



December 31, 2006

To the People of the City of Eureka
Represented by the Honorable Mayor and Members of City Council of the City of Eureka

In accordance with State and Local Statutes, the City of Eureka hereby submits the Comprehensive Annual Financial Report for the year ended June 30, 2006. Responsibility for both the accuracy of the presented data and the completeness and fairness of the presentation, including all disclosures, rests with the City. We believe the data, as presented, is accurate in all material aspects; that it is presented in a manner designed to fairly set forth the financial position and results of operations of the City as measured by the financial activity of its various funds; and that all disclosures necessary to enable the reader to gain maximum understanding of the City's financial affairs have been included.

The Comprehensive Annual Financial Report (CAFR) is presented in three sections: Introductory, Financial, and Statistical. The Introductory section includes this transmittal letter, a table of contents, the City's organizational chart, and a list of principal officers. The Financial section includes the unqualified opinion of our independent auditors, Moss, Levy & Hartzheim, Certified Public Accountants, the management's discussion and analysis, the basic financial statements and notes to these statements, followed by supplementary information. The Statistical section includes information about financial trends, revenue and debt capacity, as well as demographic, economic and operating information, generally presented on a historical basis.

Generally Accepted Accounting Principles (GAAP) for State and Local governments requires that management provide a narrative introduction, overview, and analysis to accompany the basic financial statements in the form of Management's Discussion and Analysis (MD&A). This letter of transmittal is designed to complement MD&A and should be read in conjunction with it. The City of Eureka's MD&A can be found immediately following the report of the independent auditors.

PROFILE OF CITY OF EUREKA

General Information

The City of Eureka is a charter City, incorporated as a town on April 18, 1856, under a special act of the legislature; reincorporated as a City on February 19, 1874; and incorporated under a Freeholders Charter on February 8, 1895. The City has been declared a State Historic Site because of its significance in the development of California. The City operates under a Council - Manager form of government with a five-member Council elected to four year overlapping terms, and the Mayor being elected for a four year term. The position of City Manager is filled by appointment of the Council to serve as Administrator of the Staff, and to carry out the policies of the Council. The City Attorney and City Clerk are also appointed by the Council.

The City of Eureka is located along Humboldt Bay (California's second largest deep-water port), on the Northern California coast, 280 miles north of San Francisco, and 450 miles south of Portland, Oregon. Eureka is also the county seat for the County of Humboldt. The City has an approximate population of 27,050 and its boundaries encompass 17 square miles. Extracting timber and the processing of wood byproducts, along with agriculture, fishing, tourism, and government have historically been the pillars of the local economy.

The City of Eureka provides a full range of services, including police and fire protection; the construction and maintenance of highways, streets, and other infrastructure; and various recreational activities. Certain redevelopment activities are carried out by a blended component unit of the City. The Eureka Redevelopment Agency was created by the City Council during the year ending June 30, 1992. The Agency was given the authority and responsibility to redevelop and upgrade blighted areas of the City. Of the City's 17 square miles, 1.97 square miles are included in the Agency boundaries. The City Council also functions as the Board of the Eureka Redevelopment Agency. Financing for redevelopment activities is provided through another blended component unit of the City, the Eureka Public Financing Authority. The City Council created the Authority to sell bonds and lend the proceeds of bond issues to the Agency. The City Council also functions as the Board of the Eureka Public Financing Authority.

Reporting Entity and Its Services

This report includes all of the funds of the City. Financial information for separate legal entities related to the City of Eureka, including the Eureka Redevelopment Agency, and the Eureka Public Financing Authority, are also accounted for in this City's financial statements in accordance with the Government Accounting Standards Board (GASB) Statement No. 14 *The Financial Reporting Entity*.

City Council members serve as the governing board of the Redevelopment Agency. The City provides accounting and administrative services to the Redevelopment Agency. Additional detail is provided in Note 1. A of the Notes to the Financial Statements.

