

INTRODUCTORY SECTION



March 29, 2012

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

Local and state statutes require that the City of Eureka issue a report on its financial position and activity following the close of each fiscal year. In addition, this report must be audited in accordance with generally accepted auditing standards by an independent firm of certified public accountants. Pursuant to that requirement, we hereby issue the basic financial statements of the City of Eureka for the fiscal year ended June 30, 2011.

This report consists of management's representations concerning the finances of the City. Consequently, responsibility for the accuracy of the data and the completeness and fairness of the presentation, including all disclosures, rests with management. To provide a reasonable basis for making these representations, management has established a comprehensive internal control framework that is designed both to protect the government's assets from loss, theft or misuse and to compile sufficient reliable information for the preparation of the City's financial statements in conformity with Generally Accepted Accounting Principles (GAAP). Because the cost of internal controls should not outweigh their benefits, the City's comprehensive framework of internal controls has been designed to provide reasonable rather than absolute assurance that the financial statements will be free from material misstatement. As management, we assert that, to the best of our knowledge and belief, this financial report is complete and reliable in all material respects.

The City of Eureka's financial statements have been audited by Moss, Levy & Hartzheim, LLP, a firm of licensed certified public accountants. The goal of the independent audit was to provide reasonable assurance that the financial statements of the City of Eureka for the fiscal year ended June 30, 2011, are free from material misstatement. The independent audit involved examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements; assessing the accounting principles used and significant estimates made by management; and evaluating the overall financial statement presentation. The independent auditor concluded, based upon the audit, that there was a reasonable basis for rendering an unqualified opinion and that the City of Eureka's financial statements for the fiscal year ended June 30, 2011, are fairly presented with GAAP. The independent auditor's report is presented as the first component of 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).

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 26,002 and its boundaries encompass 11 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, 1972. The Agency was given the authority and responsibility to redevelop and upgrade blighted areas of the City. Of the City's 11 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 Redevelopment Agency. Additional detail is provided in Note 1 A of the Notes to the Financial Statements.

Eureka is a full service city with 251 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.

Annual appropriated budgets are adopted for all funds of the City except agency funds. All annual appropriations lapse at fiscal year end. Any encumbrances not fully expended at year end are closed. 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.

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 contains 150 specialty shops in a redeveloped Victoria waterfront setting. The Eureka Mall is a large center with 16 stores, and the Bayshore Mall is a regional mall with approximately 100 stores. 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. Sales tax for fiscal year 2010-11 increased 19.25 percent, compared to the previous year as the economy shows signs of rebounding.

Hospitality. The City of Eureka is a popular California tourism destination and contains approximately 40 hotels, motels and inns. The City's Transient Occupancy Tax remains a strong revenue source. Fiscal year 2010-11 revenue from TOT remained stable, showing a very slight decrease of 1.5% over the previous year. 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.

Long-Term Financial Planning

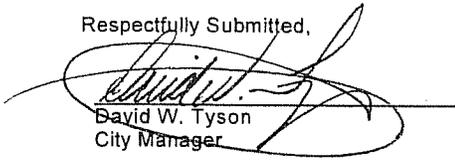
The City, in fiscal year 2012, expects the local economy to remain stable, but given the uncertainty in both the state and national economies, continues to monitor the situation daily in order to react and adjust in the most fiscally prudent manner.

The State budget situation was such in fiscal 2011 that the City experienced a reduction in property tax revenues as a result of mandated State reductions. Additional State takeaways continue to plague cities and counties throughout California, most recently with California State Supreme Court upholding AB1X26, thus eliminating Redevelopment Agencies.

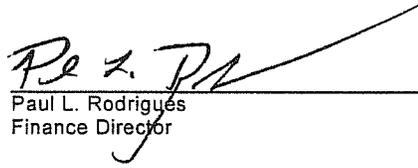
Acknowledgments

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 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 manner. Finally we recognize and appreciate the work of the members of the Finance Advisory Committee.

Respectfully Submitted,



David W. Tyson
City Manager



Paul L. Rodriguez
Finance Director

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