ 8,699,090                   | \$ 9,264,558         |
| 2,338,839  | --  | --                             | 2,338,839            |
| --   | --  | 1,397,244                      | 2,313,637            |
| 21,371   | --  | --                             | 46,972               |
| --   | --  | --                             | 9,601                |
| --   | --  | 196,351                        | 470,437              |
| --   | --  | 11,013                         | 19,028               |
| --   | --  | --                             | 2,473,669            |
| 9,533,758  | --  | --                             | 9,533,758            |
| 5,545,919  | --  | 2,877,104                      | 15,646,868           |
| --   | --  | 1,940,012                      | 15,835,016           |
| <u>\$ 17,439,887</u>   | <u>\$ --</u>  | <u>\$ 15,120,814</u>           | <u>\$ 57,952,383</u> |
| \$ --  | \$ --   | \$ 231,898                     | \$ 494,071           |
| --   | --  | 14,229                         | 220,839              |
| --   | --  | --                             | 114,237              |
| --   | --  | --                             | 123,671              |
| 9,533,758  | --  | 648,021                        | 12,655,448           |
| 264,843  | --  | 527,650                        | 1,546,124            |
| <u>9,798,601</u>   | <u>--</u>   | <u>1,421,798</u>               | <u>15,154,390</u>    |
| 5,545,919  | --  | 2,888,117                      | 29,570,501           |
| 2,095,367  | --  | 10,984,426                     | 13,079,793           |
| --   | --  | --                             | 561,482              |
| --   | --  | (173,527)                      | (413,783)            |
| <u>7,641,286</u>   | <u>--</u>   | <u>13,699,016</u>              | <u>42,797,993</u>    |
| <u>\$ 17,439,887</u>   | <u>\$ --</u>  | <u>\$ 15,120,814</u>           | <u>\$ 57,952,383</u> |

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

**CITY OF HERCULES**

Reconciliation of the Governmental Funds Balance Sheet  
to the Government-Wide Statement of Net Assets - Governmental Activities  
June 30, 2012

|  |                       |
|--|-----------------------|
| Fund Balance - total governmental funds (pages 8 and 9)  | \$ 42,797,993         |
| Amounts reported for governmental activities in the statement<br>of net assets are different because:  |                       |
| Other long-term assets are not available to pay for current-period expenditures and,<br>therefore, are deferred in the governmental funds.   |                       |
| Other post employment benefit asset  | 258,336               |
| Deferred costs   | 379,769               |
| Capital assets used in governmental activities are not financial resources and,<br>therefore, are not reported in the governmental funds.  |                       |
|  | 73,559,207            |
| Unavailable revenues represent amounts that are not available to fund current expenditures<br>and, therefore, are not reported in the governmental funds.  |                       |
|  | 12,655,448            |
| Internal service funds are used by the City to charge the cost of its vehicle replacement,<br>IT replacement and facilities maintenance activities to individual funds. The assets and<br>liabilities of the internal service funds are included in governmental activities in the<br>statement of net assets. |                       |
|  | 3,421,713             |
| Long-term liabilities, including capital leases, are not due and payable<br>in the current period, and therefore are not reported in the governmental funds.   |                       |
| Accrued interest   | (561,391)             |
| Revenue bonds payable  | (17,000,292)          |
| Notes payable  | (5,350,000)           |
| Capital leases payable   | (1,682,006)           |
| Compensated absences   | (406,939)             |
| Net assets of governmental activities (page 3)   | <u>\$ 108,071,838</u> |

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

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**CITY OF HERCULES**

Statement of Revenues, Expenditures and Changes in Fund Balances  
Governmental Funds  
For the Year Ended June 30, 2012

|  | General<br>Fund      | Redevelopment<br>Agency<br>Special Revenue<br>Fund | Redevelopment<br>Agency<br>Debt Service<br>Fund |
|--|----------------------|--|---|
| <b>Revenues:</b>   |                      |  |   |
| Taxes and assessments  | \$ 5,489,472         | \$ 5,061,535                                       | \$ --   |
| Licenses and permits   | 343,071              | --   | --  |
| Fines and forfeitures  | 62,858               | --   | --  |
| Use of money and property                                    | 222,525              | 130,536  | 7,764   |
| Intergovernmental  | 1,455,596            | --   | --  |
| Program income   | --                   | 93,624   | --  |
| Charges for services   | 1,827,556            | --   | --  |
| Other revenues   | 930,391              | 61,146   | --  |
| Total Revenues   | <u>10,331,469</u>    | <u>5,346,841</u>                                   | <u>7,764</u>                                    |
| <b>Expenditures:</b>   |                      |  |   |
| Current:   |                      |  |   |
| General government   | 4,061,861            | --   | --  |
| Public safety  | 4,727,262            | --   | --  |
| Streets and public works                                     | 211,134              | --   | --  |
| Community development  | 439,227              | 540,238  | 835,632   |
| Recreation and culture                                       | 1,902,907            | --   | --  |
| Lease expense  | 779,109              | --   | --  |
| Capital outlay   |                      | --   | --  |
| Debt service:  |                      |  |   |
| Principal  | --                   | --   | 3,465,000                                       |
| Interest and fiscal agent fees                               | --                   | --   | 3,158,289                                       |
| Total Expenditures   | <u>12,121,500</u>    | <u>540,238</u>                                     | <u>7,458,921</u>                                |
| Excess (Deficiency) of Revenues Over<br>(Under) Expenditures | <u>(1,790,031)</u>   | <u>4,806,603</u>                                   | <u>(7,451,157)</u>                              |
| <b>Other Financing Sources (Uses):</b>                       |                      |  |   |
| Transfers in   | 117,500              | 598,773  | 9,858,593                                       |
| Transfers out  | <u>(2,019,507)</u>   | <u>(6,395,172)</u>                                 | <u>(801,716)</u>                                |
| Total Other Financing Sources (Uses)                         | <u>(1,902,007)</u>   | <u>(5,796,399)</u>                                 | <u>9,056,877</u>                                |
| Extraordinary item - RDA dissolution                         | <u>--</u>            | <u>18,113,727</u>                                  | <u>(16,591,379)</u>                             |
| Net Changes in Fund Balances                                 | (3,692,038)          | 17,123,931   | (14,985,659)                                    |
| Fund Balances, Beginning of Year                             | <u>25,149,729</u>    | <u>(17,123,931)</u>                                | <u>14,985,659</u>                               |
| Fund Balances, End of Year                                   | <u>\$ 21,457,691</u> | <u>\$ --</u>                                       | <u>\$ --</u>                                    |

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

| Hercules<br>Public Financing<br>Authority Debt<br>Service Fund | Redevelopment<br>Agency<br>Capital Projects<br>Fund | Other<br>Governmental<br>Funds | Total                |
|--|---|--------------------------------|----------------------|
| \$ --  | \$ --   | \$ 48,324                      | \$ 10,599,331        |
| --   | --  | --                             | 343,071              |
| --   | --  | --                             | 62,858               |
| 1,388,873  | (2,798)   | 331,029                        | 2,077,929            |
| --   | --  | 1,471,154                      | 2,926,750            |
| --   | --  | --                             | 93,624               |
| --   | --  | 2,285,955                      | 4,113,511            |
| --   | --  | --                             | 991,537              |
| <u>1,388,873</u>   | <u>(2,798)</u>                                      | <u>4,136,462</u>               | <u>21,208,611</u>    |
| --   | --  | --                             | 4,061,861            |
| --   | --  | --                             | 4,727,262            |
| --   | --  | 2,594,840                      | 2,805,974            |
| --   | --  | 266,979                        | 2,082,076            |
| --   | --  | --                             | 1,902,907            |
| --   | --  | --                             | 779,109              |
| --   | 334,078   | 336,253                        | 670,331              |
| 320,000  | --  | 121,223                        | 3,906,223            |
| 1,174,076  | --  | 83,876                         | 4,416,241            |
| <u>1,494,076</u>   | <u>334,078</u>                                      | <u>3,403,171</u>               | <u>25,351,984</u>    |
| <u>(105,203)</u>   | <u>(336,876)</u>                                    | <u>733,291</u>                 | <u>(4,143,373)</u>   |
| --   | 1,065,128   | 295,019                        | 11,935,013           |
| --   | (1,376,075)   | (1,342,543)                    | (11,935,013)         |
| --   | (310,947)   | (1,047,524)                    | --                   |
| --   | (37,016,673)  | --                             | (35,494,325)         |
| (105,203)  | (37,664,496)  | (314,233)                      | (39,637,698)         |
| <u>7,746,489</u>   | <u>37,664,496</u>                                   | <u>14,013,249</u>              | <u>82,435,691</u>    |
| <u>\$ 7,641,286</u>  | <u>\$ --</u>  | <u>\$ 13,699,016</u>           | <u>\$ 42,797,993</u> |

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

**CITY OF HERCULES**

Reconciliation of the Statement of Revenues, Expenditures, and  
Changes in Fund Balances of Governmental Funds to the  
Government-Wide Statement of Activities - Governmental Activities  
For the Year Ended June 30, 2012

|  |                    |                             |
|--|--------------------|-----------------------------|
| Net change to fund balance - total governmental funds (pages 12 and 13)  |                    | \$ (39,637,698)             |
| Amounts reported for governmental activities in the statement of activities are different because:   |                    |                             |
| <p>Governmental funds report capital outlay as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense.</p>  |                    |                             |
| Expenditures for general capital assets, infrastructure, and other related capital assets adjustments  | \$ 405,135         |                             |
| Less: current year depreciation  | <u>(3,468,134)</u> | (3,062,999)                 |
| <p>Governmental fund revenues deferred at year end due to unavailability, under the modified accrual method of accounting, are recognized as revenue on the full accrual method of accounting</p>  |                    |                             |
|  |                    | (1,813)                     |
| <p>Long-term debt proceeds provide current resources to governmental funds, but issuing debt increases long-term liabilities in the statements of net asset. Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduced long-term liabilities in the statement of net assets. Also governmental funds report the effect issuance costs when debt is first issued, whereas these amounts are deferred and amortized in the statement of activities.</p> |                    |                             |
| Principal repayments   | 3,906,223          |                             |
| Amortization of bond issuance costs, premiums and discounts  | <u>31,917</u>      | 3,938,140                   |
| <p>Some expenses reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds.</p>   |                    |                             |
| Change in compensated absences   |                    | 89,712                      |
| Change in accrued interest payable   |                    | 3,236,909                   |
| <p>Other post employment benefits are reported as an expenditure when contributions are made in the governmental funds, but are deferred assets for contributions made in excess of required amounts.</p>  |                    |                             |
|  |                    | 36,650                      |
| <p>Extraordinary item from the dissolution of the Redevelopment Agency</p>   |                    |                             |
|  |                    | 78,300,999                  |
| <p>Internal service funds are used by management to charge the costs of certain activities to individual funds. The net revenue of certain activities of the internal service funds is reported with governmental activities.</p>  |                    |                             |
|  |                    | <u>99,991</u>               |
| Change in net assets of governmental activities (pages 4 and 5)  |                    | <u><u>\$ 42,999,891</u></u> |

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

## PROPRIETARY FUNDS FINANCIAL STATEMENTS

**Sewer Fund** – This fund accounts for wastewater treatment to the cities of Hercules and Pinole and for the maintenance of the City's sewer lines and related facilities. It is a self-supporting activity which provides services on a user charge basis to residences and businesses.

**Hercules Municipal Utilities Fund** – This fund accounts for the operations of the City's electric utility that provides electrical power to areas of new development within Hercules' city limits.

**Internal Service Funds** – These funds account for activities related to vehicle replacement, IT equipment replacement, and facilities maintenance.

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**CITY OF HERCULES**

Statement of Fund Net Assets  
Proprietary Funds  
June 30, 2012

|                                     | <u>Business-Type Activities - Enterprise Funds</u> |  |                      | <u>Governmental Activities</u> |
|-------------------------------------|--|--|----------------------|--------------------------------|
|                                     | <u>Sewer Fund</u>                                  | <u>Hercules Municipal Utility Fund</u> | <u>Totals</u>        | <u>Internal Service Funds</u>  |
|                                     |  |  |                      |                                |
| <b>ASSETS</b>                       |  |  |                      |                                |
| Current Assets:                     |  |  |                      |                                |
| Cash and investments                | \$ 6,932,840                                       | \$ 1,081,220                           | \$ 8,014,060         | \$ 2,280,574                   |
| Cash with fiscal agent              | 7,360,360  | 6,687,395                              | 14,047,755           | --                             |
| Accounts receivable - net           | 227  | 412,534                                | 412,761              | 270                            |
| Interest receivable                 | --   | --                                     | --                   | --                             |
| Due from other funds                | --   | --                                     | --                   | 753,631                        |
| Inventory                           | --   | 262,156                                | 262,156              | --                             |
| Land held for resale                | 8,500,651  | 5,273,494                              | 13,774,145           | --                             |
| Total Current Assets                | <u>22,794,078</u>                                  | <u>13,716,799</u>                      | <u>36,510,877</u>    | <u>3,034,475</u>               |
| Noncurrent Assets:                  |  |  |                      |                                |
| Deferred bond issuance costs        | 333,346  | 256,868                                | 590,214              | --                             |
| Advances to other funds             | 313,047  | --                                     | 313,047              | --                             |
| Capital assets:                     |  |  |                      |                                |
| Non-depreciable :                   |  |  |                      |                                |
| Land                                | 150,000  | --                                     | 150,000              | --                             |
| Construction in progress            | 2,255,233  | 600,412                                | 2,855,645            | --                             |
| Total Nondepreciable Capital Assets | <u>2,405,233</u>                                   | <u>600,412</u>                         | <u>3,005,645</u>     | <u>--</u>                      |
| Depreciable:                        |  |  |                      |                                |
| Buildings and improvements          | 11,335,199   | --                                     | 11,335,199           | --                             |
| Infrastructure                      | 8,531,556  | 8,988,621                              | 17,520,177           | --                             |
| Machinery and equipment             | 156,072  | 108,159                                | 264,231              | 3,010,487                      |
| Total Depreciable Capital Assets    | <u>20,022,827</u>                                  | <u>9,096,780</u>                       | <u>29,119,607</u>    | <u>3,010,487</u>               |
| Less Accumulated Depreciation       | <u>(9,478,659)</u>                                 | <u>(1,461,264)</u>                     | <u>(10,939,923)</u>  | <u>(2,398,513)</u>             |
| Net Depreciable Capital Assets      | <u>10,544,168</u>                                  | <u>7,635,516</u>                       | <u>18,179,684</u>    | <u>611,974</u>                 |
| Net Capital Assets                  | <u>12,949,401</u>                                  | <u>8,235,928</u>                       | <u>21,185,329</u>    | <u>611,974</u>                 |
| Total Noncurrent Assets             | <u>13,595,794</u>                                  | <u>8,492,796</u>                       | <u>22,088,590</u>    | <u>611,974</u>                 |
| Total Assets                        | <u>\$ 36,389,872</u>                               | <u>\$ 22,209,595</u>                   | <u>\$ 58,599,467</u> | <u>\$ 3,646,449</u>            |

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

continued

**CITY OF HERCULES**

Statement of Fund Net Assets (continued)  
 Proprietary Funds  
 June 30, 2012

|   | Business-Type Activities - Enterprise Funds |  |                      | Governmental<br>Activities   |
|---|---|--|----------------------|------------------------------|
|   | Sewer<br>Fund                               | Hercules<br>Municipal<br>Utility<br>Fund | Totals               | Internal<br>Service<br>Funds |
| <b>LIABILITIES</b>                              |   |  |                      |                              |
| Current Liabilities:                            |   |  |                      |                              |
| Accounts payable                                | \$ 292,546                                  | \$ 826,860                               | \$ 1,119,406         | 201,912                      |
| Salaries and benefits payable                   | 5,555                                       | 4,162                                    | 9,717                | 4,222                        |
| Accrued interest payable                        | 210,297                                     | 267,255                                  | 477,552              | --                           |
| Compensated absences                            | 25,781                                      | 11,519                                   | 37,300               | 18,602                       |
| Long term debt, due within one year             | 230,000                                     | 105,000                                  | 335,000              | --                           |
| Total Current Liabilities                       | <u>764,179</u>                              | <u>1,214,796</u>                         | <u>1,978,975</u>     | <u>224,736</u>               |
| Noncurrent Liabilities:                         |   |  |                      |                              |
| Advances from other funds                       | --  | 1,634,104                                | 1,634,104            | --                           |
| Long term debt, due in more than one year       | 11,101,390                                  | 12,549,887                               | 23,651,277           | --                           |
| Total Noncurrent Liabilities                    | <u>11,101,390</u>                           | <u>14,183,991</u>                        | <u>25,285,381</u>    | <u>--</u>                    |
| Total Liabilities                               | <u>11,865,569</u>                           | <u>15,398,787</u>                        | <u>27,264,356</u>    | <u>224,736</u>               |
| <b>NET ASSETS</b>                               |   |  |                      |                              |
| Invested in capital assets, net of related debt | 8,978,371                                   | 2,268,436                                | 11,246,807           | 611,974                      |
| Unrestricted                                    | 15,545,932                                  | 4,542,372                                | 20,088,304           | 2,809,739                    |
| Total Net Assets                                | <u>24,524,303</u>                           | <u>6,810,808</u>                         | <u>31,335,111</u>    | <u>3,421,713</u>             |
| Total Liabilities and Net Assets                | <u>\$ 36,389,872</u>                        | <u>\$ 22,209,595</u>                     | <u>\$ 58,599,467</u> | <u>\$ 3,646,449</u>          |

