

**COMMUNITY DEVELOPMENT AGENCY  
OF THE  
CITY OF SEBASTOPOL**

**Basic Financial Statements  
for the  
Fiscal Year Ended June 30, 2006**

**COMMUNITY DEVELOPMENT AGENCY OF THE CITY OF SEBASTOPOL**  
**Basic Financial Statements**  
**for the**  
**Fiscal Year Ended June 30, 2006**

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**Independent Auditor's Report**

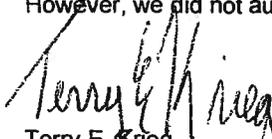
Board of Directors  
Community Development Agency of the City of Sebastopol  
Sebastopol, California

We have audited the accompanying financial statements of the governmental activities, each major fund, of the Community Development Agency of the City of Sebastopol, California, (the Agency) as of and for the year ended June 30, 2006, which collectively comprise the Agency's basic financial statements as listed in the Table of Contents. These financial statements are the responsibility of the Agency's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, of the Community Development Agency of the City of Sebastopol, California, as of June 30, 2006, and the respective changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Management Discussion and Analysis and Budgetary Comparison Information on pages 2 through 8 and page 23 through 24 are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

  
Terry E. Krieg  
Certified Public Accountant  
December 12, 2006

## **MANAGEMENT'S DISCUSSION AND ANALYSIS**

This section of the Sebastopol Community Development Agency's financial report presents our discussion and analysis of the Agency's financial performance during the fiscal year that ended on June 30, 2006.

### **FINANCIAL HIGHLIGHTS**

- The Agency's total net assets increased by about \$ 1,150,900 over the course of this year's operations.
- Incremental property tax revenues increased in fiscal year 2006 by about 8.2 percent to a total of \$1,648,100
- Investment revenues increased in 2006 by about 53.6 percent compared to 2005 as a result of the Agency having more cash invested in fiscal 2006 than in fiscal 2005 and higher rates of return.
- Operating expenses in fiscal 2006 increased a net \$210,000 or 43.8 percent more than in fiscal year 2005.

### **OVERVIEW OF THE FINANCIAL STATEMENTS**

This financial report consists of three parts – *management's discussion and analysis* (this section), the *basic financial statements and note disclosures*, and *required supplementary information*. The basic financial statements include two kinds of statements that present different views of the Agency:

- The first two statements are *government-wide financial statements* that provide both long-term and short-term information about the Agency's *overall* financial status.
- The remaining statements are *fund financial statements* that focus on individual parts of the Agency, reporting the Agency's operations in more detail than the government-wide statements.
  - The *governmental funds* statements tell how *general government* services like community development projects were financed in the *short term* as well as what remains for future spending.

The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data. The statements are followed by a section of required supplementary information that further explains and supports the information in the financial statements.

Figure A-1 summarizes the major features of the Agency's financial statements, including the portion of the Agency they cover and the types of information they contain. The remainder of this overview section of management's discussion and analysis explains the structure and contents of each of the statements.

**MANAGEMENT'S DISCUSSION AND ANALYSIS**

**Figure A-1 Major Features of the Agency's Financial Statements**

	<u>Government-Wide Statements</u>	<u>Fund Statements</u>
<u>Scope</u>	<ul style="list-style-type: none"> <li>• Entire Agency</li> </ul>	The activities of the Agency that are not proprietary or fiduciary, such as community development projects, capital outlay, and debt service
<u>Required financial statements</u>	<ul style="list-style-type: none"> <li>• Statement of net assets</li> <li>• Statement of activities</li> </ul>	<ul style="list-style-type: none"> <li>• Balance sheet</li> <li>• Statement of revenues, expenditures, and changes in fund balances</li> </ul>
<u>Accounting basis and measurement focus</u>	<ul style="list-style-type: none"> <li>• Accrual accounting and economic resources focus</li> </ul>	Modified accrual accounting and current financial resources focus
<u>Type of asset/liability information</u>	<ul style="list-style-type: none"> <li>• All assets and liabilities, both financial and capital, and short-term and long-term</li> </ul>	Only assets expected to be used up and liabilities that come due during the year or soon thereafter; no capital assets included and no long-term debt obligations included
<u>Type of inflow/outflow information</u>	<ul style="list-style-type: none"> <li>• All revenues and expenses during year, regardless of when cash is received or paid</li> </ul>	Revenues for which cash is received during or soon after the end of the year; expenditures when goods or services have been received and payment is due during the year or soon thereafter

**Government-wide Statements**

The government-wide statements report information about the Agency as a whole using accounting methods similar to those used by private-sector companies. The statement of net assets includes *all* the government's assets and liabilities. All of the current year's revenues and expenses are accounted for in the statement of activities regardless of when cash is received or paid.

The two government-wide statements report the Agency's *net assets* and how they have changed. Net assets – the difference between the Agency's assets and liabilities – is one way to measure the Agency's financial health, or *position*.

- Over time, increases or decreases in the Agency's net assets are an indicator of whether its financial health is improving or deteriorating, respectively.

The government-wide financial statements of the Agency are divided into one category:

- *Governmental activities* – All of the Agency's basic services are included here, such as administration, projects, and debt service. Incremental property taxes and loans from the City have in the past financed most of these activities.

## **MANAGEMENT'S DISCUSSION AND ANALYSIS**

### **Fund Financial Statements**

The fund financial statements provide more detailed information about the Agency's most significant funds – not the Agency as a whole. Funds are accounting devices that the Agency uses to keep track of specific sources of funding and spending for particular purposes. The funds in use are:

- The Capital Projects Fund to keep track of proceeds from the sale of the tax allocation bonds(loaned to the Agency by the City's Financing Authority) to be used for future improvement projects and operations of the Agency. This is the Agency's main capital projects fund.
- The Low and Moderate Income Housing Fund required by law to be maintained to account for the 20 percent set-aside of tax increment required to be used to provide and or improve low and moderate income housing.