Eureka is a full service city with 272 authorized full-time and regular part-time personnel. This includes public safety (Police and Fire), highways and streets, public improvements, land use, building and housing standards, culture - recreation programs, parks and recreation areas, water, harbor and sewer utilities, public transit, and administration and fiscal services.

Accounting System and Budgetary Control

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.

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 sheet. The Statement of Revenue, Expenditures and Changes in Net Assets present increases (revenue 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.

In developing and evaluating the City's accounting system, consideration is given to the adequacy of internal accounting controls. Internal accounting controls are designed to provide reasonable, but not absolute, assurances regarding (1) the safeguarding of assets against loss from unauthorized use or dispositions, and (2) the reliability of financial records for preparing financial statements and maintaining accountability of assets. The concept of reasonable assurances recognizes that the cost of a control should not exceed the benefits likely to be derived; and the evaluation of costs and benefits requires estimates and judgments by management.

All internal control evaluations occur within the above framework. The City's internal accounting controls adequately safeguard assets and provide reasonable assurances of proper recording of financial transactions.

Annual appropriated budgets are adopted for all funds of the City except agency funds. Appropriations include amounts encumbered at year end, and these encumbrances are not reappropriated in the following year. All annual appropriations lapse at fiscal year end. Legally adopted budgetary appropriations are enacted by fund at the department level for current operating expenditures, with separate appropriations for capital and other projects, debt service, reserves, transfers and contingencies. Expenditures cannot legally exceed appropriations at these control levels. Amendments to the budget at the legal appropriation level must be approved by City Council. Amendments to the budget at less than the legal appropriation level may be made by management.

Project-length financial plans are adopted for capital and other projects. Appropriations for these projects are included in the annual appropriated budgets for each of the applicable funds. Unspent project amounts are included in the annual budgets of subsequent years until project completion. The objective of these budgetary controls is to ensure compliance with legal provisions contained in the annual appropriated budget approved by the City Council.

ECONOMIC CONDITIONS AND OUTLOOK

The growth and health of Eureka's economy can be traced to a variety of indicators.

Employment Rate. The average unemployment rate for the calendar Year 2006 for Humboldt County was 6.4 percent compared to 5.1 percent for the State. This was a decrease of .05 percent from the preceding year. The County labor force decreased during the year by 1,700 to 59,800. The number of employed decreased during that time by 1,500 to 56,400.

Building Activity. During the fiscal year 1,067 construction permits were drawn, as presented in the Statistical Section table "Operating Indicators by Function/Program".

Housing. A wide variety of homes and land are available in the Eureka area, from modest residences to estates. Based on 2006 Information. Humboldt County's median cost for housing was \$295,500 compared with a statewide average of \$555,290 and a national existing home average of \$218,000. Median 2006 home sales in Eureka averaged \$290,000 with prices ranging from \$189,000 to \$1,399,000.

Retail Sales. Shopping districts are abundant throughout the City of Eureka. There is a traditional downtown region offering over 700 retail and service related businesses - Old Town Eureka - with 150 specialty shops in a redeveloped Victorian waterfront setting; the Eureka Mall a large center with 16 stores; the Bayshore Mall, a regional mall with approximately 100 stores; and a variety of neighborhood shopping centers.

This multitude of retail opportunities strengthens Eureka's dominance as a regional trade center and is clearly supported by the fact that the City has higher retail sales for taxable items per capita than other cities in the Humboldt County area. Eureka is strong in the areas of fuel/service stations, business/industry, and building materials. In 2006, there were 1,566 retail permits issued in Eureka, with a total of \$854,912,000 in taxable transactions.

Industrial Property. 756.2 acres in the City limits are zoned light and heavy industrial with about 25.4 percent vacant and available in one parcel of 38 acres. Typical sales prices in 2006 ranged from \$0.30 to \$0.45 per square foot for parcel with flat terrain and adequate drainage. Subsoil is fair, and piling is required in some areas. Sewer mains and lines range from 8 to 12 inches.