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

**CITY OF HERCULES**

Statement of Revenues, Expenses and Changes in Fund Net Assets  
Proprietary Funds  
For the Year Ended June 30, 2012

|  | <u>Business-Type Activities - Enterprise Funds</u> |  |                     | <u>Governmental<br/>Activities</u>    |
|--|--|--|---------------------|---------------------------------------|
|  | <u>Sewer<br/>Fund</u>                              | <u>Hercules<br/>Municipal<br/>Utility<br/>Fund</u> | <u>Totals</u>       | <u>Internal<br/>Service<br/>Funds</u> |
| Operating Revenues:                    |  |  |                     |                                       |
| Sales and charges for services         | \$ 4,970,329                                       | \$ 2,693,486                                       | \$ 7,663,815        | \$ 638,452                            |
| Other operating revenue                | --   | 46,310   | 46,310              | 88,019                                |
| Total Operating Revenues               | <u>4,970,329</u>                                   | <u>2,739,796</u>                                   | <u>7,710,125</u>    | <u>726,471</u>                        |
| Operating Expenses:                    |  |  |                     |                                       |
| Salaries and benefits                  | 380,162  | 395,087  | 775,249             | 224,235                               |
| Services and supplies                  | 1,922,441  | 419,684  | 2,342,125           | 160,991                               |
| Purchase of electricity                | --   | 1,504,526  | 1,504,526           | --                                    |
| Depreciation                           | 394,510  | 209,119  | 603,629             | 268,286                               |
| Total Operating Expenses               | <u>2,697,113</u>                                   | <u>2,528,416</u>                                   | <u>5,225,529</u>    | <u>653,512</u>                        |
| Operating Income (Loss)                | <u>2,273,216</u>                                   | <u>211,380</u>                                     | <u>2,484,596</u>    | <u>72,959</u>                         |
| Non-Operating Revenue (Expenses):      |  |  |                     |                                       |
| Interest income                        | 96,854   | 26,296   | 123,150             | 2,557                                 |
| Interest expense                       | (539,034)  | (669,255)  | (1,208,289)         | --                                    |
| Gain (loss) on sale of capital assets  | --   | --   | --                  | 24,475                                |
| Fees and taxes                         | --   | (131,677)  | (131,677)           | --                                    |
| Total Non-Operating Revenue (Expenses) | <u>(442,180)</u>                                   | <u>(774,636)</u>                                   | <u>(1,216,816)</u>  | <u>27,032</u>                         |
| Change in Net Assets                   | 1,831,036  | (563,256)  | 1,267,780           | 99,991                                |
| Net Assets - Beginning of Year         | <u>22,693,267</u>                                  | <u>7,374,064</u>                                   | <u>30,067,331</u>   | <u>3,321,722</u>                      |
| Net Assets - End of Year               | <u>\$24,524,303</u>                                | <u>\$ 6,810,808</u>                                | <u>\$31,335,111</u> | <u>\$ 3,421,713</u>                   |

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

**CITY OF HERCULES**

Statement of Cash Flows  
Proprietary Funds  
For the Year Ended June 30, 2012

|  | Business-Type Activities - Enterprise Funds |  |                              | Governmental                 |
|--|---|--|------------------------------|------------------------------|
|  | Sewer<br>Fund                               | Hercules<br>Municipal<br>Utility<br>Fund | Total<br>Enterprise<br>Funds | Internal<br>Service<br>Funds |
|  |   |  |                              |                              |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>   |   |  |                              |                              |
| Cash receipts from customers   | \$ 4,974,988                                | \$ 2,821,955                             | \$ 7,796,943                 | \$ --                        |
| Cash receipts from internal fund services provided                                     | --  | --                                       | --                           | 727,032                      |
| Cash paid to suppliers for goods and services  | (2,824,882)                                 | (2,301,910)                              | (5,126,792)                  | (110,661)                    |
| Cash paid to employees for services  | (400,966)                                   | (434,382)                                | (835,348)                    | (218,738)                    |
| Net Cash Provided (Used) by Operating Activities                                       | 1,749,140                                   | 85,663                                   | 1,834,803                    | 397,633                      |
| <b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:</b>                                |   |  |                              |                              |
| Fees and taxes   | --  | (131,677)                                | (131,677)                    | --                           |
| Net Cash Provided (Used) by Noncapital Financing Activities                            | --  | (131,677)                                | (131,677)                    | --                           |
| <b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:</b>                       |   |  |                              |                              |
| Payments related to the acquisition of capital assets                                  | (336,113)                                   | (18,972)                                 | (355,085)                    | (33,994)                     |
| Sale of capital assets   | --  | --                                       | --                           | 36,100                       |
| Principal repayments related to capital purposes                                       | (230,000)                                   | --                                       | (230,000)                    | --                           |
| Interest repayments related to capital purposes  | (511,163)                                   | (651,288)                                | (1,162,451)                  | --                           |
| Net Cash Provided (Used) by Capital and Related Financing Activities                   | (1,077,276)                                 | (670,260)                                | (1,747,536)                  | 2,106                        |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>  |   |  |                              |                              |
| Interest received (paid)   | 96,854                                      | 27,702                                   | 124,556                      | 2,557                        |
| Net Cash Provided (Used) by Investing Activities                                       | 96,854                                      | 27,702                                   | 124,556                      | 2,557                        |
| <b>Net Increase (Decrease) in Cash and Cash Equivalents</b>                            | 768,718                                     | (688,572)                                | 80,146                       | 402,296                      |
| <b>Cash and Cash Equivalents, Beginning of Year, restated</b>                          | 13,524,482                                  | 8,457,187                                | 21,981,669                   | 1,878,278                    |
| <b>Cash and Cash Equivalents, End of Year</b>  | <u>\$ 14,293,200</u>                        | <u>\$ 7,768,615</u>                      | <u>\$ 22,061,815</u>         | <u>\$ 2,280,574</u>          |
| <b>Reconciliation of Cash and Cash Equivalents to the Statement of Fund Net Assets</b> |   |  |                              |                              |
| Cash and investments   | \$ 6,932,840                                | \$ 1,081,220                             | \$ 8,014,060                 | \$ 2,280,574                 |
| Cash with fiscal agent   | 7,360,360                                   | 6,687,395                                | 14,047,755                   | --                           |
| <b>Total Cash and Cash Equivalents</b>   | <u>\$ 14,293,200</u>                        | <u>\$ 7,768,615</u>                      | <u>\$ 22,061,815</u>         | <u>\$ 2,280,574</u>          |

continued

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

**CITY OF HERCULES**

Statement of Cash Flows (continued)  
 Proprietary Funds  
 For the Year Ended June 30, 2012

|   | Business-Type Activities - Enterprise Funds |  |                              | Governmental                 |
|---|---|--|------------------------------|------------------------------|
|   |   |  |                              | Activities                   |
|   | Sewer<br>Fund                               | Hercules<br>Municipal<br>Utility<br>Fund | Total<br>Enterprise<br>Funds | Internal<br>Service<br>Funds |
| <b>Reconciliation of Operating Income (Loss)<br/>to Net Cash Provided (Used) by<br/>Operating Activities:</b> |   |  |                              |                              |
| Operating income (loss)   | \$ 2,273,216                                | \$ 211,380                               | \$ 2,484,596                 | \$ 72,959                    |
| Adjustments to reconcile operating income<br>(loss) to net cash provided (used) by<br>operating activities:   |   |  |                              |                              |
| Depreciation  | 394,510                                     | 209,119                                  | 603,629                      | 268,286                      |
| Changes in assets and liabilities:  |   |  |                              |                              |
| (Increase) decrease in:   |   |  |                              |                              |
| Receivables   | 4,659                                       | 82,159                                   | 86,818                       | 561                          |
| Increase (decrease) in:   |   |  |                              |                              |
| Accounts payable  | (902,441)                                   | (377,700)                                | (1,280,141)                  | 50,330                       |
| Accrued salaries and benefits   | (28,054)                                    | (39,273)                                 | (67,327)                     | (3,201)                      |
| Compensated absences  | 7,250                                       | (22)                                     | 7,228                        | 8,698                        |
| <b>Net Cash Provided (Used) by Operating Activities</b>   | <b>\$ 1,749,140</b>                         | <b>\$ 85,663</b>                         | <b>\$ 1,834,803</b>          | <b>\$ 397,633</b>            |

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

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## FIDUCIARY FUND FINANCIAL STATEMENTS

*OPEB Trust Fund* is used to account for funds set aside by the City each year to pre-fund future medical expenses for retired police officers.

*Agency Funds* are used to account for assets held by the government in a trustee capacity. Agency funds are used to account for assets held by the government as an agent for individuals, private organizations, other governments, and/or other funds.

The *Private Purpose Trust Fund* is a fiduciary fund type used by the City to report trust arrangements under which principal and income benefit other governments. This fund reports the assets, liabilities and activities of the Hercules Redevelopment Successor Agency. The sole purpose of this fund is to retire debt of the former redevelopment agency.

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**CITY OF HERCULES**

Statement of Fiduciary Net Assets  
June 30, 2012

|  | OPEB<br>Trust<br>Fund | Private<br>Purpose<br>Trust<br>Fund | Agency<br>Funds     |
|--|-----------------------|-------------------------------------|---------------------|
|  | <u>          </u>     | <u>          </u>                   | <u>          </u>   |
| <b>ASSETS</b>                          |                       |                                     |                     |
| Cash and investments                   | \$ 1,160,932          | \$ 1,174,733                        | \$ 7,562,698        |
| Cash and investments with fiscal agent | --                    | 14,295,103                          | 1,454,651           |
| Accounts receivable                    | --                    | 376,229                             | 283,377             |
| Interest receivable                    | --                    | 465,608                             | --                  |
| Due from City of Hercules              | --                    | 322,056                             | --                  |
| Loans receivable                       | --                    | 11,842,656                          | --                  |
| Prepays                                | --                    | --                                  | 13,808              |
| Land held for resale                   | --                    | 4,259,684                           | --                  |
| Accumulated project costs              | --                    | 40,612,332                          | --                  |
| Capital assets:                        |                       |                                     |                     |
| Depreciable                            | --                    | 28,024,463                          | --                  |
| Nondepreciable                         | --                    | 5,923,509                           | --                  |
|  | <u>          </u>     | <u>          </u>                   | <u>          </u>   |
| Total Assets                           | <u>\$ 1,160,932</u>   | <u>\$ 107,296,373</u>               | <u>\$ 9,314,534</u> |
| <b>LIABILITIES</b>                     |                       |                                     |                     |
| Accounts payable                       | \$ 9,625              | \$ 11,929,805                       | \$ 180,400          |
| Unavailable revenue                    | --                    | 12,306,298                          | --                  |
| Advances from City of Hercules         | --                    | 14,513,959                          | --                  |
| Compensated absences                   | --                    | --                                  | 24,087              |
| Deposits payable                       | --                    | --                                  | 9,110,047           |
| Long-term debt                         | --                    | 128,003,165                         | --                  |
|  | <u>          </u>     | <u>          </u>                   | <u>          </u>   |
| Total Liabilities                      | <u>9,625</u>          | <u>166,753,227</u>                  | <u>9,314,534</u>    |
| <b>NET ASSETS</b>                      |                       |                                     |                     |
| Held in trust for others               | <u>1,151,307</u>      | <u>(59,456,854)</u>                 | <u>--</u>           |
|  | <u>          </u>     | <u>          </u>                   | <u>          </u>   |
| Total Net Assets                       | <u>\$ 1,151,307</u>   | <u>\$ (59,456,854)</u>              | <u>\$ --</u>        |

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

## CITY OF HERCULES

### Statement of Changes in Fiduciary Net Assets For the Year Ended June 30, 2012

|   | OPEB<br>Trust<br>Fund | Private<br>Purpose<br>Trust<br>Fund |
|---|-----------------------|-------------------------------------|
| Additions   |                       |                                     |
| Contributions from City                           | \$ 216,000            | \$ --                               |
| Taxes and assessments                             | --                    | 4,012,183                           |
| Investment income                                 | 20,359                | (136,616)                           |
| Other revenue                                     | --                    | 453,744                             |
| Total Additions                                   | 236,359               | 4,329,311                           |
| Deductions  |                       |                                     |
| Employee benefits                                 | 41,878                | --                                  |
| Community development                             | --                    | 68,375                              |
| Debt service:                                     |                       |                                     |
| Principal   | --                    | 1,655,000                           |
| Interest and fiscal charges                       | --                    | 3,088,523                           |
| Total Deductions                                  | 41,878                | 4,811,898                           |
| Change in net assets before extraordinary item    | 194,481               | (482,587)                           |
| Extraordinary item:                               |                       |                                     |
| Dissolution of Hercules City Redevelopment Agency | --                    | (58,974,267)                        |
| Change in net assets                              | 194,481               | (59,456,854)                        |
| Net Assets - Beginning of Year                    | 956,826               | --                                  |
| Net Assets - End of Year                          | \$ 1,151,307          | \$ (59,456,854)                     |

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

## CITY OF HERCULES

Notes to Financial Statements  
June 30, 2012

### NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### A. Reporting Entity

The City of Hercules (City) was incorporated under the General Laws of the State of California and enjoys all the rights and privileges pertaining to such "General Law" cities. The City uses the City Council/Manager form of government. The financial reporting entity consists of (a) the primary government, the City, (b) organizations for which the primary government is financially accountable, and (c) other organizations for which the primary government is not accountable, but for which the nature and significance of their relationship with the primary government are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete.

Component units are legally separate organizations for which the elected officials of the primary government are financially accountable. In addition, component units can be other organizations for which the primary government's exclusion would cause the reporting entity's basic financial statements to be misleading or incomplete.

The following is a brief review of the component units included in the accompanying basic financial statements of the City.

##### Hercules Public Financing Authority

The Hercules Public Financing Authority (Authority) was established July 24, 2001, by and between the City and the Agency, pursuant to the State of California Government Code. The purpose of the Authority is to finance the acquisition, construction and improvement of public capital improvements, working capital requirements or insurance programs.

The criteria used in determining the scope of the reporting entity are based on the provisions of GASB Statement No. 14 as amended by GASB Statement No. 39. The City is the primary government unit. Component units are those entities which are financially accountable to the primary government, either because the City appoints a voting majority of the component unit's board, or because the component unit will provide a financial benefit or impose a financial burden on the City. The Agency and the Authority have been accounted for as "blended" component units of the City. Despite being legally separate, the entities are so intertwined with the City that they are, in substance, part of the City's operations. Accordingly, the balances and transactions of these component units are reported within the funds of the City.

Separate detailed financial statements are available for the above component unit from the City's Finance Department.

#### B. Basis of Accounting and Measurement Focus

The accounts of the City are organized and operated on the basis of funds, each of which is defined as a separate fiscal and accounting entity with a self-balancing set of accounts. These funds are established for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions or limitations.

##### Government-wide Financial Statements

The Government-wide Financial Statements include a Statement of Net Assets and a Statement of Activities. These statements present summaries of Governmental and Business-type Activities for the City accompanied by a total column. Fiduciary Activities of the City are not included in these statements.

## CITY OF HERCULES

Notes to Financial Statements  
June 30, 2012

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

#### B. Basis of Accounting and Measurement Focus (continued)

##### Government-wide Financial Statements (continued)

The basic financial statements are presented on an “*economic resources*” measurement focus and the accrual basis of accounting. Accordingly, all of the City’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 types of transactions reported as program revenues for the City are reported in three categories:

- Charges for services
- Operating grants and contributions
- Capital grants and contributions

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 except those representing balances between the governmental activities and the business-type activities, which are presented as internal balances and eliminated in the total primary government column. In the Statement of Activities, internal service fund transactions have been eliminated. However, transactions between governmental and business-type activities have not been eliminated. The following interfund activities have been eliminated:

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

##### 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 and nonmajor funds aggregated. An accompanying schedule is presented to reconcile and explain the differences in net assets as presented in these statements to the net assets presented in the Government-wide financial statements. The City has presented all major funds that met the qualifications for major fund reporting.

The following are the description of the major funds:

General Fund accounts for all revenues and expenditures necessary to carry out basic governmental activities of the City that are not accounted for through other funds. For the City, the General Fund includes such activities as police, planning, engineering, public works, operations and maintenance, and legal and administrative services.

Redevelopment Agency Special Revenue Fund accounts for the operating costs of the former Redevelopment Agency and for the tax increment monies to be expended for low and moderate income housing purposes.

Redevelopment Agency Debt Service Fund accounts for the accumulation of resources used for the payment of principal and interest on the former Redevelopment Agency tax allocation bonds and notes payable.

## CITY OF HERCULES

Notes to Financial Statements  
June 30, 2012

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

#### B. Basis of Accounting and Measurement Focus (continued)

##### Governmental Fund Financial Statements (continued)

Hercules Public Financing Authority Debt Service Fund accounts for the accumulation of resources for, and the payment of, principal and interest on the Lease Revenue Bonds, Series 2003A issued to cover capital costs for the Hercules Municipal Utility and principal and interest on the Lease Revenue Bonds, Series 2003B issued to cover the financing of the original City Hall debt issue and to generate additional resources to assist in the construction of a new library building.

Redevelopment Agency Capital Projects Fund accounts for major capital projects undertaken by the former Redevelopment Agency.

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 present increases (revenues and other financing sources) and decreases (expenditures and other financing uses) in net current assets. Under the modified accrual basis of accounting, revenues are recognized in the accounting period in which they become both measurable and available to finance expenditures of the current period. Accordingly, revenues are recorded when received in cash, except that revenues subject to accrual (generally 60 days after yearend) are recognized when due.