The Agency has only one kind of fund type:

- *Governmental funds* – All of the Agency's basic services are included in governmental funds, which focus on (1) *how cash and other financial assets* that can readily be converted to cash flow in and out and (2) the balances left at year-end that are available for spending. Consequently, the governmental funds statements provide a detailed *short-term view* that helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the Agency's programs. Because this information does not encompass the additional long-term focus of the government-wide statements, we provide additional information at the bottom of the governmental funds statement, or on the subsequent page, that explains the relationship (or differences) between them.

### **FINANCIAL ANALYSIS OF THE AGENCY AS A WHOLE**

**Net Assets.** The Agency's *combined* net assets increased about \$1,151,000 between fiscal years 2005 and 2006. (See Table A-1.)

**TABLE A-1**

**Net Assets of the Agency**

	Governmental Activities (Rounded to Nearest Thousand)		Total Percentage Change
	2005	2006	2005-2006
Current assets	\$ 3,195,000	\$ 3,611,000	13.0%
Other assets	363,000	354,000	-2.5%
Capital assets	2,892,000	2,892,000	0.0%
<b>Total assets</b>	<b>6,450,000</b>	<b>6,857,000</b>	<b>6.3%</b>
Long-term debt outstanding	8,061,000	7,305,000	-9.4%
Other liabilities	33,000	45,000	36.9-3%
<b>Total liabilities</b>	<b>8,094,000</b>	<b>7,350,000</b>	<b>-9.2%</b>
<b>Net assets</b>			
Invested in capital assets, net	(4,877,000)	(4,413,000)	9.5%
Restricted	1,116,000	1,528,000	36.9%
Unrestricted	2,117,000	2,392,000	13.0%
<b>Total net assets</b>	<b>\$ (1,644,000)</b>	<b>\$ (493,000)</b>	<b>70.0%</b>

**MANAGEMENT'S DISCUSSION AND ANALYSIS**

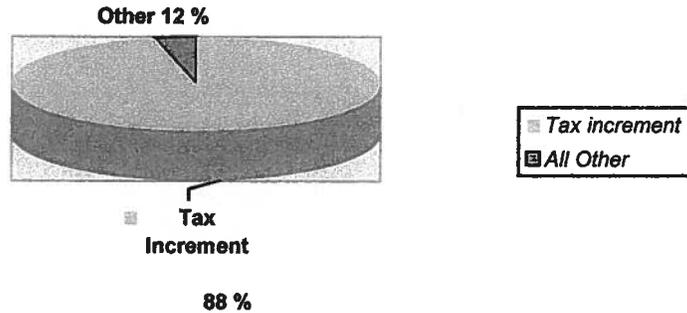
**FINANCIAL ANALYSIS OF THE AGENCY AS A WHOLE**

This increase in net assets decreased the net deficit of the Agency to about \$493,000. The Agency at year end had about \$7.3 million in long-term debt obligations outstanding. During the 2006 year the \$262,000 loan made by the City of Sebastopol to help finance Agency operations was repaid in full by the Agency. At year end, the Agency had about \$ 3.65 million in cash and investments available for agency activities including required debt service reserves.

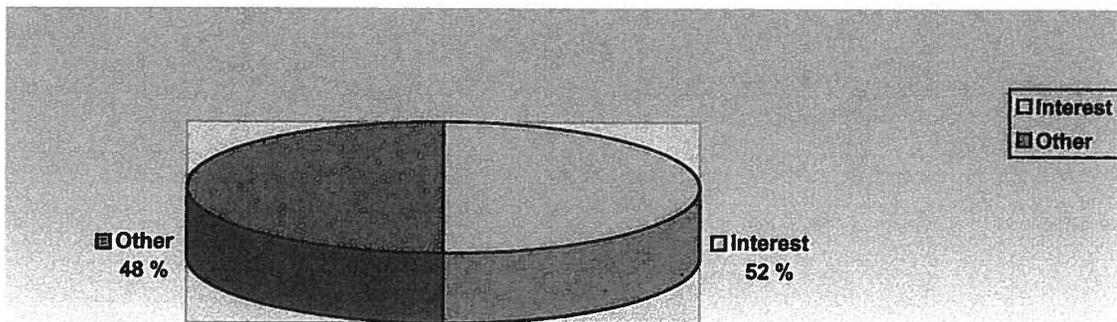
**Changes in net assets.** The Agency's total program and general revenues in 2006 increased by about \$266,900 to about \$1.88 million. (See Table A-2.) About 88 percent of the Agency's revenue comes from incremental property taxes; the remaining 12 percent comes from investment earnings and other revenues.

The total cost of all programs and services increased by about \$250,000 or about 52.1 percent.

**Agency Governmental-Type Activity Revenues  
Fiscal Year 2006**



**Agency Governmental-Type Activity Expenses - Fiscal Year 2006**



About 52 percent of the Agency's expenses are for interest on borrowed funds and about 48 percent for housing activities and other projects.

Total expenses increased by about \$250,000 or about 52.1 percent more than was spent on housing and projects in 2005.