Eureka has been designated as one of 42 Enterprise Zones in the State of California, providing existing, new, and expanding businesses with numerous economic benefits and tax incentives.

Financial Planning - Fiscal Year 2005-06

The financial plan for the year, as adopted by the City Council, represents a balance between planning for the future and delivering services to our citizens today. The operating programs were designed to maintain existing service levels. The 2005-06 budget included financial support for a number of future planning efforts. At the same time, the capital budget primarily consisted of projects intended to maintain or rehabilitate existing City facilities, as opposed to constructing new facilities.

Major progress was made in a number of areas critical to the well-being of the City. These include:

- The Fiscal Year 2005-06 Budget continued our approach to budgeting which is the measurement of service performance. The basis for this was our continued focus of giving priority to programs which produce outcomes desired by the citizens and to ensure citizens get at least a dollar's worth of service for each dollar invested. For each program, measures of effort and resources were identified. These include: income, expenditures, and employees used to provide a program. Measures of performance were identified and related to measures of effort. From this the efficiency and effectiveness of the process being used to convert resources into outcomes can be determined. The public and elected officials can readily see what level of resources is needed for each service. Decisions can then be made about what modifications in service delivery should be implemented.
- In response to slow General Fund revenue growth and the revenue losses due to the State budget crisis, a number of proactive budget actions were taken with the adoption of the Fiscal Year 2005-06 Financial Plan, including minimal increases in operating expenditures, deferral of capital improvement projects, and maintenance deferral.
- A Cost-of-Service study update was completed on the City's Water System. The study analyzed the City's rate structure for the Water Utility and developed a microcomputer model of the City's rate structure so various rate structures could be considered. The information gained from the model has provided the detail for implementing a 12 percent rate adjustment during 2005-06. Another Cost-of-Service study was completed on the City's Wastewater System resulting in a 3 percent rate adjustment during 2005-06 to the sewer rates.

- Internal Service Fund Balances. The administration of the City's Workers Compensation Insurance Fund, and the Liability Insurance Fund were addressed during Fiscal Year 1992-93, by the City joining a Joint Powers Authority for Insurance Coverage. To offset the unfunded deficits which existed in the Worker's Compensation and Liability Insurance Funds, an advance was made in fiscal year 1995-96 from the City's Wastewater Fund to be repaid over a 10 year period with interest. With the recurring losses in the City's Group Health and Benefit fund along with health care benefits continuing to increase, the City Council made the decision to no longer be self-funded for health care benefits as of August 1, 2002.
- A major water transmission line replacement project totaling \$8 million dollars began during the 2001-02 fiscal year and continued into the 2005-06 fiscal year.
- The City was awarded a \$1 million loan from the State HOME program, and a \$500,000 State CDBG grant to purchase and rehabilitate the Multiple Assistance Center (MAC) during fiscal year 2001-02. During the 2002-03 fiscal year an additional \$500,000 EHAP grant was received and \$750,000 has been earmarked from Eureka Redevelopment Agency funds. Additional local funding grants and loans totaling \$765,000 will go towards this \$3.5 million project. The MAC project provides on-site housing, job training and care of homeless persons and their families, and is intended to provide a more efficient and effective distribution of existing homeless services. Construction on this project completed during the 2004-05 fiscal year and the City continued monitoring of this county wide facility during the 2005-06 fiscal year.
- A major harbor revitalization project that has been in the planning stages for many years began the funding stage during the 2004-05 fiscal year. The Fisherman's Terminal Project constitutes Phase II of the Inner Channel Dock and Boardwalk Revitalization Project. Phase I of the Boardwalk project was completed in the 2002-03 fiscal year. Total costs of Phase II are estimated at \$5.8 million and construction began in the 2003-04 fiscal year. Funding will come from various sources: State Coastal Conservancy grant of \$1.5 million; US Department of Commerce grants of \$700,000; State Department of Fish and Game, Wildlife Conservation bond of \$500,000 and Eureka Redevelopment Agency funding of \$2.4 million. Construction continued throughout the 2005-06 fiscal year.
- The City of Eureka completed its annual process of updating a comprehensive schedule of fees and service charges. This schedule provides operating departments, within the City, the means to distribute information regarding fees and service charges.
- With the November, 1996 passage of Proposition 218, the "taxpayers right to vote," the City took its Utility User Tax to the voters and received validation to charge this tax on electric, gas, telephone and cable TV utilities. Extended in November 1997 for five years, this tax went back to the voters in November 2002 and also November 2006 and was extended for four more years until July 1, 2011.