Non-exchange transactions, in which the City gives or receives value without directly receiving or giving equal value in exchange, include property taxes, grants, entitlements, and donations. On an accrual basis, revenues from property taxes are recognized in the fiscal year for which the taxes are levied. Revenues from grants, entitlements, and donations are recognized in the fiscal year in which all eligibility requirements have been satisfied.

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

Reconciliations of the Governmental Fund Financial Statements to the Government-wide Financial Statements are provided to explain the differences created by the integrated approach.

##### Proprietary Fund Financial Statements

Proprietary Fund Financial Statements include a Statement of Net Assets, a Statement of Revenues, Expenses, and Changes in Net Assets, and a Statement of Cash Flows for each proprietary fund. A column representing internal service funds is also presented in these statements. However, internal service balances and activities have been combined with the governmental activities in the Government-wide Financial Statements.

Sewer Fund accounts for wastewater treatment to the cities of Hercules and Pinole and for the maintenance of the City's sewer lines and related facilities. It is a self-supporting activity which provides services on a user charge basis to residences and businesses.

Hercules Municipal Utility Fund accounts for the operations of the City's electric utility that provides electrical power to areas of new development within Hercules' city limits.

Internal Service Funds accounts for activities related to vehicle replacement, IT equipment replacement, and facilities maintenance.

## CITY OF HERCULES

Notes to Financial Statements  
June 30, 2012

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

#### B. Basis of Accounting and Measurement Focus (continued)

##### Proprietary Fund Financial Statements (continued)

All proprietary fund types are accounted for on an "economic resources" measurement focus and accrual basis of accounting. Accordingly, all assets and all liabilities (whether current or noncurrent) associated with their activity are included on the Statement of Net Assets. The Statement of Revenues, Expenses, and Changes in Net Assets presents increases (revenues) and decreases (expenses) in total net assets. Under the accrual basis of accounting wherein revenues are recognized in the accounting period in which they are earned and expenses are recognized in the accounting period incurred.

Operating revenues in the proprietary funds are those revenues that are generated from the primary operations of the funds. All other revenues are reported as non-operating revenues. Operating expenses are those expenses that are essential to the primary operations of the fund. All other expenses are reported as non-operating expenses.

##### Fiduciary Fund Financial Statements

Fiduciary Fund Financial Statements include a Statement of Net Assets. The City's Fiduciary funds are used to account for assets held by the City in a trustee capacity or as an agent for individuals, private organizations and other governmental units. When these assets are held under the terms of a formal trust agreement, a trust fund is used.

The Other Postemployment Benefits (OPEB) trust fund is accounted for using the "economic resources" measurement focus. The OPEB trust fund is used to account for resources legally held in trust for special purposes. The Agency funds are custodial in nature (assets equal liabilities) and do not involve measurement of results of operations. The OPEB trust fund is accounted for using the accrual basis of accounting.

The City maintains ten fiduciary funds — OPEB Trust Fund, Westcat Transit Fund, West Contra Costa Integrated Waste Management Authority Fund, Reassessment District 91-1 Debt Service Fund, Reassessment District 05-1 Debt Service Fund, A. Nobel Reassessment Debt Service Fund, Taylor Woodrow Maintenance LMOD Fund, Hercules Community Library Fund, Hercules Golf Club Fund, and Pinole/Hercules Wastewater Treatment Plant Fund.

The Private Purpose Trust Fund is a fiduciary fund type used by the City to report trust arrangements under which principal and income benefit other governments. This fund reports the assets, liabilities and activities of the Hercules Redevelopment Successor Agency. The sole purpose of this fund is to retire debt of the former redevelopment agency.

#### C. Cash and Investments

The City pools cash resources from all funds 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, Custodial Credit Risk, and Concentrations of Credit Risk.

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**C. Cash and Investments (continued)**

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

The City 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 Local Agency Investment Fund (LAIF) factor to selected funds by the City.

The City participates in an investment pool LAIF, which has invested a portion of the pooled funds in Structured Notes and Asset-Backed Securities. LAIF's investments are subject to credit 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 City and are presented as "Cash and Investments" in the accompanying basic financial statements.

**D. Inventory, Property Held for Resale, and Accumulated Project Costs**

Inventories consist of materials and supplies held for future consumption and are priced at average cost using the first-in, first-out method. Property held for resale and accumulated project costs consists of land and project costs relating to property acquired or constructed which is available to be sold and is not used in City operations. The property held for resale is recorded at the lower of cost or estimated net realizable value.

**E. Capital Assets**

Capital assets including infrastructure capital assets were reported using the Basic Approach whereby accumulated depreciation and depreciation expense have been recorded.

Capital assets, which include land, buildings, improvements, equipment, and infrastructure assets (e.g., roads, bridges, sidewalks, and similar items), are reported in the applicable governmental or business-type activities in the Government-wide Financial Statements. Capital assets are recorded at historical cost or estimated historical cost if actual cost is not available. Donated assets are valued at their estimated, fair value on the date donated. City policy has set the capitalization thresholds for reporting capital assets at the following:

|                               |          |
|-------------------------------|----------|
| General Capital Assets        | \$ 2,500 |
| Infrastructure Capital Assets | \$ 5,000 |

Depreciation is recorded on a straight-line method (with half-year convention applied to the first year of acquisition and final year of useful life) over the useful lives of the assets as follows:

|                            |               |
|----------------------------|---------------|
| Buildings and improvements | 15 – 50 years |
| Land improvements          | 20 years      |
| Machinery and equipment    | 5 – 20 years  |
| Infrastructure             | 15 – 50 years |

## CITY OF HERCULES

Notes to Financial Statements  
June 30, 2012

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

#### E. Capital Assets (continued)

The Governmental Accounting Standards Board (GASB) Statement No. 34 requires the inclusion of infrastructure capital assets in local governments' basic financial statements. In accordance with Statement No. 34, the City has included the value of all infrastructure capital assets into its Basic Financial Statements.

The City defines infrastructure assets as the basic physical assets that allow the City to function. The assets include:

- Street system
- Site amenities such as parking and landscaped areas used by the City in the conduct of its business.

Each major infrastructure system can be divided into subsystems. For example, the street system can be subdivided into pavement, curb and gutters, sidewalks, medians, streetlights, traffic control devices (signals), and land. These subsystems were not delineated in the Basic Financial Statements. The appropriate operating department maintains information regarding the subsystems.

The accumulated depreciation, defined as the total depreciation from the date of construction/acquisition to the current date was computed on a straight-line method using industry accepted life expectancies for each infrastructure subsystem. The book value was then computed by deducting the accumulated depreciation from the original cost.

Interest accrued during capital assets construction, if any, is capitalized for the business-type activities and proprietary funds as part of the asset cost.

Capital assets are not capitalized in the governmental funds used to acquire or construct them. Capital assets acquired or constructed for proprietary funds are capitalized in their respective individual funds.

#### F. Long-Term Obligations

In the Government-wide Financial Statements, long-term debt and other long-term obligations are reported as liabilities in the appropriate activities. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the straight-line method. Bonds payable are reported net of the applicable premium or discount. Issuance costs are reported as deferred charges.

In the Governmental 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.

#### G. Compensated Absences

Compensated absences are comprised of unpaid vacation and compensated time off. The City accrues the costs of these absences when they are earned. For governmental funds, compensated absences are recorded as current and non-current liabilities only on the government-wide financial statements. For proprietary funds, current and noncurrent liabilities for compensated absences are recorded as expenses in both the Government-wide Financial Statements and the Fund Financial Statements.

## CITY OF HERCULES

Notes to Financial Statements  
June 30, 2012

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

#### H. Net Assets

In the Government-wide Financial Statements, net assets are classified in the following categories:

Invested in Capital Assets, Net of Related Debt – This amount consists of capital assets net of accumulated depreciation and reduced by outstanding debt that attributed to the acquisition, construction, or improvement of the assets.

Restricted – This represents amounts 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" as defined above.

Included in total restricted net assets at June 30, 2012 are net assets restricted by enabling legislation of \$4,688,217.

As prescribed by GASB Statement No. 54, governmental funds report fund balance in classifications that comprise a hierarchy based primarily on the extent to which the government is bound to honor constraints on the specific purpose for which amounts in the funds can be spent. As of June 30, 2012, fund balances for governmental funds consist of the following categories:

Nonspendable Fund Balance – includes amounts that are not in a spendable form or are legally or contractually required to be maintained intact (such as inventories or prepaid amounts).

Restricted Fund Balance – includes amounts that can be spent only for specific purposes stipulated by external parties (such as creditors, grant providers, or contributors) or by law.

Committed Fund Balance – includes amounts that can be used only for the specific purpose determined by the City Council. Commitments may be changed or lifted only by the City Council taking the same formal action. The formal action must occur prior to the end of the reporting period. The amount which will be subject to the constraint may be determined in the subsequent period.

Assigned Fund Balance – is comprised of amounts intended to be used by the City for specific purposes that are neither restricted nor committed. Intent can be expressed by the City Council or by an official or body to which the Council delegates the authority. Assigned fund balance can be used to eliminate a projected budgetary deficit in the subsequent year's budget.

Unassigned Fund Balance – is the residual classification for the General Fund and includes all amounts not contained in the other classifications. Unassigned amounts are technically available for any purpose.

The City Council establishes, modifies or rescinds fund balance commitments and assignments by passage of a resolution or an ordinance. This can be done through the adoption of the budget and subsequent budget amendments that occur throughout the year.

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

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

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**J. Property Taxes, Tax Increment and Special Assessment Revenue**

Revenue is recognized in the fiscal year for which the tax and assessment is levied. The County of Contra Costa levies, bills and collects property taxes and special assessments for the City and remits the full assessment regardless of the amounts received under a Teeter plan arrangement.

|                 | <u>Secured Property Tax</u>     | <u>Unsecured Property Tax</u>   |
|-----------------|---------------------------------|---------------------------------|
| Lien Date       | January 1 preceding fiscal year | January 1 preceding fiscal year |
| Due Date        | November 1 & February 1         | August 31                       |
| Delinquent Date | December 10 & April 10          | September 1                     |

**K. Use of Estimates**

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

**L. New Accounting Pronouncements – Current Year**

The following Governmental Accounting Standards Board (GASB) Statements have been implemented in the current financial statements.

Governmental Accounting Standards Board Statement No. 61

Statement No. 61, *The Financial Reporting Entity: Omnibus – An Amendment of GASB Statements No. 14 and No. 34*. The objective of this statement is to improve guidance for including, presenting, and disclosing information about component units and equity interest transactions of a financial reporting entity. The requirements of GASB Statement No. 14, *The Financial Reporting Entity*, and the related financial reporting requirements of GASB Statement No. 34, *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments*, were amended to better meet user needs and to address reporting entity issues that have arisen since the issuance of those statements.

Governmental Accounting Standards Board Statement No. 62

GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. The Statement improves financial reporting by contributing to GASB’s efforts to codify all sources of generally accepted accounting principles for state and local governments so that they derive from a single source.

**M. New Accounting Pronouncements – Future Years**

Governmental Accounting Standards Board Statement No. 63

GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position* is effective for periods beginning after December 15, 2011. GASB Statement No. 63 provides financial reporting guidance for deferred outflows of resources and deferred inflows of resources. Previously, GASB Concepts Statement No. 4, *Elements of Financial Statements*, introduced and defined those elements as a consumption of net position by the government that is applicable to a future reporting period, and an acquisition of net position by the government that is applicable to a future reporting period, respectively. Previous financial

## CITY OF HERCULES

Notes to Financial Statements  
June 30, 2012

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

#### M. New Accounting Pronouncements – Future Years (continued)

reporting standards do not include guidance for reporting those financial statement elements, which are distinct from assets and liabilities. Concepts Statement No. 4 also identifies net position as the residual of all other elements presented in a statement of financial position. GASB Statement No. 63 amends the net asset reporting requirements in GASB Statement No. 34 and other pronouncements by incorporating deferred outflows of resources and deferred inflows of resources into the definitions of the required components of the residual measure and by renaming that measure as net position, rather than net assets.

##### Governmental Accounting Standards Board Statement No. 65

GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*, is effective for periods beginning after December 15, 2012. It improves the financial reporting for state and local governments by reclassifying, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities.

##### Governmental Accounting Standards Board Statement No. 66

GASB Statement No. 66, *Technical Corrections – 2012*, is effective for periods beginning after December 15, 2012. It improves financial reporting for state and local governments by resolving conflicting guidance that resulted from the issuance of GASB Statement Nos. 54 and 62.

##### Governmental Accounting Standards Board Statement No. 67

GASB Statement No. 67, *Financial Reporting for Pension Plans*, is effective for periods beginning after June 15, 2013. It improves financial reporting for state and local governments by improving the usefulness of pension information included in the general purpose external financial reports of state and local governmental pension plans for making decisions and assessing accountability.

##### Governmental Accounting Standards Board Statement No. 68

GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*, is effective for periods beginning after June 15, 2014. The principal objective of this statement is to improve the usefulness of information for decisions made by the various users of the general purpose external financial reports of governments whose employees – both active employees and inactive employees – are provided with pensions. An additional objective is to improve the information provided in government financial reports about pension-related financial support provided by certain nonemployer entities that make contributions to pension plans that are used to provide benefits to the employees of other entities.

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 2: CASH AND INVESTMENTS**

The City maintains a cash and investment pool for all funds. Certain restricted funds, which are held and invested by independent outside custodians through contractual agreements, are not pooled.

Statement of Net Assets:

|   |               |
|---|---------------|
| Cash and investments                    | \$ 19,559,192 |
| Cash and investments with fiscal agents | 16,386,594    |

Statement of Fiduciary Net Assets:

|   |                   |
|---|-------------------|
| Cash and investments                    | 9,898,363         |
| Cash and investments with fiscal agents | <u>15,749,754</u> |

|       |                      |
|-------|----------------------|
| Total | <u>\$ 61,593,903</u> |
|-------|----------------------|

Cash and investments as of June 30, 2012 consist of the following:

|                                      |                   |
|--------------------------------------|-------------------|
| Cash on hand                         | \$ 2,255          |
| Deposits with financial institutions | 7,340,183         |
| Investments                          | <u>54,251,465</u> |

|       |                      |
|-------|----------------------|
| Total | <u>\$ 61,593,903</u> |
|-------|----------------------|

Investments Authorized by the California Government Code and the City's Investment Policy

The table below identifies the investment types that are authorized for the City of Hercules by the California Government Code (or the City's investment policy, where more restrictive). The table also identifies certain provisions of the California Government Code (or the City's investment policy, where more restrictive) that addresses interest rate risk, credit risk, and concentration of credit risk. This table does not address investments of debt proceeds held by bond trustee that are governed by the provisions of debt agreements of the City, rather than the general provisions of the California Government Code or the City's investment policy.

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 2: CASH AND INVESTMENTS (CONTINUED)**

| Authorized<br>Investment Type                     | Maximum<br>Maturity | Maximum<br>Percentage<br>of Portfolio | Maximum<br>Investment<br>in One Issuer |
|---|---------------------|---------------------------------------|--|
| Local Agency Investment Fund (State Pool)         | N/A                 | \$50 million                          | \$50 million                           |
| U.S. Treasury Obligations                         | 5 years             | None                                  | None                                   |
| U.S. Government Agency Issues                     | 5 years             | None                                  | None                                   |
| Insured Deposits with Banks and Savings and Loans | N/A                 | None                                  | None                                   |
| Bankers Acceptance (must be dollar denominated)   | 180 days            | 40%                                   | 30%                                    |
| Commercial Paper                                  | 270 days            | 15%                                   | 10%                                    |
| Negotiable Time Certificates of Deposits          | 5 years             | 30%                                   | \$100,000                              |
| Non-negotiable Time Certificates of Deposits      | 5 years             | 30%                                   | \$100,000                              |
| Federally Insured Time Deposits                   | 5 years             | None                                  | \$100,000                              |
| Repurchase Agreements                             | 30 days             | None                                  | 10%                                    |
| Reverse Repurchase Agreements                     | 92 days             | 20%                                   | None                                   |
| Medium-Term Notes                                 | 5 years             | 30%                                   | 15%                                    |
| Money Market Mutual Funds                         | N/A                 | 20%                                   | 10%                                    |
| Insured or Passbook Savings Accounts              | N/A                 | None                                  | \$100,000                              |

At June 30, 2012, the City held two negotiable certificates of deposit which were in excess of the City's investment policy of \$100,000 per issuer limit. The City was in compliance with state law.

