

# City of Merced

Merced, California

*Single Audit Report*

*For the year ended June 30, 2012*

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**CITY OF MERCED**  
**Single Audit Report**  
**For the year ended June 30, 2012**

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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 City Council  
of the City of Merced  
Merced, 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 Merced (City), as of and for the year ended June 30, 2012, which collectively comprise the City's financial statements and have issued our report thereon dated February 6, 2013. 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 first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the 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 City Council  
of the City of Merced  
Merced, California

This report is intended solely for the information and use of management, the City Council, and federal awarding agencies and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

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

Roseville, California  
February 6, 2013



**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH  
REQUIREMENTS THAT COULD HAVE A DIRECT AND MATERIAL EFFECT  
ON EACH MAJOR PROGRAM AND INTERNAL CONTROL OVER  
COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133**

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

Compliance

We have audited the compliance of the City of Merced (City), with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the City's major federal programs for the year ended June 30, 2012. The City's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the City's management. Our responsibility is to express an opinion on the City's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the City's compliance with those requirements.

In our opinion, the City complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2012.

Internal Control Over Compliance

The management of the City is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the City's internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over compliance.

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

*A deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

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

#### Schedule of Expenditures of Federal Awards

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 Merced as of and for the year ended June 30, 2012, and have issued our report thereon dated February 6, 2013 which contained unqualified opinions on those financial statements. Our audit was performed for the purpose of forming opinions on the financial statements as a whole. The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

This report is intended solely for the information and use of management, the City Council, others within the City, and federal awarding agencies and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.



Roseville, California  
February 28, 2013, except for the Schedule  
of Expenditures of Federal Awards as to  
which the date is February 6, 2013



**CITY OF MERCED**  
**Schedule of Expenditures of Federal Awards**  
**For the Year Ended June 30, 2012**

Federal Grantor/Pass-Through Grantor/Program Title	Federal CFDA Number	Agency or Pass-Through Grantor's Number	Expenditures
<b>U.S. Department of Housing and Urban Development</b>			
<i>Direct Programs:</i>			
CDBG - Entitlement Grants Cluster			
- Community Development Block Grant (CDBG)	14.218	B-10-MC-06-0044	\$ 512,432
- Community Development Block Grant (CDBG)	14.218	B-11-MC-06-0044	942,837
Subtotal			<u>1,455,269</u>
CDBG - State's Program and Non-Entitlement Grants in Hawaii			
- Neighborhood Stabilization Program	14.228	B-11-MN-06-0012	591,895
- Neighborhood Stabilization Program	14.228	10-NSPR-6571	1,300,000
Subtotal			<u>1,891,895</u>
<i>Passed through California Department of Housing and Community Development:</i>			
HOME Investment Partnership Program			
- HOME Investment Partnership Act	14.239	M08-MC060227	176,597
- HOME Investment Partnership Act	14.239	M-09-MC-060227	276,673
- HOME Investment Partnership Act	14.239	M-10-MC-060227	10,528
- HOME Investment Partnership Act	14.239	M11-MC060227	32,331
Subtotal			<u>496,129</u>
- HUD Economic Development Investment	14.251	B-09-SP-CA-0149	237,500
- Sustainable Communities Regional Planning Grant Program	14.703	SC360080-11-06	2,984
<b>Total U.S. Department of Housing and Urban Development</b>			<u>4,083,777</u>
<b>U.S. Department of Justice</b>			
<i>Direct Programs:</i>			
- ARRA - COPS Hiring Recovery Program (CHRP)	16.710	2009RKWX0128	606,036
- Justice Assistance Grant	16.738	2009-DJ-BX-0878	20,101
- Justice Assistance Grant	16.738	2011-DJ-BX-2459	18,694
- Justice Assistance Grant	16.738	2012-DJ-BX-1100	401
Subtotal			<u>39,196</u>
- ARRA - Justice Assistance Grant	16.804	2009-SB-B9-2673	41,335
<b>Total U.S. Department of Justice</b>			<u>686,567</u>
<b>U.S. Department of Transportation</b>			
Federal Aviation Administration			
<i>Direct Programs:</i>			
- Airport Improvement Program	20.106	3-06-0152-19	121,223