Prospects for the Future

The City continually strives to improve the level and quality of service provided to its citizens as has been demonstrated through the various on-going and enhanced service levels contained with the City's Fiscal Year 2005-06 budget. In future years, the City's goals and objectives will continue to be reflective of the desire to improve the quality of life for Eureka's citizens.

- The General Fund. For several consecutive years we have adopted balanced General Fund budgets. Still, we need to remind ourselves that simply making ends meet one year to the next is not the same thing as sufficiently financing this organization's future.

The full financial picture is made up of several components: contingency reserves that cushion annual fluctuations in revenue collections, sufficient fund balance that protect against disaster and uncertainty, ongoing and consistent capital planning and improvements, adequate funding of liabilities, and continuation of competitive compensation for our workforce. For the continuation of current services to this community, our long-term General Fund financial planning must include revenue enhancement, expenditures reduction through increased efficiencies, or some combination of the two.

Changes in the legal environment have made matters worse. Propositions 62 and 218, with their requirement for voter approval of nearly all fees and taxes, have created severe restriction on our ability to offset growth in the cost of doing business. Budget challenges at the State level have taken their toll on local revenues.

- **Street & Road Maintenance.** Clearly, one of the greatest challenges facing us is the need to maintain the City's street and road infrastructure. In FY 2005-06 and beyond, the City is faced with the need to fund approximately \$1.5 million per year related to street maintenance. This equates to the portion of the operating budget that has been funded historically with "one-time" funding rather than with operating revenue. It is staff's belief that based on revenue and expenditure trends, the Eureka economy, and prudent budget development and monitoring, this needed level of funding will be available for not only street maintenance but for sidewalk maintenance as well.

- **Federal and State Government Actions.** State government deficits will affect counties and cities for the next six to eight years. The trend toward greater and more frequent intrusions on local government finance has been firmly established by State elected officials in Sacramento. Consider, for example, the current reductions in Vehicle License Fees, the reduction in State Mandated Claim reimbursements and ERAF shifts from the City and Redevelopment Agencies. Again we find ourselves pitted against the State government and in competition for scarce economic resources. Add to the list of our obligations the need to vigilantly watch over the actions of State government officials who are, in the final analysis, unaccountable to our community.

- **Business Development and Retention.** We continue to work in partnership with the business community, strengthening our formal and informal ties to local commerce, to develop our community's business potential. We emphasize assistance for businesses considering relocation into our community equally with retention efforts for businesses considering relocation outside of Eureka.

- **Technology.** Intensified deployment of technology will continue to be an important priority for the City. The city will strengthen its presence on the World Wide Web to provide continued access to a wide range of useful information and more convenient ways of transacting City business. The City's web site was reconstructed during the 2005-06 fiscal year.

- **Infrastructure Construction and Improvements.** With the exception of the water and wastewater capital improvements we embark upon this year, we fall far short of meeting the City's infrastructure needs. Most available funding continues to find application in operational budgeting areas, meaning that the rate of decline in the usefulness of our City's infrastructure base has outpaced our ability to carry out needed capital upgrading and replacement.