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 City'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<br>Investment Type                     | Maximum<br>Maturity | Maximum<br>Percentage<br>of Portfolio | Maximum<br>Investment<br>in One Issuer |
|---|---------------------|---------------------------------------|--|
| Local Agency Investment Fund (State Pool)         | N/A                 | \$50 million                          | \$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 Deposits          | 5 years             | 30%                                   | \$100,000                              |
| Non-negotiable Time Certificates of Deposits      | 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%                                    |
| Mutual Funds                                      | N/A                 | 20%                                   | None                                   |
| Money Market Funds                                | N/A                 | None                                  | None                                   |
| Insured or Passbook Savings Accounts              | N/A                 | None                                  | \$100,000                              |
| Guaranteed Investment Contracts                   | N/A                 | None                                  | None                                   |

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**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 City 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 City'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 City's investments by maturity:

| Investment Type                    | Totals               | Remaining Maturity (in Months) |                    |                    |                    |                     |                        |
|------------------------------------|----------------------|--------------------------------|--------------------|--------------------|--------------------|---------------------|------------------------|
|                                    |                      | 12 Months<br>or Less           | 13 to 24<br>Months | 25 to 36<br>Months | 37 to 48<br>Months | 49 to 60<br>Months  | More Than<br>60 Months |
| State Investment Pool              | \$ 18,149,234        | \$ 18,149,234                  | \$ -               | \$ -               | \$ -               | \$ -                | \$ -                   |
| Certificates of Deposit            | 707,372              | 197,834                        | -                  | -                  | -                  | 509,538             | -                      |
| U.S. Agency Securities             | 2,322,797            | 74,738                         | 182,869            | -                  | -                  | 2,065,190           | -                      |
| OPEB Trust Mutual Fund             | 935,713              | 935,713                        | -                  | -                  | -                  | -                   | -                      |
| Held by Debt Trustees:             |                      |                                |                    |                    |                    |                     |                        |
| Money Market Funds                 | 29,923,536           | 29,923,536                     | -                  | -                  | -                  | -                   | -                      |
| Guaranteed Investment<br>Contracts | 1,639,388            | -                              | -                  | -                  | -                  | -                   | 1,639,388              |
| State Investment Pool              | 573,425              | 573,425                        | -                  | -                  | -                  | -                   | -                      |
| <b>Total</b>                       | <b>\$ 54,251,465</b> | <b>\$ 49,854,480</b>           | <b>\$ 182,869</b>  | <b>\$ -</b>        | <b>\$ -</b>        | <b>\$ 2,574,728</b> | <b>\$ 1,639,388</b>    |

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 City's portfolio, not to exceed three years.

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

| <u>Maturity</u>        | <u>% of Portfolio</u> |
|------------------------|-----------------------|
| 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 City's investment policy, or debt agreements, and the actual rating as of fiscal year end for each investment type.

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 2: CASH AND INVESTMENTS (CONTINUED)**

Disclosures Relating to Credit Risk (continued)

| Investment Type                    | Amounts              | Minimum<br>Legal<br>Rating | Exempt<br>from<br>Disclosure | Rating at Fiscal Year End |             |             |                      |
|------------------------------------|----------------------|----------------------------|------------------------------|---------------------------|-------------|-------------|----------------------|
|                                    |                      |                            |                              | AAA                       | AA          | A           | Not<br>Rated         |
| State Investment Pool              | \$ 18,149,234        | N/A                        | N/A                          | \$ -                      | \$ -        | \$ -        | \$ 18,149,234        |
| Certificates of Deposit            | 707,372              | N/A                        | N/A                          | -                         | -           | -           | 707,372              |
| U.S. Agency Securities             | 2,322,797            | N/A                        | N/A                          | 2,065,190                 | -           | -           | 257,607              |
| OPEB Trust Mutual Fund             | 935,713              | N/A                        | N/A                          | 935,713                   | -           | -           | -                    |
| Held by Debt Trustees:             |                      |                            |                              |                           |             |             |                      |
| Money Market Funds                 | 29,923,536           | N/A                        | N/A                          | -                         | -           | -           | 29,923,536           |
| Guaranteed Investment<br>Contracts | 1,639,388            | N/A                        | N/A                          | 920,000                   | -           | -           | 719,388              |
| State Investment Pool              | 573,425              | N/A                        | N/A                          | -                         | -           | -           | 573,425              |
| <b>Total</b>                       | <b>\$ 54,251,465</b> |                            |                              | <b>\$ 3,920,903</b>       | <b>\$ -</b> | <b>\$ -</b> | <b>\$ 50,330,562</b> |

Concentration of Credit Risk

The investment policy of the City contains limitations on the amount that can be invested in any one issuer. Investments in any one issuer (other than U.S. Treasury securities, mutual funds, and external investment pools) that represent more than 5% of total City investments are as follows:

| Issuer | Investment Type        | Reporting<br>Amount |
|--------|------------------------|---------------------|
| FNMA   | U.S. Agency Securities | \$ 2,185,342        |

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 City'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 City deposits by pledging first trust deed mortgage notes having a value of 150% of the secured public deposits.

As of June 30, 2012, \$4,555,662 of the City's deposits with financial institutions in excess of federal depository insurance limits was held in collateralized accounts.

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 2: CASH AND INVESTMENTS (CONTINUED)**

Custodial Credit Risk (continued)

The City's investments are carried at fair value as required by accounting principles generally accepted in the United States of America. The City 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.

Investment in State Investment Pool

The City is a voluntary participant in the Local Agency Investment Fund (LAIF) that is regulated by the California Government Code under the oversight of the Treasurer of the State of California. The fair value of the City's investment in this pool is reported in the accompanying financial statements at amounts based upon the City's pro-rata share of the fair value provided by LAIF for the entire LAIF portfolio (in relation to the amortized cost of that portfolio). The balance available for withdrawal is based on the accounting records maintained by LAIF, which are recorded on an amortized cost basis.

**NOTE 3: LOANS RECEIVABLE**

Loans Receivable

Loans receivable at June 30, 2012, consisted of the following:

|                     |                     |
|---------------------|---------------------|
| Sycamore by the Bay | \$ 300,000          |
| Bio-Rad Loan        | 1,923,669           |
| Employee Loans      | <u>250,000</u>      |
| Total               | <u>\$ 2,473,669</u> |

**A. Employee Loan (Related Party)**

The City loaned \$250,000 to the City Manager for the purchase of a residence within the City of Hercules. The loan is to be repaid from the proceeds of the sale of the house with no interest when the contract between the City and the City Manager is terminated. The balance outstanding as of June 30, 2012 was \$250,000. In December 2010, the City Manager terminated his employment with the City and signed a separation agreement that extends the repayment of the loan to January 9, 2016.

**B. Bio-Rad Loan**

The City advanced Bio-Rad Laboratories, Inc. \$2,000,000 in order to construct various tenant improvements in one or more of the buildings located at 203-295 Linus Pauling Drive. The terms of the loan call for monthly payments of \$10,418, at an interest rate of 4.5% per annum, with repayments commencing May 15, 2010 through September 14, 2038. The balance outstanding as of June 30, 2012 was \$1,923,669.

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 3: LOAN RECEIVABLE (CONTINUED)**

**C. Sycamore by the Bay**

The City entered into a settlement agreement with Semik and Laura Oungoulian (Oungoulian) on April 6, 2006 concerning a dispute over development fees owed by Oungoulian for a 91 unit Senior Housing Project located at 1550 Sycamore Avenue, Hercules (Project). Under the settlement agreement, Oungoulian will pay the City the sum of \$550,000 to resolve all claims concerning development fees that Oungoulian owes to the City for the Project. Oungoulian paid \$250,000 to the City on May 22, 2008 prior to the final settlement agreement. The rest of the settlement amount, \$300,000, was setup as an installment note with the City with a 3.25% interest rate per annum. The balance outstanding as of June 30, 2012 was \$300,000.

**NOTE 4: UNAVAILABLE REVENUE**

**Fund Financial Statements**

At June 30, 2012, the following unavailable revenues were recorded in the Governmental Fund Financial Statements because either the revenues had not been earned or the funds were not available to finance expenditures of the current period:

|                            |                      |
|----------------------------|----------------------|
| Loans Receivable:          |                      |
| Sycamore by the Bay        | \$ 300,000           |
| Bio-Rad Loan               | 1,923,669            |
| Employee Loans             | 250,000              |
| Lease Receivable:          |                      |
| Capital Lease - Sales Type | 9,533,758            |
| Accounts Receivable        | <u>648,021</u>       |
| Total                      | <u>\$ 12,655,448</u> |

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 5: CAPITAL ASSETS**

At June 30, 2012, the City's capital assets consisted of the following:

|                               | <u>Governmental<br/>Activities</u> | <u>Business-Type<br/>Activities</u> | <u>Total</u>         |
|-------------------------------|------------------------------------|-------------------------------------|----------------------|
| Nondepreciable Assets:        |                                    |                                     |                      |
| Land                          | \$ 4,096,336                       | \$ 150,000                          | \$ 4,246,336         |
| Construction in progress      | <u>3,241,019</u>                   | <u>2,855,645</u>                    | <u>6,096,664</u>     |
| Total Nondepreciable Assets   | <u>7,337,355</u>                   | <u>3,005,645</u>                    | <u>10,343,000</u>    |
| Depreciable Assets:           |                                    |                                     |                      |
| Land improvements             | 9,985,733                          | -                                   | 9,985,733            |
| Buildings and improvements    | 25,861,711                         | 11,335,199                          | 37,196,910           |
| Machinery and equipment       | 4,101,106                          | 264,231                             | 4,365,337            |
| Infrastructure                | <u>79,446,948</u>                  | <u>17,520,177</u>                   | <u>96,967,125</u>    |
| Total Depreciable Assets      | <u>119,395,498</u>                 | <u>29,119,607</u>                   | <u>148,515,105</u>   |
| Less Accumulated Depreciation | <u>(52,561,672)</u>                | <u>(10,939,923)</u>                 | <u>(63,501,595)</u>  |
| Total Depreciable Assets, Net | <u>66,833,826</u>                  | <u>18,179,684</u>                   | <u>85,013,510</u>    |
| Total Capital Assets, Net     | <u>\$ 74,171,181</u>               | <u>\$ 21,185,329</u>                | <u>\$ 95,356,510</u> |

The following is a summary of capital assets for governmental activities:

| <u>Governmental Activities</u>      | <u>Balance<br/>July 1, 2011</u> | <u>Additions</u>      | <u>Deletions</u>  | <u>RDA<br/>Dissolution</u> | <u>Balance<br/>June 30, 2012</u> |
|-------------------------------------|---------------------------------|-----------------------|-------------------|----------------------------|----------------------------------|
| Nondepreciable Capital Assets:      |                                 |                       |                   |                            |                                  |
| Land                                | \$ 4,313,376                    | \$ -                  | \$ -              | \$ (217,040)               | \$ 4,096,336                     |
| Construction in progress            | <u>30,169,791</u>               | <u>336,020</u>        | <u>-</u>          | <u>(27,264,792)</u>        | <u>3,241,019</u>                 |
| Total Nondepreciable Capital Assets | <u>34,483,167</u>               | <u>336,020</u>        | <u>-</u>          | <u>(27,481,832)</u>        | <u>7,337,355</u>                 |
| Depreciable Capital Assets:         |                                 |                       |                   |                            |                                  |
| Land improvements                   | 9,997,112                       | -                     | -                 | (11,379)                   | 9,985,733                        |
| Buildings and improvements          | 30,827,489                      | -                     | -                 | (4,965,778)                | 25,861,711                       |
| Machinery and equipment             | 4,335,813                       | 33,994                | (152,256)         | (116,445)                  | 4,101,106                        |
| Infrastructure                      | <u>83,617,804</u>               | <u>61,866</u>         | <u>-</u>          | <u>(4,232,722)</u>         | <u>79,446,948</u>                |
| Total Depreciable Capital Assets    | <u>128,778,218</u>              | <u>95,860</u>         | <u>(152,256)</u>  | <u>(9,326,324)</u>         | <u>119,395,498</u>               |
| Accumulated Depreciation:           |                                 |                       |                   |                            |                                  |
| Land improvements                   | (3,399,895)                     | (597,831)             | -                 | 11,379                     | (3,986,347)                      |
| Buildings and improvements          | (6,571,465)                     | (716,632)             | 6,963             | 2,306,407                  | (4,974,727)                      |
| Machinery and equipment             | (3,215,440)                     | (305,204)             | 140,653           | 15,009                     | (3,364,982)                      |
| Infrastructure                      | <u>(39,059,915)</u>             | <u>(2,116,753)</u>    | <u>264</u>        | <u>940,788</u>             | <u>(40,235,616)</u>              |
| Total Accumulated Depreciation      | <u>(52,246,715)</u>             | <u>(3,736,420)</u>    | <u>147,880</u>    | <u>3,273,583</u>           | <u>(52,561,672)</u>              |
| Net depreciable capital assets      | <u>76,531,503</u>               | <u>(3,640,560)</u>    | <u>(4,376)</u>    | <u>(6,052,741)</u>         | <u>66,833,826</u>                |
| Net Capital Assets                  | <u>\$ 111,014,670</u>           | <u>\$ (3,304,540)</u> | <u>\$ (4,376)</u> | <u>\$ (33,534,573)</u>     | <u>\$ 74,171,181</u>             |

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 5: CAPITAL ASSETS (CONTINUED)**

Depreciation Allocation

Depreciation expense was charged to functions and programs based on their usage of the related assets. The amounts allocated to each function or program were as follows:

|   |                                |
|---|--------------------------------|
| Governmental Activities:  |                                |
| General government  | \$ 464,003                     |
| Public safety   | 31,365                         |
| Public works  | 2,518,738                      |
| Parks and recreation  | 271,106                        |
| Community development   | 182,922                        |
| Capital assets held by internal service funds are charged to the various functions based on usage of the assets | <u>268,286</u>                 |
| <br>Total Depreciation Expense - Governmental Activities  | <br><u><u>\$ 3,736,420</u></u> |

| <u>Business-Type Activities</u>     | Balance<br>July 1, 2011     | Additions                 | Deletions          | Transfers          | Balance<br>June 30, 2012    |
|-------------------------------------|-----------------------------|---------------------------|--------------------|--------------------|-----------------------------|
| <b><u>Sewer</u></b>                 |                             |                           |                    |                    |                             |
| Nondepreciable Capital Assets:      |                             |                           |                    |                    |                             |
| Land                                | \$ 150,000                  | \$ -                      | \$ -               | \$ -               | \$ 150,000                  |
| Construction in progress            | <u>2,203,028</u>            | <u>52,205</u>             | <u>-</u>           | <u>-</u>           | <u>2,255,233</u>            |
| Total Nondepreciable Capital Assets | <u>2,353,028</u>            | <u>52,205</u>             | <u>-</u>           | <u>-</u>           | <u>2,405,233</u>            |
| Depreciable Capital Assets:         |                             |                           |                    |                    |                             |
| Buildings and improvements          | 11,335,199                  | -                         | -                  | -                  | 11,335,199                  |
| Machinery and equipment             | 117,117                     | 38,955                    | -                  | -                  | 156,072                     |
| Infrastructure                      | <u>8,286,603</u>            | <u>244,953</u>            | <u>-</u>           | <u>-</u>           | <u>8,531,556</u>            |
| Total Depreciable Capital Assets    | <u>19,738,919</u>           | <u>283,908</u>            | <u>-</u>           | <u>-</u>           | <u>20,022,827</u>           |
| Less accumulated depreciation       | <u>(9,084,149)</u>          | <u>(394,510)</u>          | <u>-</u>           | <u>-</u>           | <u>(9,478,659)</u>          |
| Net depreciable capital assets      | <u>10,654,770</u>           | <u>(110,602)</u>          | <u>-</u>           | <u>-</u>           | <u>10,544,168</u>           |
| Net Capital Assets                  | <u><u>\$ 13,007,798</u></u> | <u><u>\$ (58,397)</u></u> | <u><u>\$ -</u></u> | <u><u>\$ -</u></u> | <u><u>\$ 12,949,401</u></u> |

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 5: CAPITAL ASSETS (CONTINUED)**

Depreciation Allocation (continued)

| <u>Business-Type Activities</u>     | <u>Balance<br/>July 1, 2011</u> | <u>Additions</u>    | <u>Deletions</u> | <u>Transfers</u>           | <u>Balance<br/>June 30, 2012</u> |
|-------------------------------------|---------------------------------|---------------------|------------------|----------------------------|----------------------------------|
| <b>Hercules Municipal Utility</b>   |                                 |                     |                  |                            |                                  |
| Nondepreciable Capital Assets:      |                                 |                     |                  |                            |                                  |
| Construction in progress            | \$ 600,412                      | \$ -                | \$ -             | \$ -                       | \$ 600,412                       |
| Total Nondepreciable Capital Assets | <u>600,412</u>                  | <u>-</u>            | <u>-</u>         | <u>-</u>                   | <u>600,412</u>                   |
| Depreciable Capital Assets:         |                                 |                     |                  |                            |                                  |
| Machinery and equipment             | 89,187                          | 18,972              | -                | -                          | 108,159                          |
| Infrastructure                      | 8,988,621                       | -                   | -                | -                          | 8,988,621                        |
| Total Depreciable Capital Assets    | <u>9,077,808</u>                | <u>18,972</u>       | <u>-</u>         | <u>-</u>                   | <u>9,096,780</u>                 |
| Less accumulated depreciation       | <u>(1,252,145)</u>              | <u>(209,119)</u>    | <u>-</u>         | <u>-</u>                   | <u>(1,461,264)</u>               |
| Net depreciable capital assets      | <u>7,825,663</u>                | <u>(190,147)</u>    | <u>-</u>         | <u>-</u>                   | <u>7,635,516</u>                 |
| Net Capital Assets                  | <u>\$ 8,426,075</u>             | <u>\$ (190,147)</u> | <u>\$ -</u>      | <u>\$ -</u>                | <u>\$ 8,235,928</u>              |
| <br>                                |                                 |                     |                  |                            |                                  |
| <u>Private Purpose Trust Fund</u>   | <u>Balance<br/>July 1, 2011</u> | <u>Additions</u>    | <u>Deletions</u> | <u>RDA<br/>Dissolution</u> | <u>Balance<br/>June 30, 2012</u> |
| Nondepreciable Capital Assets:      |                                 |                     |                  |                            |                                  |
| Land                                | \$ -                            | \$ -                | \$ -             | \$ 217,040                 | \$ 217,040                       |
| Construction in progress            | -                               | 542,631             | -                | 27,264,792                 | 27,807,423                       |
| Total Nondepreciable Capital Assets | <u>-</u>                        | <u>542,631</u>      | <u>-</u>         | <u>27,481,832</u>          | <u>28,024,463</u>                |
| 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                      | -                               | -                   | -                | 4,232,722                  | 4,232,722                        |
| Total Depreciable Capital Assets    | <u>-</u>                        | <u>-</u>            | <u>-</u>         | <u>9,326,324</u>           | <u>9,326,324</u>                 |
| Accumulated Depreciation:           |                                 |                     |                  |                            |                                  |
| Land improvements                   | -                               | -                   | -                | (11,379)                   | (11,379)                         |
| Buildings and improvements          | -                               | (41,432)            | -                | (2,306,407)                | (2,347,839)                      |
| Machinery and equipment             | -                               | (2,421)             | -                | (15,009)                   | (17,430)                         |
| Infrastructure                      | -                               | (85,379)            | -                | (940,788)                  | (1,026,167)                      |
| Total Accumulated Depreciation      | <u>-</u>                        | <u>(129,232)</u>    | <u>-</u>         | <u>(3,273,583)</u>         | <u>(3,402,815)</u>               |
| Net depreciable capital assets      | <u>-</u>                        | <u>(129,232)</u>    | <u>-</u>         | <u>6,052,741</u>           | <u>5,923,509</u>                 |
| Net Capital Assets                  | <u>\$ -</u>                     | <u>\$ 413,399</u>   | <u>\$ -</u>      | <u>\$ 33,534,573</u>       | <u>\$ 33,947,972</u>             |