**MANAGEMENT'S DISCUSSION AND ANALYSIS**

**FINANCIAL ANALYSIS OF THE AGENCY AS A WHOLE**

TABLE A-2  
Agency Revenues and Expenses

	Governmental Activities (rounded to nearest Thousand)		Percentage Change 2005-2006
	2005	2006	
<b>Revenues</b>			
<b>Program revenues</b>			
Charges for services	\$ 14,000	\$ 27,000	92.9%
Contributions	-	88,000	100.0%
<b>General revenues:</b>			
Property taxes	1,523,000	1,648,000	8.2%
Interest	77,000	118,000	53.2%
<b>Total revenues</b>	<b>1,614,000</b>	<b>1,881,000</b>	<b>16.5%</b>
<b>Expenses</b>			
Housing	20,000	113,000	465.0%
Projects	79,000	260,000	229.1%
Interest	381,000	357,000	-6.2%
<b>Total expenses</b>	<b>480,000</b>	<b>730,000</b>	<b>52.1%</b>
Excess (deficiency)	1,134,000	1,151,000	1.5%
Transfers	-	-	-
<b>Increase (decrease) in net assets</b>	<b>\$ 1,134,000</b>	<b>\$ 1,151,900</b>	<b>1.5%</b>

Interest expense decreased 6.2 percent primarily because of the normal reductions in outstanding principal balances.

Project expenses increased by about \$181,000 as a result of the Northwest Area Alternative Plan Study. Housing costs increased about \$93,000 resulting from costs associated with maintaining the land parcels purchased for the development of affordable housing.

## **MANAGEMENT'S DISCUSSION AND ANALYSIS**

### **FINANCIAL ANALYSIS OF THE AGENCY'S FUNDS**

As the Agency completed the year, its governmental funds reported a *combined* fund balance of about \$ 3.59 million, about a \$402,000 increase from 2005. Of that increase, almost all was the result of the Agency spending less resources than revenues in fiscal 2006.

The combined ending \$ 3.59 million fund balance consisted of:

- About \$ 4.3 million in the Capital Projects Fund to be used for future projects and activities, Of this \$4.3 million, \$1.4 million is not available as it is reserved for the cash advance made to the Low and Moderate Income Housing Fund to acquire land.
- The \$ 678,000 deficit in the Low and Moderate Income Housing Fund exists because of the land purchase in fiscal 2004 and the borrowing of money from the Agency's capital projects fund.

The net changes in fund balances for the 2006 fiscal year were:

- About a \$46,300 increase in the Capital Projects Fund
- About a \$356,000 increase in the Low and Moderate Income Housing Fund as a result of the less spending on capital assets in fiscal year 2006

### **Low and Moderate Income Housing Special Revenue Fund Budgetary Highlights**

Over the course of a year, the Agency may have a need to revise its adopted budget. When budget amendments are made, the amendments would fall into two categories:

- Changes made at the midyear budget review for unanticipated revenues and costs.
- Increases in appropriations to prevent budget overruns.

During the 2006 fiscal year, the Agency's budget for the low moderate income housing was amended. Actual expenditures in the Low and Moderate Income Housing Fund were \$620,725 less than final budget amounts. This positive spending variance from budget existed primarily because less was spent on housing projects than was originally believed to be necessary.

### **CAPITAL ASSET AND DEBT ADMINISTRATION**

#### **Capital Assets**

The Agency at year end had \$ 2.9 million invested in capital assets which consisted principally of land parcels acquired for the future development of affordable housing. During the 2004 year, the Agency acquired several parcels for about \$2.9 million to be used to develop affordable housing for first-time home buyers.

#### **Long-term Debt**

The long-term debt obligations of the Agency were about \$7.31 million at the end of 2006, and consisted primarily of the \$4,845,000 of tax allocation bonds and \$2,460,038 of the refunding capital lease arrangement. All debt service payments were made as required and debt service reserve requirements were maintained by the Agency. Additional information about the Agency's long-term obligations can be found in the notes to the basic financial statements on page 20

## **MANAGEMENT'S DISCUSSION AND ANALYSIS**

### **ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES**

For the 2007 fiscal year, the Agency in its budget for 2007 has:

- Anticipated that the Agency will receive about \$1.9 million in tax increment revenues in 2007 which is about a 19 percent increase over 2006 fiscal year
- Expected that operating expenditures will be about the same level as in 2006 with no additional capital asset purchases planned

### **CONTACTING THE AGENCY'S FINANCIAL MANAGEMENT**

This financial report is designed to provide our citizens, taxpayers, customers, and investors and creditors with a general overview of the Agency's finances and to demonstrate the Agency's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Finance Director, City of Sebastopol, 7120 Bodega Avenue, Sebastopol, California 95473.

**COMMUNITY DEVELOPMENT AGENCY OF THE CITY OF SEBASTOPOL**  
**Statement of Net Assets**  
**Governmental Activities**

<b>ASSETS</b>	<b>June 30</b>	
	<b>2006</b>	<b>2005</b>
Cash and investments	\$ 3,610,613	\$ 3,194,452
Interest receivable	718	718
<b>Total current assets</b>	<b>3,611,331</b>	<b>3,195,170</b>
<b>Noncurrent assets:</b>		
Loans	324,031	270,391
Loan to City of Sebastopol	-	62,728
Debt issue costs	30,078	30,078
Capital assets not being depreciated	2,891,696	2,891,696
<b>Total noncurrent assets</b>	<b>3,245,805</b>	<b>3,254,893</b>
<b>Total assets</b>	<b>\$ 6,857,136</b>	<b>\$ 6,450,063</b>
<b>LIABILITIES</b>		
<b>Current liabilities</b>		
Accounts payable	\$ 16,603	\$ 275
Deposits	-	2,500
Interest payable	28,546	30,542
Tax allocation bonds and capital leases due in one year	515,600	493,400
<b>Total current liabilities</b>	<b>560,749</b>	<b>526,717</b>
<b>Noncurrent liabilities due in more than one year</b>		
Tax allocation bonds	4,640,000	4,845,000
Capital Lease-Refunding	2,149,438	2,460,140
Loan payable to City of Sebastopol	-	262,182
<b>Total noncurrent liabilities</b>	<b>6,789,438</b>	<b>7,567,322</b>
<b>Total liabilities</b>	<b>7,350,187</b>	<b>8,094,039</b>
<b>NET ASSETS</b>		
Invested in capital assets, net of related debt	(4,413,264)	(4,876,766)
Restricted for:		
Debt service	516,326	515,631
Housing projects	1,012,171	600,662
Unrestricted	2,391,716	2,116,497
<b>Total net assets</b>	<b>\$ (493,051)</b>	<b>\$ (1,643,976)</b>