See accompanying Notes to Schedule of Expenditures of Federal Awards

**CITY OF MERCED**  
**Schedule of Expenditures of Federal Awards**  
**For the Year Ended June 30, 2012**

Federal Grantor/Pass-Through Grantor/Program Title	Federal CFDA Number	Agency or Pass-Through Grantor's Number	Expenditures
<b>U.S. Department of Transportation</b> (continued)			
<i>Passed through California Department of Transportation:</i>			
Highway Planning and Construction Cluster			
- ARRA - Central Merced Reconstruction - 18th Street	20.205	ESPL-5085(20)	\$ 1,038,412
- Black Rascal Bike Path	20.205	CML-5085(28)	26,370
- Bear Creek Bike Path	20.205	CML-5085(29)	31,905
- South/Central Bike Path	20.205	CML-5085(32)	2,719
Total Highway Planning and Construction Cluster			<u>1,099,406</u>
<i>Passed through California Office of Traffic Safety:</i>			
Highway Safety Cluster			
- DUI Enforcement & Awareness Program	20.600	AL1150	13,856
- AVOID the 11 DUI Campaign	20.600	AL11101	36,048
- DUI Enforcement & Awareness Program	20.600	20236	44,571
- AVOID the 11 DUI Campaign	20.600	20238	31,967
Total Highway Safety Cluster			<u>126,442</u>
<b>Total U.S. Department of Transportation</b>			<u>1,347,071</u>
<b>U.S. Environmental Protection Agency</b>			
<i>Direct Programs:</i>			
- ARRA - Merced Center Brownfield	66.818	2B-00T16001-0	40,697
- Costco Parking Lot	66.818	BF-00T16701-0	13,556
<b>Total U.S. Environmental Protection Agency</b>			<u>54,253</u>
<b>U.S. Department of Energy</b>			
<i>Direct Programs:</i>			
- ARRA - Energy Efficiency Activities	81.128	DE-SC0001848	352,724
<b>Total U.S. Department of Energy</b>			<u>352,724</u>
<b>U.S. Department of Homeland Security</b>			
Federal Emergency Management Agency			
<i>Direct Programs:</i>			
- Assistance to Firefighter Grant	97.044	EMW-2010-FO-03204	386,497
<i>Passed through the California Emergency Management Agency:</i>			
Legislative Pre-Disaster Mitigation Grant	97.047	EMF-2010-PD-0001	26,611
<b>Total U.S. Department of Homeland Security</b>			<u>413,108</u>
<b>Total Expenditures of Federal Awards</b>			<u>\$ 6,937,500</u>

See accompanying Notes to Schedule of Expenditures of Federal Awards

**CITY OF MERCED**  
**Notes to Schedule of Expenditures of Federal Awards**  
**For the Year Ended June 30, 2012**

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**1. REPORTING ENTITY**

The City of Merced (City) was incorporated in 1889 as a charter city. It has a council-manager form of government. The City Council is composed of six members-at-large elected to serve four-year terms, and the mayor who is elected to serve a two-year term. The City Council appoints the City Manager, City Attorney and Finance Officer. The financial reporting entity consists of: (1) the City; (2) organizations for which the City is financially accountable; and (3) organizations for which the nature and significance of their relationship with the City are such that exclusion would cause the City's financial statements to be misleading or incomplete. The following entities are component units of the City:

- The City of Merced Redevelopment Agency
- The City of Merced Public Financing and Economic Development Authority
- The City of Merced Parking Authority

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 financial statements to be misleading or incomplete.

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

*Basis of Accounting*

Funds received under the various grant programs have been recorded within the General, Special Revenue, Capital Projects, and Enterprise funds of the City. The City utilizes the modified accrual method of accounting for General, Special Revenue and Capital Projects funds and accrual basis of accounting for Enterprise funds. The accompanying schedule of expenditures of federal awards (schedule) is presented in accordance with the requirements of the Office of Management and Budget (OMB) Circular A-133, *Audits of States, and Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in the Schedule may differ from amounts presented in, or used in, the presentation of the City's basic financial statements.