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 5: CAPITAL ASSETS (CONTINUED)**

Depreciation Allocation (continued)

Depreciation expense was charged to functions and programs based on their usage of the related assets. The amounts allocated to each function or program were as follows:

|   |                              |
|---|------------------------------|
| Business-Type Activities:                                 |                              |
| Sewer   | \$ 209,119                   |
| Hercules Municipal Utility                                | <u>394,510</u>               |
| <br>Total Depreciation Expense - Business-Type Activities | <br><u><u>\$ 603,629</u></u> |

**NOTE 6: LONG-TERM OBLIGATIONS**

Governmental activities long-term liability activity for the fiscal year ended June 30, 2012, was as follows:

| Governmental Activities                     | Balance<br>July 1, 2011   | Additions       | Reductions                | RDA<br>Dissolution          | Balance<br>June 30, 2012 | Due Within<br>One Year |
|---|---------------------------|-----------------|---------------------------|-----------------------------|--------------------------|------------------------|
| 2005 Tax Allocation Bonds                   | \$ 49,085,000             | \$ -            | \$ (1,640,000)            | \$ (47,445,000)             | \$ -                     | \$ -                   |
| Premium on 2005 Tax Allocation Bonds        | 1,740,776                 | -               | (72,532)                  | (1,668,244)                 | -                        | -                      |
| Deferred Amount on refunding                | (232,930)                 | -               | 9,705                     | 223,225                     | -                        | -                      |
| 2007 Housing Tax Allocation Bonds, Series A | 12,415,000                | -               | (270,000)                 | (12,145,000)                | -                        | -                      |
| 2007 Housing Tax Allocation Bonds, Series B | 12,015,000                | -               | (315,000)                 | (11,700,000)                | -                        | -                      |
| Premium on issuance                         | 69,222                    | -               | (3,146)                   | (66,076)                    | -                        | -                      |
| 2007 Tax Allocation Bonds                   | 56,095,000                | -               | (1,240,000)               | (54,855,000)                | -                        | -                      |
| 2003B PFA Lease Revenue Bonds               | 7,855,000                 | -               | (205,000)                 | -                           | 7,650,000                | 210,000                |
| 2009 PFA Taxable Lease Revenue Bonds        | 9,915,000                 | -               | (115,000)                 | -                           | 9,800,000                | 120,000                |
| Discount on issuance                        | (467,005)                 | -               | 17,297                    | -                           | (449,708)                | -                      |
| Long-Term Notes Payable                     | 347,070                   | -               | -                         | (347,070)                   | -                        | -                      |
| H.E.L.P. Loan                               | 1,600,000                 | -               | -                         | -                           | 1,600,000                | -                      |
| R.D.L.P. Loan                               | 3,750,000                 | -               | -                         | -                           | 3,750,000                | -                      |
| Suntrust Lease                              | 1,803,229                 | -               | (121,223)                 | -                           | 1,682,006                | 127,024                |
| Compensated absences                        | 506,555                   | -               | (81,014)                  | -                           | 425,541                  | 319,156                |
| <br>Total Long-Term Obligations             | <br><u>\$ 156,496,917</u> | <br><u>\$ -</u> | <br><u>\$ (4,035,913)</u> | <br><u>\$ (128,003,165)</u> | <br><u>\$ 24,457,839</u> | <br><u>\$ 776,180</u>  |

Compensated Absences

Compensated absences are comprised of unpaid vacation and compensated time off. The City accrues the cost of these absences when they are earned. The City expects the liability for compensated absences to be utilized and records this liability in the Government-Wide Financial Statements. The City liquidates the majority of governmental activities portion of the liability in the general fund.

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 6: LONG-TERM OBLIGATIONS (CONTINUED)**

2003B Public Financing Authority Lease Revenue Bonds

The Public Financing Authority issued lease revenue bonds, series 2003B, dated October 15, 2003, totaling \$9,150,000. The purpose of the bonds was to refinance the 1994 Refunding Certificates of Participation and to finance a portion of the construction for a public library. The interest rate on the bonds ranges from 2.00% to 5.00%. The interest is payable semiannually on June 1 and December 1, commencing December 1, 2003. The bonds are subject to optional and mandatory early redemption provisions. The bonds are payable from and secured by revenues consisting primarily of the base rental payments of the facility lease. Principal is due annually beginning on December 1, 2005, in amounts ranging from \$170,000 to \$2,480,000. The bonds mature on December 1, 2033. The balance at June 30, 2012 is \$7,650,000.

Future debt service requirements on the 2003B Public Financing Authority Lease Revenue bonds are:

| Fiscal Year<br>Ended<br>June 30, | Principal           | Interest            | Total                |
|----------------------------------|---------------------|---------------------|----------------------|
| 2013                             | \$ 210,000          | \$ 356,585          | \$ 566,585           |
| 2014                             | 220,000             | 348,468             | 568,468              |
| 2015                             | 230,000             | 339,688             | 569,688              |
| 2016                             | 235,000             | 330,153             | 565,153              |
| 2017                             | 245,000             | 320,073             | 565,073              |
| 2018-2022                        | 1,410,000           | 1,415,979           | 2,825,979            |
| 2023-2027                        | 1,780,000           | 1,038,475           | 2,818,475            |
| 2028-2032                        | 2,255,000           | 556,500             | 2,811,500            |
| 2033                             | <u>1,065,000</u>    | <u>53,875</u>       | <u>1,118,875</u>     |
| Total                            | <u>\$ 7,650,000</u> | <u>\$ 4,759,796</u> | <u>\$ 12,409,796</u> |

2009 Public Financing Authority Taxable Lease Revenue Bonds (Bio-Rad Project)

The Authority issued taxable lease revenue bonds, series 2009, dated July 29, 2009, totaling \$10,080,000. The purpose of the bonds was to finance the acquisition of certain commercial condominium properties, consisting of approximately 96,847 square feet located at 203-295 Linus Pauling Drive within the City from the City, funding a reserve fund for the Bonds and to paying the costs of issuance of the Bonds. The interest rates on the bonds range from 6.00% to 8.40%. The interest is payable semiannually on January 1 and July 1, commencing January 1, 2010. The bonds are subject to optional special mandatory redemption, and mandatory sinking account redemption provisions. The bonds are payable from and secured by revenues consisting primarily of the base rental payments of the property lease, Principal is due annually beginning on July 1, 2010, in amounts ranging from \$165,000 to \$845,000. The bonds mature on July 1, 2038. The balance at June 30, 2012 is \$9,800,000.

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 6: LONG-TERM OBLIGATIONS (CONTINUED)**

2009 Public Financing Authority Taxable Lease Revenue Bonds (Bio-Rad Project) (continued)

Future debt service requirements on the 2009 Public Financing Authority Taxable Lease Revenue bonds are:

| Fiscal Year<br>Ended<br>June 30, | Principal           | Interest             | Total                |
|----------------------------------|---------------------|----------------------|----------------------|
| 2013                             | \$ 120,000          | \$ 794,315           | \$ 914,315           |
| 2014                             | 130,000             | 786,815              | 916,815              |
| 2015                             | 135,000             | 778,865              | 913,865              |
| 2016                             | 145,000             | 769,740              | 914,740              |
| 2017                             | 155,000             | 759,240              | 914,240              |
| 2018-2022                        | 950,000             | 3,607,150            | 4,557,150            |
| 2023-2027                        | 1,390,000           | 3,142,200            | 4,532,200            |
| 2028-2032                        | 2,065,000           | 2,436,495            | 4,501,495            |
| 2033-2037                        | 3,085,000           | 1,372,350            | 4,457,350            |
| 2038-2039                        | 1,625,000           | 139,230              | 1,764,230            |
| Subtotal                         | 9,800,000           | 14,586,400           | 24,386,400           |
| Less: Discount                   | (449,708)           | -                    | (449,708)            |
| Total                            | <u>\$ 9,350,292</u> | <u>\$ 14,586,400</u> | <u>\$ 23,936,692</u> |

H.E.L.P. Loan Payable

In April 2005 the City of Hercules entered into an agreement with the California Housing Finance Agency (Agency), a public instrumentality and political subdivision of the State of California to develop a 50-unit multifamily rental project that is a component to a mixed-used development, also consisting of 26,825 square feet of ground-floor commercial space. The Agency has authorized the making of a loan in the amount of \$1,600,000 known as the Housing Enabled by Local Partnerships (HELP) to the City of Hercules for the purpose of assisting in operating a local housing program. Under the terms of this original agreement the City of Hercules agreed to reimburse the Agency \$1,600,000, 10 years from April 11, 2005 at a 3% simple per annum interest. Interest is to be charged only on funds disbursed. In October 2013, the City and Agency amended the agreement to extend the due date of the loan and accumulated interest until April 2027 and to reduce the interest rate to 1.5 percent simple interest effective October 31, 2013.

R.D.L.P. Loan Payable

In February 2007, the City of Hercules entered into a loan agreement with the California Housing Finance Agency (Agency) in the amount of \$3,750,000 (\$1,750,000 for predevelopment costs and \$2,000,000 for construction costs). The funds will be used to assist with site acquisition, predevelopment, and construction costs for 23 affordable ownership units within a 52-unit condominium project, which is a component to the Sycamore Downtown Street project, a mixed-use, mixed-income development. Under the terms of the original agreement, the City of Hercules agreed to repay the Agency \$3,750,000, 4 years from February 2007 at 3% simple per annum interest. In August 2010, the repayment date was extended to August 15, 2011. In October 2013, the City and Agency amended the agreement to extend the due date of the loan and accumulated interest until August 2026 and to reduce the interest rate to 1.5 percent simple interest effective October 31, 2013.

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 6: LONG-TERM OBLIGATIONS (CONTINUED)**

SunTrust Lease

On September 27, 2007, the City entered into master lease agreements with SunTrust Leasing Corporation in order to provide funds for the financing of the EMS Project performed by Siemens Building Technologies in the amount of \$2,185,538. Payments are due semiannually on September 27 and March 27, at an interest rate of 4.73%. The Master Lease Agreement matures on September 27, 2022. As of June 30, 2012, the outstanding balance of the master lease agreement is \$1,682,006.

The annual debt service requirements to maturity for the SunTrust master lease agreement as of June 30, 2012 are as follows:

| Fiscal Year<br>Ended<br>June 30, | <u>Principal</u>    | <u>Interest</u>   | <u>Total</u>        |
|----------------------------------|---------------------|-------------------|---------------------|
| 2013                             | \$ 127,025          | \$ 78,074         | \$ 205,099          |
| 2014                             | 133,104             | 71,995            | 205,099             |
| 2015                             | 139,474             | 65,625            | 205,099             |
| 2016                             | 146,149             | 58,950            | 205,099             |
| 2017                             | 153,144             | 51,955            | 205,099             |
| 2018-2022                        | 882,930             | 142,563           | 1,025,493           |
| 2023                             | <u>100,180</u>      | <u>2,369</u>      | <u>102,549</u>      |
| Total                            | <u>\$ 1,682,006</u> | <u>\$ 471,531</u> | <u>\$ 2,153,537</u> |

Business-Type Activities

Long-term liability activity for the fiscal year ended June 30, 2012, was as follows:

| <u>Business-Type Activities</u>   | <u>Balance<br/>July 1, 2011</u> | <u>Additions</u> | <u>Reductions</u>   | <u>Balance<br/>June 30, 2012</u> | <u>Due Within<br/>One Year</u> |
|-----------------------------------|---------------------------------|------------------|---------------------|----------------------------------|--------------------------------|
| 2010 PFA Wastewater Revenue Bonds | \$ 11,765,000                   | \$ -             | \$ (230,000)        | \$ 11,535,000                    | \$ 230,000                     |
| Discount on Issuance              | (210,882)                       | -                | 7,272               | (203,610)                        | -                              |
| 2010 PFA Electric System Project  | 5,775,000                       | -                | -                   | 5,775,000                        | 105,000                        |
| Discount on Issuance              | (149,992)                       | -                | 5,172               | (144,820)                        | -                              |
| 2010 PFA Revenue Refunding Bonds  | 7,425,000                       | -                | -                   | 7,425,000                        | -                              |
| Discount on Issuance              | (210,001)                       | -                | 7,778               | (202,223)                        | -                              |
| Loss on Refunding                 | (205,688)                       | -                | 7,618               | (198,070)                        | -                              |
| Compensated absences              | <u>30,072</u>                   | <u>7,228</u>     | <u>-</u>            | <u>37,300</u>                    | <u>37,300</u>                  |
| Total Long-Term Obligations       | <u>\$ 24,218,509</u>            | <u>\$ 7,228</u>  | <u>\$ (202,160)</u> | <u>\$ 24,023,577</u>             | <u>\$ 372,300</u>              |

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 6: LONG-TERM OBLIGATIONS (CONTINUED)**

2010 Public Financing Authority Wastewater Revenue Bonds

The Public Financing Authority issued revenue bonds, series 2010, dated August 1, 2010, totaling \$11,765,000. The purpose of the bonds was to finance improvements to the City's wastewater system, fund a reserve fund for the bonds, and pay the costs of issuances of the bonds. The interest rates on the bonds range from 2.00% to 5.130%. Principal is due annually beginning August 1, 2011, in amounts ranging from \$230,000 to \$700,000. The bonds mature on August 1, 2040. The balance at June 30, 2012 is \$11,535,000.

Future debt service requirements on the 2010 Public Financing Authority Wastewater Revenue Bonds are:

| Year Ended<br>June 30, | Principal            | Interest            | Total                |
|------------------------|----------------------|---------------------|----------------------|
| 2013                   | \$ 230,000           | \$ 502,413          | \$ 732,413           |
| 2014                   | 235,000              | 497,763             | 732,763              |
| 2015                   | 240,000              | 493,013             | 733,013              |
| 2016                   | 245,000              | 487,856             | 732,856              |
| 2017                   | 250,000              | 481,975             | 731,975              |
| 2018-2022              | 1,380,000            | 2,288,119           | 3,668,119            |
| 2023-2027              | 1,655,000            | 1,995,306           | 3,650,306            |
| 2028-2032              | 2,065,000            | 1,568,350           | 3,633,350            |
| 2033-2037              | 2,625,000            | 993,125             | 3,618,125            |
| 2038-2041              | 2,610,000            | 269,000             | 2,879,000            |
| Subtotal               | 11,535,000           | 9,576,920           | 21,111,920           |
| Less: Discount         | (203,610)            | -                   | (203,610)            |
| Total                  | <u>\$ 11,331,390</u> | <u>\$ 9,576,920</u> | <u>\$ 20,908,310</u> |

2010 Public Financing Authority Electric System Project Revenue Bonds

The Public Financing Authority issued revenue bonds, series 2010, dated August 1, 2010, totaling \$5,775,000. The purpose of the bonds was to finance improvements to the City's electric system, fund a reserve fund for the bonds, and pay the costs of issuance of the bonds. The interest rates on the bonds range from 2.00% to 5.58%. Principal is due annually beginning August 1, 2012 in amounts ranging from \$105,000 to \$370,000. The bonds mature on August 1, 2040. The balance at June 30, 2012 is \$5,775,000.

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 6: LONG-TERM OBLIGATIONS (CONTINUED)**

2010 Public Financing Authority Electric System Project Revenue Bonds (continued)

Future debt service requirements on the 2010 Public Authority Electric System Project Revenue Bonds are:

| Year Ended<br>June 30, | Principal           | Interest            | Total                |
|------------------------|---------------------|---------------------|----------------------|
| 2013                   | \$ 105,000          | \$ 278,588          | \$ 383,588           |
| 2014                   | 110,000             | 276,300             | 386,300              |
| 2015                   | 110,000             | 273,688             | 383,688              |
| 2016                   | 115,000             | 270,588             | 385,588              |
| 2017                   | 115,000             | 266,922             | 381,922              |
| 2018-2022              | 510,000             | 1,268,247           | 1,778,247            |
| 2023-2027              | 285,000             | 1,168,913           | 1,453,913            |
| 2028-2032              | 1,045,000           | 979,625             | 2,024,625            |
| 2033-2037              | 1,140,000           | 691,775             | 1,831,775            |
| 2038-2041              | 2,240,000           | 421,400             | 2,661,400            |
| Subtotal               | 5,775,000           | 5,896,046           | 11,671,046           |
| Less: Discount         | (144,820)           | -                   | (144,820)            |
| Total                  | <u>\$ 5,630,180</u> | <u>\$ 5,896,046</u> | <u>\$ 11,526,226</u> |

2010 Public Financing Authority Revenue Refunding Bonds (Electric System Project)

The Authority issued revenue refunding bonds, series 2010, dated June 28, 2010, totaling \$7,425,000. The purpose of the bonds was to refund the Hercules Public Financing Authority Lease Revenue Bonds Series 2003A currently outstanding in the principal amount of \$6,495,000, fund a reserve fund for the Bonds, and pay the costs of issuance of the Bonds. The interest rates on the bonds range from 2.500% to 5.375%. The interest is payable semiannually on February 1 and August 1, commencing February 1, 2011. The bonds are subject to special mandatory redemption, mandatory sinking fund redemption, and redemption from optional prepayment of Installment Payments prior to maturity. The bonds are payable from and secured by installment payments to be paid by the City under the Installment Sale Agreement and the City's advance payments under the Cooperation Agreement. Principal is due annually beginning on August 1, 2011, in amounts ranging from \$160,000 to \$495,000. The bonds mature on August 1, 2038, The balance at June 30, 2012 is \$7,425,000.