See accompanying notes to the basic financial statements



**Community Development Agency of The City of Sebastopol  
Balance Sheet  
Governmental Funds  
June 30, 2006**

	<b>Capital Project Fund</b>	<b>Low and Moderate Income Housing Fund</b>	<b>Total Governmental Funds</b>
<b>ASSETS</b>			
Cash and investments	\$ 2,862,555	\$ 748,058	\$ 3,610,613
Receivables:			
Interest	718	-	718
Notes	50,190	273,841	324,031
Internal balances	1,416,827	-	1,416,827
<b>Total assets</b>	<b>\$ 4,330,290</b>	<b>\$ 1,021,899</b>	<b>\$ 5,352,189</b>
<b>LIABILITIES AND FUND BALANCES</b>			
Liabilities:			
Accounts payable	\$ 6,875	\$ 9,728	\$ 16,603
Internal balances	-	1,416,827	1,416,827
Deferred revenue	50,190	273,841	324,031
<b>Total liabilities</b>	<b>57,065</b>	<b>1,700,396</b>	<b>1,757,461</b>
Fund balances:			
Reserved for internal balances	1,416,827	-	1,416,827
Reserved for debt service	489,513	26,813	516,326
Unreserved, undesignated	2,366,885	(705,310)	1,661,575
<b>Total fund balances</b>	<b>4,273,225</b>	<b>(678,497)</b>	<b>3,594,728</b>
<b>Total liabilities and fund balances</b>	<b>\$ 4,330,290</b>	<b>\$ 1,021,899</b>	<b>\$ 5,352,189</b>
Total Governmental Fund Balances			3,594,728
Amounts reported for governmental activities in the statement of net assets are different because:			
Capital assets are not financial resources for governmental activities and therefore are not reported in the funds			2,891,696
Long-term notes are not available to pay obligations of the current period and therefore are deferred in the funds			324,031
Interest payable is not due and payable in the current period and is therefore not reported in the funds			(28,546)
Debt issue costs are capitalized in the statement of net assets, but are reported as an outflow of resources in the funds			30,078
Long-term debt obligations due to third parties are not due and payable in the current period and therefore are not reported in the funds.			(7,305,038)
Net Assets of Governmental Activities			<u>\$ (493,051)</u>

See accompanying notes to the basic financial statements

**Community Development Agency of The City of Sebastopol  
Statements of Revenues, Expenditures, and  
Changes in Fund Balances  
Governmental Funds  
For the Fiscal Year Ended June 30, 2006**

	<b>Capital Project Fund</b>	<b>Low and Moderate Income Housing Fund</b>	<b>Total Governmental Funds</b>
<b>REVENUES</b>			
Property taxes, incremental	\$ 1,228,261	\$ 419,872	\$ 1,648,133
Interest and rents	89,936	28,321	\$ 118,257
Miscellaneous	1,825	121,762	123,587
<b>Total revenues</b>	<b>1,320,022</b>	<b>569,955</b>	<b>1,889,977</b>
<b>EXPENDITURES</b>			
Current:			
Community development:			
Housing projects	260,154	112,673	372,827
Debt service:			
Principal	667,495	88,189	755,684
Interest	346,085	13,048	359,133
<b>Total expenditures</b>	<b>1,273,734</b>	<b>213,910</b>	<b>1,487,644</b>
<b>Net change in fund balances</b>	<b>46,288</b>	<b>356,045</b>	<b>402,333</b>
<b>Fund balances, July 1</b>	<b>4,226,937</b>	<b>(1,034,542)</b>	<b>3,192,395</b>
<b>Fund balances, June 30</b>	<b>\$ 4,273,225</b>	<b>\$ (678,497)</b>	<b>\$ 3,594,728</b>

See accompanying notes to the basic financial statements

**COMMUNITY DEVELOPMENT AGENCY OF THE CITY OF SEBASTOPOL**  
**Reconciliation of the Statement of Revenues,**  
**Expenditures and Changes in Fund Balances of**  
**Governmental Funds to the Statement of Activities**  
**For the Fiscal Year Ended June 30, 2006**

Net Change in Fund Balances - Total Governmental Funds	<u>\$ 402,333</u>
Amounts reported for governmental activities in the statement of activities are different because:	
Increases in deferred revenue from long-term receivables are not reported as revenues in the funds, but are reported as revenues in the statement of activities	53,640
Collections on long-term loans to the City increase revenues in the fund statements but are not revenues in the statement of activities	(62,728)
Interest on long-term debt is recorded as an expense in the statement of activities but does not require the use of current financial resources and are not recorded as expenditures in the funds until paid	1,996
Repayment of long-term debt principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net assets	<u>755,684</u>
Net adjustment to reconcile to changes in net assets	<u>748,592</u>
Change in Net Assets of Governmental Activities	<u>\$ 1,150,925</u>

See accompanying notes to the basic financial statements

**COMMUNITY DEVELOPMENT AGENCY OF THE CITY OF SEBASTOPOL**  
**Notes to the Basic Financial Statements**  
**June 30, 2006**

**1. Summary of Significant Accounting Policies**

**A. Reporting Entity**

*Component unit.* The Sebastopol Community Development Agency is a separate entity created for the purpose of revitalizing and improving the condition of the City through the removal of blight, construction of public improvements, and stimulation of business. The Agency is governed by members of the City Council, and it is reported as if it were part of the primary government because the City Council has ultimate control of the Agency. The Agency's activities are accounted for as part of the City's special revenue fund types within the governmental activities section of the City's financial report. These separate financial statements present financial data for only the Community Development Agency.