*Schedule of Expenditures of Federal Awards*

The accompanying Schedule of Expenditures of Federal Awards presents the activity of all federal financial assistance programs of the City. Federal financial assistance received directly from federal agencies as well as federal financial assistance passed through the State of California is included in the schedule.

The schedule was prepared only from accounts of various grant programs and, therefore, does not present financial position or results of operations of the City.

**3. RELATIONSHIP TO FINANCIAL STATEMENTS**

The amounts reported in the accompanying Schedule of Expenditures of Federal Awards agree, in all material respects, to amounts reported within the City's financial statements. Federal award revenues are reported principally in the City's financial statements as intergovernmental revenues in the General, Special Revenue, Capital Projects and Enterprise funds.

**CITY OF MERCED**  
**Notes to Schedule of Expenditures of Federal Awards**  
**For the Year Ended June 30, 2012**

**4. PASS-THROUGH ENTITIES' IDENTIFYING NUMBER**

When federal awards were received from a pass-through entity; the Schedule of Expenditures of Federal Awards shows, if available, the identifying number assigned by the pass-through entity.

**5. OUTSTANDING LOANS OF FEDERAL FUNDS AT JUNE 30, 2012**

The City administers federal award programs that fund revolving loans. The principal and interest payments collected are returned to the programs. The federal government has imposed certain continuing compliance requirements with respect to the loans under the Community Development Block Grants/Entitlement Grants (CDBG), HOME Investment Partnership Program, and Community Development Block Grants/State's Program and Non-Entitlement Grants in Hawaii. In accordance with Subpart B, Section 205 of the Office of Management and Budget Circular A-133, the City has reported the prior year loans that have continuing compliance requirements as of June 30, 2012, along with the values of total outstanding and new loans made during the current fiscal year in the SEFA.

The following is a summary of the loan programs maintained by the City and their balances at June 30, 2012:

Program Title	CFDA Number	Amount Outstanding	Prior Year Loans with Continuing Compliance Requirements	New Loans
Community Development Block Grants/ Entitlement Grants	14.218	\$ 5,515,489	\$ 5,476,476	\$ 39,013
HOME Investment Partnership Program	14.239	11,678,588	11,658,972	19,616
Community Development Block Grants/ State's Program and Non-Entitlement Grants in Hawaii	14.228	1,722,647	1,674,136	48,511
		<u>\$ 18,916,724</u>	<u>\$ 18,809,583</u>	<u>\$ 107,140</u>

**6. EXTRAORDINARY ITEM - REDEVELOPMENT AGENCY DISSOLUTION**

On June 28, 2011, the California Legislature adopted Assembly Bill 1X 26 (Dissolution Act), which provided for the elimination of redevelopment agencies. 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.

If no local agency elects to serve as a successor agency for a dissolved redevelopment agency, a public body, referred to as a "designated local authority" (DLA) shall be immediately formed. The Governor shall appoint three residents of the county to serve as the governing board of the authority. The designated local authority shall serve as successor agency until a local agency elects to become the successor agency in accordance with the legislation. Because neither the City nor any other local government agreed to serve as the "successor agency", the Governor appointed three residents who met for the first time on August 2, 2012.

**CITY OF MERCED**  
**Notes to Schedule of Expenditures of Federal Awards**  
**For the Year Ended June 30, 2012**

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**6. EXTRAORDINARY ITEM - REDEVELOPMENT AGENCY DISSOLUTION**

After enactment of the law, redevelopment agencies in the State of California cannot enter into new projects, obligations or commitments. Subject to the review of a newly established oversight board, remaining assets of the former redevelopment agency 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 obligations -- including contracts.

The California Redevelopment Association along with others filed suit challenging the constitutionality of Dissolution Act. On December 29, 2011, the California Supreme Court upheld most of the Dissolution Act which effectively dissolved all Redevelopment Agencies as of February 1, 2012.

On January 12, 2012, the Merced City Council took action to retain the housing assets and functions performed by the Redevelopment Agency, but elected not to serve as the successor agency for the non-housing elements of redevelopment.

Effective February 1, 2012, the Redevelopment Agency of the City of Merced was dissolved and all funds closed. The housing assets and liabilities were transferred to the City's Low and Moderate Income Housing Funds and all remaining non-housing assets and liabilities became the responsibility of the successor agency and therefore are not reflected in the financial statement.