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 6: LONG-TERM OBLIGATIONS (CONTINUED)**

2010 Public Financing Authority Revenue Refunding Bonds (Electric System Project) (continued)

Future debt service requirements on the 2010 Public Financing Authority Revenue Refunding bonds are:

| Fiscal Year<br>Ended<br>June 30, | Principal           | Interest            | Total                |
|----------------------------------|---------------------|---------------------|----------------------|
| 2013                             | \$ -                | \$ 361,775          | \$ 361,775           |
| 2014                             | 160,000             | 359,775             | 519,775              |
| 2015                             | 165,000             | 355,506             | 520,506              |
| 2016                             | 170,000             | 350,688             | 520,688              |
| 2017                             | 175,000             | 345,075             | 520,075              |
| 2018-2022                        | 770,000             | 1,619,525           | 2,389,525            |
| 2023-2027                        | 1,175,000           | 1,469,531           | 2,644,531            |
| 2028-2031                        | <u>4,810,000</u>    | <u>533,956</u>      | <u>5,343,956</u>     |
| Subtotal                         | 7,425,000           | 5,395,831           | 12,820,831           |
| Less: Discount                   | (202,223)           | -                   | (202,223)            |
| Less: Deferred Loss on Refunding | <u>(198,070)</u>    | <u>-</u>            | <u>(198,070)</u>     |
| Total                            | <u>\$ 7,024,707</u> | <u>\$ 5,395,831</u> | <u>\$ 12,420,538</u> |

In connection with the issuance of the 2010 PFA Revenue Refunding Bonds, the Authority 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 and the write-off of the cost of issuance of the defeased 2003A Public Financing Authority Lease Revenue Bonds. The total amount of the deferred loss was \$213,306 which will be amortized over the life of the bond.

**NOTE 7: NON-CITY OBLIGATIONS**

The District Bonds are not general obligations of the City nor any other political subdivision and the full faith and credit of the City is not pledged for repayment thereof since these debts do not constitute an obligation of the City and the City is not obligated to make payment beyond the available bond reserves, these bonds have not been reflected in the long-term debt in the accompanying financial statements.

| <u>Description</u>                               | <u>Original<br/>Issuance</u> | <u>Balance as of<br/>June 30, 2012</u> |
|--|------------------------------|--|
| Reassessment District 2001-01 (Alfred Nobel)     | \$ 9,810,000                 | \$ 3,730,000                           |
| Reassessment District 2005-1 (John Muir Parkway) | 6,550,345                    | 5,860,000                              |

**NOTE 8: RISK MANAGEMENT**

General Liability Insurance

Coverage is maintained with the Municipal Pooling Authority (MPA) with coverage limits of \$10,000,000 per occurrence. The City maintains a deductible of \$5,000 per occurrence.

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 8: RISK MANAGEMENT (CONTINUED)**

Workers' Compensation

The City has coverage limits for the following without a deductible:

|                                |                             |
|--------------------------------|-----------------------------|
| MPA                            | \$0 to \$500,000            |
| American Safety Insurance      | \$500,000 to \$1,000,000    |
| CSAC-EIA                       | \$1,000,000 to \$4,000,000  |
| ACE American Insurance Company | \$5,000,000 to \$45,000,000 |

As of June 30, 2012, the City's estimated claims liabilities were as follows.

|                      |                              |
|----------------------|------------------------------|
| General Liability    | \$ 115,800                   |
| Workers Compensation | <u>7,871</u>                 |
| <br>Total            | <br><u><u>\$ 123,671</u></u> |

Changes in the claims liabilities for the fiscal years ended June 30, 2011 and 2012 are as follows:

| <u>Fiscal Year</u> | <u>Balance at<br/>Beginning of<br/>Fiscal Year</u> | <u>Current Year<br/>Claims and<br/>Changes in<br/>Estimates</u> | <u>Claim<br/>Payments</u> | <u>Balance at<br/>End of<br/>Fiscal Year</u> |
|--------------------|--|---|---------------------------|--|
| 2010-2011          | \$ 210,968   | \$ 559,583  | \$ (638,881)              | \$ 131,670                                   |
| 2011-2012          | 131,670  | 547,958   | (555,957)                 | 123,671                                      |

Miscellaneous Coverages

The MPA provides additional coverage for the following risks incurred by the City:

| <u>Coverage Type</u>     | <u>Deductibles</u> | <u>Coverage<br/>Limits</u> |
|--------------------------|--------------------|----------------------------|
| Auto - Physical damage:  |                    |                            |
| Police vehicles          | \$ 3,000           | \$ 250,000                 |
| All other vehicles       | 2,000              | 250,000                    |
| All risk fire & property | 5,000              | 500,000,000                |
| Boiler & machinery       | 5,000              | 100,000,000                |

The MPA is governed by a Board consisting of representatives from member municipalities. The Board controls the operations of the MPA, including selection of management and approval of operating budgets, independent of any influence by member municipalities beyond their representation on the Board.

The City's deposits with the MPA are in accordance with formulas established by the MPA. Actual surpluses or losses are shared according to a formula developed from overall loss costs and spread to member entities on a percentage basis after a retrospective rating.

Audited financial statements can be obtained from the Municipal Pooling Authority, 1911 San Miguel Drive, #200, Walnut Creek, California 94596.

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 9: FUND BALANCES**

Details of the fund balance classifications of the governmental funds as of June 30, 2012 are as follows:

|  | General<br>Fund      | Hercules<br>Public Financing<br>Authority Debt<br>Service Fund | Other<br>Governmental<br>Funds | Total                |
|--|----------------------|--|--------------------------------|----------------------|
| <b>Nonspendable:</b>                               |                      |  |                                |                      |
| Accumulated project costs/ land held<br>for resale | \$ 7,223,845         | \$ 5,545,919   | \$ 2,877,104                   | \$ 15,646,868        |
| Advances to other funds                            | 13,895,004           | -  |                                | 13,895,004           |
| Prepays and inventory                              | 17,616               | -  | 11,013                         | 28,629               |
| <b>Total Nonspendable</b>                          | <b>21,136,465</b>    | <b>5,545,919</b>   | <b>2,888,117</b>               | <b>29,570,501</b>    |
| <b>Restricted for:</b>                             |                      |  |                                |                      |
| Streets and roads                                  | -                    | -  | 4,598,488                      | 4,598,488            |
| Public safety                                      | -                    | -  | 82,726                         | 82,726               |
| Development  | -                    | -  | 6,303,212                      | 6,303,212            |
| Debt service                                       | -                    | 2,095,367  | -                              | 2,095,367            |
| <b>Total Restricted</b>                            | <b>-</b>             | <b>2,095,367</b>   | <b>10,984,426</b>              | <b>13,079,793</b>    |
| <b>Assigned for:</b>                               |                      |  |                                |                      |
| Economic uncertainty                               | 561,482              | -  | -                              | 561,482              |
| <b>Total Assigned</b>                              | <b>561,482</b>       | <b>-</b>   | <b>-</b>                       | <b>561,482</b>       |
| Unassigned   | (240,256)            | -  | (173,527)                      | (413,783)            |
| <b>Total Fund Balance</b>                          | <b>\$ 21,457,691</b> | <b>\$ 7,641,286</b>  | <b>\$ 13,699,016</b>           | <b>\$ 42,797,993</b> |

**NOTE 10: CAPITAL LEASE – SALES TYPE**

On August 14, 2008, the City of Hercules and Bio-Rad Laboratories, Inc. entered in to a lease agreement, which Bio-Rad agreed to lease from the City of Hercules, the premises, consisting of the land located in the City of Hercules, County of Contra Costa, State of California, commonly known as the Venture Commerce Center located at 203-295 Linus Pauling Drive, including five (5) buildings consisting of approximately 96,847 rentable square feet, together with the parking lot and associated improvements serving the buildings.

The term of this lease shall be for thirty (30) years, commencing on September 15, 2008 and ending on September 14, 2038, or terminated sooner pursuant to the terms of this lease. Bio-Rad Laboratories, Inc. has the option to terminate this lease anytime on or after the fifteenth (15<sup>th</sup>) anniversary date as to a portion or the entire premises by delivering to the City of Hercules not later than three (3) months prior to said fifteenth (15<sup>th</sup>) anniversary date or any applicable later termination date, a notice of such election.

The City of Hercules granted to Bio-Rad Laboratories, Inc. the option to purchase the premises, Bio-Rad Laboratories, Inc. may elect to exercise the Purchase Option by delivering to the City of Hercules written notice of such election within 30 days prior to either of the following dates: (i) the fifteenth (15<sup>th</sup>) anniversary date; (ii) the twentieth (20<sup>th</sup>) anniversary date; or (iii) the twenty-fifth (25<sup>th</sup>) anniversary date, If Bio-Rad Laboratories, Inc. has not elected to exercise the Purchase Option during the time period said above, then the Purchase Option shall automatically be deemed elected by Bio-Rad Laboratories, Inc. as of the expiration date unless Bio-Rad Laboratories, Inc., provides prior written notice to the City of Hercules within fifteen (15) days prior to the expiration date electing not to pursue the Purchase Option, If Bio-Rad Laboratories, Inc. elects to exercise the Purchase Option on the expiration date, the purchase price for the premises shall be one dollar (\$1.00).

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 10: CAPITAL LEASE – SALES TYPE (CONTINUED)**

Total lease revenue of \$26,723,100 will be received from the Bio-Rad Laboratories, Inc. during the term of lease. The interest rate on the lease payments is 8.0381%. Monthly lease payments vary from \$55,300 to \$83,699 will be received on the first day of each month without notice, offset, deduction or demand, in advance, during the lease term.

Future estimated minimum lease payments to be received are as follows:

| Fiscal Year<br>Ended<br>June 30,   | Amounts             |
|------------------------------------|---------------------|
| 2013                               | \$ 750,678          |
| 2014                               | 773,394             |
| 2015                               | 796,110             |
| 2016                               | 818,826             |
| 2017                               | 841,542             |
| 2018-2022                          | 4,457,898           |
| 2023-2027                          | 4,636,150           |
| 2028-2032                          | 4,840,950           |
| 2033-2037                          | 4,967,600           |
| 2038-2041                          | 1,171,214           |
|                                    | <u>24,054,362</u>   |
| Less: Unearned Income              | <u>(14,520,604)</u> |
| Net Investment in Lease Receivable | <u>\$ 9,533,758</u> |

**NOTE 11: INTERFUND TRANSACTIONS**

Long-Term Advances

At June 30, 2012, the City had the following long-term advances:

|                                 | <u>Interfund<br/>Receivables</u> | <u>Interfund<br/>Payables</u> |
|---------------------------------|----------------------------------|-------------------------------|
| Major Funds:                    |                                  |                               |
| General Fund                    | \$ 13,895,004                    | \$ -                          |
| Major Proprietary Funds:        |                                  |                               |
| Sewer Fund                      | 313,047                          | -                             |
| Hercules Municipal Utility Fund | -                                | 1,634,104                     |
| Nonmajor Governmental Fund:     |                                  |                               |
| DIF Special Revenue Fund        | 1,776,812                        | -                             |
| Community Development Fund      | 163,200                          | -                             |
| Fiduciary Fund:                 |                                  |                               |
| Private Purpose Trust Fund      | -                                | 14,513,959                    |
|                                 | <u>\$ 16,148,063</u>             | <u>\$ 16,148,063</u>          |

Advances to the General Fund were to provide for the construction of the Hercules Municipal Utility electric system.

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 11: INTERFUND TRANSACTIONS (CONTINUED)**

Long-Term Advances (continued)

Advances to the Redevelopment Agency from the General Fund, the Public Financing Authority, DIF Special Revenue Fund, and the Sewer Fund were for the New Town Center project, Hercules Municipal Utility electric system, construction of the community library, a park and teen center, and upgrades to the wastewater treatment plant.

Advances to the Hercules Municipal Utility from the General Fund were to provide funding for the Hercules Municipal Utility's operations

Due To/From Other Funds

Due to/from other funds as of June 30, 2012 were as follows:

|   | <u>Interfund<br/>Receivables</u> | <u>Interfund<br/>Payables</u> |
|---|----------------------------------|-------------------------------|
| Major Funds:  |                                  |                               |
| General Fund  | \$ 274,086                       | \$ 753,631                    |
| Hercules Public Financing Authority Debt Service Fund | -                                | 264,843                       |
| Nonmajor Governmental Funds:                          |                                  |                               |
| AB 3229 COPS Program Special Revenue Fund             | -                                | -                             |
| State Gas Tax Special Revenue Fund                    | 69,796                           | -                             |
| Grant Special Revenue Fund                            | -                                | 527,650                       |
| DIF Special Revenue Fund                              | -                                | -                             |
| Community Development Fund                            | -                                | -                             |
| Development Fee Fund                                  | -                                | -                             |
| City Capital Projects Fund                            | 126,555                          | -                             |
| Stormwater Assessment Fund                            | -                                | -                             |
| Internal Service Funds:                               |                                  |                               |
| Vehicle Replacement Fee                               | 753,631                          | -                             |
| Fiduciary Funds:                                      |                                  |                               |
| Private Purpose Trust Fund                            | 322,056                          | -                             |
|   | <u>\$ 1,546,124</u>              | <u>\$ 1,546,124</u>           |

The due to/from other funds are to provide cash flow for the funds with negative cash and for other short-term borrowings between funds.

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 11: INTERFUND TRANSACTIONS (CONTINUED)**

Transfers

| <u>Transfer from</u>                       | <u>Transfer to</u>                         | <u>Amount</u>               |
|--|--|-----------------------------|
| Redevelopment Agency Special Revenue Fund  | Redevelopment Agency Debt Service Fund     | \$ 6,395,172                |
| General Fund                               | Redevelopment Agency Debt Service Fund     | 2,019,507                   |
| Redevelopment Agency Debt Service Fund     | Redevelopment Agency Special Revenue Fund  | 573,336                     |
|  | Redevelopment Agency Capital Projects Fund | 228,380                     |
| Redevelopment Agency Capital Projects Fund | Redevelopment Agency Special Revenue Fund  | 14,499                      |
|  | Redevelopment Agency Debt Service Fund     | 1,361,576                   |
| Nonmajor Governmental Funds                | General Fund                               | 117,500                     |
|  | Redevelopment Agency Special Revenue Fund  | 10,938                      |
|  | Redevelopment Agency Debt Service Fund     | 82,338                      |
|  | Redevelopment Agency Capital Projects Fund | 836,748                     |
|  | Nonmajor Governmental Funds                | 295,019                     |
|  |  | <u><u>\$ 11,935,013</u></u> |

The transfers are to reimburse expenditures made on behalf of another fund, to fund capital projects or for debt service payments. The General Fund transferred \$2,019,507 to the Redevelopment Agency Debt Service Fund to transfer the proceeds and related activity from the sale of land held for resale previously transferred from the Redevelopment Agency to the City in lieu of repayment of an advance.

**NOTE 12: PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

Plan Description

The City contributes to the California Public Employees' Retirement System (PERS), a cost sharing multiple-employer public employee 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. Copies of PERS' annual financial reports may be obtained from their Executive Office located at 400 Q Street, Sacramento, California 95811.

Funding Policy

The City makes the contribution required of City employees on their behalf and for their account in the amount of 7% for miscellaneous employees and 9% for safety employees. The employee rates are set by statute and therefore generally remain unchanged from year to year. The present employer actuarially determined rates of annual covered payroll were 11.614% for miscellaneous employees and 34.414% for safety employees. For the year ended June 30, 2012, the City contributed \$1,245,457 on employees' behalf and for their account.

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 12: PUBLIC EMPLOYEES' RETIREMENT SYSTEM (CONTINUED)**

Annual Pension Cost

For fiscal year 2011-2012, the City's annual pension cost of \$1,245,457 for PERS was equal to the City's required and actual contributions. The required contribution was determined as part of the June 30, 2010 actuarial report. The assumptions included 7.75% investment rate of return (net of administrative expenses) and projected annual salary increases of 3.55% to 14.45%, depending on age, service, and type of employment, and included an inflation component of 3.0%. The actuarial value of PERS assets was determined using techniques that smooth the effects of short-term volatility in the market value of investments over a three year period. PERS unfunded actuarial accrued liability (or surplus) is being amortized as a level percentage of projected payroll on a closed basis.