**B. Government-wide and Fund Financial Statements**

The government-wide financial statements (i.e., the statement of net assets and the statement of changes in net assets) report information on all of the nonfiduciary activities of the Agency. For the most part, the effect of interfund activity has been removed from these statements. *Governmental activities*, which normally are supported by taxes and intergovernmental revenues, are reported separately from *business-type activities*, which rely to a significant extent on fees and charges for support. The Agency has no business-type activities.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. *Direct expenses* are those that are clearly identifiable with a specific function or segment. *Program revenues* include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as *general revenues*.

Separate financial statements are provided for governmental funds. Major individual governmental funds are reported as separate columns in the fund financial statements.

**C. Measurement Focus, Basis of Accounting, and Financial Statement Presentation**

The government-wide financial statements are reported using the *economic resources measurement focus* and the *accrual basis of accounting*. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be *available* when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenues to be available if they are collected within 60 days of the end of the current fiscal period.

**COMMUNITY DEVELOPMENT AGENCY OF THE CITY OF SEBASTOPOL**  
**Notes to the Basic Financial Statements**  
**June 30, 2006**

**Note 1 Summary of Significant Accounting Policies (Continued)**

**C. Measurement Focus, Basis of Accounting, and Financial Statement Presentation (Continued)**

Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due. Property taxes and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when cash is received by the government.

The Agency reports the following major governmental funds:

The *Capital Projects Fund* is the agency's project operating fund. It is used to account for financial resources and proceeds of long-term debt to be used for major agency projects.

The *Low and Moderate Income Housing special revenue fund* accounts for the resources accumulated to provide low and moderate income housing as well as to account for the 20 percent of tax increment set-aside required by law to be deposited into this fund.

As a general rule the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are loans from or to the City of Sebastopol. Elimination of these loans would distort the statement of net assets and the Agency's assets or obligations.

Amounts reported as *program revenues* include 1) charges to customers or applicants for goods, services, or privileges provided, 2) operating grants and contributions, and 3) capital grants and contributions. Internally dedicated resources are reported as *general revenues* rather than as program revenues. Likewise, general revenues include all taxes.

**D. Asset, Liabilities, and Net Assets or Equity**

**1. Deposits and Investments**

State statutes authorize the Agency to invest in obligations of the U.S. Treasury, commercial paper, corporate bonds, repurchase agreements, the State Treasurer's Investment Pool, and other permitted investments. The Agency has followed a policy of investing its idle cash primarily only with the City of Sebastopol in the City's pooled investments in the Sonoma County Investment Pool and an investment agreement and money market funds held by a trustee bank.

Investments for the Agency are reported at fair value. The Sonoma County Treasurer's Investment Pool operates in accordance with appropriate state laws and regulations. The reported value of the pool is the same as the fair value of the pool shares. The investment agreement is carried at cost because it is a fixed rate agreement not subject to market conditions.

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds."

**COMMUNITY DEVELOPMENT AGENCY OF THE CITY OF SEBASTOPOL**  
**Notes to the Basic Financial Statements**  
**June 30, 2006**

**Note 1. Summary of Significant Accounting Policies (Continued)**

**D. Assets, Liabilities, and Net Assets or Equity(Continued)**

**2. Receivables and Payables (Continued)**

Advances between Agency funds, if any, are reported in the fund financial statements and are offset by a fund balance reserve account in applicable government funds to indicate that they are not available for appropriation and are not expendable available financial resources.

All trade and property tax receivables are not shown net of an allowance for uncollectibles.

Property taxes are levied as of March 1 on property values assessed as of the same date. State statutes provide that the property tax rate be limited generally to one percent of market value, be levied by only the County, and be shared by applicable jurisdictions. The County collects the taxes and distributes them to taxing jurisdictions on the basis of assessed valuations subject to voter-approved debt. Property taxes are due on November 1 and March 1, and become delinquent on December 10 and April 10. The Agency receives property taxes pursuant to an arrangement with the County known as the "Teeter Plan". Under the plan, the County assumes responsibility for the collection of delinquent taxes and pays the full allocation to the Agency. The Agency recognizes property tax revenues in the fiscal year in which they are due to the Agency.

**3. Inventories and Prepaid Items**

All inventories are valued at cost using the first-in/first-out (FIFO) method. Inventories of governmental funds are recorded as expenditures when purchased. Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both government-wide and fund financial statements.

**4. Capital Assets**

Capital assets, which include property, plant, equipment, and infrastructure assets (e.g., roads, bridges, sidewalks, and similar items), are reported in the applicable governmental -type activities columns in the government-wide financial statements. Capital assets are defined by the government as assets with an initial, individual cost of more than \$ 3,000 and an estimated useful life in excess of one year. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

Under the GASB 34 Implementation Rules, the Agency was not required to record infrastructure assets existing or acquired prior to July 1, 2003; and the Agency has not recorded such assets. The Agency may elect to record such infrastructure assets in the future.