- **Redevelopment Project Financing.** The Eureka Redevelopment Agency took advantage of the opportunity to refinance outstanding 1993 tax allocation bonds during the 2003-04 budget year. Low interest rates and a "call" date in November 2003 afforded the agency a savings of approximately \$700,000 annually over the next ten years. With this savings in debt service payments the deficit position within the Eureka Tomorrow Project area will be reduced and funds will become available to use for continued development within the Agency boundaries.

RELEVANT FINANCIAL POLICIES

Cash Management

Cash temporarily idle during the year was invested in certain eligible securities as constrained by law and the City's Investment Policy. The City invests in demand deposits, time deposits, securities of the U.S. Government or its Agencies, bankers acceptances, corporate notes and bonds, repurchase agreements, mortgage backed securities, money-market and other mutual funds, commercial paper, and the Local Agency Investment Fund. The goals of the City's investment policy are safety, liquidity, and yield. The average yield on pooled investments at June 30, 2006 was 5.06 percent with an average maturity of 1.86 years.

Risk Management

As more fully explained in Note 10 of the notes to the financial statements, the City participates in a public entity risk pool for general liability, workers' compensation, and property insurance coverage. All funds of the City are participants in these programs and make payments to internal service funds based upon estimates of the amounts needed to pay operating expenditures of the fund, prior- and current year claims, and where applicable to establish reserve for losses.

Independent Audit

The City requires an annual audit by an independent certified public accountant. The accounting firm of Moss, Levy & Hartzheim, Certified Public Accountants conducted this year's audit. The auditors report on the basic financial statements and schedules is included in the financial section of this report. The audit was also designed to meet the requirements of the Federal Single Audit Act as amended in 1996, and related OMB Circular A-133, *Audits of States; Local Governments; and Non-Profit Organizations* (68 FR 38401).

AWARDS AND ACKNOWLEDGMENTS

Awards

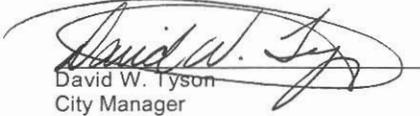
The Government Financial Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the City of Eureka for its Comprehensive Annual Financial Report for the fiscal year ended June 30, 2005. In order to be awarded a Certificate of Achievement, a government must publish an easily readable and efficiently organized Comprehensive Annual Financial Report. This report must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe that our current Comprehensive Annual Financial Report continues to meet the Certificate of Achievement Program's requirements and we are submitting it to the GFOA to determine its eligibility for another certificate.

Acknowledgments

The preparation of this report could not have been accomplished without the efficient and dedicated services of the staff of the Finance Department. We would like to express our appreciation to the independent auditing firm of Moss, Levy & Hartzheim, Certified Public Accountants for their guidance. We would also like to thank the Mayor and members of the City Council for their interest and support in planning and conducting the financial operation of the City in a responsible and progressive manner.