**THREE-YEAR TREND INFORMATION FOR PERS**

| <u>Fiscal<br/>Year Ended</u> | <u>Annual<br/>Pension<br/>Cost (APC)</u> | <u>Percentage<br/>of APC<br/>Contributed</u> | <u>Net Pension<br/>Obligation</u> |
|------------------------------|--|--|-----------------------------------|
| 6/30/2010                    | \$ 1,596,456                             | 100%   | \$ -                              |
| 6/30/2011                    | 2,175,603                                | 100%   | -                                 |
| 6/30/2012                    | 1,245,457                                | 100%   | -                                 |

Funding Status

This information is no longer available for the Miscellaneous and Safety Plans, which are only available on a pooled basis and can be obtained from CalPERS.

The schedule of funding progress presented as required supplementary information (RSI) immediately following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the AAL for benefits.

**NOTE 13: DEFERRED COMPENSATION PLAN**

457 Plan

The City offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The Plan is available to full-time employees. The Internal Revenue Service regulations allow an employer to designate a 457(b) Deferred Compensation Plan as an alternative to social security. The plan permits employees to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death or unforeseeable emergency.

All amounts of compensation deferred under the plan, all property and rights purchased with those amounts, and all income attributable to those amounts, property, or rights are (until paid or made available to the employee or other beneficiary) held in trust by a third party administrator (ICMA) for the exclusive benefit of the plan participants and their beneficiaries as prescribed by Internal Revenue Code Section 457(g). Accordingly, these assets have been excluded from the City's Comprehensive Annual Financial Report.

## CITY OF HERCULES

Notes to Financial Statements  
June 30, 2012

### **NOTE 13: DEFERRED COMPENSATION PLAN (CONTINUED)**

#### 401A Plan

The City contributes 4% of total gross salary to the plan for senior managers. For unrepresented group, the City also contributes 4% with a maximum contribution of \$4,000 per year. In addition both groups can contribute to the group plan.

#### PARS

Part-time employees who do not participate in the Public Employees Retirement System are covered through the City's participation in Public Alternative Retirement System (PARS). Employees contribute 6.2% and the City contributes 1.3%.

### **NOTE 14: POST-EMPLOYMENT BENEFITS OTHER THAN PENSIONS**

#### Plan Description

The City provides certain health insurance benefits to retired employees in accordance with memorandums of understanding with each employee group as follows:

For employees who retire from the City of Hercules after at least five (5) years of service with the City and who have reached the age of fifty (50) years old, and who continue health insurance through a City-sponsored health insurance plan, the City will contribute the minimum monthly amount of \$108 of the health insurance premium. For police and police management retirees who have at least ten (10) years of service, or twenty (20) years of service if they retire on disability and continue receiving health insurance through a City-sponsored health insurance plan, the City will contribute a percentage of \$272.14/month, based on the retirees accumulated sick leave and years of service, at retirement. As soon as the retiree is eligible for Medicare, the City will contribute a percentage of the retirees' Kaiser Medicare supplement.

#### Funding Policy

The City's policy is to contribute an amount sufficient to pay the current year's premiums and set-aside an amount equal to the annual required contribution, based on a twenty (20) year amortization. For fiscal year 2011-2012, the City contributed \$34,650, which covered current premiums, and also transferred \$216,000 to the Public Agency Retirement Services. Currently, there are 7 retirees who are receiving benefits.

#### Annual OPEB and Net OPEB Obligation

The City's annual other postemployment benefit (OPEB) cost (expense) is calculated based on the annual required contribution of the employer (ARC), and an amount actuarially determined in accordance with the parameters of GASB Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years (the City has elected a twenty year amortization period). The following table shows the components of the City's annual OPEB cost for the fiscal year, the amount actually contributed to the plan, and changes in the City's net OPEB obligation.

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 14: POST-EMPLOYMENT BENEFITS OTHER THAN PENSIONS (CONTINUED)**

Annual OPEB and Net OPEB Obligation (continued)

|  |              |
|--|--------------|
| Annual required contribution                           | \$ 214,000   |
| Annual OPEB cost (expense)                             | 214,000      |
| Contributions made                                     | (250,650)    |
| Change in net OPEB obligation (asset)                  | (36,650)     |
| Net OPEB obligation (asset) - beginning of fiscal year | (221,686)    |
| Net OPEB obligation (asset) - end of fiscal year       | \$ (258,336) |

The City's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for 2010, 2011, and 2012 were as follows:

| Year Ended | Annual OPEB Cost | Annual OPEB Cost Contribution | Obligation (Asset) |
|------------|------------------|-------------------------------|--------------------|
| 6/30/2010  | \$ 216,000       | 285%                          | \$ (188,612)       |
| 6/30/2011  | 212,000          | 116%                          | (221,686)          |
| 6/30/2012  | 214,000          | 117%                          | (258,336)          |

Funded Status and Funding Progress

As of June 30, 2012, the most recent actuarial valuation date, the plan was 43% funded. The actuarial accrued liability for benefits was \$2,155,000, and the actuarial value of assets was \$935,000, resulting in an unfunded actuarial accrued liability (UAAL) of \$1,220,000. The covered payroll (annual payroll of active employees covered by the plan) was \$4,798,000, and the ratio of the UAAL to the covered payroll was 25.4 percent.

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future.

Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the June 30, 2012 actuarial valuation, the entry age normal cost method was used. The actuarial assumptions included a 6.5 percent investment rate of return, which is the expected long-term investment returns on plan assets, a projected salary increase assumption rate of 3.25 percent, and an annual healthcare cost trend rate of 5 percent. The actuarial value of asset gains or losses are recognized over five years. The UAAL is being amortized as a level percentage of covered payroll over twenty years. The remaining amortization period at June 30, 2012 was seventeen years.

## CITY OF HERCULES

Notes to Financial Statements  
June 30, 2012

### NOTE 15: COMMITMENTS AND CONTINGENCIES

#### A. Lawsuits

The City is presently involved in certain matters of litigation that have arisen in the normal course of conducting City business. City management believes, based upon consultation with the City Attorney, that these cases, in the aggregate, will not have a material adverse effect on the City's Annual Financial Statements. Additionally, City management believes that the City's insurance programs are sufficient to cover any potential losses should an unfavorable outcome materialize.

Hercules LLC – The Redevelopment Agency audited 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 final round of mediation was successful and the case was settled. During fiscal year 2010-2011, the City paid \$968,816 to Hercules, LLC, the balance of project tax increment due for fiscal year 2009-2010, to settle the lawsuit.

#### B. Commitments

AMBAC Litigation – On January 30, 2012, AMBAC filed an action in the Contra Costa County Superior Court against the City, the Agency and each individual member of the City Council, seeking to, among other things, compel the City to transfer \$4,100,000 from the Pooled Cash Account, which AMBAC alleges constitute the December 2011 tax increment receipts, to the Trustee, and in the alternative to impose a constructive trust on such funds and prevent the City from using those funds for any other purpose. The City, Agency and Council members intend to vigorously oppose this action. The City believes that, unless the \$4,100,000 of December receipts are allowed to be accounted for to reimburse the temporary advance from the Pooled Cash Account made on August 1, 2011 to the Trustee, that advance will have been an unlawful diversion of legally restricted funds which itself would need to be reversed in order to avoid violation of various state statutory and constitutional restrictions on the use of those funds. On January 31, 2012, AMBAC filed an ex parte application seeking, among other thing, a temporary restraining order effectively freezing \$4,100,000 of City funds and, in the alternative, a writ of attachment on certain real estate owned by the City. The court denied AMBAC's request for immediate relief on all points, but issued an order to show cause why a preliminary injunction freezing the funds should not issue against the City in several weeks. The City and AMBAC briefed the issue for the court and at a hearing on February 21, 2012, the Court was to evaluate whether AMBAC had demonstrated sufficient urgency to warrant issuing a preliminary injunction against the City, which injunction would have compelled the City in some way to set aside \$4,100,000.

On March 8, 2012, a stipulation and Writ of Attachment was signed between AMBAC and the Hercules Redevelopment Agency and the City of Hercules. It was agreed that as consideration for AMBAC's forbearance on seeking an immediate writ of mandate and preliminary injunction on March 20, 2012, AMBAC received a Writ of Attachment on the real property commonly known as "Parcel C" (Contra Costa County Assessor's Parcel No. 404-020-076-0) (Property "A") and the real property commonly known as "Victoria Crescent" (Contra Costa County Assessor's Parcel No. 404-040-062-6)(Property "B"). These properties are to be sold in 2014 to satisfy what is owed to AMBAC.

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 16: JOINT POWERS AGREEMENTS**

The City is a member of the joint powers agencies described below. Each of these agencies is governed by a Board, which controls their operation, including selection of management and approval of operating budgets, independent of influence by member municipalities beyond their representation on the Board.

**A. West Contra Costa Transportation Advisory Committee (WCCTAC)**

WCCTAC was established in 1990 to develop regional strategies and meet regional requirements established by Measure "C" and to cooperatively address West Contra Costa County transportation issues.

The City's payments to WCCTAC are in accordance with a formula under which each member Agency pays a proportionate share of the expenditures based on the number of voting members representing each agency. Audited financial statements can be obtained from the WCCTAC, One Alvarado Square, San Pablo, California 94806, The City has one voting member on the WCCTAC and pays 10% of expenditures, which amounted to \$42,772 for fiscal year 2011-2012.

**B. West Contra Costa Integrated Waste Management Authority (WCCIWMA)**

WCCIWMA was established in 1991 to coordinate landfill use reduction in the West Contra Costa County Area as mandated by the State of California. The City is represented by one Director. Funding for WCCIWMA is provided for through a surcharge collected from the ratepayers within WCCIWMA's jurisdiction.

Audited financial statements can be obtained from the WCCIWMA, One Alvarado Square, San Pablo, California 94806.

**C. Pinole/Hercules Wastewater Treatment Plant**

On January 23, 2001, the cities of Pinole and Hercules entered into a joint powers agreement for the operation and ownership of the Pinole/Hercules Wastewater Treatment Plant (Plant). The City retains responsibility for the operation and maintenance of its wastewater collection system. The City of Hercules has an undivided fifty percent (50%) ownership interest in the Plant. The City of Pinole has the right and responsibility to manage and operate the Plant. Also, the City of Pinole maintains the records and accounts for all the transactions.

The records are available and can be obtained from the City of Pinole, 2131 Pear Street, Pinole, California 94564.

**NOTE 17: STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY**

Deficit Fund Balances/Net Assets

As of June 30, 2012, the following funds had a deficit fund balance:

|  | <u>Deficit Fund<br/>Balances</u> |
|--|----------------------------------|
| Nonmajor Governmental Funds:               |                                  |
| Stormwater Assessment Special Revenue Fund | \$ 69,013                        |
| City Capital Projects Fund                 | 104,514                          |
| Fiduciary Fund:                            |                                  |
| Private Purpose Trust Fund                 | \$ 59,456,854                    |

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 17: STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY (CONTINUED)**

Expenditures in Excess of Appropriations

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

|                                   | <u>Excess of<br/>Appropriations</u> |
|-----------------------------------|-------------------------------------|
| Major Governmental Funds:         |                                     |
| General Fund:                     |                                     |
| General Government                | \$ 339,906                          |
| Redevelopment Agency Debt Service | 1,609,284                           |
| Nonmajor Governmental Funds:      |                                     |
| Landscape and Lighting Districts  | 47,120                              |
| Stormwater Assessment             | 56,158                              |
| Development Impact Fees (DIF)     | 167,358                             |
| Development Fee                   | 81,660                              |

**NOTE 18: EXTRAORDINARY ITEM**

Redevelopment Agency Dissolution

On December 29, 2011, the California Supreme Court upheld Assembly Bill 1X 26 (Bill) that provides for the dissolution of all redevelopment agencies in the State of California. This action impacted the reporting entity of the City that previously had reported a redevelopment agency blended component unit.

The Bill provides that upon dissolution of a redevelopment agency, either the City or another unit of local government will agree to serve as the "successor agency" to hold the assets until they are distributed to other units of state and local government.

After enactment of the law, which occurred on June 28, 2011, redevelopment agencies in the State of California cannot enter into new projects, obligations or commitments. Subject to the control of a newly established oversight board, remaining assets can only be used to pay enforceable obligations in existence at the date of dissolution (including the completion of any unfinished projects that were subject to legally enforceable contractual commitments).

In future fiscal years, successor agencies will only be allocated revenue in the amount that is necessary to pay the estimated annual installment payments on enforceable obligations of the former redevelopment agency until all enforceable obligations of the prior redevelopment agency have been paid in full and all assets have been liquidated.

The Bill directs the State Controller to review the propriety of any transfers of assets between redevelopment agencies and other public bodies that occurred after January 1, 2011. If the public body that received such transfers is not contractually committed to a third party for the expenditure or encumbrance of those assets, the State Controller is required to order the available assets to be transferred to the public body designated as the successor agency by the Bill.

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 18: EXTRAORDINARY ITEM (CONTINUED)**

Redevelopment Agency Dissolution (continued)

Management believes, in consultation with legal counsel, that the obligations of the former RDA due to the City are valid enforceable obligations payable by the Successor Agency trust under the requirements of the Bill. The City's position on this issue is not a position of settled law and there is considerable legal uncertainty regarding this issue. It is reasonably possible that a legal determination may be made at a later date by an appropriate judicial authority that would resolve this issue unfavorably to the City.

In accordance with the timeline set forth in the Bill (as modified by the California Supreme Court on December 29, 2011), all redevelopment agencies in the State of California were dissolved and ceased to operate as a legal entity as of February 1, 2012.

Prior to that date, the final seven months of the activity of the RDA are reported in the governmental funds of the City. After the date of dissolution, as allowed under Section 34176(a) of the Bill, the City elected not to retain the housing assets and functions previously performed by the former RDA. The assets, liabilities, and activities of the dissolved RDA, are reported in the Successor Agency fiduciary fund (private purpose trust fund) in the financial statements of the City.

The transfer of the assets and liabilities of the former RDA as of February 1, 2012 (effectively the same date as January 31, 2012) from governmental funds of the City to fiduciary funds was reported as an extraordinary loss in the governmental fund financial statements and an extraordinary gain in the government wide statement of activities. The receipt of these assets and liabilities as of January 31, 2012 was reported in the private-purpose trust fund financial statements as an extraordinary loss.

**NOTE 19: SUBSEQUENT EVENTS**

Renegotiation of loan repayment terms for H.E.L.P. and R.D.L.P. loans

In October 2013, the City negotiated a new repayment plan with the California Housing Finance Agency (Agency) to repay its H.E.L.P and R.D.L.P. loans.

H.E.L.P. Loan Payable: The City and Agency amended the agreement to extend the due date of the H.E.L.P. loan and accumulated interest until April 2027 and to reduce the interest rate to 1.5 percent simple interest effective October 31, 2013.

Future debt service requirements of the H.E.L.P. loan are:

| Fiscal Year<br>Ended<br>June 30, | Principal           | Interest          |
|----------------------------------|---------------------|-------------------|
| 2013                             | \$ -                | \$ -              |
| 2014                             | 50,000              | -                 |
| 2015                             | 50,000              | -                 |
| 2016                             | 50,000              | -                 |
| 2017                             | 50,000              | -                 |
| 2018-2022                        | 500,000             | -                 |
| 2023-2027                        | 900,000             | 307,988           |
|                                  | <u>\$ 1,600,000</u> | <u>\$ 307,988</u> |

**CITY OF HERCULES**

Notes to Financial Statements  
June 30, 2012

**NOTE 19: SUBSEQUENT EVENTS (CONTINUED)**

Renegotiation of loan repayment terms for H.E.L.P. and R.D.L.P. loans (continued)

R.D.L.P. Loan Payable: The City and Agency amended the agreement to extend the due date of the R.D.L.P. loan and accumulated interest until August 2026 and to reduce the interest rate to 1.5 percent simple interest effective October 31, 2013.

Future debt service requirements of the H.E.L.P. loan are:

| Fiscal Year<br>Ended<br>June 30, | Principal           | Interest          |
|----------------------------------|---------------------|-------------------|
| 2013                             | \$ -                | \$ -              |
| 2014                             | 50,000              | -                 |
| 2015                             | 50,000              | -                 |
| 2016                             | 50,000              | -                 |
| 2017                             | 50,000              | -                 |
| 2018-2022                        | 500,000             |                   |
| 2023-2027                        | <u>3,050,000</u>    | <u>440,759</u>    |
|                                  | <u>\$ 3,750,000</u> | <u>\$ 440,759</u> |

Transfer of Land from the City’s Former Redevelopment Agency to the City

Subsequent to June 30, 2012, the City will transfer back the land held for sale to the former Hercules Redevelopment Agency (former RDA), now a Private Purpose Trust Fund of the City. Land was originally transferred by the former RDA to the City in lieu of repayment for various advances owed to several funds on March 8, 2011 through the adoption of Resolution 11-027. Total advances owed were greater than the value of the land transferred and the difference was reported as a special item on the 2010-11 financial statements. In January 2012, the General Fund sold land valued at \$2,019,507 and transferred the net proceeds of \$1,248,876 to the former RDA. A recap of the remaining land that what will be transferred back to the former RDA follows:

|  | Land Held<br>for Resale<br>Transfer |
|--|-------------------------------------|
| General Fund   | \$ 7,223,845                        |
| Nonmajor Governmental Fund                               | 2,877,104                           |
| Public Financing Authority                               | 5,545,919                           |
| Sewer Fund   | 8,500,651                           |
| Hercules Municipal Utility                               | 5,273,495                           |
|  | <u>\$ 29,421,014</u>                |
| Former RDA Capital Projects (Private Purpose Trust Fund) | <u>\$ (29,421,014)</u>              |

## CITY OF HERCULES

Notes to Financial Statements  
June 30, 2012

### **NOTE 19: SUBSEQUENT EVENTS (CONTINUED)**

#### Sale of Hercules Municipal Utility Assets

On May 28, 2013, the Hercules City Council approved an agreement with Pacific Gas and Electric Company (PG&E) to purchase the assets of Hercules Municipal Utility (HMU). On June 5, 2012, residents of the City voted to pass Measure N, authorizing the sale of HMU. Measure N was approved by 77% of voters. On August 28, 2012, the Hercules City Council adopted procedures for accepting bids for sale of the HMU assets, as required by the California Public Utilities Code. Representatives of the City solicited bid proposals and ultimately determined that PG&E offered the highest and best bid. Hercules and PG&E then engaged in negotiations to prepare the Asset Purchase Agreement containing all of the necessary terms and conditions for the sale. The City intends to retire the HMU bond debt with the proceeds from the sale.