**5. Compensated Absences**

The Agency has no employees to accumulate earned but unused vacation and sick pay benefits. The obligation for these liabilities is recorded in the government-wide financial statements when the liability is incurred; and they are recorded in the fund financial statements only when payment is due such as for employee terminations.

**6. Long-term Obligations**

In the government-wide financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities type statement of net assets.

**COMMUNITY DEVELOPMENT AGENCY OF THE CITY OF SEBASTOPOL**  
**Notes to the Basic Financial Statements**  
**June 30, 2006**

**Note 1 Summary of Significant Accounting Policies (Continued)**

**D. Assets, Liabilities, and Net Assets or Equity (Continued)**

**7. Fund Equity**

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

**2. Reconciliation of Government-Wide and Fund Financial Statements**

**A. Explanation of Certain Differences Between the Governmental Fund Balance Sheet and the Government-Wide Statement of Net Assets**

The governmental fund balance sheet includes a reconciliation between fund balance – total governmental funds and net assets – governmental activities as reported in the government-wide statements of net assets. One element of that reconciliation explains that "long-term liabilities" are not due and payable in the current period and are therefore not reported in the funds. The details of this \$ 7,305,038 difference are as follows:

Long-Term Debt Obligations:

Refunding capital lease	\$ 2,460,038
Tax allocation refunding bonds	<u>4,845,000</u>

Net adjustment to decrease fund balance total governmental Funds to arrive at net assets - governmental activities	<u>\$ (7,305,038)</u>
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**B. Explanation of Certain Differences Between the Governmental Fund Statement of Revenues, Expenditures, and Changes in Fund Balances and the Government-wide Statement of Activities**

The governmental fund statement of revenues, expenditures, and changes in fund balances includes a reconciliation between *net changes in fund balances – total governmental funds and changes in net assets of governmental activities* as reported in the government-wide statement of activities. One element of that reconciliation explains that proceeds of long-term debt provide current financial resources to governmental funds, but issuing debt increases long-term liabilities in the statement of net assets. The details of this \$ 748,592 difference are as follows:

Repayments of long-term debt recorded as expenditures in the funds	\$ 755,684
Decrease in accrued interest payable	1,996
Other items	<u>(9,088)</u>

Net adjustment to increase <i>net changes in fund balances – total governmental funds</i> to arrive at <i>changes in net assets of governmental activities</i>	<u>\$ 748,592</u>
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**COMMUNITY DEVELOPMENT AGENCY OF THE CITY OF SEBASTOPOL**  
**Notes to the Basic Financial Statements**  
**June 30, 2006**

**3. Stewardship, Compliance, and Accountability**

**A. Budgetary Information**

Annual budgets are adopted on a basis of consistent with generally accepted accounting principles for all governmental funds. All annual appropriations lapse at fiscal year end. On or before the end of each fiscal year, all agencies of the City submit requests for appropriations to the City Manager so that a budget may be prepared. The proposed budget is presented to the Council for review. The Council holds public hearings and a final budget is approved by the Council. The appropriated budget is prepared by fund, function, and department. Transfers of appropriations between departments require the approval of the City Manager. The legal level of budgetary control (i.e., the level at which expenditures may not legally exceed appropriations) is the fund level. The Council made several supplemental budgetary appropriations throughout the year. The supplemental budgetary appropriations made were not material. Encumbrance accounting is not employed in governmental funds.

**4. Detailed Notes on All Funds**

**A. Deposits and Investments**

Cash and investments consisted of the following at June 30, 2006:

Demand deposits	\$ 121,087
Pooled investments held by the City of Sebastopol	2,973,200
Available demand deposits and investments	3,094,287
Investments held by bank trustee:	
Investment agreement	481,513
Money market funds	34,813
Total cash and investments	<u>\$3,610,613</u>

*Custodial credit risk*-Deposits. Custodial credit risk is the risk that in the event of a bank failure, the Agency's deposits may not be returned to it. The Agency's policy for deposits is that they will be made only in institutions in California and they shall be insured or collateralized with securities. At June 30, 2005, all of the Agency's bank balances of \$117,605 were covered by Federal Depository Insurance, and none was exposed to credit risk. Investments at June 30, 2005 consisted of the following:

Investment	Maturity	Fair Value
Pooled investments with the City of Sebastopol-Sonoma County Treasurers Pool	Average 344 days	\$2,973,200
Investment agreement-Morgan Guaranty Bank	November 25, 2021	481,513
Money market funds-Wells Fargo Treasury	Average 200 days	34,813
Totals		<u>\$3,489,526</u>

*Interest rate risk*- As a means of limiting its exposure to fair value losses arising from interest rates, the Agency limits its investments to maturities prescribed in the California Government Code. The Investment agreement is held by a bond trustee and is a fixed rate 6.15% agreement.

*Credit Risk* - State law limits investments in various securities to certain level of risk ratings issued by nationally recognized statistical rating organizations. The County Investment Pool and the Investment Agreement are unrated. The money market is rated AAA.

*Custodial Credit Risk*- For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Agency would not be able to recover the value of its investments or collateral securities that are in possession of an outside party. The County Pool is not subject to custodial credit risk as it is not evidenced by specific securities. The Investment Agreement is held by the counterparty in the name of the Agency.