On June 27, 2012, the California Legislature adopted Assembly Bill 1484 (AB 1484), which amended the Dissolution Act. Per Health and Safety Code Section 34183, under AB 1484, the county auditor-controller was to determine the amount, if any, owed by each successor agency to taxing entities and was to provide a demand for payment to the successor agency by July 9, 2012, the "true-up payment".

The true-up payment funds were to be paid to the county by the successor agency no later than July 12, 2012 for deposit into the Redevelopment Property Tax Trust Fund and subsequent distribution by July 16, 2012 to taxing entities.

The County of Merced did not provide such a demand and because no successor agency had been formed, and in order to comply with the legislation, and to avoid both the potential interruption of either sales and use taxes or property taxes or both as well as penalties under AB 1484, the City of Merced remitted all uncommitted funds in the amount of \$5,634,827 from the former Redevelopment Agency to the County of Merced on July 12, 2012.

In order to further prevent the accrual of penalties or the interruption of revenue to the Merced Designated Local Authority or the City, the DLA filed suit on December 24, 2012 against the State Department of Finance, the State Board of Equalization, and the County Auditor-Controller to prevent the immediate application of AB 1484's tax interruption or penalty provisions (*Merced Designated Local Authority V. State Department of Finance et al., Sacramento County Superior Court Case No. 34-2012-80001351-CU-WM-GDS*). A stipulated temporary restraining order was issued by the court on January 2, 2013.

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**CITY OF MERCED**  
**Schedule of Findings and Questioned Costs**  
**For the Year Ended June 30, 2012**

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**Section 1**

Financial Statements

Summary of Auditor's Results

- |  |               |
|--|---------------|
| 1. Type of auditor's report issued:  | Unqualified   |
| 2. Internal controls over financial reporting:                                   |               |
| a. Material weaknesses identified?   | No            |
| b. Significant deficiencies identified not considered to be material weaknesses? | None Reported |
| 3. Noncompliance material to financial statements noted?                         | No            |

Federal Awards

- |   |                                     |
|---|-------------------------------------|
| 1. Internal control over major programs:  |                                     |
| a. Material weaknesses identified?  | No                                  |
| b. Significant deficiencies identified not considered to be material weaknesses?  | None Reported                       |
| 2. Type of auditor's report issued on compliance for major programs:  | Unqualified for all major programs. |
| 3. Any audit findings disclosed that are required to be reported in accordance with OMB Circular A-133, Section 510(a)? | No                                  |
| 4. Identification of major programs:  |                                     |

<b>CFDA</b>		
<b>Number</b>	<b>Grantor's Number</b>	<b>Program Title</b>
CDBG - Entitlement Grants Cluster		
14.218	B-10-MC-06-0044	Community Development Block Grant (CDBG)
14.218	B-11-MC-06-0044	Community Development Block Grant (CDBG)
CDBG - State's Program and Non-Entitlement Grants in Hawaii		
14.228	B-11-MN-06-0012	Neighborhood Stabilization Program
14.228	10-NSPR-6571	Neighborhood Stabilization Program
14.251	B-09-SP-CA-0149	HUD Economic Development Investment
97.044	EMW-2010-FO-03204	Assistance to Firefighter Grant

**CITY OF MERCED**  
**Schedule of Findings and Questioned Costs**  
**For the Year Ended June 30, 2012**

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Federal Awards

Summary of Auditor's Results

- |   |           |
|---|-----------|
| 5. Dollar threshold used to distinguish between Type A and Type B programs?       | \$300,000 |
| 6. Auditee qualified as a low-risk auditee under OMB Circular A-133, Section 530? | Yes       |

**Section 2**

Financial Statement Findings

No financial statement findings were noted for the year ended June 30, 2012

**Section 3**

Federal Award Findings and Questioned Costs

No findings or questioned costs were noted on the City's major programs for the year ended June 30, 2012

**Section 4**

Prior Year Findings and Questioned Costs

No findings or questioned costs were noted on the City's major programs for the year ended June 30, 2011.