#### Adoption of Local Measures A and O

Subsequent to June 30, 2012, the City adopted local Measures O and A which were approved by the voters in elections held on June 5, 2012 and June 4, 2013, respectively, Measure A increases the utility users tax by 2 percent from 6 percent to 8 percent for five years. Measure O temporarily increases the sales tax rate by one-half of one percent from 8.25 percent to 8.75 percent for four years unless extended by the voters.

### **NOTE 20: FINANCIAL CONDITION**

While the City defaulted on repayment of a \$3.9 million loan to the California Housing Finance Agency on August 15, 2011, it was able to modify the payment terms as disclosed in note 19, with the final payment being due in August 2027.

Of the \$25.4 million reported as assets in the General Fund, 83 percent of the balance represents interfund loans with the former Redevelopment Agency (Agency), including \$7.2 million of land held for resale that was transferred back to Agency subsequent to June 30, 2012, as described in note 19.

With the dissolution of the redevelopment agency on February 1, 2012, as described in note 18, there is uncertainty as to whether the City's General Fund will be repaid the accumulated \$21.1 million loan owed by the Agency, now a private purpose trust fund of the City. However, the written agreement between the Agency and the City to fund costs on behalf of the Agency was signed within two years of the creation of the agency. Under Assembly Bill X1 26 (Redevelopment Dissolution Act), a written agreement between a redevelopment agency and the city that created it that provided loans or other startup funds for the redevelopment agency that were entered into within two years of the formation of the redevelopment agency are not invalid. The City is currently working with the State Department of Finance to determine the outcome of these loans. The possible outcome of this matter cannot presently be determined. Accordingly, no provision for any allowance for doubtful accounts has been made in the financial statements for possible forgiveness of these loans.

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## **REQUIRED SUPPLEMENTARY INFORMATION**

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**CITY OF HERCULES**

Required Supplementary Information  
June 30, 2012

1. SCHEDULE OF FUNDING PROGRESS – PENSION

FUNDED STATUS OF MISCELLANEOUS PLAN

This information is no longer available for the Miscellaneous Plan. Information is available on a pooled basis only and can be obtained from Cal PERS, P.O. Box 942709, Sacramento, CA 94229-2709.

FUNDED STATUS OF SAFETY PLAN

This information is no longer available for the Safety Plan. Information is available on a pooled basis only and can be obtained from Cal PERS, P.O. Box 942709, Sacramento, CA 94229-2709.

2. SCHEDULE OF FUNDING PROGRESS – OTHER POST EMPLOYMENT BENEFITS PLAN (OPEB)

The table below shows an analysis of the actuarial value of assets as a percentage of the actuarial accrued liability and the unfunded actuarial accrued liability as a percentage of the annual covered payroll as of June 30:

| Actuarial<br>Valuation<br>Date | (a)<br>Entry Age<br>Actuarial<br>Accrued<br>Liability | (b)<br>Actuarial<br>Value of<br>Assets (AVA) | (a)-(b)<br>Unfunded<br>Actuarial<br>Accrued<br>Liability (UAAL) | (b)/(a)<br>Funded<br>Ratio | (c)<br>Covered<br>Payroll | [(a)-(b)/(c)]<br>UAAL as a<br>% of<br>Payroll |
|--------------------------------|---|--|---|----------------------------|---------------------------|---|
| 6/30/2007                      | \$ 1,116,000  | \$ -   | \$ 1,116,000  | 0.0%                       | \$ 6,830,000              | 16.3%   |
| 6/30/2011                      | 2,155,000   | 884,000                                      | 1,271,000   | 41.0%                      | 4,798,000                 | 26.5%   |
| 6/30/2012                      | 2,155,000   | 935,000                                      | 1,220,000   | 43.0%                      | 4,798,000                 | 25.4%   |

**CITY OF HERCULES**

Budgetary Comparison Schedule  
General Fund  
For the Year Ended June 30, 2012

|  | Budgeted Amounts  |                   | Actual            | Variance with<br>Final Budget |
|--|-------------------|-------------------|-------------------|-------------------------------|
|  | Original          | Final             |                   |                               |
| <b>Revenues:</b>                       |                   |                   |                   |                               |
| Taxes                                  | \$ 5,560,000      | \$ 5,560,000      | \$ 5,489,472      | \$ (70,528)                   |
| Licenses and permits                   | 418,800           | 418,800           | 343,071           | (75,729)                      |
| Fines, forfeits and penalties          | 55,000            | 55,000            | 62,858            | 7,858                         |
| Revenue from use of money and property | 2,768,885         | 2,768,885         | 188,055           | (2,580,830)                   |
| Aid from other governments             | 1,454,000         | 1,454,000         | 1,455,596         | 1,596                         |
| Charges for services                   | 2,292,616         | 2,292,616         | 1,827,556         | (465,060)                     |
| Miscellaneous revenue                  | 1,185,895         | 1,185,895         | 930,391           | (255,504)                     |
| <b>Total Revenues</b>                  | <b>13,735,196</b> | <b>13,735,196</b> | <b>10,296,999</b> | <b>(3,438,197)</b>            |
| <b>Expenditures:</b>                   |                   |                   |                   |                               |
| <b>Current:</b>                        |                   |                   |                   |                               |
| <b>General government:</b>             |                   |                   |                   |                               |
| City Council                           | 301,026           | 301,105           | 267,662           | 33,443                        |
| Community events                       | --                | --                | 857               | (857)                         |
| City manager                           | 377,971           | 397,300           | 429,284           | (31,984)                      |
| Legal services                         | 147,000           | 219,015           | 486,902           | (267,887)                     |
| Management services                    | 238,030           | 238,047           | 216,182           | 21,865                        |
| City clerk                             | --                | 16,846            | 139               | 16,707                        |
| Cable TV                               | 70,531            | 82,567            | 71,603            | 10,964                        |
| Risk management                        | 1,028,472         | 1,048,981         | 1,121,734         | (72,753)                      |
| Recruitment                            | 290,160           | 300,283           | 211,656           | 88,627                        |
| Finance/operations                     | 876,611           | 901,811           | 1,038,042         | (136,231)                     |
| Miscellaneous                          | 216,000           | 216,000           | 217,800           |                               |
| <b>Total general government</b>        | <b>3,545,801</b>  | <b>3,721,955</b>  | <b>4,061,861</b>  | <b>(339,906)</b>              |
| <b>Public safety:</b>                  |                   |                   |                   |                               |
| Police administration                  | 2,257,976         | 2,258,063         | 1,864,823         | 393,240                       |
| Police patrol                          | 2,802,035         | 2,802,186         | 2,862,439         | (60,253)                      |
| <b>Total public safety</b>             | <b>5,060,011</b>  | <b>5,060,249</b>  | <b>4,727,262</b>  | <b>332,987</b>                |
| <b>Streets and public works:</b>       |                   |                   |                   |                               |
| Street facilities                      | 186,987           | 187,080           | 184,528           | 2,552                         |
| Engineering                            | 54,286            | 54,703            | 26,606            | 28,097                        |
| <b>Total streets and public safety</b> | <b>241,273</b>    | <b>241,783</b>    | <b>211,134</b>    | <b>30,649</b>                 |
| <b>Parks and recreation:</b>           |                   |                   |                   |                               |
| Library                                | 110,745           | 126,874           | 79,474            | 47,400                        |
| Administration                         | --                | 7,272             | 3,686             | 3,586                         |
| Facility rental                        | 123,792           | 128,882           | 142,006           | (13,124)                      |
| Day camp                               | 172,491           | 172,491           | 126,226           | 46,265                        |
| Child care                             | 614,617           | 611,117           | 551,969           | 59,148                        |
| Recreation classes                     | 79,679            | 81,775            | 72,569            | 9,206                         |
| Senior citizens                        | 60,205            | 60,205            | 88,413            | (28,208)                      |
| Tiny tots                              | 151,366           | 154,866           | 158,155           | (3,289)                       |
| Swim center                            | 362,389           | 370,329           | 354,035           | 16,294                        |
| Sports program                         | 130,335           | 132,018           | 116,162           | 15,856                        |
| Teen program                           | 73,887            | 76,317            | 48,795            | 27,522                        |
| Youth and teen resource center         | 161,088           | 161,088           | 161,417           | (329)                         |
| <b>Total parks and recreation</b>      | <b>2,040,594</b>  | <b>2,083,234</b>  | <b>1,902,907</b>  | <b>180,327</b>                |

continued

**CITY OF HERCULES**

Budgetary Comparison Schedule (continued)  
General Fund  
For the Year Ended June 30, 2012

|  | Budgeted Amounts     |                      | Actual            | Variance with<br>Final Budget |
|--|----------------------|----------------------|-------------------|-------------------------------|
|  | Original             | Final                |                   |                               |
| Expenditures (continued):                                    |                      |                      |                   |                               |
| Current (continued):   |                      |                      |                   |                               |
| Community development:                                       |                      |                      |                   |                               |
| Business and regional planning                               | \$ 475,577           | \$ 593,389           | \$ 349,800        | \$ 243,589                    |
| Building inspection  | 194,214              | 194,258              | 89,427            | 104,831                       |
| Total community development                                  | 669,791              | 787,647              | 439,227           | 348,420                       |
| Lease expense  | 1,703,074            | 1,703,074            | 779,109           | 923,965                       |
| Total Expenditures   | 13,260,544           | 13,597,942           | 12,121,500        | 1,476,442                     |
| <br>   |                      |                      |                   |                               |
| Excess (Deficiency) of Revenues<br>Over (Under) Expenditures | 474,652              | 137,254              | (1,824,501)       | (1,961,755)                   |
| <br>   |                      |                      |                   |                               |
| Other Financing Sources (Uses):                              |                      |                      |                   |                               |
| Transfers in   | 1,380,612            | 1,380,612            | 117,500           | (1,263,112)                   |
| Transfers out  | (1,855,064)          | (1,855,064)          | (2,019,507)       | (164,443)                     |
| Total Other Financing Sources (Uses)                         | (474,452)            | (474,452)            | (1,902,007)       | (1,427,555)                   |
| <br>   |                      |                      |                   |                               |
| Net Change in Fund Balances                                  | 200                  | (337,198)            | (3,726,508)       | (3,389,310)                   |
| <br>   |                      |                      |                   |                               |
| Budgetary Fund Balances - Beginning of Year                  | 25,149,729           | 25,149,729           | 25,149,729        | --                            |
| <br>   |                      |                      |                   |                               |
| Budgetary Fund Balances - End of Year                        | <u>\$ 25,149,929</u> | <u>\$ 24,812,531</u> | <u>21,423,221</u> | <u>\$ (3,389,310)</u>         |

Explanation of differences between statement of revenues, expenditures and changes in fund balance:

|                                      | Budgetary<br>Comparison<br>Schedule | Trust Funds<br>Not<br>Budgeted | Statement of<br>Revenues,<br>Expenditures<br>and Changes in<br>Fund Balance |
|--------------------------------------|-------------------------------------|--------------------------------|---|
| Total revenues                       | \$ 10,296,999                       | \$ 34,470                      | \$ 10,331,469   |
| Total expenditures                   | 12,121,500                          | --                             | 12,121,500  |
| Revenues over (under) expenditures   | (1,824,501)                         | 34,470                         | (1,790,031)   |
| Total other financing sources (uses) | (1,902,007)                         | --                             | (1,902,007)   |
| Net change in fund balances          | <u>\$ (3,726,508)</u>               | <u>\$ 34,470</u>               | <u>\$ (3,692,038)</u>   |

**CITY OF HERCULES**

Budgetary Comparison Schedule  
 Redevelopment Agency Special Revenue Fund  
 For the year Ended June 30, 2012

|  | Budgeted Amounts       |                        | Actual              | Variance with<br>Final Budget |
|--|------------------------|------------------------|---------------------|-------------------------------|
|  | Original               | Final                  |                     |                               |
| Revenues:  |                        |                        |                     |                               |
| Taxes and assessments  | \$ 9,550,310           | \$ 9,550,310           | \$ 5,061,535        | \$ (4,488,775)                |
| Use of money and property                                    | (192,000)              | (192,000)              | 130,536             | 322,536                       |
| Program income   | 1,526,918              | 1,526,918              | 93,624              | (1,433,294)                   |
| Charges for services   | 2,200                  | 2,200                  | --                  | (2,200)                       |
| Other revenues   | 102,907                | 102,907                | 61,146              | (41,761)                      |
| Total Revenues   | <u>10,990,335</u>      | <u>10,990,335</u>      | <u>5,346,841</u>    | <u>(5,643,494)</u>            |
| Expenditures:  |                        |                        |                     |                               |
| Current:   |                        |                        |                     |                               |
| Community development  | 3,061,038              | 3,191,475              | 540,238             | 2,651,237                     |
| Total Expenditures   | <u>3,061,038</u>       | <u>3,191,475</u>       | <u>540,238</u>      | <u>2,651,237</u>              |
| Excess (Deficiency) of Revenues<br>Over (Under) Expenditures | <u>7,929,297</u>       | <u>7,798,860</u>       | <u>4,806,603</u>    | <u>(2,992,257)</u>            |
| Other Financing Sources (Uses):                              |                        |                        |                     |                               |
| Transfers in   | 3,634,064              | 3,634,064              | 598,773             | (3,035,291)                   |
| Transfers out  | (9,840,215)            | (9,840,215)            | (6,395,172)         | 3,445,043                     |
| Total Other Financing Sources (Uses)                         | <u>(9,840,215)</u>     | <u>(6,206,151)</u>     | <u>(5,796,399)</u>  | <u>409,752</u>                |
| Extraordinary item - RDA dissolution                         | <u>--</u>              | <u>--</u>              | <u>18,113,727</u>   | <u>18,113,727</u>             |
| Net Change in Fund Balances                                  | (1,910,918)            | 1,592,709              | 17,123,931          | 15,531,222                    |
| Fund Balances - Beginning of Year                            | <u>(17,123,931)</u>    | <u>(17,123,931)</u>    | <u>(17,123,931)</u> | <u>--</u>                     |
| Fund Balances - End of Year                                  | <u>\$ (19,034,849)</u> | <u>\$ (15,531,222)</u> | <u>\$ --</u>        | <u>\$ 15,531,222</u>          |

## CITY OF HERCULES

### Notes to Required Supplementary Information June 30, 2012

#### BUDGETARY PRINCIPLES

The City follows these procedures in establishing the budgetary data reflected in the financial statements:

1. In June, the City Manager submits to the City Council a proposed operating budget for the following fiscal year. This budget includes proposed expenditures, by fund and department, and the revenues expected to finance them.
2. Public hearings are conducted to obtain taxpayer comments.
3. The budget is legally enacted through passage of a resolution before July 1.
4. The City Manager is authorized to transfer budgeted amounts between objects within the same department; however, any revisions, which alter total expenditures of any fund, must be approved by the City Council.
5. Formal budgetary integration is employed as a management control device. Special Revenue Fund budgets are adopted on a basis consistent with accounting principles generally accepted in the United States (USGAAP) and are consistent with the basis used for financial reporting. Accordingly, actual revenues and expenditures can be compared with related budget amounts without any reconciliation. The General Fund budget is adopted on the budgetary basis, which is not consistent with accounting principles generally accepted in the United States of America. Commitments for material and services, such as purchase orders and contracts, are recorded during the year as encumbrances to assist in controlling expenditures. Appropriations, which are encumbered at year-end lapse, then are added to the following year's budgeted appropriations. However, encumbrances at year-end are reported as reservations of fund balance.
6. Under Article XIII B of the California Constitution (the Gann Spending Limitation Initiative), the City is restricted as to the amount of annual appropriations from the proceeds of taxes, and if proceeds of taxes exceed allowed appropriations, the excess must either be refunded to the State Controller, returned to the taxpayers through revised tax rates or revised fees schedules, or an excess in one year may be offset against a deficit in the following year. For the fiscal year ended June 30, 2012, based on the calculations by City Management, proceeds of taxes did not exceed the appropriations limit.
7. Budget 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 City Manager must approve adjustments to departmental budgets; however, management may amend the budgeted amounts within departmental expenditure classifications, with approval of the Finance Director,
8. Certain appropriations carryover and are rebudgeted for the subsequent year.
9. Budget appropriations for the various governmental funds become effective July 1. The City Council may amend the budget during the fiscal year. The legal level of budgetary control has been established at the fund level.

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

To the Honorable Mayor and Members  
of the City Council of the City of Hercules  
Hercules, California

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Hercules (City), as of and for the year ended June 30, 2012, which collectively comprise the City's basic financial statements and have issued our report thereon dated April 1, 2014. 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 City's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over financial reporting.

*A deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. *A material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the City'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 preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

To the Honorable Mayor and Members  
of the City Council of the City of Hercules  
Hercules, California

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the City's internal control or in compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in cursive script that reads "Gallina LLP".

Roseville, California  
April 1, 2014