**COMMUNITY DEVELOPMENT AGENCY OF THE CITY OF SEBASTOPOL**  
**Notes to the Basic Financial Statements**  
**June 30, 2006**

**4. Detail Notes on All Funds(Continued)**

**B. Receivables**

The Agency's receivables at year end consisted of:

Interest	718
Housing rehabilitation loans	<u>324,031</u>
Totals	<u>\$ 324,749</u>

The housing rehabilitation loans bears interest at 3 to 6 percent with some loans deferred with no interest. Repayable loans are to be repaid in monthly installments of principal and interest taken together over terms of 15 to 30 years.

**C. Interfund Receivables, Payables, and Transfers**

Internal balances(receivables and payables) at June 30, 2006 were as follows:

Receivable Fund	Payable Fund	Amounts
Capital project	Low Moderate Income Housing	<u>\$ 1,416,827</u>
		<u>\$ 1,416,827</u>

The internal receivable in the capital project fund was made to provide financing to the Low and Moderate Income Housing Fund for the purpose of purchasing two sites for the development of affordable housing. The advance is repayable from future tax increment revenues to be deposited into the housing fund(the 20 percent set-aside amount).

**D. Capital Assets**

Capital asset activity for the year ended June 30, 2006 was as follows:

**Governmental Activities:**

Capital assets not being depreciated:	Beginning Year	Increases	Decreases	End of Year
Land	\$2,891,696	\$ -	\$ -	\$2,891,696
Total capital assets	\$2,891,696	\$ -	\$ -	\$2,891,696

**COMMUNITY DEVELOPMENT AGENCY OF THE CITY OF SEBASTOPOL**  
**Notes to the Basic Financial Statements**  
**June 30, 2006**

**4. Detail Notes on All Funds(Continued)**

**E. Long-Term Debt**

*Changes in Long-term liabilities*

Long-term debt activity for the 2006 fiscal year was as follows:

<b>Governmental Activities:</b>	<u>Beginning</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending</u>	<u>Due In One Year</u>
Loan from the City of Sebastopol	\$ 262,182	\$ -	\$ 262,182	\$ -	\$ -
Capital lease refunding	2,758,540	-	298,502	2,460,038	310,600
Tax allocation bonds	5,040,000	-	195,000	4,845,000	205,000
<b>Totals</b>	<u>\$8,060,722</u>	<u>\$ -</u>	<u>\$ 755,684</u>	<u>\$ 7,305,038</u>	<u>\$ 515,600</u>

*Loan From City of Sebastopol*

The loan was made in an original amount \$262,182 to provide funds for community development projects. The loan is repayable to the extent tax increment revenues are available and bears interest at 10 per cent per annum. The entire loan was repaid in fiscal year 2005-2006.

*Capital Lease-Refunding*

In March 2004, the City and it's agency entered into a capital lease arrangement with West America Bank in an original amount of \$3,217,000 in order to obtain financing to advance refund and defease the Agency's \$3,485,000 1994 Certificates of Participation. The lease bears interest at 4.05 percent and is payable in semiannual installments of about \$203,500 each June 1 and December 1 through June 1, 2013. The Agency entered into the lease arrangement to advance refund the outstanding All 1994 certificates have been retired. Future minimum lease payments are:

<u>Fiscal Year</u>	<u>Total</u>
2007	\$ 407,125
2008	407,119
2009	407,191
2010	407,121
2011	407,191
2012-2013	814,312
<b>Total minimum lease payments</b>	<b>2,850,059</b>
<b>Amounts representing interest</b>	<b>(390,021)</b>
<b>Present value of net minimum lease payments</b>	<b>\$ 2,460,038</b>

**COMMUNITY DEVELOPMENT AGENCY OF THE CITY OF SEBASTOPOL**  
**Notes to the Basic Financial Statements**  
**June 30, 2006**

**4. Detail Notes on All Funds(Continued)**

**E. Long-Term Debt**

*Tax Allocation Refunding Bonds 1997 Series*

On September 16, 1997, the Agency issued \$6,300,000 in subordinate tax allocation bonds to advance refund and retire the Agency's 1986 and 1991 bond issues. The tax allocation bonds consisted of \$3,195,000 in serial bonds bearing interest at rates from 3.5 percent to 5.2 percent and \$3,105,000 in term bonds. The term bonds are subject to mandatory sinking fund early redemption commencing October 1, 2013. The bonds are secured by a pledge of the Agency's tax increment revenues. Future debt service is:

<u>Fiscal Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Totals</u>
2007	\$ 205,000	\$ 241,651	\$ 446,651
2008	215,000	232,199	447,199
2009	225,000	222,019	447,019
2010	235,000	211,092	446,092
2011	275,000	198,715	473,715
2012-2016	1,585,000	767,633	2,352,633
2017-2021	2,055,000	279,300	2,334,200
2022	50,000	1,313	51,313
<b>Totals</b>	<b>\$ 4,845,000</b>	<b>\$ 2,153,922</b>	<b>\$ 6,998,922</b>

**5. Other Information**

**A. Risk Management**

The Agency is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; and natural disasters for which the City carries insurance.

The City is a member of the Redwood Empire Municipal Insurance Fund, a joint powers authority, which provides joint protection programs for public entities covering automobile, general liability, errors and omission losses, property and workers compensation claims. Under the program, the City has a \$ 5,000 general liability retention limit similar to a deductible. The risk of loss is transferred to the Fund. The Fund is responsible for losses above that amount up to \$500,000 for liability losses, \$300,000 for workers compensation claims, and \$25,000 for property claims. The Fund carries purchased excess commercial liability coverage of \$9.5 million in excess of its \$500,000 retention limit, \$5 million in excess of the \$25,000 limit for property with an additional \$200 million in excess coverage. The Agency paid no material uninsured losses during the 2005-2006 fiscal year. There has been no significant changes in insurance coverages in fiscal 2006. Settlements have not exceeded coverage for each of the past three fiscal years.