Respectfully Submitted,


David W. Tyson
City Manager


Carolynn Thomas
Finance Director

Certificate of Achievement for Excellence in Financial Reporting

Presented to

City of Eureka
California

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
June 30, 2005

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



President

Executive Director

City of Eureka, California
Principal City Officials
June 30, 2006

Peter La Vallee
Mayor

City Council

Chris Kerrigan
Council Member

Virginia Bass-Jackson
Council Member

Mike Jones
Council Member

Jeff Leonard
Council Member

Mary Beth Wolford
Council Member

Administration

David W. Tyson
City Manager

Kathleen Franco Simmons
City Clerk

David Tranberg
City Attorney

David Douglas
Police Chief

Eric Smith
Fire Chief

Kevin Hamblin
Director of Community Development

Brent Siemer
City Engineer

Mike Knight
Public Works Director/Building Official

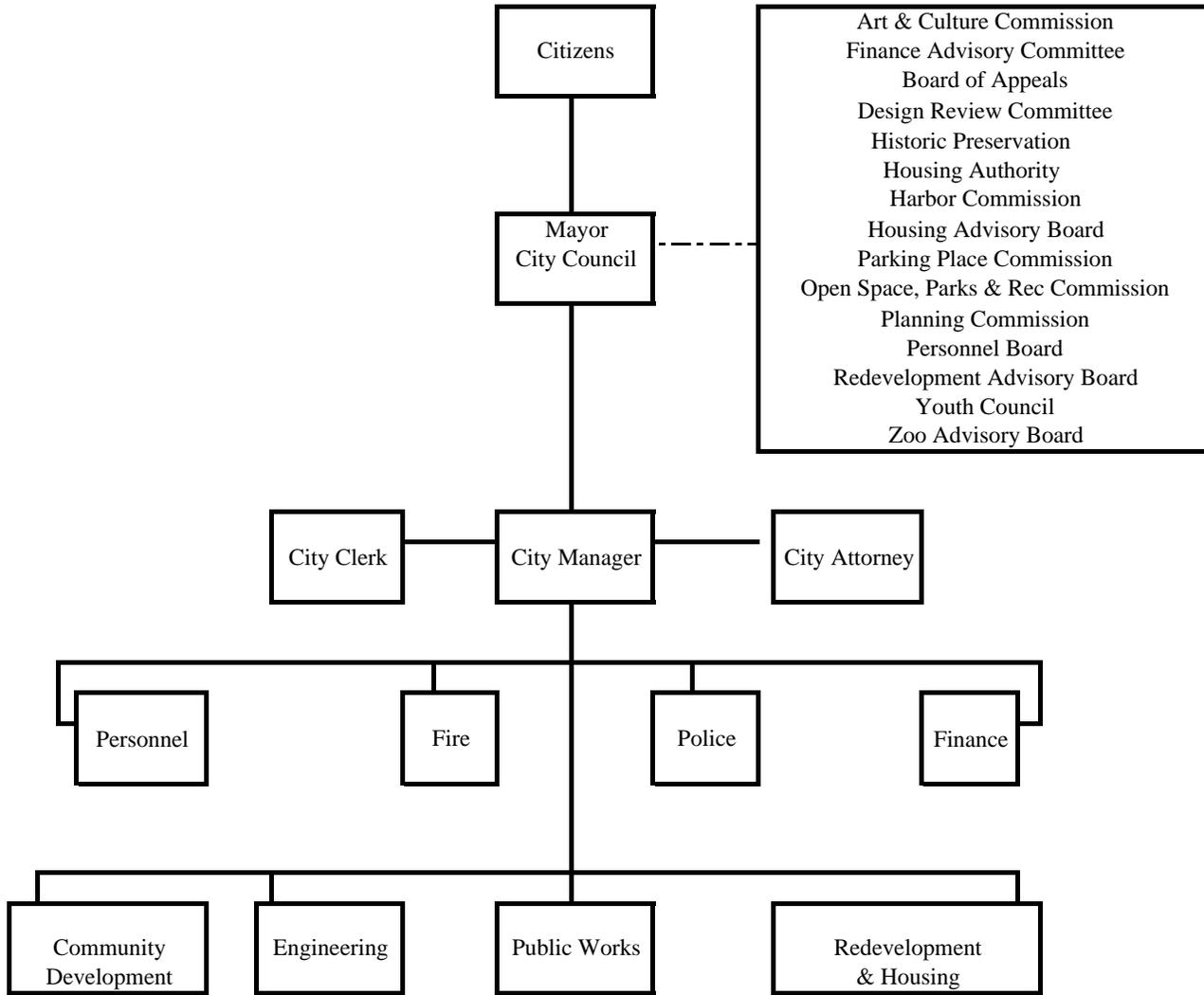
Carolynn Thomas
Finance Director

Cindy Trobitz-Thomas
Redevelopment & Housing Director

Susan Christie
Personnel Director

City of Eureka

Organizational Chart



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