Liabilities of the Agency are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. Liabilities include an amount for claims that have been incurred but not reported (IBNRs). The result of the process to estimate the claims liability is not an exact amount as it depends on many complex factors, such as inflation, changes in legal doctrines, and damage awards. Accordingly, claims are reevaluated periodically to consider the effects of inflation, recent claim settlement trends (including frequency and amount of pay-outs), and other economic and social factors. The Agency had no material claim liabilities not covered by insurance at June 30, 2005 or June 30, 2006.

**COMMUNITY DEVELOPMENT AGENCY OF THE CITY OF SEBASTOPOL**  
**Notes to the Basic Financial Statements**  
**June 30, 2006**

**Note 5 Other Information(Continued)**

**B. Contingencies and Commitments**

*Litigation.* The Agency and City are involved in litigation incurred in the normal course of conducting City business. City management believes that, based upon consultation with its counsel, these cases, in the aggregate, are not expected to result in a material adverse financial impact on the City or Agency

**C. Restricted Net Assets**

The \$516,326 restricted for debt service in the statement of net assets represents the net amount available in the debt service fund for future debt service. The \$1,012,171 restricted for housing projects represents low and moderate income housing funds which by law can only be used for related housing projects and activities.

**REQUIRED SUPPLEMENTAL INFORMATION**

**Required Supplementary Information**  
**COMMUNITY DEVELOPMENT AGENCY OF THE CITY OF SEBASTOPOL**  
**Budgetary Comparison Schedule - Low and Moderate Income Housing Special Revenue Fund**  
**For the Fiscal Year Ended June 30, 2006**

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget Positive (Negative)</u>
	<u>Original</u>	<u>Final</u>		
<b>Fund Balance, July 1</b>	\$(1,034,542)	\$(1,034,542)	\$(1,034,542)	\$ -
Resources (inflows):				
Incremental property taxes	351,645	351,645	419,872	68,227
Interest	1,000	1,000	28,321	27,321
Miscellaneous	18,000	18,000	121,762	103,762
	<u>(663,897)</u>	<u>(663,897)</u>	<u>(464,587)</u>	<u>199,310</u>
Amounts available for charges to appropriations				
<b>Charges to appropriations:</b>				
<b>Community Development:</b>				
Housing projects	832,500	811,200	112,673	698,527
Debt service:				
Principal	10,160	10,160	88,189	(78,029)
Interest	13,275	13,275	13,048	227
	<u>855,935</u>	<u>834,635</u>	<u>213,910</u>	<u>620,725</u>
Total charges to appropriations				
Fund Balance, June 30	<u><u>\$(1,519,832)</u></u>	<u><u>\$(1,498,532)</u></u>	<u><u>\$ (678,497)</u></u>	<u><u>\$ 820,035</u></u>

**Required Supplementary Information**  
**COMMUNITY DEVELOPMENT AGENCY OF THE CITY OF SEBASTOPOL**  
**Budgetary Comparison Schedule - Low and Moderate Income Housing Fund Special Revenue Fund**  
**Note to RSI**  
**For the Fiscal Year Ended June 30, 2006**

**Note A. Explanation of Difference Between Budgetary Inflows and Outflows and GAAP Revenues and Expenditures:**

**Sources/inflows resources:**

Actual amounts "available for appropriation" from budgetary comparison schedule:	\$ (464,587)
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Differences - budget to GAAP:

The fund balance at the beginning of the year is a budgetary resource but is not a current year revenue for financial reporting purposes	1,034,542
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Total revenues as reported in the statement of revenues, expenditures and changes in fund balances - governmental funds	<hr style="border: 0.5px solid black;"/> <u>\$ 569,955</u>
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Board of Directors  
Community Development Agency of the City of Sebastopol  
Sebastopol, California

*Report On Compliance and On Internal Control Over Financial Reporting  
Based On an Audit of Financial Statements Performed In Accordance  
With Auditing Standards Generally Accepted in the United States of America*

I have audited the component unit financial statements of the Community Development Agency of the City of Sebastopol as of and for the year ended June 30, 2006, and have issued my report thereon dated December 12, 2006. I conducted my audit in accordance with auditing standards generally accepted in the United States of America.

Compliance

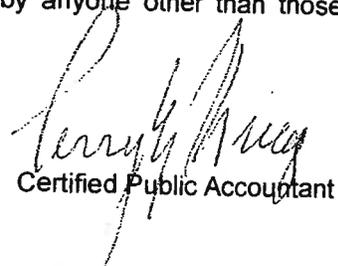
As part of obtaining reasonable assurance about whether the component unit financial statements of the Community Development Agency of the City of Sebastopol are free of material misstatement, I performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. Such provisions include those provisions of laws and regulations identified in the *Guidelines for Compliance Audits of California Redevelopment Agencies*, issued by the State Controller. However, providing an opinion on compliance with those provisions was not an objective of my audit and, accordingly, I do not express such an opinion. The results of my tests disclosed no instances of noncompliance that are required to be reported under *auditing standards generally accepted in the United States of America*.

Internal Control Over Financial Reporting

In planning and performing my audit, I considered the Community Development Agency of the City of Sebastopol's internal control over financial reporting in order to determine my auditing procedures for the purpose of expressing my opinion on the financial statements and not to provide assurance on the internal control over financial reporting. My consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. I noted no matters involving the internal control over financial reporting and its operation that I consider to be material weaknesses.

This report is intended for the information of the Board of Directors, management, and the State Controller, and it is not intended to be and should not be used by anyone other than those specified parties.

December 12, 2006

  
Certified Public Accountant